

Reliance Carpet case and GST on forfeited deposits

You will recall from our newsflash in late May 2008 that the High Court unanimously held that GST is payable on forfeited deposits.

There seems to have been a number of misconceptions in the marketplace with respect to the effect of this decision and we highlight the following:

- If the vendor is registered for GST purposes and the vendor has entered into a contract as part of an enterprise, then GST is payable on the forfeited deposit (in an amount equivalent to 1/11th of the forfeited amount) regardless of whether the contract relates to the sale of residential or commercial property.
- The fact that the contract states that the margin scheme will be utilised does not affect the amount of GST payable where the deposit is forfeited. In those circumstances GST will still be 1/11th of the forfeited deposit, as the deposit paid is security for the performance of an obligation and this is the taxable supply.

The margin scheme only becomes relevant if the transaction proceeds to completion.

There has been a significant amount of case law over the years which has held that a deposit of more than 10% (which is deemed to be the norm) is a penalty. We do not believe that increasing the deposit to 11% of the purchase price (to cover the GST element if the purchaser defaults and the deposit is forfeited) would constitute a penalty if the reason for this was clearly set out in the contract.

In New South Wales this would mean that the standard contract provision requiring the deposit to be not more than 10% of the purchase price would need to be appropriately amended.

Of course, this may be more problematic where a deposit bond or bank guarantee has been provided rather than a cash deposit but again the issuing insurer company or bank may be able to be convinced that all that a developer is doing is protecting its entitlement to a full 10% deposit (net of GST) if a forfeiture takes place.

If you have any queries as to how the Reliance Carpet case may impact upon your business, please feel free to contact the writer or any other professional staff member of the property group.

Chris Rumore
Partner

T: 02 8281 4555
E: acr@cbp.com.au