Tax Consequences: Businessman or Investor

By Michael Bennett

Significantly different tax outcomes arise when a taxpayer sells an asset as an investor (on capital account) or as part of a business or with a profit making intention (on revenue account). The difference arises because an asset held for more than 12 months will have the capital gain halved before it is brought to tax.[1] For this reason the Full Court of the Federal Court's decision in *August v Commissioner of Taxation* [2013] FCAFC 85 is a cause of great concern to those taxpayers.

The question – are an investor's activities taxed on revenue or capital account – is a difficult question to answer. Two cases[2] that were almost identical subdivisions of farm land resulted in the courts holding one was a business and the other merely the realisation of a capital asset. These, and other cases on the issue, show significant weight is put on the taxpayer's intention when purchasing the property. Being able to prove just what those intentions were is critical. It is in this context that *August's Case* is relevant.

Mr August acquired various shops in the same centre from 1997 to 1999, did them, put tenants in them on long-term leases and sold them in 2006. Despite holding the properties for up to 9 years, and claiming he intended to hold them until his death, the Full Court found his primary intention in purchasing the properties was to resell them at a profit.

Against his arguments of long-term investing was the following. First, Mr August had sought advice on where to purchase from a friend who was in the business of property investing. Secondly, soon after the last lease was secured Mr August had consulted a real estate agent about selling, though he said it was merely out of interest in their then value. Mr August had also obtained a bank valuation 6 months prior and, although he subsequently wanted a non-bank[3] valuation, the court held the later valuation was unnecessary other than for sale purposes. Thirdly, that agent took it on themself to source potential purchasers and, having obtained a good offer, persuaded Mr August to sell. The Court did not accept the good offer as the reason for the sale. Finally, Mr August's circumstances did not change at the time of selling, "So why sell?" reasoned the court.

Although Mr August's explanations might be considered reasonable, especially in the face of 7 to 9 years of stated intention, the Full Court held the purchases were made to resell at a profit. It seems any taxpayers selling assets should consider their entire circumstances as their long held intentions may not be accepted.

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[1] There may also be a different tax outcome depending on the taxpayer's revenue and capital loss position.
[2] *Stevenson v Commissioner of Taxation* (1991) 29 FCR 282 and *George Casimaty v Commissioner of Taxation* (1997) 151 ALR 242
[3] Which can be significantly higher than a bank valuation.