

**MEDIA RELEASE**

**TAX CASE A BLOW FOR SMALL BREEDERS**

Many small commercial horse breeders in Australia risk having their GST/Income Tax status removed as a result of a landmark AAT decision on 13 August 2008.

It is very common in the horse industry for smaller boutique breeders to invest in a multiple number of quality and costly mares, but due to the high cost of doing so and the desire to diversify their investment, choose to own a **partial interest** in each mare. For example, 10%, 25%, 33 1/3% etc of the mare is acquired with like minded breeders.

Back in October 2007, the tax community was rejoicing at the common sense decision reached by the WA Administrative Appeals Tribunal (AAT) in the landmark “Block’s” case, a case where a family partnership was held to be in business in a period where significant losses were present.

Now, some 11 months or so later, we are in despair about the findings of a “business v hobby” case recently decided at the NSW AAT.

This case involved a small NSW breeder, Greg D’Arcy, appealing against a previous ATO decision that disallowed his GST claims, these being disallowed on the basis that Mr. D’Arcy was not conducting a Horse Breeding “enterprise” in this period. Furthermore, Mr. D’Arcy’s income tax returns were amended to disallow his horse breeding losses for the 2003, 2004 and 2005 income tax years.

Mr. D’Arcy co-owned his mares in syndicates normally consisting of his uncle and 3 to 4 other like minded breeders. His uncle was always the major shareholder and had a wealth of knowledge and experience within the industry.

***AAT decision – lack of “control” present***

The AAT decided in favour of the ATO, primarily on the basis that Mr. D’Arcy did not have sufficient “control” of his business stock, notwithstanding that his activities demonstrated many strong business elements, especially in terms of quality of stock, industry expertise and profit making purpose.

In my opinion, the AAT has placed a disproportionate weighting in the ATO assertion that Mr. D’Arcy was not making his own decisions in relation to this venture and the best he could do was provide “input” to the decision-making process. Mr. D’Arcy raised a compelling argument that he had strong say in decision making and would not have contemplated co-ownership unless his uncle and like minded investors were involved, alleviating the need for a formal written agreement between the owners.

Other “non-business” elements were raised by the AAT in its decision, such as lack of a formal business plan and prospect of profit, however the former has never held much weight in these AAT decisions and it could be very reasonably argued that Mr. D’Arcy’s activities had at least had as much “prospect of profit” as the activities within “Block’s” and other well known horse breeding cases. I found this latter AAT conclusion particularly disappointing.

As a tax adviser with an extensive horse industry client base, I can only hope that, in the event that the decision is not subsequently overturned on appeal, the ATO use common sense when applying this decision as every case has its own peculiar facts and these “business v hobby” cases should always be decided on this basis.

This “control” principle in deciding “business v hobby” cases has wider application than just the racing industry, which is the most interesting (and troubling) aspect of this decision.

The writer was drafted at the last moment by Mr. D’Arcy’s tax advisers to help fight this case. Like Greg and the rest of the tax team, we were bitterly disappointed with the decision and as I write we are seriously contemplating an appeal to the Federal Court.

#### **Facts of the case**

- ❑ On average, 6-8 current or potential broodmares were held at any one time. 14 mare interests were held in total over the period. Total investment on mares was approximately \$230,000;
- ❑ On average, Mr. D’Arcy owned approximately 23% of each mare and one mare was owned 100% outright. This latter mare was his most costly;
- ❑ Mr. D’Arcy was a regular seller and little racing was present;
- ❑ No formal business plan was prepared;
- ❑ Between Mr. D’Arcy and his uncle, they owned greater than 50% of each mare;
- ❑ There was never a dispute where a dispute resolution mechanism would have been needed. There was no formal written agreement between the owners;
- ❑ Books of account and records could not be produced to the tribunal, though the taxpayer kept computer spreadsheets of all financial transactions and they were tabled with the ATO as part of a previous GST review, together with copies of income tax returns, profit and loss accounts, receipts, invoices etc;
- ❑ Losses were made in each of the tax years; and
- ❑ Though strongly argued to the contrary, the AAT resolved that a profit was not likely “within any reasonable time frame”.

**End of release**

**Prepared by:**

**PAUL CARRAZZO CPA**

**CARRAZZO CONSULTING CPAs**

**22 BLACKWOOD ST, NORTH MELBOURNE VIC 3051**

**TEL: (03) 9329 7044**

**FAX: (03) 9329 8355**

**MOB: 0417 549 347**

**E-mail: [paul.carrazzo@carrazzo.com.au](mailto:paul.carrazzo@carrazzo.com.au)**

**Web Site: [www.carrazzo.com.au](http://www.carrazzo.com.au)**