

***PS LA 2013/3 (GA) - Treatment of input tax credits claimed by a recipient of a non-taxable supply where the Commissioner has the discretion to give a refund of the overpaid goods and services tax to the supplier due to the operation of former section 105-65 of Schedule 1 to the Taxation Administration Act 1953***

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# Law Administration Practice Statement (General Administration)

**PS LA 2013/3 (GA)**

*This Practice Statement is an internal ATO document and an instruction to ATO staff.*

*Taxpayers can rely on this Practice Statement to provide them with protection from interest and penalties in the following way. If a statement turns out to be incorrect and taxpayers underpay their tax as a result, they will not have to pay a penalty, nor will they have to pay interest on the underpayment provided they reasonably relied on this Practice Statement in good faith. However, even if they do not have to pay a penalty or interest, taxpayers will have to pay the correct amount of tax provided the time limits under the law allow it.*

|                 |                                                                                                                                                                                                                                                                                                                   |
|-----------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <b>SUBJECT:</b> | <b>Treatment of input tax credits claimed by a recipient of a non-taxable supply where the Commissioner has the discretion to give a refund of the overpaid goods and services tax to the supplier due to the operation of former section 105-65 of Schedule 1 to the <i>Taxation Administration Act 1953</i></b> |
| <b>PURPOSE:</b> | <b>To explain the circumstances in which the Commissioner will use their powers of general administration to allow a recipient to retain an input tax credit that it has claimed where a transaction was incorrectly treated by a supplier as giving rise to a taxable supply.</b>                                |

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## BACKGROUND

1. Former section 105-65 of Schedule 1 to the *Taxation Administration Act 1953* (TAA) applies to an amount that relates to a tax period starting before 31 May 2014. Former subsection 105-65(1) of that Act provides that the Commissioner need not give a refund, or apply that amount<sup>1</sup>, if an entity overpaid its net amount or an amount of goods and services tax (GST) because:
  - a supply was treated as a taxable supply, or an arrangement was treated as giving rise to a taxable supply, to any extent<sup>2</sup>, and
  - the supply is not a taxable supply, or the arrangement does not give rise to a taxable supply, to that extent<sup>3</sup>, and
  - either:
    - we are not satisfied that the entity has reimbursed a corresponding amount to the recipient of the supply (or in the case of an arrangement treated as giving rise to a taxable supply, to the purported recipient)<sup>4</sup>, or
    - the recipient (or in the case of an arrangement treated as giving rise to a taxable supply, the purported recipient)<sup>5</sup> is registered or required to be registered for GST.<sup>6</sup>
2. All legislative references in this Practice Statement are to Schedule 1 to the TAA, unless otherwise indicated.
3. Where former paragraphs 105-65(1)(a) and (b) apply:
  - but neither of the conditions in former paragraph 105-65(1)(c) are met – former section 105-65 does not apply and the Commissioner must refund the overpaid GST to the supplier
  - and either or both of the conditions in former paragraph 105-65(1)(c) are met – the Commissioner need not refund the overpaid GST to the supplier but has a discretion to do so.
4. Miscellaneous Taxation Ruling MT 2010/1 *Miscellaneous tax: restrictions on GST refunds under section 105-65 of Schedule 1 to the Taxation Administration Act 1953* outlines our views on former section 105-65. In particular, paragraph 128 of MT 2010/1 sets out guiding principles in relation to when the Commissioner may exercise the discretion to give a supplier a refund.
5. This Practice Statement applies to circumstances where:
  - a supply has incorrectly been treated as taxable to any extent in relation to a tax period starting before 31 May 2014<sup>7</sup>
  - the supplier is registered for GST and has overpaid GST
  - the supplier has issued a tax invoice to the recipient<sup>8</sup>

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<sup>1</sup> In accordance with the running balance account rules (see Division 3 and Division 3A of Part IIB).

<sup>2</sup> Former paragraph 105-65(1)(a).

<sup>3</sup> Former paragraph 105-65(1)(b).

<sup>4</sup> Former subparagraph 105-65(1)(c)(i).

<sup>5</sup> In this Practice Statement, references to 'supply' include an arrangement that was treated as giving rise to a taxable supply, and references to 'recipient' include a purported recipient.

<sup>6</sup> Former subparagraph 105-65(1)(c)(ii).

<sup>7</sup> Division 142 of the *A New Tax System (Goods and Services Tax) Act 1999* (GST Act) applies to excess GST in tax periods starting on or after 31 May 2014. This Practice Statement does not apply to excess GST under Division 142.

<sup>8</sup> Alternatively, the recipient of the supply has issued a recipient created tax invoice.

- the recipient has over-claimed an input tax credit (ITC) and would have been entitled to claim that ITC if the supply had been a taxable supply
- the recipient has treated the acquisition as a creditable acquisition when applying other taxation laws, such as the income tax law and the fringe benefits tax law
- should the supplier request a refund, former section 105-65 would apply such that we need not refund the supplier the overpaid GST, and
- we have not given a refund of the overpaid GST to the supplier.

## STATEMENT

6. This Practice Statement is concerned with the recipient's ability to retain ITCs. Our view on the circumstances in which it is appropriate to exercise the Commissioner's discretion to refund the overpaid GST to the supplier is set out in MT 2010/1.
7. In the circumstances described in paragraph 5 of this Practice Statement, we generally do not require the recipient to repay the overclaimed ITC or pay any general interest charge related to the overclaimed ITC.<sup>9</sup> This is referred to as the 'preserving the status quo' approach.
8. The factors listed in paragraph 5 of this Practice Statement are intended to provide a list of pre-conditions that must be satisfied before adopting an approach that preserves the status quo. However, we acknowledge that there will be other circumstances where it may also be appropriate to adopt such an approach.<sup>10</sup>
9. Preserving the status quo will not apply in those limited circumstances where the Commissioner exercises the discretion under former section 105-65 to pay a refund of the overpaid GST to the supplier. Subject to an assessment of the facts in such cases, we will seek to recover the overclaimed ITCs from the recipient of the supply. The overclaimed ITCs will be recovered by us where failure to do so would produce an outcome inconsistent with the principles upon which the GST system is based.<sup>11</sup>
10. Preserving the status quo will also not apply where the supplier reimburses the recipient for the amount of GST incorrectly included in the price of the supply. In such cases, we will generally seek to recover the overclaimed ITCs from the recipient of the supply to obviate a potential windfall gain as the recipient has ultimately not borne the cost of the GST.
11. Preserving the status quo is only applicable to historical transactions where the supply has been incorrectly treated as taxable.<sup>12</sup> We expect the incorrect treatment of supplies as taxable to be rectified for future transactions.
12. Where a recipient considers that an acquisition is not a creditable acquisition because they believe the supply is not a taxable supply, the preserving the status quo approach is not to be used as a basis for supporting ongoing incorrect GST treatment of future transactions. Where uncertainty exists as to the correct GST treatment of the transaction, we will consider, subject to our

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<sup>9</sup> In accordance with Law Administration Practice Statements PS LA 1998/1 *Law administration practice statements* and PS LA 2009/4 *Decisions made by the Commissioner in the general administration of the taxation laws*, recipients can choose whether to adopt this approach or not.

<sup>10</sup> See paragraphs 24 and 25 of this Practice Statement.

<sup>11</sup> See paragraphs 17 and 18 of this Practice Statement.

<sup>12</sup> Paragraphs 26 and 27 of this Practice Statement provide commentary on what a 'historical transaction' is.

risk criteria (likelihood and consequence of error), whether it needs to take action to confirm the treatment with both parties.

13. Preserving the status quo relates only to not disturbing the ITC claimed by the recipient. It is an administrative approach with the purpose of avoiding unnecessary compliance costs, it does not change the underlying nature of the supply and acquisition or the consequences of these transactions.<sup>13</sup>
14. Where the incorrect treatment of a supply as a taxable supply gives rise to the incorrect treatment of other transactions to which the supplier or recipient is a party, and which may give rise to an unintended benefit, it may not be appropriate to preserve the status quo.
15. The recipient's entitlement to an ITC can impact upon the application of other taxation laws, such as the income tax law and the fringe benefits tax law. For the preserving the status quo approach to apply, the recipient should also have treated the acquisition as a creditable acquisition when working out their obligations or entitlements under these other laws.<sup>14</sup>
16. The approach does not extend to circumstances outside those covered by former section 105-65. For example, the approach cannot be applied where a taxable supply has been incorrectly treated as non-taxable. Such errors must be corrected by the supplier and recipient and reported by either activity statement revision or by applying the principles in *A New Tax System (Goods and Services Tax) (Correcting GST Errors) Determination 2023*.<sup>15</sup>

## EXPLANATION

17. The scheme of the GST law is premised on the following principles:
  - It is the supplier that determines if the supply it makes is taxable in the first instance – by determining that its supply is a taxable supply, GST is included in the price.
  - Double taxation is avoided by a registered recipient being entitled to claim an ITC for that taxable supply where it is acquired for a creditable purpose.
  - Once GST is embedded in the supply chain, it is the unregistered end consumer that bears the economic burden of the GST.
18. Two important policy considerations behind the operation of former section 105-65, based on the principles in paragraph 17 of this Practice Statement, are:
  - The economic burden of GST charged on a taxable supply is ordinarily borne by the unregistered end consumer.
  - There should not be a refund of overpaid GST to a supplier where it would result in a windfall gain to the supplier.<sup>16</sup>
19. From the supplier's perspective, former subparagraph 105-65(1)(c)(ii) reflects those policy reasons by providing that the Commissioner need not give the supplier a refund of overpaid GST where the recipient is registered for GST. This principle is explained in paragraph 2.3 of the Explanatory Memorandum

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<sup>13</sup> See Example 1 of this Practice Statement for further details on this point.

<sup>14</sup> See paragraphs 42 to 46 of this Practice Statement for further details.

<sup>15</sup> Further information may also be found in [Correcting GST errors](#).

<sup>16</sup> See paragraph 37 of MT 2010/1.

to the Tax Laws Amendment (2008 Measures No. 3) Bill 2008, which states that:

In the case of business-to-business transactions, the Commissioner is not required to refund overpaid GST because the purchasing business is potentially entitled to input tax credits to offset the GST included in the price of its acquisition.

20. Similarly, from the recipient's perspective, the preserving the status quo approach is consistent with the policy reasons behind the operation of former section 105-65 by ensuring symmetry between the GST paid and the ITC claimed in respect of a business-to-business transaction.
21. Even where there is not complete symmetry between the amount paid as GST by the supplier and the ITC claimed by the recipient (for example, where the recipient claims a partial ITC), we will generally adopt an approach that preserves the status quo. In these situations, it is envisaged that the registered recipient of the supply will pass on the cost of the unclaimed GST to their customers as a foreseeable cost of business.<sup>17</sup>
22. MT 2010/1 sets out the factors that the Commissioner will have regard to in exercising the discretion in former section 105-65.<sup>18</sup> A number of these principles are also relevant in determining whether it is appropriate to not apply the preserving the status quo approach, including where:
  - it results in a windfall gain to the recipient or disturbs the inherent symmetry in the GST system, or
  - it produces an unreasonable outcome, for example, an asymmetrical revenue outcome.
23. Applying the Commissioner's powers of general administration, it is appropriate for us not to take any compliance action to reverse a transaction in the circumstances outlined in paragraph 5 of this Practice Statement. The approach aims to overcome unnecessary administrative and compliance costs for the parties involved in the transaction that would otherwise arise if reversal of the transaction were to be required.
24. As noted in paragraph 8 of this Practice Statement, there will be other circumstances in which it will also be appropriate to preserve the status quo. Such an approach may be adopted providing it does not produce an outcome that departs from the policy intent underpinning the GST law.
25. For example, an Australian-based agent of a non-resident recipient may engage an Australian supplier to make supplies to the non-resident recipient. The supplier may incorrectly treat these supplies made to the non-resident recipient as taxable where the supplies are GST-free<sup>19</sup> and the Australian-based agent of the non-resident recipient may claim an ITC corresponding to the overpaid GST.<sup>20</sup> This may occur where the Australian supplier mistakenly deals with the Australian-based agent as if it were the principal rather than an agent of the non-resident recipient. In these circumstances, the recipient (the non-resident) would not have been entitled to a full or partial ITC if the supply had been a taxable supply.<sup>21</sup> However, it is a scenario where preserving the status quo provides an appropriate outcome.

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<sup>17</sup> See paragraphs 124 and 128 of MT 2010/1.

<sup>18</sup> See paragraph 128 of MT 2010/1.

<sup>19</sup> Section 38-190 of the GST Act.

<sup>20</sup> Division 57 of the GST Act.

<sup>21</sup> The non-resident recipient is not registered or required to be registered for GST.

## **Transactions to which the preserving the status quo approach applies**

### ***Historical transactions***

26. The approach is only applicable to historical transactions where the GST was overpaid and an ITC was overclaimed in an earlier tax period. If a supply is incorrectly treated as taxable in the current tax period, the supplier and recipient should correct the transaction before lodging their activity statements.
27. We expect the incorrect treatment of supplies as taxable to be rectified for future transactions.

### ***Related transactions***

28. The approach relates only to not disturbing the ITC claimed by the recipient. It does not change the underlying nature of the supply or the consequences of that supply (see Example 1 of this Practice Statement).
29. Where the incorrect treatment of a supply as taxable has GST implications for other transactions to which the recipient is a party, and the application of the approach gives rise to an unintended benefit, it may be appropriate to reverse the transaction rather than to preserve the status quo.

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### ***Example 1 – related transactions***

30. *Entity BB sells an interest in a building project to registered Entity CC. Entity BB treats the sale as a taxable supply and remits an amount as GST to us, and Entity CC claims a corresponding ITC.*
  31. *It is subsequently determined that the disposal of the interest was an input-taxed financial supply. The Commissioner may determine that it is appropriate to preserve the status quo in relation to this transaction by not requiring the ITC wrongly claimed by Entity CC to be returned.*
  32. *However, Entity BB also claims \$5,000 of ITCs for acquisitions made from Entity DD in relation to the supply it made to Entity CC.*
  33. *Entity BB is not entitled to claim ITCs for the acquisition from Entity DD. Therefore, the Commissioner would ordinarily recover the ITCs claimed by Entity BB on the acquisitions from Entity DD.*
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## **Transactions to which the preserving the status quo approach does not apply**

### ***The Commissioner exercises the discretion under former section 105-65 to pay a refund to the supplier***

34. The approach will not apply in circumstances where the supplier seeks a refund of the overpaid GST from us, and we exercise the discretion under former section 105-65 to pay a refund to the supplier.
35. Subject to an assessment of the facts of the case, we will seek to recover the overclaimed ITCs from the recipient of the supply. To not recover in such instances would produce an unreasonable result, being one that provides an asymmetrical revenue outcome.

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**Example 2 – Commissioner’s discretion exercised – recovery of overclaimed input tax credits from recipient**

36. Supplier (S) treats a supply to registered recipient (R) as GST-free and determines the price of the supply accordingly. Subsequently, we audit S and determine that S should have remitted GST on the supply. An assessment is raised and S remits the amount assessed as GST to us and issues a tax invoice to R, who claims a corresponding ITC. Contractually, S cannot seek to recover the GST from R that was not included in the price charged for the supply.
37. S objects to the assessment on the basis that the supply was not taxable. We reverse the audit decision and give a favourable objection decision. S seeks a refund of the overpaid GST from us.
38. In these circumstances, S overpaid the amount as GST because we incorrectly treated the supply as taxable, therefore it is appropriate to exercise the discretion in former section 105-65 to refund the overpaid GST to S.<sup>22</sup>
39. In this situation, it is not appropriate for us to allow R to retain the ITC. If R was able to retain the ITC, R would obtain a windfall gain because GST was not included in the original price paid by R and S bore the cost of the GST we assessed as it was unable to recover the GST under the contract between S and R.
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**The supplier reimburses the GST component of the price to the recipient**

40. The supplier may reimburse the GST component of the GST-inclusive price charged for the supply to the recipient. Examples of where this may occur include:
- where the reimbursement occurs as a pre-condition to the Commissioner exercising the discretion in former section 105-65 to refund the overpaid GST to the supplier, and
  - where the recipient agrees to reimburse in the course of settling a contractual dispute between the supplier and the recipient relating to the GST-inclusive price of the supply.
41. In these cases, we will generally seek to recover the overclaimed ITCs from the recipient of the supply. To preserve the status quo in these circumstances would result in the recipient receiving a windfall gain, being the retention of an ITC where GST was ultimately not included in the price of the acquisition.

**Other taxation laws**

42. The recipient’s entitlement to an ITC can impact upon the application of other taxation laws, such as the income tax law and the fringe benefits tax law.
43. For example, Division 27 of the *Income Tax Assessment Act 1997* outlines the effect of the GST in determining the amount of a deduction. Provisions such as sections 27-5 (losses or outgoings) and 27-80 (capital allowances) of the *Income Tax Assessment Act 1997* provide that the quantum of certain income

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<sup>22</sup> This example is based on Example 15 in Appendix 3 to MT 2010/1.

tax deductions will vary depending upon whether the acquirer is entitled to an ITC for the acquisition.

44. To ensure appropriate and consistent outcomes, a condition of adopting the preserving the status quo approach is that the recipient has treated the acquisition as a creditable acquisition (that is, it has treated the overclaimed ITC as if it were an ITC to which it is entitled) when working out its obligations and entitlements under the income tax law. The recipient would not request any amendment to the relevant income tax assessment to alter that position, in maintaining the status quo approach.
45. A similar issue arises in applying section 149A of the *Fringe Benefits Tax Assessment Act 1986*. A benefit provided in respect of the employment of an employee is a 'GST-creditable benefit' (and is therefore subject to a higher gross-up factor) if the person who provided the benefit<sup>23</sup> is or was entitled to an ITC because of the provision of the benefit. Again, a condition of adopting the preserving the status quo approach is that the person has treated the overclaimed ITC as if it were an ITC to which the person is entitled when calculating their fringe benefits tax liability. Again, the person would not request any amendment to the relevant fringe benefits tax assessment to alter that position.

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### **Example 3 – other taxation laws**

46. *Brendan makes a GST-free supply to John, but mistakenly believes the supply to be taxable and charges a GST-inclusive price of \$550. Brendan pays the GST to us and John, who is registered for GST, claims an ITC of \$50. Brendan later discovers his mistake and advises John. In order to preserve the status quo, John can only claim a tax deduction of \$500. He should treat the \$50 overclaimed ITC as being not tax-deductible. Brendan will only declare \$500 as income.*

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### **General interest charge**

47. Since the preserving the status quo approach does not require the recipient to repay the overclaimed ITC, it follows that the recipient is not required to pay any general interest charge in respect of the overclaimed ITC.

**Date issued:** 1 August 2013

**Date of effect:** This Practice Statement applies before and after its date of issue

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<sup>23</sup> Or a person who is or was a member of the same GST group as the person who provided the benefit.

## Amendment history

20 February 2025

| Part       | Comment                                                                                                                        |
|------------|--------------------------------------------------------------------------------------------------------------------------------|
| Throughout | Content checked for technical accuracy and currency.<br>Updated in line with current ATO style and accessibility requirements. |

23 June 2016

| Part        | Comment                                                         |
|-------------|-----------------------------------------------------------------|
| Paragraph 1 | Updated as a result of law change.                              |
| Footnote 7  | Footnote inserted as a result of law change.                    |
| References  | Updated to add a new legislative reference and contact details. |

## References

|                             |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                        |
|-----------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Legislative references      | TAA 1953 Part IIB Div 3<br>TAA 1953 Part IIB Div 3A<br>TAA 1953 Sch 1 former 105-65<br>TAA 1953 Sch 1 former 105-65(1)<br>TAA 1953 Sch 1 former 105-65(1)(a)<br>TAA 1953 Sch 1 former 105-65(1)(b)<br>TAA 1953 Sch 1 former 105-65(1)(c)<br>TAA 1953 Sch 1 former 105-65(1)(c)(i)<br>TAA 1953 Sch 1 former 105-65(1)(c)(ii)<br>ANTS(GST)A 1999 38-190<br>ANTS(GST)A 1999 Div 57<br>ANTS(GST)A 1999 Div 142<br>ITAA 1997 Div 27<br>ITAA 1997 27-5<br>ITAA 1997 27-80<br>FBTAA 1986 149A |
| Related public rulings      | MT 2010/1                                                                                                                                                                                                                                                                                                                                                                                                                                                                              |
| Related practice statements | PS LA 1998/1<br>PS LA 2009/4                                                                                                                                                                                                                                                                                                                                                                                                                                                           |
| Other references            | <a href="#">Correcting GST errors</a><br>Explanatory Memorandum to the Tax Laws Amendment (2008 Measures No. 3) Bill 2008<br>A New Tax System (Goods and Services Tax) (Correcting GST Errors) Determination 2023                                                                                                                                                                                                                                                                      |

## ATO references

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