Draft Goods and Services Tax Ruling

Goods and Services Tax: financial acquisitions threshold

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Preamble

This document is a draft for industry and professional comment. As such, it represents the preliminary, though considered views of the Australian Taxation Office. This draft may not be relied on by taxation officers, taxpayers and practitioners. When officially released it will be a public ruling for the purposes of section 37 of the ***Taxation Administration Act 1953*** *and may be relied upon by any entity to whom it applies.*

What this Ruling is about

1. This Ruling explains:

- how Division 189 of A New Tax System (Goods and Services Tax) Act 1999 ('the GST Act') affects your entitlement to input tax credits for acquisitions relating to financial supplies;
- when you exceed the financial acquisitions threshold;
- the meaning of the terms 'likely to make', 'financial acquisition', 'borrowing' and 'relates to' for the purposes of Division 189;
- what is included in calculating the amount of the input tax credits to which you would be entitled in relation to financial acquisitions (first limb test);
- what is included in calculating the total amount of the input tax credits to which you would be entitled in relation to all acquisitions (second limb test);
- how an entity that is a member of a GST group exceeds the financial acquisitions threshold;
- the application of the financial acquisitions threshold to members of a GST religious group;
- the interaction of Division 72 with the financial acquisitions threshold;

- the interaction of Division 84 with the financial acquisitions threshold; and
- how often the financial acquisitions threshold should be tested.

2. This Ruling applies to all entities that are registered, or required to be registered for the goods and services tax ('GST') that make financial supplies in the course of conducting their enterprise.

3. All legislative references are to the GST Act or A New Tax System (Goods and Services Tax) Regulations 1999 ('the GST regulations'), unless otherwise stated. Unless otherwise stated, the examples given in this Ruling assume that the consideration for all acquisitions is GST inclusive.

Date of effect

4. This draft Ruling represents the preliminary, though considered, view of the Australian Taxation Office. This draft may not be relied on by taxation officers, taxpayers or practitioners. When the final Ruling is officially released, it will explain our view of the law as it applied from 1 July 2000. The final Ruling will be a public ruling for the purposes of section 37 of the *Taxation Administration Act 1953* and may be relied upon, after it is issued, by any entity to whom it applies. 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.

Background

5. Under sections 11-15 and 15-10 of the GST Act, an entity acquires a thing or imports goods for a creditable purpose to the extent it is acquired in carrying on an enterprise of that entity. However, an entity does not acquire a thing or import goods for a creditable purpose to the extent that the acquisition or importation relates to making input taxed supplies (such as financial supplies) or is of a private or domestic nature. This means that an entity is not entitled to input tax credits for an acquisition or importation in those circumstances.

6. Subsections 11-15(4) and 15-10(4) provide that an acquisition or importation is not treated as relating to supplies that would be input taxed if:

- the only reason it would be treated as relating to input taxed supplies is because it relates to making financial supplies; and
- the entity does not exceed the financial acquisitions threshold.

7. Division 189 deals with the financial acquisitions threshold. The purpose of the Division is to enable an entitlement through subsections 11-15(4) and 15-10(4) to input tax credits for acquisitions and importations that relate to making financial supplies even though financial supplies are normally input taxed.

8. The GST Act provides that 'financial supply' has the meaning given by the GST regulations. Something is a financial supply only if it is mentioned as a financial supply in regulation 40-5.09 or is an incidental financial supply under regulation 40-5.10. Regulation 40-5.12 has the effect of excluding things that might otherwise have been included as a financial supply by regulation 40-5.09. Regulation 40-5.12 does not exclude from being a financial supply something that is also an incidental financial supply.[1]

9. The interest supplied must be an interest in, or under, one of the categories set out in the table in subregulation 40-5.09(3) of the GST regulations. These categories are:

- an account made available by an Australian ADI (authorised deposit-taking institution) in the course of its banking business or its State banking business (subregulation 40-5.09(3), item 1);
- a debt, credit arrangement or right to credit, including a letter of credit (subregulation 40-5.09(3), item 2);
- a charge or mortgage over real or personal property (subregulation 40-5.09(3), item 3);
- specified superannuation arrangements (subregulation 40-5.09(3), item 4);
- an annuity or allocated pension (subregulation 40-5.09(3), item 5);
- specified life insurance business or related reinsurance business (subregulation 40-5.09(3), item 6);
- a guarantee, including an indemnity (except a warranty for goods or a contract of insurance or reinsurance) (subregulation 40-5.09(3), item 7);

[1] Regulation 40-5.10 of the GST regulations.

- credit under a hire purchase agreement (subregulation 40-5.09(3), item 8);
- Australian currency or foreign currency or agreements to buy or sell either of those currencies (subregulation 40-5.09(3), item 9);
- securities (subregulation 40-5.09(3), item 10); and
- a derivative (subregulation 40-5.09(3), item 11).

10. Subregulation 40-5.09(1) of the GST regulations describes the circumstances under which the provision, acquisition or disposal of an interest mentioned in subregulations 40-5.09(3) or (4) is a financial supply. The circumstances are that the provision, acquisition or disposal is for consideration, in the course or furtherance of an enterprise and connected with Australia. Furthermore, the supplier must be registered or required to be registered and a financial supply provider in relation to the supply of the interest.[2]

Ruling and Explanation

Financial acquisitions threshold

11. Entities that make financial supplies in the course of conducting their enterprise without exceeding the financial acquisitions threshold are entitled to input tax credits for acquisitions and importations that relate to making those financial supplies. Division 189 provides for a test based on current acquisitions and a separate test based on future acquisitions to determine whether an entity exceeds the financial acquisitions threshold at a particular time. If the threshold is exceeded under either the current or future acquisitions test, the entity will not be entitled to input tax credits on acquisitions that relate to the making of financial supplies.

Current acquisitions threshold

12. To test whether an entity exceeds the financial acquisitions threshold at a time during a particular month, the entity is required to assume that all the financial acquisitions[3] it has made, or is likely to make, during the 12 months ending at the end of that month were made solely for a creditable purpose. The entity will exceed the financial acquisitions threshold if during a particular month either or both of the following would apply:

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[2] For a full discussion of financial supplies, see Goods and Services Tax Ruling GSTR 2002/2.

[3] See paragraph 20 of this Ruling for the meaning of financial acquisition.

- the amount of all the input tax credits to which the entity would be entitled for its financial acquisitions would exceed $50,000 or such other amount specified in the GST regulations (first limb test);
- the amount of the input tax credits to which the entity would be entitled for its financial acquisitions would be more than 10% of the total amount of input tax credits to which it would be entitled for all its acquisitions and importations (including the financial acquisitions) during that 12 months (second limb test).[4]

Example 1 – threshold not exceeded (current acquisitions)

13. *In August 2002, Beech & Co Pty Ltd (Beech) calculates that its total acquisitions (including financial acquisitions) during the months from 1 September 2001 to 31 August 2002 are $374,000. Of that amount, Beech calculates that $33,000 was for financial acquisitions.*

14. *Assuming these financial acquisitions were made solely for a creditable purpose, Beech's input tax credits for its total acquisitions would be $34,000 (1/11th of $374,000) and its input tax credits for financial acquisitions would be $3,000 (1/11th of $33,000). This $3,000 does not exceed the $50,000 threshold and also does not exceed 10% of $34,000 ($3,400). Beech therefore does not exceed the current acquisitions threshold.*

Future acquisitions threshold

15. An entity will exceed the financial acquisitions threshold at a time during a particular month if, assuming that all the financial acquisitions it has made, or is likely to make, during that month and the next 11 months were made solely for a creditable purpose, either or both of the following would apply:

- the amount of all the input tax credits to which the entity would be entitled for its financial acquisitions would exceed $50,000 or such other amount specified in the GST regulations (first limb test);
- the amount of the input tax credits to which the entity would be entitled for its financial acquisitions would be more than 10% of the total input tax credits to which the entity would be entitled for all its acquisitions and

[4] See subsection 189-5(1).

importations (including the financial acquisitions) during those months (second limb test).[5]

Therefore an entity calculates whether it exceeds the financial acquisitions threshold by reference to its potential entitlement to input tax credits for its financial acquisitions and for its total acquisitions.

Example 2 – threshold exceeded (future acquisitions)

16. *Following on from example 1, although Beech does not exceed the current acquisitions threshold, it must also determine whether it exceeds the future acquisitions threshold. Beech calculates that the total acquisitions for the 12 month period from 1 August 2002 to 31 July 2003 are likely to be $308,000 and that its financial acquisitions are likely to be $38,500.*

17. *Assuming these financial acquisitions were made solely for a creditable purpose, the total input tax credits for that year would therefore be $28,000 (1/11th of $308,000) and input tax credits for financial acquisitions would be $3,500 (1/11th of $38,500). Although the $3,500 does not exceed $50,000, it exceeds 10% of the total input tax credits ($2,800). Beech exceeds the financial acquisitions threshold and is therefore not entitled to input tax credits for its acquisitions relating to its financial supplies.*[6]

18. *If Beech had exceeded the current acquisitions threshold, it would not be necessary to determine whether it exceeds the future financial acquisitions threshold.*

19. Although the financial acquisitions threshold, calculated at a time in a particular month, is based on acquisitions made in the twelve months ending with that month and acquisitions likely to be made in that month plus the next eleven months, the entitlement to input tax credits for acquisitions that relate to the making of financial supplies is only denied from the time that the entity first exceeds the threshold. It does not affect the input tax credits for acquisitions made prior to the time the threshold is exceeded.

Defining a financial acquisition

20. A financial acquisition is an acquisition that relates to the making of a financial supply (other than a financial supply consisting of a borrowing).[7]

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[5] See subsection 189-10(1).

[6] A reduced input tax credit is still available to the extent that the acquisition is a reduced credit acquisition under Division 70.

[7] Section 189-15.

What is an acquisition?

21. An acquisition is defined in section 11-10 of the GST Act as 'any form of acquisition whatsoever'. The definition is very broad and is intended to encompass acquisitions as widely as possible.[8] For the purposes of the definition of 'financial acquisition' an acquisition may be a taxable acquisition, or may be an acquisition of a supply that is input taxed, GST-free or outside the GST system. However, there can be no entitlement to input tax credits for acquisitions where there is no GST on the supply of the thing acquired. Such acquisitions will have no effect on whether the threshold is exceeded (see paragraph 82 of this Ruling).

What is the meaning of 'relates to the making of a financial supply'?

22. The meaning of the term 'relates to' as used in section 189-15 must be addressed on a number of different levels:

- First, there is the question of how closely an acquisition must relate to the making of a financial supply. That is, is there sufficient nexus?
- Second, the issue of the timing of the acquisition in relation to the making of a financial supply is also relevant.
- Third, there is the question of the extent to which an acquisition relates to the making of a financial supply.

Nexus

23. The term 'relates to' as used in section 189-15, requires a nexus, link or connection between an acquisition and the making of a financial supply.

24. There is a sufficient connection where the acquisition is used or intended to be used solely or to some extent for the making of a financial supply. Where the acquisition is to be used for the making of a financial supply, it is a financial acquisition regardless of the ultimate purpose of the financial supply. For example, the cost of professional services acquired in connection with the supply of shares would relate to that financial supply even if the ultimate purpose of the supply was to raise funds for making taxable supplies.

25. In addition, an acquisition relates to the making of a financial supply where it is to be used for making both a financial supply and

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[8] Paragraph 3.21 of the Explanatory Memorandum to the A New Tax System (Goods and Services Tax) Bill 1998.

another supply that is not a financial supply. However, such an acquisition is a financial acquisition only to the extent that it relates to the making of a financial supply (see paragraphs 41 to 47 of this Ruling).

26. Acquisitions which relate to the making of financial supplies may be described as either direct or indirect. Direct acquisitions relate to the making of a particular supply or supplies. For example, a computer used by a bank to monitor loans will be a direct acquisition which relates to the making of financial supplies. Indirect acquisitions may also be described as overheads. They are acquisitions that provide an environment in which the entity makes supplies. Examples include rent, gas, electricity and fittings. These overheads may not be capable of a direct connection with the individual supplies made by the entity, however they relate to the making of those supplies. For the purposes of applying section 11-15 and Division 189 it is necessary to allocate those overheads according to the character of the supplies made and in accordance with the entity's apportionment methodology.

Example 3 – overheads that relate to the making of financial supplies

27. *A truck retailer, Smack Trucks, sells trucks to retail customers and also offers finance to customers by way of loans. It has a staff of ten salespersons and two loans officers. The facilities used by the sales staff and the loans officers are comparable. There are specified direct acquisitions that can be identified as relating to the loans activity e.g., specialist software. The acquisition of that software therefore relates to the making of financial supplies. Other acquisitions relate to the making of both the supply of trucks and the supply of loans. Those acquisitions may include the purchase of carpet for the offices of all twelve staff. Therefore for Division 189 purposes, Smack Trucks decides that its most appropriate apportionment method (following GSTR 2000/22) is to allocate 2/12^{ths} of all its overheads, including the acquisition of the carpet, to the financial supplies made by its loans staff.*

28. Where the acquisition relates to the making of a financial supply consisting of a borrowing, it is not necessary to consider whether the borrowing itself relates to the making of a financial supply for the purpose of Division 189.

Timing

29. For the purposes of calculating whether the financial acquisitions threshold is exceeded, an entity takes into account acquisitions that relate to the making of financial supplies. An acquisition relates to the making of a financial supply if it relates to

the making of an actual financial supply or a financial supply that the entity intends to make.

30. At the time something is acquired, the supply to which it relates may not yet have been made. However, it would be a financial acquisition while there is an intention to use the acquisition for the making of a financial supply.

31. An intention to use the acquisition for the making of a financial supply may be evidenced through such things as a business plan, accounting budget, previous experience concerning usage of similar acquisitions, correspondence with third parties relating to a proposed financial supply or a resolution passed by the board of directors.

32. For the purposes of Division 189, an entity determines whether a particular acquisition relates to the making of a financial supply when it is calculating whether the financial acquisitions threshold is exceeded. An entity may subsequently change the intended or actual use of a financial acquisition, for example, where the entity decides not to proceed with the financial supply. In this case, the acquisition is no longer a financial acquisition for Division 189 purposes from the time at, and the extent to which, the intended or actual use of the acquisition is changed.

33. Conversely, if an acquisition was intended to be used for the making of supplies other than financial supplies, and subsequently the acquisition was to be used for the making of financial supplies, the acquisition becomes a financial acquisition from the time of the change in use.

34. These later events do not alter the outcome of the Division 189 threshold test retrospectively. The entity need not go back and recalculate whether it exceeded the threshold at a time prior to the change in use of the acquisition. However, where there is a change in intention, the entity will need to take that change into account when calculating whether it exceeds the threshold for future acquisitions from that point of time onwards.

35. Once a decision is made not to proceed with a proposed financial supply, an acquisition that related to that intended financial supply is no longer a financial acquisition for Division 189 purposes. For this reason, each time the calculation is made to determine whether the entity exceeds the financial acquisitions threshold at a particular time, an entity needs to revisit whether a proposed financial supply is still intended to be made.[9]

[9] See paragraphs 266 to 274 of Goods and Services Tax Ruling GSTR 2002/2 for a discussion on how the intention to make a financial supply affects whether an acquisition relates to the making of a financial supply.

36. Should an entity's actual use of an acquisition change from its planned use[10], an adjustment may be necessary under Division 129 to reflect any change in the extent of creditable purpose.

Example 4 – intention to make a financial supply where the supply does not eventuate

37. *At the board meeting of Thunderbolt Enterprises, a decision to make a rights issue to its shareholders is made and recorded in the minutes. Thunderbolt makes an acquisition of professional advice in January in relation to the rights issue. Three months later, based on the advice it receives, Thunderbolt decides not to go ahead with the rights issue.*

38. *At the time the professional advice was acquired, Thunderbolt had the intention of making a financial supply. The minutes of the board meeting are evidence of the intention to make the supply. The acquisition is therefore a financial acquisition for Division 189 purposes. Any further advice acquired after Thunderbolt decides not to proceed with the issue is not a financial acquisition.*

39. *When calculating whether it exceeds the threshold at a time after the decision not to go ahead with the rights issue, Thunderbolt does not include the professional advice as a financial acquisition. However, it does not recalculate whether it exceeded the threshold at a time prior to the change in use of the acquisition.*

40. Where a financial acquisition is made for a period, or on a progressive basis and Division 156 applies, the acquisition is treated for the purposes of attribution as if each progressive or periodic component were a separate acquisition. In circumstances where Division 156 applies, the input tax credits for the financial acquisition are only included in the Division 189 threshold calculation to the extent the input tax credit entitlement would arise during the period in relation to each component.[11]

Extent

41. In circumstances where an acquisition relates to the making of both financial supplies and other supplies such as taxable supplies and/or GST-free supplies, we consider that for Division 189 purposes, the acquisition is a financial acquisition *to the extent* that it relates to the making of financial supplies.

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[10] See Goods and Services Tax Ruling GSTR 2000/24 and paragraph 267 of Goods and Services Tax Ruling GSTR 2002/2.

[11] For a detailed explanation of the GST treatment of progressive or periodic acquisitions see Goods and Services Tax Ruling GSTR 2000/35.

42. Division 189 can be interpreted in this way despite the absence of the words 'to the extent' in the definition of 'financial acquisition' in section 189-15 as the general scheme of the GST Act is to identify that part of the acquisition that relates to financial supplies.

43. The words 'relates to', as used in section 189-15, are not defined in the GST Act. Such terms must be read in the context in which they appear and courts have ruled that the terms be interpreted in accordance with the intent of the relevant statute. In *Hatfield v. Health Insurance Commission* (1987) 15 FCR 487 at page 491 Davies J stated:

> Expressions such as 'relating to', 'in relation to', 'in connection with' and 'in respect of" are commonly found in legislation but invariably raise problems of statutory interpretation. They are terms that fluctuate in operation from statute to statute… The terms may have a very wide operation but they do not usually carry the widest possible ambit, for they are subject to the context in which they are used, to the words with which they are associated and to the object or purpose of the statutory provision in which they appear.

44. The purpose of Division 189 is to ensure that most entities are not denied input tax credits for making financial supplies that are not part of their principal commercial activities.[12] The object of the Division as set out in section 189-1 is to enable an entitlement through subsection 11-15(4) to input tax credits for acquisitions relating to financial supplies (even though financial supplies are normally input taxed) if the financial acquisitions threshold is not exceeded. To determine the meaning of the term 'relates to' from its legislative context it is necessary to consider the interaction of the words of Division 189 with those of Division 11 which deals with creditable acquisitions.

45. Paragraph 11-15(2)(a) provides that an entity does not acquire a thing for a creditable purpose *to the extent* that it relates to making supplies that would be input taxed (such as financial supplies). Subsection 11-15(4) states that for the purposes of paragraph (2)(a), an acquisition that relates to making a financial supply is not treated as one that would be input taxed if the entity does not exceed the financial acquisitions threshold.

46. The effect of these provisions is that, if an entity does not exceed the financial acquisitions threshold, it may be entitled to input tax credits to the extent to which the acquisition relates to the making of a financial supply. This gives effect to the financial acquisitions threshold test in Division 189 which determines whether an entity would exceed the threshold if these potential input tax credits were allowed.

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[12] See Treasurer's Press Release No 013, 15 March 2000.

Example 5 – acquisition for use in the making of both financial supplies and taxable supplies

47. *Flutterby Enterprises (Flutterby) purchases new computer equipment for $770,000. The computer equipment is used 95% for making taxable supplies and 5% for making financial supplies other than borrowings. In calculating whether it exceeds the financial acquisitions threshold, Flutterby does not treat the full purchase price of $770,000 as a financial acquisition. It treats only $38,500 (5% of $770,000) as a financial acquisition as this is the extent to which the computer equipment is used to make financial supplies.*

What is the meaning of 'making of a financial supply'?

48. The term 'making of a financial supply' means the provision, acquisition or disposal of an interest mentioned as a financial supply in regulation 40-5.09 or an incidental financial supply in regulation 40-5.10 (see paragraphs 8 to 10 of this Ruling).[13]

49. A financial supply includes an acquisition-supply.[14] An acquisition-supply is a supply which is the acquisition of a financial interest. Acquisitions that relate to the making of acquisition-supplies are also financial acquisitions.

Example 6 – financial acquisition

50. *Company A sells shares to Company B through Company C who acts as a broker. Company A is making a financial supply of an interest in or under a security (the shares) to Company B. Company C is making a taxable supply to Company A in the form of brokerage services. Brokerage services provided by Company C are financial acquisitions made by Company A.*

51. *Company B makes an acquisition-supply of the shares. Company D, an investment adviser, supplies services to Company B in relation to the acquisition of the shares. The services acquired by Company B from Company D are financial acquisitions because they relate to making the acquisition-supply.*

What is the meaning of 'borrowing'?

52. An acquisition that relates to the making of a financial supply consisting of a borrowing is not a financial acquisition for the purpose

[13] Goods and Services Tax Ruling GSTR 2002/2 explains and clarifies what is a financial supply.
[14] See paragraphs 22 to 24 of Goods and Services Tax Ruling GSTR 2002/2.

of section 189-15. For the borrowing entity, this means that its financial acquisitions do not include acquisitions to the extent they relate to its borrowings. For the entity that lends the money, acquisitions that relate to loans it makes are not excluded from its financial acquisitions.

53. 'Borrowing' is defined in section 195-1 of the GST Act as having the meaning given by section 995-1 of the *Income Tax Assessment Act 1997*. That section defines 'borrowing' as any form of borrowing, whether secured or unsecured, and includes the raising of funds by the issue of a bond, debenture, discounted security or other document evidencing indebtedness. The requirement for a document evidencing indebtedness leads to the conclusion that for the purposes of the GST Act, a borrowing must involve a debtor/creditor relationship. This would not include equity issues such as the issue of preference shares.

54. The definition of borrowing refers to 'the raising of funds' and the 'issue' of a bond, these being activities undertaken by the borrower. The definition clearly refers to a borrowing in terms of the borrower. Consequently, acquisitions that relate to the making of financial supplies consisting of borrowings are only those acquisitions made by the borrowing entity and not those made by the entity that lends the money.

55. A borrowing in the form of a loan is the acquisition of an interest in a credit arrangement by the borrower. For the purposes of the GST regulations the provision, acquisition or disposal of an interest mentioned in the table in regulation 40-5.09 is the supply of a financial interest. The acquisition of an interest in a credit arrangement is mentioned in item 2 of subregulation 40-5.09(3) and is an acquisition-supply which is the supply of a financial interest.[15] Provided the other elements of regulation 40-5.09 are met, a borrowing in the form of a loan is a financial supply.

56. Acquisitions that relate to the making of the financial supply consisting of the borrowing are not financial acquisitions and are not taken into account under the first limb test. However, it is still necessary to determine the extent to which they are creditable acquisitions to calculate the total input tax credit entitlements under the second limb test.

Example 7 – borrowing related expenses

57. *Anyhow Enterprise borrows $250,000 from R.E.N.E. Co for the purchase of a warehouse. Anyhow pays a valuation fee of $1,100*

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[15] For a more detailed explanation of acquisitions (including borrowings) that are financial supplies, see paragraphs 22 to 24 and 37 to 42 of Goods and Services Tax Ruling GSTR 2002/2.

to an independent valuer and also pays $5,500 in legal fees for negotiating the loan contract. Anyhow is entitled to an input tax credit of $600 (1/11 of $6,600) as these expenses relate to borrowing and the money borrowed does not relate to making input taxed supplies.[16]

58. *Because the valuation and legal fees relate to the making of a financial supply which consists of a borrowing, they are not financial acquisitions for Division 189 purposes. Anyhow is entitled to an input tax credit for these acquisitions under Division 11. Therefore, Anyhow includes the input tax credit in the total amount of input tax credits in calculating whether it exceeds the second limb tests in paragraphs 189-5(1)(b) and 189-10(1)(b).*

Reduced credit acquisitions

59. Financial acquisitions for Division 189 purposes include those acquisitions that are listed in the table in regulation 70 as reduced credit acquisitions[17] because they are acquisitions that relate to the making of financial supplies. A reduced credit acquisition may give rise to an entitlement to a reduced input tax credit under Division 70 of the GST Act.

60. However, a reduced input tax credit is not available to the extent the entity is otherwise entitled to input tax credits for the acquisition, for example, as a result of the application of subsection 11-15(4).[18] The effect of subsection 11-15(4) is that an entity can be entitled to input tax credits for its acquisitions relating to financial supplies, if it does not exceed the financial acquisitions threshold.

61. The entity needs to establish whether it exceeds the financial acquisitions threshold under Division 189 to determine whether it is entitled to input tax credits. If it exceeds the financial acquisitions threshold, and is therefore not otherwise entitled to input tax credits, it may be entitled to a reduced input tax credit.

62. When determining whether it exceeds the financial acquisitions threshold, the entity treats potential reduced credit acquisitions in the same way as other financial acquisitions, and assumes they are solely for a creditable purpose. Therefore, the entity includes the whole of the input tax credits to which it would be entitled being an amount equal to the GST payable on the supply of the thing acquired.

[16] Subsection 11-15(5).
[17] Subsection 70-5(1) defines 'reduced credit acquisitions'.
[18] See subsection 70-5(1A).

Example 8 – reduced credit acquisitions

63. *Big Pty Ltd (Big) acquires debt collection services from Carrie Incorporated in relation to its outstanding debts. The acquisition is of a type listed in the table in regulation 70 as a reduced credit acquisition. The cost of the services is $11,000. Big includes the figure of $1,000 (1/11th of $11,000) in the input tax credits for its financial acquisitions when calculating whether it exceeds the financial acquisitions threshold.*

Acquisitions that are used to make financial supplies that are also GST-free supplies

64. To the extent acquisitions are used for the making of financial supplies that are also GST-free supplies (e.g., exported financial supplies) they are financial acquisitions for Division 189 purposes. They are taken into account in determining whether an entity exceeds the financial acquisitions threshold.

65. Section 189-15 provides that a financial acquisition is an acquisition that relates to the making of a financial supply. Financial supply is defined in section 195-1 as having the meaning given by the GST regulations. Subsection 9-30(3) deals with supplies that are both GST-free and input taxed, and applies to make such supplies GST-free and not input taxed.[19] The GST regulations do not exclude from financial supplies those supplies which are also GST-free by operation of subsection 9-30(3).

66. An acquisition does not need to relate to the making of an 'input taxed' financial supply to be a financial acquisition. Division 189 applies to an acquisition that relates to the making of a supply that is a financial supply under the GST regulations, notwithstanding that the GST-free treatment of the supply (for example, an exported supply) may override its input taxed status.[20]

Example 9 – financial supply that is also GST-free

67. *Scorpion Pty Ltd, an entity that carries on an enterprise in Australia and is registered for GST, wants to raise funds through the issue of shares to UK residents. It acquires legal and professional services at a cost of $275,000 (including GST of $25,000) from an adviser in relation to the issue of the shares.*

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[19] Except where the provision under which it is input taxed requires the supplier to have chosen it to be so.
[20] Subsection 9-30(3) provides that a supply that would be both GST-free and input taxed is treated as a GST-free supply.

68. *As the shares are to be issued to UK residents, they may be GST-free under section 38-190. However, the issue of the shares is also a financial supply under regulation 40-5.09, and would be input taxed but for the operation of subsection 9-30(3). The issue of shares is a financial supply but is GST-free.*

69. *The acquisition of the legal and professional services is a financial acquisition for the purposes of Division 189 because it relates to the making of a financial supply. The input tax credit entitlement of $25,000 is for a financial acquisition and will therefore be taken into account when determining whether Scorpion exceeds the financial acquisitions threshold.*

Isolated transactions

70. Acquisitions to the extent they relate to the making of a financial supply are included as financial acquisitions and contribute towards the calculation of the financial acquisitions threshold even where the financial supply is made as part of an isolated transaction. Where an entity makes a financial supply on a one-off basis, for example in a capital raising exercise or a restructure, this transaction is part of carrying on the enterprise of the entity. Any acquisitions, to the extent they relate to the making of that financial supply, are included as financial acquisitions.

Calculating the financial acquisitions threshold

71. For the purposes of the financial acquisitions threshold test in sections 189-5 and 189-10, an entity needs to work out all the financial acquisitions it has made or is likely to make in:

- the current month and the previous eleven months; and
- the current month and the next eleven months.

What is the meaning of 'likely to make'?

72. The phrase 'likely to make', which appears in sections 189-5 and 189-10, is not defined in the GST Act and therefore takes on its ordinary meaning. Acquisitions an entity is likely to make are those which are probable. This requires a reasonable estimation of future acquisitions undertaken in good faith.

73. In *Australian Telecommunications Commission v. Krieg Enterprises Pty Ltd* (1976) 14 SASR 303, Bray CJ considered the meaning of 'likely' in the phrase 'likely to interfere with or damage property'. His Honour said at pages 312-313:

> Here we are concerned with the word 'likely' in a statute. As I have said, the ordinary and natural meaning of the word is synonymous with the ordinary and natural meaning of the word 'probable' and both words mean,… that there is an odds-on chance of the thing happening. That is the way in which statutes containing the words have usually been construed. …I think that 'likely' in the sub-section means 'probable' and I think that that means that there is a more than fifty per cent chance of the thing happening.

74. In *Mercantile Mutual (Workers Compensation) Ltd v. FC of T* [21], Foster J when considering an estimation process, noted the reference by Fullagar J in *Ballarat Brewing Co Ltd. v. FC of T*[22] to the comments of Lord Loreburn in *Sun Insurance Office v. Clarke* [23]:

> There is no rule of law as to the proper way of making an estimate. There is no way of estimating which is right or wrong in itself. It is a question of fact and figures whether the way of making the estimate in any case is the best way for that case.[24]

75. In *Australia and New Zealand Banking Group Ltd v. FC of T* (1994) 48 FCR 268; 94 ATC 4026; (1994) 27 ATR 559, the Full Federal Court in a similar context considered an argument from the Commissioner that the estimates in question there related to claims for which no reasonable estimate was possible or, if an estimate was possible, it was unreasonable. Hill J said (Northrop and Lockhardt JJ agreeing) at FCR 280; ATC 4035-4036; ATR 571:

> The concept of 'estimate' does not involve arbitrarily seizing upon any figure. What is involved is the formation of a judgment or opinion based upon reason. That judgment or opinion must necessarily be made bona fide but it need not be exact for the process of estimation involves a process of approximation.[25]

76. It is clear from these remarks that while a reasonable estimate need only be an approximation, it must be based on a sound and reasoned process of estimation that has been undertaken in good faith.

77. Whether or not an estimate will be regarded as reasonable will also depend on the circumstances of the entity at the time it makes its estimate of future financial acquisitions.

78. For the purpose of calculating financial acquisitions likely to be made, the estimate may be based on the entity's previous experience concerning similar acquisitions, transactions that the entity is negotiating, a business plan, accounting budget or some other reasonable basis.

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[21] (1998) 39 ATR 467; 98 ATC 4814.
[22] (1951) 82 CLR 364; (1951) 25 ALJR 220; (1951) 9 ATD 254.
[23] (1912) AC 443, at 454; [1911-13] All ER Rep 495, at 498; 6 TC 57, at 77.
[24] See paragraph 97 of Taxation Ruling TR 2002/11.
[25] See paragraph 98 of Taxation Ruling TR 2002/11.

The first limb test – exceeding $50,000

79. Under paragraphs 189-5(1)(a) and 189-10(1)(a), you exceed the financial acquisitions threshold if you make or are likely to make, financial acquisitions where the input tax credits related to making those acquisitions would exceed $50,000 or such other amount specified in the GST regulations, assuming the acquisitions were solely for a creditable purpose (the first limb test).

80. Under this test you include the input tax credits to which you would be entitled for:

- direct acquisitions that relate solely to the making of financial supplies (other than a financial supply consisting of a borrowing);
- direct acquisitions that relate partly to the making of financial supplies, but only to the extent that they relate to the making of the financial supplies (other than a financial supply consisting of a borrowing); and
- indirect acquisitions to the extent they are allocated to the making of financial supplies (other than a financial supply consisting of a borrowing).

81. Under the first limb test you ***do not*** include the input tax credits to which you would be entitled for:

- direct acquisitions that relate solely to the making of taxable supplies;
- direct acquisitions that relate solely to the making of GST-free supplies that are not also financial supplies;
- direct acquisitions that relate to the making of both taxable and GST-free supplies that do not relate in any way to the making of financial supplies;
- direct acquisitions that relate partly to the making of financial supplies and partly to other supplies to the extent they relate to making other supplies;
- direct acquisitions to the extent they relate to the making of financial supplies consisting of a borrowing;
- indirect acquisitions to the extent they are allocated to the making of supplies other than financial supplies;
- indirect acquisitions to the extent they are allocated to the making of financial supplies consisting of a borrowing.

82. In calculating the input tax credits to which you would be entitled for your financial acquisitions, you are required to assume the acquisitions are solely for a creditable purpose. If the acquisitions

were taxable supplies when made to you, you would be entitled to input tax credits equal to the GST payable on the supplies. No GST is included in respect of acquisitions that are GST-free, input taxed or out of scope. The assumption that these acquisitions are solely for a creditable purpose does not entitle you to an input tax credit to which you would not be otherwise entitled. Where there is no input tax credit entitlement (because there is no amount of GST payable on the supply of the thing acquired)[26], there is no amount to include in the calculation of input tax credits to which you would be entitled.

Example 10 – acquisition outside the GST system

83. *Vertigo Pty Ltd (Vertigo) as part of its enterprise maintains a share portfolio. It engages an ex-director to advise it on its trading activities. The scale of the ex-director's enterprise is too small to require him to be registered for GST and he chooses not to register. The consideration for the supply of the advice he provides to Vertigo for a year is $15,000. As the supplier is not registered, no GST is included in the price of the supply, and the supplier is not liable for GST.*

84. *When calculating whether it exceeds the financial acquisitions threshold, Vertigo must include all its financial acquisitions. Although the advice acquired relates to the making of financial supplies, Vertigo has no entitlement to an input tax credit in relation to the acquisition of the advice, as no amount of GST is included in the price of the acquisition received. The acquisition therefore is not included in calculating whether Vertigo exceeds the financial acquisitions threshold.*

The second limb test – exceeding 10%

85. Under paragraphs 189-5(1)(b) and 189-10(1)(b), you exceed the financial acquisitions threshold if the amount you calculated under the first limb test exceeds 10% of 'the total amount of input tax credits to which you would be entitled' assuming the financial acquisitions were solely for a creditable purpose (the second limb test).

Total amount of input tax credits

86. The total amount of the input tax credits to which you would be entitled includes input tax credits for all creditable acquisitions and creditable importations. Under Division 189, it specifically includes financial acquisitions. You do not include acquisitions to the extent

[26] Section 11-25.

that they relate to making input taxed supplies (other than financial supplies that are not a borrowing), or to the extent that they are acquisitions of a private or domestic nature.

87. Division 189 requires you to assume that financial acquisitions are solely for a creditable purpose when calculating whether the financial acquisitions threshold has been exceeded. The amount of input tax credits in relation to financial acquisitions that are required by paragraph 189-5(1) (b) and paragraph 189-10(1)(b) to be included in the total amount of input tax credits is the amount calculated under the first limb test.

88. An acquisition that is used for the making of a financial supply that is also GST-free is a financial acquisition for Division 189 purposes (see paragraphs 64 to 69 of this Ruling) and also a creditable acquisition under Division 11.[27] You include the amount of input tax credits to which you would be entitled for this acquisition in the total amount of input tax credits only once.

89. To the extent an acquisition relates to the making of a financial supply consisting of a borrowing it is not a financial acquisition, and is not included in the calculation of input tax credit entitlements for financial acquisitions under the first limb test. Input tax credits for borrowing related acquisitions may be included in the calculation of total input tax credits under the second limb test only where the acquisition has a creditable purpose under Division 11. These acquisitions are not assumed to be solely for a creditable purpose under Division 189.

90. Input tax credits for an acquisition or importation to the extent it relates to a borrowing can only arise if the borrowing itself relates to making supplies that are not input taxed. This is because an acquisition or importation may be for a creditable purpose where that acquisition or importation relates to making a financial supply consisting of a borrowing and the borrowing relates to supplies that are not input taxed.[28]

91. An entity that borrows money and uses it for making taxable or GST-free supplies is entitled to input tax credits for its borrowing related acquisitions. The credits relating to these acquisitions are included in the calculation of total credits to which the entity would be entitled under the second limb test.

92. Acquisitions or importations to the extent they relate to a borrowing that itself relates to making input taxed supplies, are not for a creditable purpose and the entity is not entitled to input tax credits. There are no input tax credit entitlements for these acquisitions or importations to include in the total amount.

[27] It is a creditable acquisition because it relates to making a GST-free supply.
[28] Subsections 11-15(5) and 15-10(5).

93. For the purposes of Division 189, the input tax credit entitlement for an acquisition to the extent it relates to the making of a financial supply consisting of a borrowing:

- is not included under the first limb test because the acquisition is not a financial acquisition;
- is included in the total amount of the input tax credits under the second limb test if the borrowing itself does not relate to making input taxed supplies;
- is not included under the second limb test if the borrowing itself relates to making input taxed supplies.

Example 11 – total amount of input tax credits

94. *H.O.N.Z.A Co made the following acquisitions during the current year:*

> *(a) financial acquisitions - GST incurred was $15,000;*
>
> *(b) acquisitions in relation to a borrowing used for making taxable supplies – GST $6,000;*
>
> *(c) acquisitions in relation to a borrowing used for making other input taxed supplies - GST $5,000;*
>
> *(d) other acquisitions relating to making other input taxed supplies - GST $50,000;*
>
> *(e) acquisitions in relation to overhead costs used for making other input taxed supplies - GST $5,000;*
>
> *(f) acquisitions relating to making taxable supplies - GST $100,000; and*
>
> (g) *acquisitions in relation to overhead costs used for making taxable supplies - GST $10,000.*

95. *Assuming all the financial acquisitions were solely for a creditable purpose, the total amount of input tax credits to which H.O.N.Z.A would be entitled is $131,000 ($15,000(a) + $6,000(b) + $100,000(f) + $10,000(g)).*

GST groups

96. For members of GST groups (other than GST religious groups), the financial acquisitions threshold is a combined threshold. That is, the threshold for the whole group is the same as if it were a single entity. If the group makes financial acquisitions exceeding the threshold, each group member exceeds the threshold. If one member of the group contributes a substantial proportion of those acquisitions,

it is possible that its contribution alone may cause the group to exceed the threshold.

Current acquisitions threshold

97. A member of a GST group exceeds the financial acquisitions threshold at a time during a particular month if, assuming that all the financial acquisitions the members of the group have made, or are likely to make, during the 12 months ending at the end of that month were made solely for a creditable purpose, either or both of the following would apply:

- the amount of all the input tax credits to which the members of the group would be entitled for those acquisitions would exceed $50,000 or such other amount specified in the regulations (first limb test);
- the amount of all the input tax credits to which the members of the group would be entitled for their financial acquisitions would be more than 10% of the total amount of the input tax credits to which the members of the group would be entitled for all acquisitions and importations of any member of the group during that 12 months (including the financial acquisitions)[29] (second limb test).

98. If either or both of these tests are met, then the member of the GST group exceeds the financial acquisitions threshold.

99. The legislation, in explaining the financial acquisitions threshold for group members, refers to the 'input tax credits to which you or any other member of the group would be entitled'. We interpret this to mean 'you' if you are the representative member of the group, or if you are not, any other member of the group that is the representative member. This is because only the representative member of the group has any entitlement to input tax credits in respect of acquisitions made by any member of the group.[30]

Example 12 – current acquisitions threshold

100. *Entities A, B and C are members of a GST group. In July 2001, total acquisitions (including financial acquisitions) for the 12 months from 1 August 2000 to 31 July 2001 are $110,000 for Entity A, $55,000 for Entity B and $88,000 for Entity C. (Of these amounts,*

[29] See subsection 189-5(2).
[30] Subsection 48-45(1).

Entity A's financial acquisitions are $4,400, Entity B's are $1,100 and Entity C's $7,700.)

101. *Assuming all the financial acquisitions were solely for a creditable purpose, the input tax credits for financial acquisitions for the ABC group would be $1,200 (1/11th of ($4,400 + $1,100 + $7,700)). This $1,200 does not exceed the $50,000 threshold under the first limb test.*

102. *The total amount of input tax credits for all the acquisitions of the ABC group would be $23,000 (1/11th of ($110,000 + $55,000 + $88,000)). The amount of $1,200 does not exceed 10% of $23,000 ($2,300) under the second limb test. ABC group therefore does not exceed the current acquisitions threshold.*

Future acquisitions threshold

103. A member of a GST group may also exceed the financial acquisitions threshold at a time during a particular month if, assuming that all the financial acquisitions that the members of the group have made, or are likely to make, during that month and the next 11 months were made solely for a creditable purpose, either or both of the following would apply:

- the amount of all the input tax credits to which the members of the group would be entitled for those acquisitions would exceed $50,000 or such other amount specified in the regulations (first limb test);
- the amount of all the input tax credits to which the members of the group would be entitled for their financial acquisitions would be more than 10% of the total amount of the input tax credits to which the members of the group would be entitled for all acquisitions and importations of any member of the group during those months (including the financial acquisitions)[31] (second limb test).

Example 13 – future acquisitions threshold

104. *Following on from example 12, although the ABC group does not exceed the current acquisitions threshold, it must also determine whether it exceeds the future acquisitions threshold. Total acquisitions (including financial acquisitions) for the period from 1 July 2001 to 30 June 2002 are likely to be $220,000 for Entity A, $44,000 for Entity B and $99,000 for Entity C. Of this, Entity A's*

[31] See subsection 189-10(2).

financial acquisitions are likely to be $11,000, Entity B's are likely to be $4,400 and Entity C's are likely to be $22,000.

105. *Assuming all the financial acquisitions were solely for a creditable purpose, the input tax credits for financial acquisitions for the ABC group would be $3,400 (1/11th of ($11,000 + $4,400 + $22,000)). This $3,400 does not exceed the $50,000 threshold under the first limb test.*

106. *Input tax credits for the total acquisitions of the ABC group would be $33,000 (1/11th of ($220,000 + $44,000 + $99,000)). The amount of $3,400 does exceed 10% of $33,000 ($3,300) under the second limb test. ABC group is therefore not entitled to input tax credits for its financial acquisitions, however it may be entitled to reduced input tax credits.*

107. *If the ABC group had exceeded the current acquisitions threshold, it would not be necessary for it to determine whether it exceeds the future financial acquisitions threshold.*

Input tax credits relating to financial acquisitions

108. In determining whether a member of a GST group has exceeded the financial acquisitions threshold under paragraphs (a) and (b) of subsection 189-5(2) or 189-10(2), all of the group's input tax credits relating to financial acquisitions are included. Financial acquisitions are those acquisitions 'that relate to the making of a financial supply (other than a financial supply consisting of a borrowing)'.[32]

109. Under subsections 189-5(2) and 189-10(2) these financial acquisitions are assumed to be solely for a creditable purpose when calculating whether the financial acquisitions threshold is exceeded.

110. An acquisition by a member of a GST group from a non-group entity is a financial acquisition for Division 189 purposes, if the purpose of the group as a whole is to use the acquisition for the making of a financial supply to an entity outside the GST group. When determining whether such an acquisition by a group member is a financial acquisition, the GST group is treated as a single entity and not as a number of separate entities.[33]

111. The effect of the interaction between the grouping provisions in Divisions 48 and 189 is that an acquisition made by one group member from a non-group entity can 'relate to' a financial supply by another group member to a different non-group entity for Division 189 purposes. Although the nexus between the acquisition and the ultimate supply is less direct in the context of a group than in a

[32] Section 189-15.
[33] See subsections 48-45(2) and 11-15(4).

non-group situation, the interaction between Divisions 48 and 189 operates to establish a sufficient nexus.

Total amount of input tax credits

112. In deciding whether it has exceeded the financial acquisitions threshold under paragraph (b) of subsections 189-5(2) and 189-10(2), a GST group has to determine its entitlement to input tax credits for its total acquisitions. This entitlement includes the input tax credits to which it would be entitled for its financial acquisitions, assuming they were solely for a creditable purpose, and the input tax credits to which it is entitled for all other acquisitions and importations it makes for a creditable purpose.

113. In deciding whether acquisitions other than financial acquisitions were made for a creditable purpose, the purpose of the group as a whole is considered. This is the effect of section 48-45 which provides that a GST group is treated as a single entity for the purposes of deciding whether acquisitions by a member are for a creditable purpose.

114. Section 48-55 has the effect that, when calculating entitlement to input tax credits, a GST group is treated as a single entity and not as a number of entities. Acquisitions made wholly within the group are ignored, and it is the purpose of the group as a whole which determines whether or not an acquisition is made for a creditable purpose.

115. For the second limb test, acquisitions between members of the GST group are not included with acquisitions from external entities that are for a creditable purpose. This is because subsection 48-45(3) provides that such acquisitions are not treated as creditable acquisitions and there is no entitlement to input tax credits in relation to these acquisitions.

Example 14 – GST group is treated as a single entity

116. *Entities A, B and C are related companies but they are not grouped for GST purposes. On 31 July 2002, none of the entities exceed the $50,000 threshold under the first limb test for their financial acquisitions for the current month and the next 11 months. They therefore each need to determine whether they exceed the 10% threshold under the second limb test for this period. Assuming all the financial acquisitions were solely for a creditable purpose, the input tax credits for their financial acquisitions and total acquisitions would be as set out in the table below:*

	Input tax credits		*%*	*Financial Acquisitions Threshold*
	Financial Acquisitions	***Total Acquisitions***		
A	*$400*	*$3,000*	*13*	*Exceeded*
B	*$100*	*$5,000*	*2*	*Not exceeded*
C	*$700*	*$8,000*	*8.75*	*Not exceeded*

117. *In August 2002, Entities A, B and C decide to group for GST purposes. The entities estimate that their financial acquisitions and creditable acquisitions for August 2002 and the next 11 months are likely to be the same as for the previous 12 months.*

118. *Because each of the entities is a member of the GST group, they no longer make separate calculations in determining whether the financial acquisitions threshold is exceeded. The group is treated as a single entity.*

119. *The potential input tax credits for A, B and C's financial acquisitions and total acquisitions remain the same as in the previous year:*

	Input tax credits		*%*	*Financial Acquisitions Threshold*
	Financial Acquisitions	***Total Acquisitions***		
ABC	*$1,200*	*$16,000*	*7.5*	*Not exceeded*

120. *Assuming all the financial acquisitions of the ABC Group were solely for a creditable purpose, the input tax credits for financial acquisitions would be $1,200 ($400 + $100 + $700). This $1,200 does not exceed the $50,000 threshold under the first limb test.*

121. Input tax credits for the total acquisitions of the ABC Group are $16,000. The amount of $1,200 does not exceed 10% of $16,000 ($1,600) under the second limb test. ABC Group therefore does not exceed the future acquisitions threshold even though Entity A as an individual entity would have exceeded the threshold had it not been a member of a GST group.

Acquisitions relating to making supplies to another group member

122. Within a GST group, members may make supplies to other members. Financial acquisitions of a member do not include acquisitions used to make supplies that would be financial supplies to

another member of the group. Acquisitions between members of the GST group are not included in the calculation of the financial acquisitions threshold (see paragraph 82 of this Ruling).

123. Where a group member makes an acquisition from a non-member to make a supply to another member of the group, and the other member uses that supply to make a financial supply (other than a borrowing) to a non-group entity, the acquisition by the first member is a financial acquisition by the GST group.

124. In deciding whether something acquired by a group member from a non-group entity is a financial acquisition for Division 189 purposes, the group is treated as if it were a single entity and not a number of entities corresponding to the members of a GST group. If the purpose of the GST group as a whole is to use the acquisition for making a taxable supply to a non-group entity, the acquisition is not a financial acquisition for Division 189 purposes. If the acquisition is used by the GST group for the making of a financial supply to the non-group entity, the acquisition is a financial acquisition for Division 189 purposes.

Example 15 – a financial acquisition

125. *Entities A, B and C are members of a GST group. Entity A acquires a computer from YTK (an entity outside the group). Entity A leases the computer to Entity B who uses the computer to provide credit to customers that are not group members. The acquisition of the computer does not relate to the supply of the lease to Entity B. It relates to the financial supplies made by Entity B to the external entities. It is a financial acquisition for Division 189 purposes.*

126. *The acquisition by Entity A is not a creditable acquisition for the GST group, because the purpose of the group as a whole is to use the computer for making input taxed supplies. The acquisition will be included as a financial acquisition for the purposes of determining whether the group exceeds the financial acquisitions threshold under both the first and the second limb tests.*

Acquisitions relating to borrowings between group members

127. In deciding whether an acquisition from a non-group entity that relates to a borrowing between group members is a financial acquisition for Division 189 purposes, you look at the purpose of the GST group as a whole.

128. Where a member of a GST group borrows money from a non-group entity, it is acquiring an interest in or under a credit arrangement which is an acquisition-supply, and provided the other requirements of subregulation 40-5.09(1) are satisfied, it is a financial

supply. Any acquisitions made in relation to this acquisition-supply are not financial acquisitions because they relate to a financial supply consisting of a borrowing.

129. However, if a group member makes an acquisition from a non-group entity in relation to a borrowing from another member of the group, that acquisition is not an acquisition that relates to a borrowing. It is necessary to look at the purpose of the group as a whole in making the acquisition. Therefore, the acquisition is a financial acquisition for Division 189 purposes if the group as a whole uses the borrowing to make a financial supply to a non-group entity.

Effect of joining or leaving a GST group

130. When a new member joins a GST group, the acquisitions of the new member prior to joining the group are not taken into account for the purposes of calculating whether the group exceeds the financial acquisitions threshold.

131. For the purposes of subsection 189-5(2), only those acquisitions made, or likely to be made, by an entity after it becomes a member of the group are taken into account in determining whether the GST group exceeds the current or future financial acquisitions thresholds. When a new member joins a GST group, it is only the history of its acquisitions as a member of the group that is relevant for Division 189 purposes.

Example 16 – acquisitions made by new member prior to joining the group are not taken into account

132. *Entities A, B and C are members of a GST group. Newboy Ltd joins Group ABC on 1 August 2001. In determining whether the group exceeds the current financial acquisitions threshold, Newboy Ltd's acquisitions for the 11 months prior to joining the group (i.e., September 2000 to July 2001) are not taken into consideration. Only its acquisitions after 1 August 2001 are taken into account.*

133. When an entity which is a member of a GST group leaves the GST group, the acquisitions it is likely to make after it leaves the group are not taken into account for the purposes of determining whether the group exceeds the financial acquisitions threshold for future acquisitions. However, the acquisitions the departing member makes as a member of the group are included in the calculation of the group's current financial acquisitions threshold.

134. For the purposes of subsection 189-10(2), only those acquisitions made, or likely to be made, by the entity while it is a member of the group are taken into account in determining whether the GST group exceeds the future financial acquisitions threshold. It

is only the entity's acquisitions as a member of the group that are relevant for Division 189 purposes.

Example 17 – member leaves GST group

135. *Daffy Limited (Daffy) is the subject of a sale by its parent company. Daffy is part of a GST group which consists of its parent and other subsidiaries. Daffy is the group member that acquires office equipment for the group. The group does not make financial supplies. The sale of Daffy will be finalised six months after the contract date, and after that time Daffy will be part of a GST group that makes only financial supplies. It will acquire office equipment for the new group and the input tax credits relating to the new group's acquisitions will exceed $50,000. For the 6 months between the contract date and the time Daffy leaves the first group, the group will not exceed the financial acquisitions threshold as the acquisitions that Daffy is likely to make after it leaves the group are not included in its calculation of the threshold.*

GST religious groups

136. Subsections 189-5(1) and 189-10(1) are the provisions relevant to GST religious groups.

137. GST religious groups do not meet the requirements of a GST group under section 48-10, and are therefore not GST groups under that provision. Consequently, subsections 189-5(2) and 189-10(2) do not apply to GST religious groups.

138. GST religious groups are not the same as GST groups. They do not have representative members that are liable for any GST payable and entitled to the input tax credits of the group as a whole.

139. Instead, each individual member of a GST religious group is entitled to the input tax credits that arise in relation to its own acquisitions from entities outside the group. Therefore, each individual member needs to work out whether it exceeds the financial acquisitions threshold.

140. In determining whether a member's acquisitions and importations are for a creditable purpose, the GST religious group is treated as a single entity.[34] The effect of this is that each member looks at the purpose of the group as a whole in making the acquisition to determine the extent to which that member's acquisitions and importations are for a creditable purpose.

[34] Section 49-50.

Input tax credits relating to financial acquisitions

141. To determine whether it has exceeded the financial acquisitions threshold under paragraphs (a) and (b) of subsections 189-5(1) and 189-10(1), each member of the GST religious group includes all of the input tax credits to which it would be entitled for its financial acquisitions. Financial acquisitions for GST religious group members are those acquisitions that relate to the making of financial supplies (other than a financial supply consisting of a borrowing) looking at the purpose of the GST religious group as a whole in making the acquisition.

142. Under subsections 189-5(1) and 189-10(1) these financial acquisitions are assumed to be solely for a creditable purpose when calculating whether the financial acquisitions threshold is exceeded.

Total amount of input tax credits

143. In deciding whether it exceeds the financial acquisitions threshold under paragraph (b) of subsections 189-5(1) and 189-10(1), a member of a GST religious group has to determine its own entitlement to input tax credits for its total acquisitions. This means the total of the input tax credits to which it would be entitled for its financial acquisitions (assuming they were solely for a creditable purpose) and other creditable acquisitions.

144. In deciding whether the acquisitions that are not financial acquisitions were for a creditable purpose, the member looks at the purpose of the group as a whole. This is the effect of section 49-50 under which a GST religious group is treated as a single entity for the purposes of working out whether acquisitions by a member are for a creditable purpose and the amount of any input tax credits to which the member is entitled.

145. Acquisitions from other members of the GST religious group are not included with other acquisitions that were made for a creditable purpose. This is because section 49-35 provides that such acquisitions are not creditable acquisitions and do not give rise to an entitlement to input tax credits.

Example 18 - acquisitions not for a creditable purpose

146. *Religious group XYZ has three members: X, Y and Z. For the period 1 October 2001 to 30 September 2002, Entity X makes financial acquisitions of $275,000 from entities outside the group. The purpose of the XYZ group as a whole is for these acquisitions to be used in making financial supplies. Entity X's total acquisitions for the period, including the $275,000 financial acquisitions, are $3,300,000.*

147. *Section 49-50 requires that for the purposes of working out whether Entity X's acquisitions other than its financial acquisitions, are for a creditable purpose, religious group XYZ is to be treated as a single entity. Of Entity X's total acquisitions, $440,000 represents acquisitions used to make supplies to Entity Y. Entity Y used these acquisitions for making input taxed supplies other than financial supplies. These acquisitions are not creditable acquisitions and will be excluded when calculating the amount of input tax credits to which Entity X would be entitled for its total acquisitions. All other acquisitions for Entity X relate to making taxable supplies to non-group members.*

148. *Assuming the financial acquisitions were made solely for a creditable purpose, Entity X's input tax credits for financial acquisitions would be $25,000 (1/11th of $275,000). Therefore Entity X does not exceed the $50,000 threshold under the first limb test. Its input tax credits for total acquisitions would be $260,000 (1/11th of ($3,300,000 - $440,000 = $2,860,000)). The $25,000 does not exceed 10% of $260,000 ($26,000) under the second limb test. Entity X therefore does not exceed the current financial acquisitions threshold. Entity X also needs to calculate whether it exceeds the future acquisitions threshold for acquisitions likely to be made for the period 1 September 2002 to 31 August 2003.*

Example 19 - acquisitions for a creditable purpose

149. *Religious group LMN has three members: L, M and N. For the period 1 October 2001 to 30 September 2002, Entity L makes acquisitions of $275,000 for use in the making of financial supplies to non- group entities. Its total acquisitions (including the $275,000 financial acquisitions) amount to $3,300,000 for the 12 month period.*

150. *All of Entity L's acquisitions (apart from the financial acquisitions) are used for making supplies to Entity M which then uses the acquisitions for making taxable supplies to an external entity. Section 49-50 requires that for the purposes of working out whether Entity L's acquisitions are for a creditable purpose, religious group LMN is to be treated as a single entity.*

151. *Because the group (when treated as a single entity) has a creditable purpose in relation to these acquisitions for making taxable supplies, these acquisitions (except the financial acquisitions) are made for a creditable purpose and must be included in the calculation of total input tax credits when working out whether the financial acquisitions threshold has been exceeded under the second limb test.*

152. *Assuming the financial acquisitions were made solely for a creditable purpose, Entity L's input tax credits for financial acquisitions would be $25,000 (1/11th of $275,000). Therefore Entity*

L does not exceed the $50,000 threshold under the first limb test. Its input tax credits for total acquisitions would be $300,000 (1/11th of $3,300,000). The $25,000 does not exceed 10% of $300,000 ($30,000) under the second limb test. Entity L therefore does not exceed the current financial acquisitions threshold. However, Entity L also needs to calculate whether it exceeds the future acquisitions threshold for acquisitions likely to be made for the period 1 September 2002 to 31 August 2003.

How does Division 72 interact with the financial acquisitions threshold?

153. Under the special rules in Division 72 supplies and acquisitions between associates for no consideration or for inadequate consideration, are brought into the GST system where the associated recipient does not make the acquisition solely for a creditable purpose.

154. The assumption in Division 189 that a financial acquisition is solely for a creditable purpose is only for the purpose of determining whether the financial acquisitions threshold is exceeded. It cannot be applied for the purpose of determining whether or not the special rules in Division 72 apply.

How does Division 84 interact with the financial acquisitions threshold?

155. Where an entity acquires a service or other thing that is a taxable supply by virtue of Division 84 from offshore, the acquisition is a financial acquisition for Division 189 purposes if it is used to make financial supplies.[35]

156. Where an entity acquires a service or other thing that is a financial supply under subregulation 40-5.09(2) from offshore, any acquisitions made in relation to this financial supply are financial acquisitions for the purposes of Division 189.

157. If a supply is not connected with Australia, it will not be a taxable supply under section 9-5 of the GST Act. However, the supply of a thing (other than goods or real property) that is not connected with Australia will be a taxable supply under Division 84 if:

- the recipient is registered or required to be registered;
- the supply is for consideration;

[35] Section 189-15.

- the recipient acquires the thing supplied solely or partly for the purposes of an enterprise that it carries on in Australia; and
- the recipient does not acquire the thing solely for a creditable purpose, for example it uses it to make input taxed financial services.

However, the supply is not a taxable supply to the extent that it is GST-free or input taxed.[36]

158. Where Division 84 applies, services or other things (excluding goods and real property) acquired from offshore for use in making financial supplies are subject to a 'reverse charge' except to the extent the supply is GST-free or input taxed. A reverse charge is where GST on the supply is payable by the recipient (not the supplier) of those services.[37] This means that where an entity acquires a supply other than goods or real property from offshore and it is a taxable supply under section 84-5, the entity is required to remit GST equal to 10% of the price of the supply.[38]

159. Where an entity acquires a supply of anything other than goods or real property from offshore for use in making a financial supply, the supply of the thing will be a taxable supply under Division 84 provided it meets the other conditions for the provision to apply. This acquisition is a financial acquisition for the purposes of Division 189 and will therefore be taken into account in determining whether the entity exceeds the financial acquisitions threshold.

160. Subregulation 40-5.09(2) provides that if Division 84 applies to the provision, acquisition or disposal of an interest mentioned in subregulation 40-5.09(3), the provision, acquisition or disposal is a financial supply to the extent that it would be a financial supply, apart from the requirements that the supply be connected with Australia and the supplier be registered or required to be registered.

161. An entity may acquire from offshore a financial interest that is a financial supply by virtue of subregulation 40-5.09(2). Any acquisition, to the extent it relates to the making of this financial supply, is a financial acquisition and will be taken into account in determining whether the entity exceeds the financial acquisitions threshold.

[36] Section 84-5.
[37] Section 84-10.
[38] Section 84-12.

Example 20 – acquisition to which Division 84 applies is a financial acquisition

162. *Scorpion Pty Ltd, an entity that carries on an enterprise in Australia and is registered for GST, acquires services from an overseas broker in relation to the sale of shares. It pays brokerage fees of $1000.*

163. *The acquisition of the overseas brokerage services by Scorpion is not solely for a creditable purpose because it relates to making an input taxed supply and therefore Division 84 applies. Scorpion will be liable for GST of $100 (10% of $1000) on the brokerage services. The acquisition of the brokerage services is a financial acquisition. Assuming that the financial acquisition was solely for a creditable purpose, Scorpion would be entitled to an input tax credit of $100 which it includes in calculating whether it exceeds the financial acquisitions threshold.*

How often does an entity test whether it exceeds the financial acquisitions threshold?

164. Division 189 sets out the way to calculate whether an entity exceeds the financial acquisitions threshold at a time during a particular month. An entity's acquisitions and importations relating to financial supplies can be for a creditable purpose if the entity does not exceed the threshold at the time the acquisition or importation is made.

165. To correctly complete its Business Activity Statement (BAS), an entity that has acquisitions or importations relating to a financial supply needs to know whether it has exceeded the threshold at any time during the BAS period. This indicates a need to test whether it exceeds the financial acquisitions threshold at least each time the BAS is completed.

166. In particular, an entity should be aware of circumstances that are likely to affect whether it will exceed the threshold. For example when:

- an entity joins a GST group;
- there is a change in the actual or intended use of an acquisition so that it becomes a financial acquisition or ceases to be a financial acquisition;
- an entity makes or is reasonably likely to make financial acquisitions relating to a significant isolated transaction; or
- an entity has an increase in its regular financial acquisitions.

167. In addition, an entity may need to know whether it is sufficiently close to the threshold so that it will have time to put in place any necessary systems to enable any apportionment which would be required in calculating its input tax credit entitlements if the threshold is exceeded.

168. An entity that has exceeded the financial acquisitions threshold and whose financial acquisitions are decreasing, may need to monitor its financial acquisitions to determine when it no longer exceeds the threshold.

Example 21 – financial acquisitions threshold exceeded

169. *Humphrey Pty Ltd (Humphrey) lodges its BAS on a quarterly basis and conducts its financial acquisitions threshold test every quarter. It does not make many financial supplies in the course of its enterprise and generally does not exceed the financial acquisitions threshold. However, it makes a substantial acquisition of $539,000 in the month of May 2002 when it acquires professional advice in relation to the sale of debentures. The input tax credit to which it would be entitled for its financial acquisition is $49,000 (1/11th of $539,000). Humphrey should therefore conduct the test in May 2002 to determine whether its acquisition causes it to exceed the financial acquisitions threshold and it should continue closely monitor its acquisitions for the next 11 months until April 2003.*

What is the effect of exceeding the financial acquisitions threshold?

170. Where an entity exceeds the financial acquisitions threshold, its acquisitions and importations are not for a creditable purpose to the extent that they relate to making financial supplies. Therefore, there is no entitlement to input tax credits under Divisions 11 and 15 for those acquisitions and importations.

171. However specific acquisitions that relate to the making of financial supplies can give rise to an entitlement to a reduced input tax credit of 75% of any GST paid. These specific acquisitions are called 'reduced credit acquisitions'. Even if the financial acquisitions threshold is exceeded, a reduced input tax credit is still available to the extent that the acquisition is a reduced credit acquisition. The GST regulations contain the complete list of reduced credit acquisitions.[39]

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[39] See Regulations 70-5.02, 70-5.02A and 70-5.02B.

Detailed contents list

172. Below is a detailed content list for this draft Good and Services Tax Ruling:

Your comments

173. If you wish to comment on this draft Ruling, please send your comments promptly by **11 December 2002** to:

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Commissioner of Taxation
30 October 2002

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Related Rulings/Determinations:
GSTR 2000/2; GSTR 2000/22; GSTR 2000/24; GSTR 2000/35; GSTR 2002/2; TR 2002/11

Subject references:
- acquisition
- borrowing
- extent
- financial acquisition
- financial acquisitions threshold
- financial supplies
- GST-free supplies
- GST group
- GST religious group
- input tax credits
- likely to make
- nexus
- reduced credit acquisition
- relates to
- timing

Legislative references:
- ANTS(GST)A99 9-5
- ANTS(GST)A99 9-30(3)
- ANTS(GST)A99 Div 11
- ANTS(GST)A99 11-10
- ANTS(GST)A99 11-15
- ANTS(GST)A99 11-15(2)(a)
- ANTS(GST)A99 11-15(4)
- ANTS(GST)A99 11-15(5)
- ANTS(GST)A99 11-25
- ANTS(GST)A99 Div 15
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- ANTS(GST)A99 48-10
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- ANTS(GST)A99 Div 156
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- ANTS(GST)A99 189-1
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- ANTS(GST)A99 189-5(1)
- ANTS(GST)A99 189-5(1)(a)
- ANTS(GST)A99 189-5(1)(b)
- ANTS(GST)A99 189-5(2)
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Regulations:
- ANTS(GST)R99 40-5.09
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- ANTS(GST)R99 40-5.09(2)
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- ANTS(GST)R99 40-5.09(4)
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- ANTS(GST)R99 70
- ANTS(GST)R99 70-5.02
- ANTS(GST)R99 70-5.02A
- ANTS(GST)R99 70-5.02B

Case references:
- Australia and New Zealand Banking Group Ltd. v. FC of T (1994) 48 FCR 268; 94 ATC 4026; (1994) 27 ATR 559
- Australian Telecommunications Commission v. Krieg Enterprises Pty Ltd (1976) 14 SASR 303
- Ballarat Brewing Co Ltd. v. FC of T (1951) 82 CLR 364; (1951) 25 ALJR 220; (1951) 9 ATD 254
- Hatfield v. Health Insurance Commission (1987) 15 FCR 487
- Mercantile Mutual (Workers Compensation) Ltd v. FC of T (1998) 39 ATR 467; 98 ATC 4814
- Sun Insurance Office v. Clarke (1912) AC 443; [1911-13] All ER Rep 495

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