GSTD 2006/3 - Goods and services tax: are settlement adjustments taken into account to determine the consideration for the supply or acquisition of real property?

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Goods and Services Tax Determination

Goods and services tax: are settlement adjustments taken into account to determine the consideration for the supply or acquisition of real property?

Preamble

This document is a ruling for the purposes of section 37 of the ***Taxation Administration Act 1953****. You can rely on the information presented in this document which provides advice on the operation of the GST system.*

*[**Note:** This is a consolidated version of this document. Refer to the Tax Office Legal Database (http://law.ato.gov.au) to check its currency and to view the details of all changes.]*

1. Yes. Settlement adjustments[1] in favour of either the supplier or the recipient of the supply of real property are taken into account in determining the consideration for the supply or acquisition.

Explanation

2. The consideration may be either monetary or non-monetary or both. The consideration will not always be the price shown on the contract as, on settlement, adjustments are commonly made for rates, land tax and other outgoings.

3. For example, rates or land tax may be assessed to and paid by the supplier before the date of settlement. In such a case, the contract will usually require the recipient to pay an extra amount to the supplier for the balance of the rates or land tax period that reflects the recipient's period of ownership.

4. In the usual case where the contract stipulates that both the purchase price and the adjustment must be paid at settlement in return for possession and title documents, the supplier is receiving and the recipient is paying extra consideration for the sale and purchase of the land.

5. Even though the adjustment amounts are calculated by *reference to* rates, the adjustments form part of the calculation of the amount required under the contract to be paid by the purchaser to the vendor in return for title to the property.

[1] The term 'settlement adjustments' does not refer to any adjustments under Division 19, but in the context of this Ruling refers to adjustments for rates, taxes and other outgoings on settlement of a contract for the sale of real property. Even if settlement adjustments are considered to be adjustments for the purposes of the GST Act, they ordinarily occur on the date of the supply and consequently are in the same tax period.

Example 1 – Rates or land tax assessed to and paid by the supplier before settlement

6. *Andy sells a block of land to Mandy. The price stipulated in the contract is $1,000,000. The contract also has a standard clause dealing with settlement adjustments.*

7. *Prior to settlement, Andy receives and pays a rates notice for $600. The period of the rates notice overlaps Andy's and Mandy's periods of ownership. The break up is 100 days for Andy and 265 days for Mandy.*

8. *The consideration for the supply is $1,000,435 calculated as follows:*

Selling price	*$1,000,000*
Plus Rates adjustment	
[$600 × 265/365]	*$ 435*
	$1,000,435
Cheque to Andy	*$1,000,435*
	$1,000,435

9. In other circumstances, rates or land tax for the period in which the settlement takes place may be assessed to the supplier but remain unpaid until settlement. In this case, if the rates are paid at settlement there may be a settlement adjustment in favour of the supplier.

Example 2 – Rates or land tax assessed to the supplier that are paid at settlement

10. *Andy sells a block of land to Mandy. The price stipulated in the contract is $1,000,000. The contract also has a standard clause dealing with settlement adjustments. Prior to settlement, Andy receives a rates notice for $600. The period that the rates notice covers overlaps both Andy's and Mandy's periods of ownership. The break up is 100 days for Andy and 265 days for Mandy.*

11. *The rates notice remains unpaid. At settlement the following cheques are exchanged:*

Cheque to Andy	*$ 999,835*
Cheque to Local authority	*$ 600*
	$1,000,435

12. *The consideration for the supply of the real property is $1,000,435 calculated as follows:*

Selling price	*$1,000,000*
Plus Rates adjustment	
($600 × 265/365)	*$ 435*
	$1,000,435

13. In other cases, rates or land tax may be assessed to the recipient after settlement even though part of the period reflects the supplier's period of ownership prior to settlement. In these circumstances, the terms of the contract usually require an adjustment based on the supplier's and recipient's respective periods of ownership. In this instance, the recipient is paying less consideration to the supplier than the purchase price reflected in the contract.

Example 3 – Rates or land tax assessed to the recipient after settlement

14. *Andy sells a block of land to Mandy. The price stipulated in the contract is $1,000,000. The contract also has a standard clause dealing with settlement adjustments. Rates of $600 are assessed to Mandy after settlement. The period that the rates notice covers overlaps both Andy's and Mandy's periods of ownership. The break up is 100 days for Andy and 265 days for Mandy.*

15. *The consideration for the supply is $999,835 calculated as follows:*

Selling price	*$1,000,000*
Minus Rates adjustment	
[$600 × 100/365]	*$ 165*
	$ 999,835
Cheque to Andy	*$ 999,835*
	$ 999,835

Alternative view

16. There is an alternative view that settlement adjustments for rates paid in advance do not change the consideration for the supply of land. On this view, any adjustment made on the transfer of possession in these circumstances is not considered to be in respect of the purchase price of the property, but is a reimbursement of rates for the respective period of usage.

17. Support for this view is found in *Commissioner of Taxation v. Morgan* (1961) 106 CLR 517. The High Court held that a purchaser of income producing property was allowed an income tax deduction for the additional amount paid at settlement for a rates adjustment. In reaching this conclusion, the Court took the view that a settlement adjustment for rates paid in advance is not consideration for the property. Instead, it stated at CLR 521 that:

> [t]he payment of the apportioned part is separate and represents nothing but the reimbursement of a charge for an ensuing period of enjoyment, one of a very limited duration.

18. The Commissioner does not accept that the decision in Morgan's case is applicable in the GST context as the High Court was considering the deductibility of the rates adjustment in a capital versus revenue context under the *Income Tax Assessment Act 1936*. For GST purposes, the relevant factor is the nature of the supply and the nexus, if any, between the payment and that supply. In these circumstances, the Commissioner considers that there is a single supply of real property and the adjustments form part of the calculation of the consideration for the supply. Additionally, the High Court did not have to consider the implications of the definition of consideration under section 9-15 of the GST Act which is broader than the ordinary meaning of that term.

19. [Omitted]

20. [Omitted]

Date of Effect

21. This Determination explains our view of the law as it applied from 1 July 2000. You can rely upon this Determination on and from its date of issue for the purposes of section 37 of the *Taxation Administration Act 1953*. Goods and Services Tax Ruling GSTR 1999/1 explains the GST rulings system and our view of when you can rely on our interpretation of the law in GST public and private rulings.

22. If this Determination conflicts with a previous private ruling that you have obtained, this public ruling prevails. However, if you have relied on a private ruling, you are protected in respect of what you have done up to the date of issue of this public ruling.

23. If this Determination conflicts with an earlier public ruling (for example, the Property and Construction Industry Fact Sheets GST and the margin scheme – real property acquired before 1 July 2000 and GST and the margin scheme – real property acquired on or after 1 July 2000 this public ruling prevails. If you have relied on an earlier public ruling, you are protected in respect of what you have done up to the date of issue of this public ruling.

24. This means that if you have underpaid an amount of GST, you are not liable for the shortfall prior to the date of issue of this later ruling. Similarly, you are not liable to repay an amount overpaid by the Commissioner as a refund.

Commissioner of Taxation
26 April 2006

Previous draft:

Not previously issued as a draft

Related Rulings/Determinations:

GSTR 1999/1

Subject references:

- consideration
- rates and taxes
- real property
- recipient
- settlement adjustments
- supplier
- supply

Legislative references:

- ANTS(GST)A 1999 9-15
- ANTS(GST)A 1999 Div 19
- ITAA 1936
- TAA 1953 37

Case references:

- Commissioner of Taxation v. Morgan (1961) 106 CLR 517

ATO references

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