

VAT at issue on forfeited deposit

THE value-added tax (VAT) laws require that for VAT to become payable there must be a supply of goods or services by a vendor in the course or furtherance of an enterprise carried on by the vendor.

If there is such a supply, then the tax is payable on the consideration received for the supply.

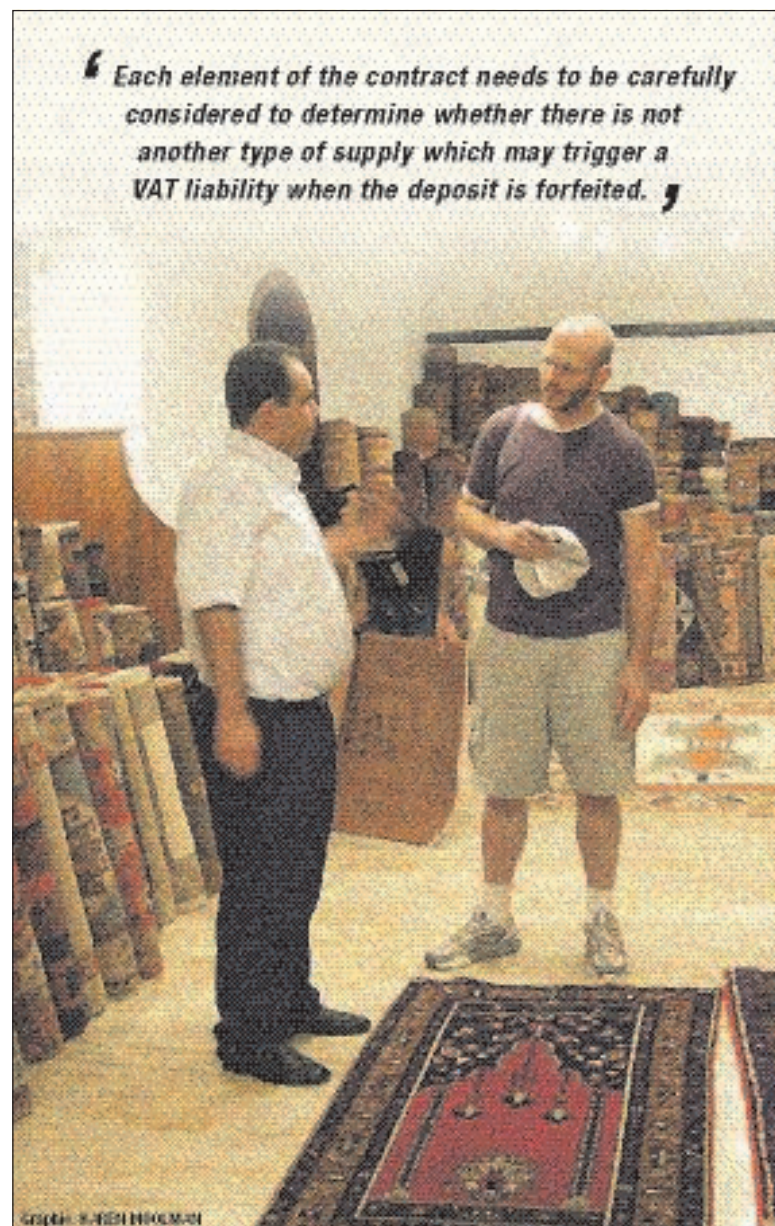
The definition of “consideration” contained in section 1 of the VAT Act specifically excludes a deposit (whether refundable or not), unless the supplier applies the deposit as consideration for the supply, or if the deposit is forfeited. VAT only becomes payable on a deposit when it is applied against the purchase consideration for a supply of goods or services, or when the deposit is forfeited.

One can understand that the tax becomes payable when the deposit is applied against the purchase consideration, because there is an underlying supply. However, because of the requirement that there must be a supply of goods or services before VAT is payable, one can argue that in the case of a deposit that is forfeited, no supply has taken place. Although a forfeited deposit falls within the definition of consideration, such consideration is not in

respect of, in response to or for the inducement of the supply of any goods or services, because no such supply took place in the first instance, hence the deposit being forfeited.

In the first Australian VAT case that was recently heard by the Australian High Court, *Commissioner of Taxation v Reliance Carpet Co (Pty) Ltd*, this was exactly what the vendor argued. The taxpayer, Reliance Carpet, entered into a contract for the sale of a commercial property. In terms of the contract, a deposit of 10% was payable. The contract of sale was entered into consequent on the exercise of an option to purchase by the purchaser. The purchaser paid the deposit but failed to pay the balance of the purchase price by the settlement date. Reliance Carpet issued a notice to the purchaser to remedy its default within 14 days. The purchaser failed to remedy its default and the deposit was forfeited. Reliance Carpet was assessed for VAT on the forfeited deposit. Reliance Carpet objected to the assessment on the basis that it did not make any supply of the property for which the deposit was paid, and therefore no VAT was payable.

The high court examined all the events that actually occurred and



found that there was a supply, and provided two reasons for reaching its conclusion. Firstly, it found that there was a supply because the vendor entered into various obligations when the contract was

concluded. There was the primary obligation to transfer title to the purchaser upon payment of the balance of purchase price, but there were also other obligations, such as maintaining the property

in its present condition, to pay all rates, taxes, assessments, fire insurance premiums and other outgoings in respect of the land and to hold the existing policy of fire insurance for itself and in trust for the purchaser to the extent of their respective interests. The carrying out of such obligations comprised a supply. Secondly, the vendor granted rights to the purchaser in relation to the land, and the granting of such rights also comprised a supply.

The court then considered whether the deposit comprised “consideration” as defined, which includes, amongst others, any payment “in connection with” a supply. The court found that such a connection was apparent in this case, and noted that there was an obvious connection between the payment of the deposit and the contract entered into between the parties. The forfeited deposit was held to be subject to VAT.

The question is whether the Australian High Court judgment will also find application in the South African context. The definition of “supply” in the South African VAT Act seems to be even wider than that of the Australian Act, and includes “all forms of supply”. The definition of “services” is equally wide and includes “anything done or to be done, including the granting, assignment, cession or surrender of any right, or the making available of any facility or advantage”.

It seems that one cannot simply argue that there was no supply if a deposit is forfeited even though it may seem so on the face of it. Each element of the contract needs to be considered to determine whether there is not another type of supply which may trigger a VAT liability when the deposit is forfeited.

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