

GST & bare trust arrangements

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GST Ruling GSTR 2008/3 considers the GST treatment of trustees and beneficiaries of a **bare** trust. In this article, we discuss the GST issues associated with bare trusts and, in particular, the implications of transfers of real property in the context of such arrangements.

Scope of GST Ruling

The ATO's new ruling does not apply to all bare trusts. To begin with, the ATO indicates that its ruling is limited in its application to bare trusts having at least one of the following features:

- created intentionally by written instrument; or
- the creation of the trust is expressly recorded (eg in a deed); or
- the creation of the trust is recorded in the minutes of a meeting of the trustee and settlor of the trust; or
- the creation of the trust is by trustee resolution; or
- certain resulting trusts, where an intending purchaser places funds in the hands of a nominee to purchase real property and the legal title is vested in the nominee rather than the intending purchaser (paragraph 4).

The ATO adds also that its ruling does not apply to situations where dealings in the trust property would result in the trust carrying on an enterprise with the property. Further, it would seem that the ruling may not apply to constructive trusts which arise by operation of law (eg in the context of certain marital arrangements).

What is a bare trust?

Under general law, a bare trust is a “trust under which the trustee or trustees hold property without any interest therein, other than that existing by reason of office and the legal title as trustee, and without any duty or further duty to perform, except to convey it upon demand to the beneficiary or beneficiaries or as directed by them, for example, on sale to a third party” (*Herdegen v FC of T* 88 ATC 4995 at 5003).

However, in addition to the above general law meaning, the ATO considers the expression “bare trust” to extend also to trusts of a kind that may not strictly fall within the accepted general law definition, but that have similar features. Also, by way of further extension, the ATO will regard a trust as a bare trust even where the trustee has certain minor active duties to perform (paragraph 12).

Treatment of bare trusts

All types of trusts, including bare trusts, are considered entities for GST purposes (section 184-1(1)(g) of the GST Act). Moreover, the GST Act does not set out any special rules relating to certain trusts, but not others.

The GST position for bare trusts, like all trusts, is simply determined by the general concepts in the legislation. However, by reason of the legal characteristics of trust arrangements themselves, trusts raise certain GST issues that need to be addressed. In particular, in the case of a bare trust arrangement, the issues arise as to who the relevant supplier is, who the relevant recipient is and whether a taxable supply or creditable acquisition can arise in the context of such an arrangement. Of note, as there are no special rules in relation to bare trusts, this will need to be determined by an application of the general rules under GST law.

Who is the supplier/acquirer?

In determining who the supplier is in the context of a bare trust situation, the ATO will adopt a commercial approach having regard to the true character of the arrangement being considered.

In the context of a trust arrangement, the ATO will take the view that for GST purposes, the entity in the course of carrying on an enterprise will not need to possess legal title to assets to be supplying or acquiring for taxable supplies or creditable acquisitions to be made.

Thus, if a bare trust arrangement exists independently of who holds title, it will be necessary to determine whether it is the trust or the beneficiary that is the entity making the supply.

In its Ruling, the ATO assumes that the beneficiary is the entity actually carrying on an enterprise and the trust itself does not carry on an enterprise in relation to the trust property (paragraph 38). That is, the trustee holds the trust property on trust for the beneficiary and the beneficiary is carrying on an enterprise in relation to the property. Accordingly, ordinarily, it will be the beneficiary that will be the entity making the relevant supply.

Having ruled that the beneficiary is the entity making the supply, the ATO also discusses the GST implications of a change in trustee and a change in beneficiary.

Change of trustee

According to the ATO, no GST implications result from a change in trustee, as such a transfer is not a taxable supply made in the course of an enterprise carried on by the outgoing trustee in respect of the trust property. However, this only applies if the incoming trustee resumes the duties of the outgoing trustee. That is, the incoming trustee has no active duties or only has minor active duties.

Also, the incoming trustee will not be making a creditable acquisition of the legal title as the incoming trustee will not be making an acquisition in the course of carrying on an enterprise (paragraphs 68 and 69).

Change of beneficiary

If there is a change of beneficiary, this may constitute a disposal of a beneficial interest in the trust property by the outgoing beneficiary to the incoming

beneficiary. As a result, a taxable supply will result if all of the requirements of a taxable supply are met by the outgoing beneficiary.

Also, the new beneficiary may be making a creditable acquisition, if the requirements in section 11-5 of the GST Act are met (paragraph 72).

Agency and bare trusts

An important issue that arises in the context of a bare trust arrangement is whether an agency relationship exists between the trustee and the beneficiary. In the ATO's view, an agency relationship does not necessarily arise in all bare trust situations. However, it may arise in some cases and the ATO discusses the circumstances where it will find an agency relationship. In particular, the ATO discusses the GST implications of such an agency for the issue of a tax invoice, the margin scheme and the going concern provision, in a real property transaction.

Tax invoices

In general, the entity that makes a taxable supply or a creditable acquisition, in a bare trust arrangement, is the beneficiary. In these circumstances, the trustee issues or holds a tax invoice on behalf of the beneficiary. Nevertheless, the requirements for a valid tax invoice under GST law must still be met (paragraphs 78 and 79). As such, if the trustee meets all of the requirements of a valid tax invoice under GST law, the beneficiary will be deemed to have met all the requirements under GST law. This will be the case even if the tax invoice includes the details of the trust, instead of the beneficiary's details. In other words, a GST outcome similar to that which arises in the context of agency arrangements applies.

Margin scheme supplies and supplies of a going concern

For the margin scheme to apply to a taxable supply of real property, the supplier and the recipient must agree in writing to its application. For the supplier (ie the beneficiary in a bare trust arrangement), this requirement will be met if the trustee agrees in writing that the margin scheme is to be applied. In such a case,

the trustee will effectively be construed as acting on behalf of the beneficiary (notwithstanding the existence of the bare trust).

Similarly, for a supply of a going concern, there is a requirement that the agreement by the supplier and the recipient be in writing. In a bare trust arrangement, this requirement will be met if the trustee agrees in writing that the supply is of a going concern. In such a case, the trustee will again be treated as acting on behalf of the beneficiary. Thus, the beneficiary will meet the requirement for a supply of a going concern, if all of the other requirements of a supply of a going concern are met (paragraphs 81 and 83).

Example: Real property development

Having examined the above specific issues relating to bare trusts, the ATO then provides an examination of the main concepts in the context of a real property development transaction.

In particular, the ATO considers the following fact scenario:

- (1) A partnership, P, carries on a property development enterprise. P would like to purchase some land on which strata titled residential units will be constructed. P acquires a shelf company, T, to act as bare trustee for P in the acquisition of the land. T executes a declaration of trust effecting a bare trust.
- (2) T enters into a contract for the acquisition of land from S with funds provided by P. T is the legal owner of the land but holds it on trust for P. P makes arrangements with contractors for the construction of the unit developments and with real estate agents for the marketing of the units. P arranges for T to execute any documents when the legal owner of the land is required.
- (3) P also arranges for several units to be leased and T executes the required leases upon P's direction.
- (4) P arranges for T to execute the necessary contracts for sale of the strata units when buyers are found. T and the buyers, in each case, agree that the margin scheme is to apply to the sale.
- (5) P also retains one of the units and T executes a transfer to P at P's direction. P later sells the unit. The sale occurs in less than 5 years after the unit was built.

Part 1: Creation of trust

No GST implications result from the creation of the trust. There is no supply of an interest in the land by T to P, as the trust is created prior to the acquisition of the land. T also does not carry on any enterprise in respect of the land (paragraph 48).

Alternatively, if P had acquired the land and transferred legal title to the land to T, there would have been no taxable supply as no consideration for the transfer would have been provided. The ATO uses a practical approach to analyse what is in fact supplied. In this instance, it was the mere supply of legal title to the property to be held on a bare trust. The transfer of a bare legal title has no economic value and has no market value. Thus, the provisions concerning a market value deeming for transfers between associates have no impact upon the GST outcome. As such, Division 72 on supplies to associates does not apply (paragraphs 49, 50 and 51).

Part 2: Acquisition of land and other acquisitions

The entity that acquires the land is P. P acquires the land in the course of carrying on its enterprise. P caused T to obtain legal title to the land from S, with funds provided by P, and the title is at all times to be held upon a bare trust for P.

P is entitled to input tax credits if all the requirements of a creditable acquisition are met. However, in this scenario, it is assumed that the margin scheme applies. Thus, P is not entitled to any input tax credits on the acquisition of the land (paragraphs 52 and 53).

However, P may have been entitled to input tax credits on other acquisitions relating to the development and sale of the units, subject to the usual rules applying to such entitlements (paragraph 55).

In all acquisitions, T will not be entitled to any input tax credits, as T does not acquire title to the land in the course of an enterprise it carries on (paragraphs 54 and 56).

Part 3: Leasing of units to third parties

P supplied the leases in the course of carrying on an enterprise and may have an increasing adjustment under Division 129 in respect of acquisitions relating to the construction of the units. As T does not have title in the properties, it will not have any increasing adjustment under Division 129 (paragraphs 57 and 58).

Part 4: Sales to third parties

P makes a taxable supply in the course of carrying on its enterprise and may have a decreasing adjustment after each sale takes place. If the margin scheme is applied, the calculation of the margin on sales is the difference between the selling price of the units and the relevant proportion of the purchase price for the land (paragraphs 59, 61 and 62).

T will not be liable for any GST on the sales, as it does not execute the transfers in the course of an enterprise that it carries on in respect of the land (paragraph 60).

Part 5: Transfer of property to beneficiary and sale by beneficiary

T does not make a taxable supply by transferring legal title to P. The transfer is not made in the course of an enterprise carried on by T in relation to the trust property (paragraph 64).

The subsequent sale by P constitutes a sale of new residential premises as the earlier transfer from T to P is not a sale. GST on the sale is calculated using the margin scheme (paragraphs 65 and 66).

Conclusion

It is perhaps not surprising that the ATO identifies the beneficiary, rather than the trustee or the bare trust, as the entity making a supply for GST purposes in the context of a bare trust arrangement. In this regard, the ATO's view would appear to be consistent with the general law position on bare trusts.

However, the application of agency law to a bare trust arrangement, in particular in its application to the necessity for writing in certain contexts is somewhat unexpected. The ATO appears to be taking a rather lenient approach to the writing requirement allowing either a principal or an agent (with no power of attorney) to reach such an agreement in writing.