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# Recoverability of GST credits

20 February 2015

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## ***In brief***

### ***Federal Court decision for the Commissioner in the Rio Tinto Services case***

In a test case before the Federal Court, Rio Tinto argued that it was entitled to input tax credits for acquisitions made in providing and maintaining residential accommodation for its workforce in remote locations. Justice Davies has confirmed that where a material or sufficient relationship or connection exists between an acquisition and the making of an input taxed supply of residential accommodation, a taxpayer is not entitled to claim input tax credits. This is regardless of the purpose for which the taxpayer made the input taxed supply.

The decision has been long awaited by the resource sector, particularly those taxpayers who incur substantial costs in providing accommodation to its workforce in remote parts of Australia. Following the concessions provided by the Commissioner in relation to camp style accommodation in Goods and Services Tax Ruling GSTR 2012/6, this decision effectively draws the line on input tax credit recovery for the sector between short term, worker only accommodation (taxable) and town based, family style accommodation (input taxed).

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## ***In detail***

On 19 February 2015, the Federal Court of Australia handed down its decision in *Rio Tinto Services Ltd v Commissioner of Taxation* [2015] FCA 94. The Federal Court decided the taxpayer (Rio Tinto), was not entitled to claim input tax credits for acquisitions made by entities in its GST group in relation to the provision and maintenance of residential accommodation for their workforce. Details of the case are as follows:

- The taxpayer is the representative member for the Rio Tinto Ltd GST Group, which includes Hamersley Iron Pty Ltd (Hamersley) and Pilbara Iron Company (Services) Pty Ltd (PICS). Hamersley and PICS provided and maintained residential accommodation for Hamersley's workforce in remote areas of Western Australia where Hamersley conducted mining operations. Hamersley made losses each year from providing the residential accommodation as its expenditure on the housing substantially exceeded the rental income it received. Hamersley subsidised the rental accommodation provided to its workforce as it would not be economically viable for most people to pay the full cost of accommodation, making it difficult to attract and retain people in the remote areas.
- Justice Davies was asked to consider whether the acquisitions made by Hamersley in relation to providing the residential accommodation were made solely or partly for a 'creditable purpose'. It was accepted that acquisitions made by Hamersley were made in the course of carrying on its enterprise and therefore satisfied the first limb of the 'creditable purpose' test in section 11-15(1) of the GST Act.

- In relation to the second limb of the ‘creditable purpose’ test in section 11-15(2)(a) (i.e. that you do not acquire the thing for a creditable purpose to the extent that the acquisition relates to making supplies that would be input taxed), the taxpayer accepted that the provision of the accommodation is an input taxed supply and accepted there is a connection between the acquisitions in question and the provision of the accommodation.
- However, the taxpayer contended that for section 11-15(2)(a) to apply, the making of an input taxed supply, not the making of a taxable supply, must be the ‘moving cause’ or ‘purpose’ of the acquisition. It was submitted the acquisitions in question did not relevantly ‘relate to’ the making of supplies that would be input taxed because the ‘moving cause’ in, or ‘purpose’ of, supplying residential accommodation was the carrying on of Hamersley’s ‘enterprise’ of mining and selling iron ore (i.e. making taxable or GST free supplies) not the leasing of accommodation as an end activity in itself (i.e. making input taxed supplies).
- Justice Davies did not agree with the taxpayers submissions and found that section 11-15(2)(a) simply denotes that there must be a relationship or connection between an acquisition and the making of input taxed supplies. The existence of such a relationship is not made to depend on a ‘purpose’ test. A finding that the provision of accommodation was an essential and necessary incident of Hamersley carrying on its mining operations would not mean that section 11-15(2)(a) is not engaged. The Court held that as the acquisitions in question had a direct and immediate connection with Hamersley’s provision of lease accommodation, section 11-15(2)(a) applied to deny the taxpayer input tax credits.

### ***The takeaway***

The decision of the Federal Court essentially confirms that taxpayers are not entitled to claim input tax credits to the extent any acquisitions made relate to an input taxed supply. This is regardless of whether the making of the input taxed supply is the main purpose of the entity’s enterprise or is merely incidental to its main activities. The decision may be subject to appeal by the Applicant.

If you make input taxed supplies, including financial supplies, you should carefully reconsider what acquisitions relate partially or wholly to those supplies and deny any GST incurred on those acquisitions as necessary.

### ***Let’s talk***

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

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