

A question of fact – what is an “Enterprise” for GST purposes?



COMMISSIONER OF TAXATION V SWANSEA SERVICES PTY LTD [2009] FCA 402.

INTRODUCTION

On 24 April 2009 the Federal Court handed down its decision in *Swansea Services*¹, which considered whether the Administrative Appeals Tribunal (**Tribunal**) had correctly determined that Swansea Services Pty Ltd (**Taxpayer**) was carrying on an enterprise for the purposes of GST. Before the Tribunal, the Taxpayer argued that during the relevant periods it had carried on an enterprise of investing in antiques and artworks. However, the Commissioner contended that the activities carried out by the Taxpayer were “hobbies” of the Taxpayer’s officeholder and, therefore, that the acquisitions were made as a consumer and not in the course of carrying on an enterprise. The case before the Tribunal provides an important reminder of the factors that must be present for an entity to be carrying on an enterprise for the purposes of GST. The Federal Court found that it was open to the Tribunal to find that the Taxpayer was carrying on an enterprise, and that the Tribunal had not erred in reaching that decision.

The Federal Court decision contains an interesting discussion of whether the determination of whether an entity is carrying on an enterprise for GST purposes is solely a question of fact and consequentially, whether an appeal of a decision made by the Tribunal to the Federal Court is permitted.

BACKGROUND FACTS

The Taxpayer was registered for GST under the *A New Tax System (Goods and Services) Tax Act 1999 (Cth)* (**GST Act**). Since 1997, the Taxpayer’s sole business had been the acquisition

(and occasionally sale) of valuable artworks and antiques. This was supported by the Taxpayer’s tax returns that identified that it acquired artwork and antiques for investment purposes. In the eight years to November 2005, the Taxpayer had spent at approximately \$4,800,000 undertaking these activities. The acquisitions had been financed partly through loans to both the Taxpayer (under which Mr Satterley, the taxpayer’s officeholder, provided a personal guarantee) and to Mr Satterley personally. The Taxpayer treated each of these acquisitions as creditable acquisitions in relation to which it claimed input credits.

Despite the many acquisitions made by the Taxpayer, the Taxpayer did not sell any of the items acquired until November 2002.

The Taxpayer was part of a wider group of companies known as the Satterley Group. The Taxpayer was controlled by Mr Satterley himself; it did not have any employees and relied mainly on services provided by contractors and employees from other companies within the Satterley Group.

In November 2005, the Taxpayer’s collection consisted of some 225 antique items and 87 paintings. Although a few of these items were kept at the head offices of the Satterley Group, or lent out for short periods of time, most of the items were kept on display at two private residences owned by the Satterley Group. Mr Satterley gave evidence that items displayed at his private residence were often viewed as part of charity functions that were regularly organized at his residence by his wife.

The Taxpayer had no written business plan, but rather an “investment strategy” or “underlying philosophy,” including:

“developing a museum quality collection and investing to achieve a 10-15% pa increase, yielding a doubling in value over seven years.”² Further, evidence was given that the intention and purpose of acquiring the artworks had always been based on the view that the artworks were to have an inherent appreciating value and that all the works of the Swansea Collection had been built up as a sound financial investment. All the works were for sale for the “right price”.

In a witness statement to the Tribunal, Mr Satterley acknowledged that, except in the case of the few specific items actually sold, “very little attempt ha[d] been made to date, to actively market the artworks/antiques”³.

On 18 November 2005 the Commissioner of Taxation (**Commissioner**) cancelled the Taxpayer’s registration under the GST Act with retrospective effect from 1 October 2001 because it did not consider that the Taxpayer was carrying on an enterprise for the purposes of s 9-20 of the Act.

RELEVANT LEGISLATION

Section 9-20 – Enterprise:

1. An enterprise is an activity, or series of activities, done:
 - (a) in the form of a business; or
 - (b) in the form of an adventure or concern in the nature of trade; or
 - (c) on a regular or continuous basis, in the form of a lease, licence or other grant of an interest in property...
2. However, enterprise does not include an activity, or series of activities, done:
 - (b) as a private recreational pursuit or hobby...

Section 195-5 definitions:

“Business” is defined to include “any profession, trade, employment, vocation or calling, but does not include occupation as an employee”

“Carrying on” means an enterprise includes doing anything in the course of the commencement or termination of the enterprise.

Section 23-10 addresses who may be registered for GST and provides

1. You may be registered under this Act if you are carrying on an enterprise (whether or not your GST turnover is at, above or below the registration turnover threshold).
2. You may be registered under this Act if you intend to carry on an enterprise from a particular date.

Section 25-55(2) provides for the Commissioner to cancel an entity’s GST registration without the entity’s application to do so and states:

“The Commissioner must cancel your registration (even if you have not applied for cancellation of your registration) if:

- (a) the Commissioner is satisfied that you are not carrying on an enterprise; **and**
- (b) the Commissioner believes on reasonable grounds that you are not likely to carry on an enterprise for at least 12 months.”

TRIBUNAL DECISION

The Tribunal was asked to determine whether the Taxpayer was carrying on an “enterprise” for the purposes of s 9-20 of the GST Act such that the Taxpayer was entitled to be registered for GST under s 23-10(1) of the GST Act. Consequently, it had to determine whether the Taxpayer’s activities were “merely an expression of Mr [Satterley]’s hobby or interest” and/or the making of a long term capital investment as had been argued by the Commissioner.

The Tribunal found in favour of the Taxpayer ruling that the Taxpayer was carrying on an enterprise either “in the form of business” or “in the form of an adventure or concern in the nature of trade” and was therefore entitled to claim input tax credits on acquisitions that relate to the enterprise. In reaching their decision, the Tribunal was assisted by an analysis of the system of value added taxation, of which GST is an example, as outlined by Hill J in

HP Mercantile Pty Ltd v FCT,⁴ where Hill J enunciated that the statutory scheme and syntax and legislative context and purpose carry the day.

The Tribunal reasoned that, in its ordinary meaning, an “enterprise” consists of any activity or activities comprised of one or more transactions entered into for business or commercial purposes. Further, the use of the phrase “in the form of” in s 9-20(1) (a) and (b) of the GST Act exemplifies; first, how the form of the activity itself will suffice to bring the activity within the definition of “enterprise” and secondly the wide scope of activities that are relevant, in accordance with the broad application that the GST Act is intended to have, as enunciated in Explanatory Memorandum. Irrespective of this intention however, the mere existence of an “enterprise” does not, of itself, create GST consequences.

In identifying the definition of “business” for the purposes of s 195-5 of the GST Act, the Tribunal looked to a large body of case law, stimulating the need to assess a number of factors also known as “the badges of trade”. There is an underlying notion that business entails a course of conduct carried on for the purpose or expectation of profit (however small) and some continuity and repetition of actions, keeping in mind that every business has to begin and even isolated activities, may in the circumstances, be held to be the commencement of carrying on business.⁵ Further, the Tribunal also noted that the presence of an intention to carry on business or some other relevant state of mind and the purpose for which the activity is carried on is relevant in characterizing the nature and extent of the activities undertaken.⁶ In the present case, the Commissioner relied heavily on the argument that the transaction of the Taxpayer was isolated and there was no repetition or regularity of sales. The Tribunal found, however that there was no doubt that, in a GST context, the activities of the Taxpayer constituted the activities of a business.

In determining the scope and meaning of “adventures in the nature of trade” for the purposes of s 9-20, the Tribunal was influenced by case law that showed that the acquisition of goods or property with the intention of a future sale, hopefully at a profit, would fall within this concept.⁷

The Tribunal enunciated that, “[i]n the case of artwork, the person acquiring it may have a dual purpose, namely the sale of the artwork at a profit, but pending the favourable sale the artwork will provide aesthetic enjoyment.”⁸

The Tribunal then turned to the issue of whether the current case fitted into any valid exclusion to “enterprise,” specifically, the private recreational pursuit or hobby exception of s 9-20(2)(b) of the GST Act. The Tribunal held that there were no facts to support the Commissioner’s argument that the Taxpayer’s activities fell within this exclusion; on the contrary, the commercial activities of the Taxpayer were “conducted in accordance with a pre-formulated policy, couple with a carefully devised investment strategy...[t]he [Taxpayer] retains specialist art consultants...keeps detailed records... uses a database of records...has an annual budget and banking facilities...its activities are characterized by system, repetition and regularity...consistent only with the carrying on of a business and the conduct of an enterprise.”⁹ The Taxpayer’s activities are not carried on for “the personal refreshment, pleasure or recreation of... persons concerned.”¹⁰ The Tribunal reasoned that the fact that the artworks are displayed or stored in premises owned by related entities of the Taxpayer does not automatically convert the activity of the Taxpayer to that of a hobby. The Tribunal highlighted that the use of a system and systemic conduct is particularly important in distinguishing between a hobby and a business operation. It therefore rejected the argument that an acquisition of an asset as a long term investment cannot be viewed as being an acquisition for business or commercial purposes. Instead, the Tribunal held that “[t]he test should be whether the [Taxpayer] has, objectively viewed, as a matter of fact, commenced or continued to engage in an enterprise, being an activity or services of activities comprised of one or more transactions entered into for business or commercial purpose, done in the form of a business or in the form of an adventure in the nature of trade”.¹¹

Ultimately, the Tribunal found that long-term investment in artwork could be an enterprise for GST purposes, as could the sale of a single asset. The fact that the Taxpayer did not make a profit was deemed to not be a deciding factor and, as the

Taxpayer had the intention to make a profit, the initial losses in sale did not prevent the Taxpayer from making a profit in the future.

to how the principles of law had been applied¹³. The Commissioner, on the other hand, contended that the conclusion that Swansea was carrying on an enterprise

“ the words “in the form of” in the definition of “enterprise” ... extend the impact of “enterprise” to activities which would not in the ordinary meaning a “business”, be considered as such ”

ISSUES BEFORE THE FEDERAL COURT

The Commissioner appealed against the decision of the Tribunal to the Federal Court. The Commissioner asked the Federal Court to determine whether there was any evidence on which the Tribunal could properly base its decision that the Taxpayer was carrying on an enterprise and thus entitled to be registered for GST purposes?

As a primary matter, it was necessary for the Federal Court to determine whether the question of whether an enterprise is being carried on pursuant to s 9-20 of the GST Act is a question of law to which the Federal Court may hear an appeal from the Tribunal pursuant to s 44 of the *Administrative Appeals Tribunal Act*?

FEDERAL COURT DECISION

Competency of the Appeal – Is there a question of Law?

The case of *Waterford v Commonwealth* upholds the proposition that “a finding by the Tribunal on a matter of fact cannot be reviewed on appeal unless the finding of fact is vitiated by an error of law”.¹² However, in the present case the Federal Court reasoned that distinguishing between a question of law and a question of fact is not always straight forward.

The Taxpayer contended that the Tribunal had correctly identified the relevant principles of law and the only question related to how the Tribunal had applied those principles of law to the facts. This, it argued, was *normally* a question of fact even though the Federal Court might have reached a different conclusion as

was so unreasonable and so incapable of support from any of the evidence before the Tribunal, that the decision that the Taxpayer was carrying on an enterprise could not possibly have been reached other than by error of law in disregarding crucial evidence that necessitated a conclusion that the relevant activities were a private hobby, interest or long term private investment strategy.¹⁴ The Commissioner’s further contention was that the Tribunal relied on irrelevant evidence.

The Federal Court accepted that the question as to whether an entity carried on an enterprise is more likely to be a question of fact and of itself not the subject of appeal. However it also reasoned that, in the circumstances, the issue of whether there was any basis upon which the Tribunal could have reached the conclusion it did, namely that the Taxpayer was carrying on an enterprise and this finding goes to a question of law, in line with *Lombardo v Commissioner of Taxation*.¹⁵ In *Lombardo*, Bowen CJ, set out a number of cases where it could be said that a question of law would be involved, relevantly “where a particular set of facts had of necessity to be within or without the statute”.¹⁶ The rationale for this view is that in a case where, only one conclusion being open on the facts and a different conclusion is arrived at, it follows that the wrong principle of law has been applied.¹⁷

An Enterprise?

The Federal Court was of the opinion that the Tribunal, based on the totality of the evidence before it, could hold that the Taxpayer was carrying on an enterprise.

Most of the factual background was not in dispute and the subjective evidence of the Taxpayer as to whether it intended to sell the artwork for a profit was relevant.

As to investment activity, the GST Act is intended to have a broad base so that activities of a wide nature can be considered as forming part of an enterprise and accordingly, that input tax credits will be available in relation to acquisitions made as part of the carrying on of that enterprise.¹ Accordingly, even if the activities of the Taxpayer can be properly characterised as being in relation to a strategy of “*long term investment*” that does not necessarily preclude those activities from amounting to the carrying on of an enterprise.

As a matter of interpretation the Federal Court was of the opinion that the words “*in the form of*” in the definition of “enterprise” in s 9-20 of the GST Act do not support the suggestion that “form” will prevail over “substance”¹⁹. The Federal Court believed that these words extended the impact of “enterprise” to activities which are in the form of a business but would not, in the ordinary meaning of “business”, be considered as such. McKerracher J stated, “*But the activity must still be reasonably intended to be profit making in the case of an individual and cannot for any entity simply be a private recreational pursuit or hobby.*”²⁰

COMMENT AND CONCLUSION

The Federal Court dismissed the Commissioner’s appeal and confirmed the Tribunal’s finding that the Taxpayer, engaging in the sole activity of the collection, maintenance and sale of art assets, was carrying on an enterprise for the purposes of s 9-20 of the GST Act. In doing so, the Federal Court rejected the Commissioner’s argument that inert investment is not an activity done in the course of carrying on an enterprise.

Although the decision of *Swansea* provide an interesting discussion of the relevant factors to consider in determining whether an enterprise is being carried on, the decision does not mean that every situation involving taxpayers engaged in the collection of artworks would lead to a finding that the taxpayer in question was carrying on an enterprise. All the facts and evidence in their entirety would

need to be evaluated on a case by case basis. “Had the Commissioner succeeded in establishing that Swansea was simply a vehicle for Mr Satterley’s hobby, the position may have been different.”²¹

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Reference notes

- 1 [2009] FCA 402.
- 2 “The Taxpayer” and Commissioner of Taxation [2008] AATA 461 at [20].
- 3 *Ibid*, at [10].
- 4 [2005] FCAFC 126.
- 5 *Federal Commissioner of Taxation v Murry* (1998) 193 CLR 605; *Thomas v FC of T* (1972) ATC 4094.
- 6 *John v FCT* (1989) 166 CLR 417 at 430.
- 7 *FCT v McNeil* [2007] HCA 5; *CIR v Frazer* 24 TC 498; *Johnston (HM Inspector of Taxes) v Heath* 46 TC 463.
- 8 *Above n 2*, at [154].
- 9 *Above n 2*, at [163].
- 10 *Case N27* (1991) 13 NZTC 3229 at 3240.
- 11 *Above n 2*, at [191].
- 12 *Waterford v Commonwealth* [1987] HCA 25; (1987) 163 CLR 54 at [77].
- 13 *Above n 1*, at [50].
- 14 *Above n 1*, at [57].
- 15 *Lombardo v Commissioner of Taxation (Cth)* [1979] FCA 66; (1979) 40 FLR 208.
- 16 *Ibid*, at [212].
- 17 *Above n 1*, at [56].
- 19 *Above n 1*, at [98].
- 20 *Above n 1*, at [99].
- 21 *Above n 1*, at [101].