
Chapter 1

Attribution of input tax credits

Outline of chapter

1.1 Schedule 1 to this exposure draft amends the goods and services tax (GST) law to clarify the rules in the GST law for attributing input tax credits to tax periods.

Context of amendments

Attribution of input tax credits

1.2 The rules for attributing input tax credits to particular tax periods play an important role in the operation of the GST. The *A New Tax System (Goods and Services Tax) Act 1999* (GST Act) provides that input tax credits (including reduced input tax credits) are attributable to the first tax period in which either any consideration is provided by the recipient, or an invoice is issued. If the taxpayer accounts on a cash basis, input tax credits will only be attributable when and to the extent that the recipient provides consideration.

1.3 There are two exceptions to this basic rule. Firstly, input tax credits cannot be attributed to a tax period unless a relevant tax invoice is held by the taxpayer in that tax period. Such input tax credits will instead be attributable to the first tax period in which the taxpayer holds a tax invoice (see subsection 29-10(3) of the GST Act). Secondly, if the GST return for a tax period does not take into account an otherwise attributable input tax credit, the input tax credit is not attributable to that tax period. Such credits are attributable to the first tax period in which a return is provided taking the credit into account (see subsection 29-10(4) of the GST Act).

1.4 Concerns have been expressed by taxpayers that the way the latter exception is expressed in the law may be ambiguous and is open to an argument that it applies only to a limited category of input tax credits.

Summary of new law

1.5 Schedule 1 amends the present rules for attributing input tax credits. These amendments clarify that taxpayers are able to defer the attribution of input tax credits, subject to the four-year restriction on claiming input tax credits contained in Schedule 1 of Tax Laws Amendment (2009 GST Administration Measures) Bill 2009.

1.6 This amendment addresses concerns by taxpayers that the present attribution rules may not give this outcome in all situations.

Comparison of key features of new law and current law

<i>New law</i>	<i>Current law</i>
<p>Attribution of input tax credits</p> <p>Input tax credits cease to be attributable to a particular tax period when they are not taken into account in the GST return for that period. Instead, the credits will be attributable to the first tax period in which they are taken into account in a return where the taxpayer holds a tax invoice.</p> <p>This is subject to the four-year restriction on claiming input tax credits contained in Schedule 1 of the Tax Laws Amendment (2009 GST Administration Measures) Bill 2009.</p>	<p>Attribution of input tax credits</p> <p>Input tax credits cease to be attributable to a particular tax period when they are not taken into account in the GST return for that period. Instead, the credits will be attributable to the first tax period in which they are taken into account in a return where a tax invoice is held by the taxpayer. However, concerns have been expressed about the effectiveness of the legislation in achieving this outcome in all cases.</p> <p>This is subject to the four-year restriction on claiming input tax credits contained in Schedule 1 of the Tax Laws Amendment (2009 GST Administration Measures) Bill 2009.</p>

Detailed explanation of new law

Clarification of the input tax credit attribution rules

1.7 The amendments clarify the attribution rules for input tax credits contained in subsection 29-10(4) of the GST Act.

1.8 Subsection 29-10(4) was introduced in 2000 to enable taxpayers to attribute input tax credits to tax periods after the period in which they first held a tax invoice. The effect of this measure was to permit

taxpayers to claim input tax credits in the current business activity statement (BAS) rather than revising a BAS for an earlier tax period.

1.9 Since the introduction of the measure, some taxpayers have expressed concern that the specific reference in subsection 29-10(4) to an earlier paragraph in the attribution rules (paragraph 29-10(3)(b)) may leave unclear the application of the provision to input tax credits not falling within this earlier paragraph.

1.10 This amendment resolves this ambiguity by revising subsection 29-10(4) to remove any reference to other provisions.
[Schedule 1, Item 1]

Application and transitional provisions

1.11 These amendments will apply in relation to net amounts for tax periods commencing on or after 1 July 2010.

Chapter 2

GST adjustments for third party payments

Outline of chapter

2.1 Schedule 2 to this exposure draft amends the GST Act to ensure that the appropriate amount of GST is collected and the appropriate amount of input tax credits claimed in situations where there are payments between parties in a supply chain which indirectly alter the price paid or received by the parties for the goods supplied.

2.2 This is achieved by creating an adjustment to apply in situations where an entity (the payer) supplying goods for re-sale makes a monetary payment to a third party (the payee) in connection with the payee's acquisition of those goods. This adjustment occurs when the payer does not supply the goods directly to the payee but rather through a supply chain.

Context of amendments

2.3 The amount of GST paid or input tax credits claimed in a previous tax period may need to be adjusted to ensure that the correct GST outcome is obtained when circumstances change. Adjustments may arise due to, among other things, changes in consideration such as a change in price due to a discount. A third party rebate may not give rise to an adjustment because it would not, ordinarily, alter the consideration for the supply by the payer to its customer, or the consideration paid for the acquisition by the payee to its supplier.

2.4 An adjustment is either an increasing or decreasing adjustment. An increasing adjustment is added to the net amount for a tax period, which will either increase the amount payable by the entity to the Australian Taxation Office (ATO), or reduce the amount payable by the ATO to the entity. A decreasing adjustment is subtracted from the net amount for a tax period, which will either decrease the amount payable by the entity to the ATO, or increase the amount payable by the ATO to the entity.

2.5 Where a registered entity supplies goods to another entity and that second entity supplies those goods to a third party, the original supplier of the goods sometimes makes a payment, such as a rebate, to the third party -a third party payment. As the law currently operates, the original supplier must remit GST based on the price for which it sells the goods to the second entity, with no adjustment for the third party payment. The third party can claim an input tax credit based on the price paid to its supplier with no adjustment for the third party payment.

Summary of new law

2.6 Where the payment to the payee indirectly reduces the payment the payer has received for the goods, the payer will be entitled to a decreasing adjustment reflecting the difference between the GST remitted on the original payment and the GST which would have been payable on the goods if the consideration was calculated net of the third party payment. The payee will have an increasing adjustment if the acquisition was for a creditable purpose. This adjustment will arise even if there are several interposed entities in the supply chain.

Comparison of key features of new law and current law

<i>New law</i>	<i>Current law</i>
<p>GST adjustments for third party payments</p> <p>The payer will be entitled to make a decreasing adjustment in the event that, having made a taxable supply of goods to an entity, it makes a payment to a third party in the supply chain which indirectly reduces the payment received by the payer for the goods.</p> <p>Where the payee acquires the goods for a creditable purpose the third party payment will also result in an increasing adjustment for the payee.</p> <p>The decreasing adjustment will be attributable to the tax period in which the payer first holds a third party adjustment note.</p> <p>The payer is responsible for issuing the third party adjustment note within</p>	<p>GST adjustments for third party payments</p> <p>A payment by a supplier to a third party in a supply chain does not ordinarily give rise to an adjustment for the payer.</p> <p>A payment received by a recipient from a third party in a supply chain does not ordinarily give rise to an adjustment for the payee.</p>

<i>New law</i>	<i>Current law</i>
<p>28 days of the earlier of becoming aware of the adjustment or a request by the payee for a copy of the note.</p> <p>If a payment gives rise to a third party payment adjustment, the payment cannot also result in an adjustment event under another provision.</p>	

Detailed explanation of new law

2.7 The amendments create an entitlement to a decreasing adjustment where an entity (the payer) makes a payment to a third party (the payee) relating to goods that the payer has supplied to another entity and which the payee has subsequently acquired. To give rise to a decreasing adjustment:

- the supply of goods by the payer must be a taxable supply;
- the payment must have a connection with the payee's acquisition of the goods (or be in response to, or for the inducement of, the payee's acquisition of the goods); and
- the payment must not be consideration for a separate supply.

[Schedule 2, item X, subsection 134-5 (1)]

2.8 The decreasing adjustment is the difference between:

- the amount of GST payable on the original supply to the other entity (taking into account any other adjustments relating to the supply); and
- the amount of GST that would have been payable on that supply if the consideration for that supply had been reduced by the amount of the third party payment (and taking into account any other adjustments relating to the supply).

[Schedule 2, item X, subsection 134-5(2)]

2.9 The amendments create an increasing adjustment for the recipient of a third party payment (the payee) in respect of goods acquired from another entity where:

- the acquisition of those goods was a creditable acquisition

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- the payment must have a connection with the payee's acquisition of the goods (or be in response to, or for the inducement of, the payee's acquisition of the goods); and
 - the payment is not consideration for a separate supply.

[Schedule 2, item X, subsection 134-10(1)]

2.10 The increasing adjustment is the difference between:

- the amount of input tax credits to which the payee was entitled for its acquisition (taking into account any other adjustments relating to the acquisition); and
- the amount of input tax credits to which the payee would have been entitled for that acquisition had the consideration for that acquisition been reduced by the amount of the third party payment (and taking into account any other adjustments relating to the acquisition).

[Schedule 2, item X, subsection 134-10(2)]

2.11 The decreasing adjustments cannot be attributed until the tax period in which the payee holds a third party adjustment note.

- This does not apply to decreasing adjustments not exceeding the adjustments notes threshold (currently \$50).

[Schedule 2, item X, section 134-15]

2.12 The amendments set out the requirements for third party adjustment notes. The payer is required to give the payee a copy of the third party adjustment note within 28 days of the earlier of a request by the payee or becoming aware of the adjustment. *[Schedule 2, item X, section 134-20]*

2.13 An anti-overlap provision specifies that a payment which gives rise to an adjustment under Division 134 cannot also give rise to an adjustment event. *[Schedule 2, item X, section 134-25]*

Example 2.1: Retail third party rebate

Fascam Ltd, a manufacturer, sells a camera to Choice Cameras Ltd, a retailer, for \$660. Choice Cameras sells the camera to a customer, Irene, for \$880 at a time when Fascam is offering a cash-back incentive to retail customers to boost its sales. Irene applies for and receives a cash-back payment of \$110 from Fascam.

Under section 134-5 Fascam is entitled to a decreasing adjustment with regard to the cash back payment.

The decreasing adjustment is calculated as follows:

(A) GST payable on supply to Choice Cameras:

$$A = \$660 \times 1 / 11 = \$60$$

(B) GST which would have been payable had the consideration been reduced by the amount of the payment to the payee:

$$B = (\$660 - \$110) \times 1 / 11 = \$50$$

$$A - B = \$60 - \$50 = \$10$$

Fascam is entitled to a decreasing adjustment of \$10.

(As the decreasing adjustment is for an amount less than \$50, Fascam is not required to issue a third party adjustment note).

Choice Cameras is not affected by the decreasing adjustment to which Fascam is entitled. Choice Cameras's GST liability remains as follows:

GST payable on sale – inputs tax credits on acquisition = GST liability:

$$(\$880 \times 1 / 11) - (\$660 \times 1 / 11) = \$80 - \$60 = \$20$$

If Irene is registered for GST as a professional photographer and has purchased the camera for use in her business, the acquisition of the camera is a creditable acquisition. She therefore has an increasing adjustment under section 134-10.

The increasing adjustment is calculated as follows:

(C) Input tax credit entitlement arising from the acquisition from the other entity (Choice Cameras):

$$C = \$880 \times 1 / 11 = \$80$$

(D) Amount of input tax credits to which the payee would have been entitled had the consideration for the acquisition been reduced by the amounts of the payer's payment:

$$D = (\$880 - \$110) \times 1 / 11 = \$70$$

$$C - D = \$80 - \$70 = \$10$$

Irene has an increasing adjustment of \$10. If Irene is not registered for GST, this increasing adjustment does not arise.

If Irene is registered for GST but intends to use the camera 50 per cent for private purposes and 50 per cent for creditable purposes she is entitled to an input tax credit of 50 per cent of the full input tax credit.

The increasing adjustment is calculated as follows:

(C) Input tax credit entitlement arising from the acquisition from the other entity (Choice Cameras):

$$C = \$880 \times 1 / 11 \times 0.50 = \$40$$

(D) Amount of input tax credits to which the payee would have been entitled had the consideration for the acquisition been reduced by the amounts of the payer's payment:

$$D = (\$880 - \$110) \times 1 / 11 \times 0.50 = \$35$$

$$C - D = \$40 - \$35 = \$5$$

Irene has an increasing adjustment of \$5.

Example 2.2: Motor vehicle industry holdback payments

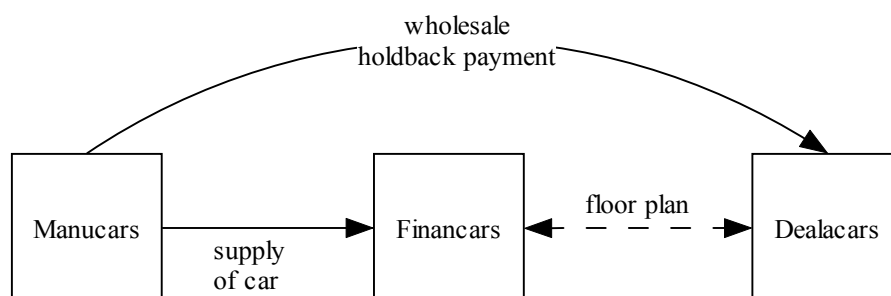
Dealers in new motor vehicles commonly use floor plan arrangements to finance their trading stock. In a typical floor plan arrangement, title to the vehicles passes from the manufacturer or importer to a finance company and the dealer is granted physical possession of the vehicle. This allows the dealer to offer the vehicles for sale without having to purchase them before securing a customer. When the dealer finds a customer for a vehicle, title to that vehicle is supplied by the finance company to the dealer immediately before the dealer supplies it to the customer. Manufacturers and importers of motor vehicles commonly make payments to their dealers known as 'holdback' payments.

A manufacturer, Manucars, supplies motor vehicles to a finance company, Financars, which obtains title to the vehicles. Financars has a floor plan arrangement with a dealer, Dealacars, that covers the vehicles it acquires from Manucars. The arrangement allows Dealacars to display the vehicles for sale to its customers. A wholesale holdback payment will be credited to Dealacars' account by Manucars when Manucars invoices Financars for a particular vehicle.

Dealacars orders a vehicle from Manucars on behalf of Financars. Manucars supplies the vehicle to Financars and invoices Financars for \$22,000 (including GST). Title in the vehicle passes from Manucars to Financars and Dealacars obtains physical possession of the vehicle.

A wholesale holdback payment of \$5,500 is credited to Dealacars' account by Manucars because Manucars has invoiced a specific motor vehicle to Financars. The arrangement looks like this:

Wholesale Holdback Payment



Manucars attributed GST of \$2,000 in relation to the supply of the car to Financars. It has a decreasing adjustment in relation to the holdback payment to Dealacars.

The decreasing adjustment is calculated as follows:

(A) GST payable on supply to Financars:

$$A = \$22,000 \times 1 / 11 = \$2,000$$

(B) GST which would have been payable had the consideration been reduced by the amount of the payment to the payee:

$$B = (\$22,000 - \$5,500) \times 1 / 11 = \$1,500$$

$$A - B = \$2000 - \$1500 = \$500$$

Dealacars has a corresponding increasing adjustment of \$500.

Financars does not have any adjustment in relation to the holdback payment.

Application and transitional provisions

2.14 Third party payment adjustments will apply to payments made on or after 1 July 2010.

Consequential amendments

2.15 As a consequence of the inclusion of Division 134, amendments have been made to:

- paragraph 19-40(c) to ensure the corrected GST amount includes adjustments resulting from the new Division 134;
- paragraph 19-45(c) to ensure the previously attributed GST amounts include decreasing adjustments arising from the new Division 134;
- paragraph 19-70(2)(a) to ensure the corrected input tax credit amount includes adjustments resulting from the new Division 134;
- paragraph 19-75(b) to ensure the previously attributed input tax credit amounts include increasing adjustments arising from the new Division 134;
- section 54-50 to apply the requirements of this section to third party adjustment notes required under the new Division 134;
- section 129-80 to include adjustments arising from the new Division 134 in the calculation of adjustments under this section; and
- section 131-55 to include adjustments arising from the new Division 134 in the calculation of the amount of increasing adjustment under this section.

