

Good GST news for developers

Due to a recent move by the ATO, property developers will be able to reduce the amount of GST they pay as increasing adjustments in situations where new residential premises for sale (and that are actively marketed that way) are temporarily leased out due to market conditions.

Division 129: Adjustments

Under Division 129 of the GST Act the need for an adjustment in relation to property development arises in respect of an acquisition where:

- there is a difference between the actual application and the planned (or intended) application of the property for a creditable purpose, or
- there is a difference between the actual application of the property up to the end of one adjustment period and the actual application of the property up to the end of the previous adjustment period.

The need for an adjustment often arises in the following scenario:

1. Acquisitions are made by the developer which is constructing new residential premises with the sole intention being construction for sale.
2. The developer claims an input tax credit in respect of the acquisitions because at the time they were acquired they were solely for a creditable purpose.
3. Since constructing the new residential premises, the developer has, in a weak selling market, leased the premises until such time as a sale take place.

The ATO's view

The ATO, in its previous communication on the subject (*"Changes in extent of creditable purpose under Division 129"* March 2008), advised that a developer is entitled to 100% input tax credit on its acquisition related to the

construction of the premises (provided it did not initially have any intention of renting the premises).

The developer is then required to make a 100% increasing adjustment (to reverse the original input tax credit in full) at the next adjustment period after the premises are first rented - this is despite the fact that the developer still intends to sell the properties in the future.

Once the properties are sold as new residential premises, the developer is entitled to reclaim some of its original credits through a decreasing adjustment.

The ATO's view was supported by the theory that the act of renting the premises (despite while trying and having the intention to sell) was applying the acquisitions to a purpose other than that which existed when they were purchased - effectively it was a change in use and purpose.

A new perspective

On 19 August 2008 the ATO published ATO Interpretative Decision (ID) 2008/114.

The interpretative decision ruled that in cases such as that described above, the wording under Division 129, and in particular the use of the word "application", could be appropriately construed to mean that "**actively marketing the premises for sale**" will be evidence of use of the premises that demonstrates that the premises have been applied to **some extent** for the creditable purpose of the sale.

Whilst the ruling is good news for property developers, it does not mean that there is no increasing adjustment but rather the increasing adjustment will need to reflect the **extent** to which the premise have been applied for a creditable purpose (being the sale of the premises) between when the relevant property was acquired and the end of the adjustment period. Simply put, adjustments will need to be calculated with a "fair and reasonable basis of apportionment" or by using the formulae contained in the provisions of Division 129. Nonetheless, in light of the fact that revenues from any future sale of the property would substantially exceed the rent received prior to the property sale, the new approach should dramatically ease the previously held concerns of developers.

"Actively marketing the premises for sale"

Particular importance should be placed on developers ensuring that residential premises so rented continue to be "actively marketed for sale". As described in the Interpretive Decision, actively marketed for sale can mean a variety of things but generally includes:

- listing the property for sale with a real estate or agents
- advertising the premises for sale in relevant publications or by internet advertising on websites for real property
- arranging open for inspection times and/or showing prospective buyers through the premises.

In the case of strata units, actual arms length sales of some of the listed units would be further evidence of active marketing, while listing premises for sale at a price that is significantly above market value maybe an indicator that the premises are not being actively marketed for sale.

Watch this space

Importantly, ATO ID2008/114 does not have the force of an ATO ruling. Whilst it is reasonable to expect the ATO to follow the decision in its own Interpretive Decision, it should be emphasised that it is not law. The ATO has indicated that this revised view will be discussed more fully in a draft GST determination , a paper that should be published in the next two to three months. Of interest the paper may also address the issue as to those developers who have relied upon the views stated in earlier ATO publications, and who have as a result, overpaid GST, and whether they may be entitled to refunds.

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