

GST ‘Division 129’ adjustments – have you decided to offer new residential stock for rent?

May 2019

Explore more insights 

In brief

In a softening residential property market, a number of developers are choosing to lease some or all of their development stock. It is important to recognise that this may give rise to an adjustment for GST purposes, pursuant to *Division 129 of the GST Act*. These provisions amend the extent of input tax credits claimable for GST incurred on costs. The adjustments must be reported as at 30 June each year.

In earlier market downturns this has been a substantial area of ATO focus, as the level of non-compliance is generally high. Accordingly, we are anticipating an increased audit focus in respect of this issue in the coming months.

If you have offered, or are proposing to offer, residential stock for lease, we strongly recommend a review of input tax credit entitlements ahead of lodging your June 2019 Business Activity Statement (BAS). The Division 129 provisions are complex and can be administratively burdensome. We can help you simplify this process and ensure you maximise your GST position.

In detail

Change in use adjustments

Input tax credits can be claimed in respect of costs that relate to taxable or GST-free supplies, including sales of new residential premises. However, input tax credits are *not* available in respect of costs relating to input taxed supplies, including residential rent.

If the intended or actual use of a property changes over time, an adjustment may arise pursuant to Division 129 of the GST Act. A common example of this is property originally constructed with an intention to sell, where a decision is made to offer the property for lease. In such a case, an adjustment is required to repay some or all the input tax credits previously claimed.

Timing

Division 129 adjustments are required to be made annually, as at 30 June each year (i.e. the June BAS). Each acquisition must be considered on an individual basis, and the number of annual adjustments depends on the size of the acquisition.

| GST-exclusive value of the acquisition | Number of adjustment periods |
|---|-------------------------------------|
| is not more than \$1,000 | 0 |
| is more than \$1,000 and is \$5,000 or less | 2 |
| is more than \$5,000 and is \$500,000 or less | 5 |
| is more than \$500,000 | 10 |

The first adjustment arises as at 30 June at least 12 months after the acquisition. For example, an acquisition in August 2018 would not have its first adjustment period until 30 June 2020.

Calculating the adjustment

As noted above, each acquisition must be considered on an individual basis. This may mean different input tax credit recoveries apply to different costs. For example:

- Costs may solely relate to residential rent, resulting in a nil recovery percentage.
- Costs may solely relate to properties that are sold, resulting in a 100% recovery percentage.
- Costs may relate to the project in entirety, and an apportionment is required to determine the extent of input tax credits available. Additionally, different apportionment rates could apply to different 'buckets' of expenditure.
- Certain properties may be held for rent while also being marketed for sale.

Broadly speaking, Division 129 adjustments are calculated as follows:

$$\text{Total GST incurred} \times (\text{actual recovery \%} - \text{intended or former recovery \%})$$

In practice, the process of calculating Division 129 adjustments is complex and can be administrative cumbersome, particularly in respect of projects involving a high volume of expenditure.

The takeaway

Compliance with the Division 129 adjustment rules is expected to be a focus of the ATO, given increased levels of lease activity arising on account of the recent market downturn. Further, transactions with respect to real property are highly searchable, and the ATO's data matching capabilities are constantly improving. Accordingly, if you have offered or intend to offer residential stock for lease we strongly recommend you review your expenditure to quantify the extent of any adjustments that may be applicable. Being able to support your position and decision making process with documentary evidence is also critical when the ATO make enquiries.

Should you require assistance, we would be pleased to assist. Please contact one of our GST property specialists below, or your regular PwC GST advisor.

Let's talk

For a deeper discussion of how these issues might affect your business, please contact:

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