GSTD 2012/2 - Goods and services tax: what are the goods and services tax consequences following the sale of commercial premises that are subject to a lease?

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Goods and Services Tax Determination

Goods and services tax: what are the goods and services tax consequences following the sale of commercial premises that are subject to a lease?

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Background

1. This Determination concerns the following goods and services tax (GST) issues:

   (a) the GST liability of the vendor and purchaser on a lease of commercial premises, following the sale of those premises subject to a continuing lease; and

   (b) how any GST liability for such a supply is attributed.[1]

2. In this Determination, when we refer to 'commercial premises' we mean all forms of premises other than residential premises supplies of which are input taxed under sections 40-35 or 40-65 of the *A New Tax System (Goods and Services Tax) Act 1999* (GST Act).[2]

[1] The GST consequences for the purchaser of a reversion in residential premises are addressed in Goods and Services Tax Determination GSTD 2012/1 *Goods and services tax: what are the goods and services tax consequences following the sale of residential premises subject to a lease?*

[2] All legislative references are to the GST Act unless otherwise indicated.

3. In this Determination, the term 'reversion' refers to the freehold interest acquired when commercial premises are sold subject to a lease. It also refers to the interest acquired when a leasehold estate is assigned subject to a sub-lease of commercial premises. Both of these interests are a form of real property as defined in section 195-1.

Ruling

4. Following a sale of commercial premises that are subject to a lease, the purchaser of the reversion is liable for GST relating to the lease where the elements of section 9-5 are satisfied.

5. The purchaser's GST liability is attributed in accordance with the rules in Divisions 29 and 156.

6. The purchaser is entitled to an input tax credit for the acquisition of the premises where the requirements of section 11-5 are satisfied and subsection 75-5(1) (the margin scheme) was not applied to work out the amount of GST payable on the sale of the premises. Further, the purchaser is entitled to input tax credits for acquisitions that relate to the purchase of the premises or to the ongoing lease of the premises where the requirements of section 11-5 are met.

7. The vendor of the commercial premises is not liable for GST relating to the lease where it is no longer in receipt of or entitled to rent or other consideration for the lease following the sale of the reversion.

8. In the following examples, all entities are registered for GST and make supplies connected with the indirect tax zone[2A] in the course or furtherance of an enterprise they carry on.

Example 1 – Sale of commercial premises subject to a lease

9. *Grays Pty Ltd owns a shopping centre that it has leased to Nation Pty Ltd. The supply of the shopping centre to Nation under the lease is a taxable supply for which the rent is consideration. Grays is liable for GST on that supply. Grays sells the shopping centre to Ultra Pty Ltd subject to the existing lease. Following the sale by Grays, Ultra is liable for GST on the supply of the shopping centre by way of lease to Nation. The GST is payable with reference to the price of the supply, which in this case is the rent.*

Example 2 – Sale of leased commercial premises where rent has been pre-paid

10. *Bench Pty Ltd accounts for GST on a non-cash basis and has leased an office block to Press Pty Ltd for a monthly GST inclusive rent of $110,000. Bench will sell the office block to Squat Ltd with the lease in place. Settlement will occur on 16 April. The sale contract lets Bench keep any rent paid before settlement, but requires a purchase price reduction to reflect the GST exclusive amount of any prepaid rent Bench receives that relates to the days in the month following settlement.*

[2A] See section 195-1 of the GST Act for the definition of 'indirect tax zone'.

11. *On 1 April, Bench invoices Press for $110,000, which it pays in full on the same day. Bench is liable for GST of $10,000 on this prepaid rent. The purchase price is reduced by $50,000 at settlement for the prepaid rent Bench has received that relates to the days in the month following the sale (that is, a $50,000 adjustment for 16 to 30 April).*[2B]

11A. The purchase price adjustment decreases the consideration Squat pays for the leased premises and is not consideration for the supply of the office block it will make to Press by way of lease.[2C]

Date of effect

12. This Determination applies both before and after its date of issue. However, this Determination will not apply to taxpayers to the extent that it conflicts with the terms of a settlement of a dispute agreed to before the date of issue of this Determination (see paragraphs 75 and 76 of Taxation Ruling TR 2006/10).

Commissioner of Taxation
22 February 2012

[2B] ATO Interpretative Decision ATO ID 2013/30 *GST and the sale of commercial premises that are subject to a lease*, previously explained the view, as outlined in Example 2 above, that the vendor of leased commercial premises would be subject to GST on prepaid rent in these circumstances. ATO ID 2013/30 has been withdrawn.

[2C] See Goods and Services Tax Determination 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?*

Appendix 1 – Explanation

This Appendix is provided as information to help you understand how the Commissioner's view has been reached. It does not form part of the binding public ruling.

Supply of leased commercial premises

13. After the sale of the reversion in commercial premises, no separate or new lease agreement need be entered into between the purchaser (as new owner of the real property) and the existing lessee to ensure the continued operation of the lease. This follows from the operation of property law.[3]

14. *Commissioner of Taxation v. MBI Properties Pty Ltd*[4] (*MBI*) was a case concerning the sale of leased residential premises. The High Court found that, in addition to a supply arising when a lease is granted, on purchasing leased premises, the purchaser assumed the vendor's obligation under the lease to provide the lessee with use and occupation of the premises.[5] The High Court concluded that, as a result of assuming and observing this obligation, the purchaser made a supply of the premises by way of lease to the lessee progressively during the remaining lease term.[6]

15. While the decision in *MBI* concerned leased residential premises, the High Court's conclusions were made in the context of its broader analysis about contracts for the lease of real property generally,[7] and confirm that the purchaser of a reversion makes a supply to the lessee.

GST consequences

Taxable supply

16. Liability for GST depends on there being a 'taxable supply'.[8] Section 9-5 contains the requirements for there to be a 'taxable supply'. Paragraph 9-5(a) requires that an entity makes a supply for consideration. Under section 9-15, consideration includes any payment in connection with a supply and any payment in response to or for the inducement of a supply.

17. Consistent with the decisions in *MBI* and *Westley Nominees Pty Ltd v. Coles Supermarkets Australia Pty* Ltd,[9] following the sale of the reversion in commercial premises, there is a supply made by the purchaser to the lessee, for which the rent paid under the lease is consideration.[10] Provided the other conditions in section 9-5 are met, this supply is a taxable supply and the purchaser is liable for GST on the lease.

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[3] This is further explained at paragraphs 14 to 16 of GSTD 2012/1.
[4] [2014] HCA 49; 2014 ATC 20-474.
[5] *MBI* at [40].
[6] *MBI* at [36] and [40].
[7] *MBI* at [35] – [37].
[8] Sections 7-1 and 9-40.
[9] [2006] FCAFC 115; (2006) 152 FCR 461; 2006 ATC 4363; (2006) 62 ATR 682.
[10] *MBI* at [45]. See also Goods and Services Tax Determination GSTD 2000/10 *Goods and services tax: are outgoings payable by a tenant under a commercial property lease part of the consideration for the supply of the premises?* for explanation on when payments other than rent can be consideration for the supply of commercial premises by way of lease.

18. The vendor of commercial premises is not liable for GST on the lease where it is no longer in receipt of, or, entitled to rent or other consideration for the lease, following the sale of the reversion. As the entitlement to rent payable under the lease passes from vendor to purchaser following the sale, the vendor no longer makes any supply to the lessee for consideration.[11] Instead, rent paid under the lease following the sale has a connection with the purchaser's supply by way of lease, sufficient to make it consideration for that supply.[12]

19. [Omitted.]

Attribution

20. Subsection 29-5(1) provides that GST payable on a taxable supply is attributable to the tax period in which any of the consideration is received for the supply, or to the period in which an invoice is issued relating to the supply if this occurs before consideration is received.

21. However, under subsection 29-5(2), if an entity accounts for GST on a cash basis, GST is attributable to a tax period to the extent consideration is received in that tax period.

22. Under subsection 156-5(1), GST payable on a taxable supply made for a period or on a progressive basis and for consideration to be provided on a progressive or periodic basis, is attributed in accordance with subsection 29-5(1) as if each progressive or periodic component of the supply were a separate supply.[13]

23. Subsection 156-5(1), and Division 156 more broadly, apply only to entities that account for GST on a basis other than cash.

24. By spreading the liability for GST and availability of input tax credits over the period during which payments are made, Division 156 produces a similar result for these entities, as for entities that account for GST on a cash basis.

25. As a result of assuming and observing the obligation to provide the lessee with use and occupation of the premises, the purchaser of a reversion makes a supply to the lessee,[14] for which rent is periodically paid.[15] Based on *MBI,* the supply made to a lessee by the purchaser of a reversion in commercial premises, is by way of lease.

26. Section 156-22 confirms that, for the purposes of the special rules in Division 156, a supply by way of lease is to be treated as being made on a progressive or periodic basis, for the period of the lease.

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[11] *Westley Nominees* at [13] and [21]. See also section 117 of the *Property Law Act 1974* (Qld), section 117 of the *Conveyancing Act 1919* (NSW), section 141 of the *Property Law Act 1958* (Vic), section 77 of the *Property Law Act 1969* (WA), section 10 of the *Conveyancing and Law of Property Act 1884* (Tas), section 124 of the *Real Property Act 1886* (SA), section 130 of the *Law of Property Act 2000* (NT) and section 113 of the *Land Titles Act 1925* (ACT).

[12] *MBI* at [45].

[13] Goods and Services Tax Ruling GSTR 2000/35 *Goods and services tax: Division 156 – supplies and acquisitions made on a progressive or periodic basis*, further explains the Commissioner's view on the application of Division 156.

[14] *MBI* at [36] and [40] - [41].

[15] *MBI* at [45].

27. Consequently, where all of the other requirements of section 9-5 are satisfied, following the sale of leased commercial premises, a purchaser to whom Division 156 applies is required to account for GST as if a separate supply is made for each tax period the lease remains in place.[16] Each such supply will, in accordance with subsection 156-5(1), be regarded as a component of the actual supply made.

28. GST payable relating to each component is, in absence of an invoice being issued, attributed under paragraph 29-5(1)(a) to the tax period in which payment for that component is received. Where an invoice for a particular component is issued prior to payment, GST in respect of that component is attributed under paragraph 29-5(1)(b) to the tax period in which the invoice is issued.[17]

29. [Omitted.]

30. [Omitted.]

[16] See also paragraph 12 of GSTR 2000/35.
[17] See also paragraph 61 of GSTR 2000/35.

References

Previous draft:

Not previously issued as a draft

Related Rulings/Determinations:

GSTR 2000/35; GSTD 2012/1; TR 2006/10

Subject references:

- goods and services tax
- GST commercial residential premises
- GST lease and real property
- GST real property
- GST residential premises
- tax invoices

Legislative references:

- ANTS(GST)A 1999
- ANTS(GST)A 1999 7-1
- ANTS(GST)A 1999 9-5
- ANTS(GST)A 1999 9-5(a)
- ANTS(GST)A 1999 9-10(2)(g)
- ANTS(GST)A 1999 9-15
- ANTS(GST)A 1999 9-40
- ANTS(GST)A 1999 11-5
- ANTS(GST)A 1999 Div 29
- ANTS(GST)A 1999 29-5(1)
- ANTS(GST)A 1999 29-5(1)(a)
- ANTS(GST)A 1999 29-5(1)(b)
- ANTS(GST)A 1999 29-5(2)
- ANTS(GST)A 1999 40-35
- ANTS(GST)A 1999 40-65
- ANTS(GST)A 1999 75-5(1)
- ANTS(GST)A 1999 Div 156
- ANTS(GST)A 1999 156-5(1)
- ANTS(GST)A 1999 156-22
- ANTS(GST)A 1999 195-1
- TAA 1953
- Conveyancing Act 1919 (NSW) 117
- Conveyancing and Law of Property Act 1884 (Tas) 10
- Land Titles Act 1925 (ACT) 113
- Law of Property Act 2000 (NT) 130
- Property Law Act 1958 (Vic) 141
- Property Law Act 1969 (WA) 77
- Property Law Act 1974 (Qld) 117
- Real Property Act 1886 (SA) 124

Case references:

- South Steyne Hotel Pty Ltd v. Federal Commissioner of Taxation [2009] FCAFC 155; (2009) 180 FCR 409; 2009 ATC 20-145; (2009) 74 ATR 41
- Westley Nominees Pty Ltd v. Coles Supermarkets Australia Pty Ltd [2006] FCAFC 115; (2006) 152 FCR 461; 2006 ATC 4363; (2006) 62 ATR 682

ATO references

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