



What happens if you receive a forfeited deposit?

Houses sales and forfeited deposits; what are the CGT implications.

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What we are talking about here is selling a house; sometimes you may enter a contract of sale and for some reason the purchaser does not complete the sale. In this case the vendor will generally be entitled to retain the deposit, what is the tax implication of this? Presuming the sale is capital in nature then this article discusses the possible tax consequences of this scenario.

The deposit from the initial sale of the property would normally form part of total proceeds from the successful sale of the property and subject to Capital Gains Tax (CGT) if the property was an investment or possibly exempt. However what happens when the sale does not proceed? In this case the deposit becomes a CGT event in it's own right and it taxable, the CGT event isa H1 event.¹ The agents fees and legal fees associated with the failed transaction would form the cost base of this event in other words they offset the CGT income to some degree.²

Despite this the deposit can still form part of the eventual sale if there was a continuum of events³ this has been established by case law and confirmed by the ATO in TR 1999/19. What this can mean is rather than being a stand alone event the deposit from a failed sale can be added to the final sale proceeds of the eventual successful sale and taxed as part of that CGT event. This can have important tax consequences for example;

- You might be selling your primary residence and so the final sale may be CGT free.⁴
- You could be selling a pre CGT Asset and so Capital Gains tax does not apply.⁵

¹ *Income Tax Assessment Act 1997* Cth s 104-150

² *Income Tax Assessment Act 1997* Cth s 104-150(3)

³ *TR 1999/19 CGT: treatment of forfeited deposits*, ATO [9]

⁴ *Income Tax Assessment Act 1997* Cth s 118-110(1)(b)

⁵ *Ibid* s 149-10



- Even if you are selling an asset where Capital Gains Tax does apply if you have held the asset for over 12 months you will be generally entitled to the 50% CGT discount.⁶

By being counted as part of the final sale the proceeds from the failed deposit will form part of the eventual A1 capital gain⁷ and have the same tax treatment as the overall transaction and so enjoy the same concessional tax treatment.

To be a continuum of events certain conditions need to be met to quote the Guy case (one of the important cases regarding continuum of events) “*the dwelling is put straight back on the market and then it is sold.*”⁸ this really is the main point. Once an initial sale falls over you should re-list and then sell. If this occurs you have no problem and the sale will be a continuum.

The principles are also discussed in at tax office ruling *TR1999/19*. Importantly a Tax Ruling is legally binding on the commissioner of tax; in other words he must follow what his written in the ruling. The Commissioner goes beyond the wording in the Guy case and allows for 2 years between the failed and eventual sale in *TR1999/19* and so this will be will be accepted by the ATO as a continuum.⁹

Hopefully this helps you understand what happens from a tax point of view if your property sale falls over and you end up retaining the sale deposit. If you want more information and help with your tax situation please get in contact.

Warning: This is general information, these tax laws are complex, please get professional tax advice before acting.

⁶ Ibid s 115-100

⁷ *Income Tax Assessment Act 1997* Cth s 104-10

⁸ See *FCT v Guy* ATC 4531 [3]

⁹ Ibid [17]