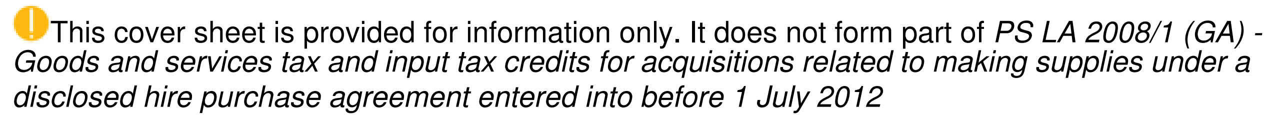
PS LA 2008/1 (GA) - Goods and services tax and input tax credits for acquisitions related to making supplies under a disclosed hire purchase agreement entered into before 1 July 2012



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Australian Government

Australian Taxation Office

Practice Statement Law Administration (General Administration)

PS LA 2008/1 (GA)

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SUBJECT: **Goods and services tax and input tax credits for acquisitions related to making supplies under a disclosed hire purchase agreement entered into before 1 July 2012**

PURPOSE: **To outline the Commissioner's approach to calculating the input tax credit entitlement for acquisitions that relate to the making of supplies under disclosed hire purchase agreements**

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BACKGROUND

1. This Practice Statement explains a method for the calculation of input tax credits (ITCs) for acquisitions related to supplies made under a disclosed hire purchase agreement that will be accepted by the Commissioner as complying with the relevant provisions of the *A New Tax System (Goods and Services Tax) Act 1999* (GST Act).

2. All legislative references in this Practice Statement are to the GST Act, unless otherwise indicated.

3. A hire purchase agreement is a ‘disclosed’ hire purchase agreement if the credit for the goods supplied under the arrangement is provided as a separate charge that is disclosed to the recipient of the goods.

4. This Practice Statement applies only to those acquisitions that relate both to the supply of the goods and to the supply of the credit made under hire purchase agreements entered into before 1 July 2012. These acquisitions are partly creditable acquisitions necessitating a fair and reasonable apportionment of acquisitions between creditable and non-creditable parts.

5. This Practice Statement does not apply to the acquisition of goods (for example, motor vehicles) for supply under a disclosed hire purchase agreement.

STATEMENT

6. Applying the law to determine the extent of creditable purpose in relation to disclosed hire purchase agreements is inherently uncertain and can give rise to practical difficulties and disproportionately high compliance costs for taxpayers. It is also unlikely to be cost-effective in most cases for the ATO to

undertake compliance action in this area in an attempt to find a precise extent of creditable purpose.

7. Given that level of uncertainty, it is appropriate for the Commissioner to accept as complying with the law an approach to determining the extent of creditable purpose for a partly creditable acquisition that is in line with those set out in this Practice Statement.

8. This Practice Statement outlines a range of scenarios in which the extent of creditable purpose for a partly creditable acquisition is required to be determined. These scenarios include circumstances where:

- there is no entitlement to reduced input tax credits (RITCs)
- there is entitlement to RITCs
- there is no entitlement to RITCs and the acquisition is allocated to a dedicated asset finance cost centre – no floor plan finance[1] activities, and
- there is no entitlement to RITCs and the acquisition is allocated to a dedicated asset finance cost centre – floor plan finance activities.

Our approach to arrangements pre-1 April 2008

9. For a tax period up to and including a tax period ending 31 March 2008[2], the Commissioner will accept an approach that applies a revenue-based formula (incorporating consistent values for both financial supplies and non-financial supplies) to determine the extent of creditable purpose for partly creditable acquisitions.

10. However, the Commissioner may commence an audit on a business activity statement (BAS) period up to and including 31 March 2008[3] where the taxpayer has applied a revenue-based formula that includes:

- the value of 'floor plan payouts' as non-financial supply revenue in both the numerator and denominator of the formula, or
- gross revenues for non-financial supplies in both the numerator and the denominator, and net revenues for financial supplies in the denominator of the formula.

Our approach to arrangements from 1 April 2008

11. For a tax period ending on or after 1 April 2008, the Commissioner will accept as being fair and reasonable an apportionment method (including a set-rate method) that achieves an extent of creditable purpose for partly creditable acquisitions of less than or equal to 15%.

12. The Commissioner considers that an extent of creditable purpose of 15% is likely to be at the top end of the range of the proportions that could be expected in disclosed hire purchase agreements and therefore, in most cases, is likely to be a fair reflection of the apportionment required by the law.

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[1] Schedule 1 to Goods and Services Tax Ruling GSTR 2002/2 *Goods and services tax: GST treatment of financial supplies and related supplies and acquisitions* defines 'floor plan finance' as an agreement under which a financier purchases capital goods from a manufacturer or distributor for the purposes of display and sale by a wholesaler or retailer. The financier retains legal title to the goods, while possession and limited rights over the goods (and the obligation to return goods if unsold) are granted to the dealer. Floor plan finance is a form of bailment.

[2] Subject to the application of section 105-50 of Schedule 1 to the *Taxation Administration Act 1953*.

[3] Subject to the application of section 105-50 of Schedule 1 to the *Taxation Administration Act 1953*.

13. However, there is no requirement for a taxpayer to adopt an extent of creditable purpose of 15% where a proportion in excess of 15% is fair and reasonable on a proper application of the law to the taxpayer's particular circumstances. Taxpayers may wish, and are encouraged, to seek a goods and services tax (GST) private ruling before applying a higher percentage.

Our approach to arrangements from 1 July 2012

14. Amendments to the *A New Tax System (Goods and Services Tax) Regulations 1999* (GST Regulations 1999)[4] to change the GST treatment of supplies made under hire purchase agreements are effective for agreements entered into on or after 1 July 2012.[5]

15. Under a hire purchase agreement entered into before 1 July 2012, credit provided for a separate charge and disclosed to the recipient of the goods, is an input-taxed financial supply.[6] However, no supplies made under a hire purchase agreement entered into on or after 1 July 2012 are financial supplies, regardless of whether the credit provided under the agreement is charged separately and disclosed to the recipient of the goods.[7]

16. A credit charge that is separately identified and disclosed under a hire purchase agreement entered into on or after 1 July 2012 is consideration for a supply separate from the underlying supply of goods and is a taxable supply if the underlying supply is taxable. If the credit charge is not separately disclosed, the total consideration under the agreement relates to the supply of the goods. This is more fully explained in paragraphs 190 to 217 of Goods and Services Tax Ruling GSTR 2000/29 *Goods and services tax: attributing GST payable, input tax credits and adjustments and particular attribution rules made under section 29-25.*

17. It follows that acquisitions that relate both to the supply of goods and the supply of credit made under hire purchase agreements entered into on or after 1 July 2012 will no longer be made partly for a creditable purpose.

EXPLANATION

18. For the purposes of the GST Act, 2 separate and distinct supplies are made under a disclosed hire purchase agreement entered into before 1 July 2012. These are the taxable (or GST-free) supply of the goods and the input-taxed (financial) supply of an interest in or under a credit arrangement.

19. A taxpayer is entitled to an ITC for any creditable acquisitions that it makes. Under section 11-15, a thing is acquired for a creditable purpose to the extent that it is acquired in carrying on the taxpayer's enterprise. However, a thing is not acquired for a creditable purpose to the extent that the acquisition relates to making supplies that would be input taxed.

20. Under subsection 11-30(1), an acquisition is partly creditable where, among other things, the acquisition is made partly for a creditable purpose.

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[4] In 2019, the GST Regulations 1999 were replaced by the *A New Tax System (Goods and Services Tax) Regulations 2019* (GST Regulations). The remade GST Regulations did not alter the GST treatment of hire purchase agreements.

[5] Amendments made to the GST Regulations 1999 by the *A New Tax System (Goods and Services Tax) Amendment Regulation 2012 (No. 1).*

[6] Where the requirements of subsection 40-5.09(1) of the GST Regulations are satisfied.

[7] Table items 19 and 20 of section 40-5.12 of the GST Regulations.

21. Therefore, an acquisition which relates to both the taxable (or GST-free) activity and the input taxed activity of the entity under a disclosed hire purchase agreement is a partly creditable acquisition.

22. An example of a type of acquisition which relates to both activities under the arrangement is an introductory or arrangement service. This service may be acquired from an entity that facilitates the supply of a disclosed hire purchase agreement for the taxpayer. A retail motor vehicle dealership may be such an entity.

23. Overheads are another example of the type of acquisitions which are partly creditable because they relate to both activities under the arrangement. These acquisitions such as leased premises, utilities and stationery may also relate to other activities of the entity.

24. Where a taxpayer makes a partly creditable acquisition, the ITC amount is determined by applying the following formula set out in subsection 11-30(3):

$$\text{Full input tax credit} \times \text{Extent of creditable purpose} \times \text{Extent of consideration}$$

> where:
>
> …
>
> ***extent of creditable purpose*** is the extent to which the creditable acquisition is for a creditable purpose, expressed as a percentage of the total purpose of the acquisition.

25. Some partly creditable acquisitions may also be subject to the application of Division 70, which provides for a RITC for certain acquisitions, where credit has been denied (either wholly or partly) because the acquisition relates to some extent to making financial supplies. Reduced credit acquisitions are listed in subsection 70-5.02(1) of the GST Regulations.

26. For example, the acquisition of introductory and arrangement services discussed in paragraph 22 of this Practice Statement qualifies as a reduced credit acquisition under table item 18 of subsection 70-5.02(1) of the GST Regulations.

27. Division 70 makes a reduced credit acquisition creditable to the extent it relates to making financial supplies. Section 70-5.03 of the GST Regulations specifies the percentage of ITC for each kind of reduced credit acquisition as 75%.

28. Where a reduced credit acquisition is partly for a creditable purpose because of Division 11 and partly for a creditable purpose because of Division 70, the extent to which the acquisition is acquired for a creditable purpose is worked out using the formula in subsection 70-20(2).

Previous position

29. On 28 October 2002, the Commissioner set out the ATO view on disclosed hire purchase arrangements and the treatment of related acquisitions in the GST issues registers – Financial services – questions and answers. This advice has since been amended to clarify its application.

30. The Commissioner expressed the view that:

    - the use of a general formula approach incorporating gross revenues for non-financial supplies (for example, bailment and the supply of vehicles) and net revenues for financial supplies under hire purchase agreements is not a fair and reasonable method of determining the

extent of creditable purpose for overheads. This inconsistent treatment of financial supplies and taxable supplies in the general formula gives a weighting to taxable supplies which is out of proportion to the input taxed activities carried out, and

- a method that reflects the extent of input taxed activities is preferred. While no particular approach was advocated, the Commissioner suggested that a method based on current contracts modified to reflect the extent of taxable activities associated with a hire purchase contract may be a more appropriate method of determining the extent of creditable purpose of overheads.

Current position

31. Goods and Services Tax Ruling GSTR 2006/3 *Goods and services tax: determining the extent of creditable purpose for providers of financial supplies* calls for a fair and reasonable approach to determining extent of creditable purpose and apportioning ITCs. In practical terms, the 'fair and reasonable' concept is merely a way of saying that the method chosen to determine 'use' of an acquisition must be justifiable.

32. A justifiable apportionment methodology in this context is one that takes into account the level of enterprise activities or business effort devoted to the taxable and input taxed elements of a disclosed hire purchase agreement. In this regard, the Commissioner considers that the main activity of such an enterprise predominantly involves the provision of credit and consequently the majority of expenditure would be related to the making of input taxed supplies.

33. While the making of a taxable supply by the taxpayer to the customer is an integral part of the arrangement, the nature of the surrounding commercial circumstances to the arrangement establishes that the taxpayer typically employs little in the way of business effort in making such a supply. Consequently, a justifiable apportionment methodology in this context should reflect that acquisitions are predominantly used by the taxpayer in the carrying out of its financial intermediary role and to a much lesser extent in the making of taxable supplies.

34. On this basis, the Commissioner maintains the view that the use of a revenue-based formula approach is not a fair and reasonable method of determining the creditable purpose of partly creditable acquisitions because it allocates a disproportionate amount of expenditure to the taxable activity which is contrary to the fundamental nature of the typical enterprise offering this type of credit arrangement.

35. The Commissioner's view that the appropriate proportion of expenditure to be allocated to the taxable activity ought to be a small percentage has led to consideration of practices in other jurisdictions in order to arrive at an acceptable practical approach to the problem. Both the United Kingdom (UK) and New Zealand (NZ) use a set rate for apportioning credit on overheads under hire purchase agreements.

36. In September 1984, in HM Revenue & Customs' Agreement with the Finance Houses Association Ltd, the UK accepted a rate of 15% based upon research and negotiation. The Agreement was cancelled with effect from

31 January 2000 and advice received is that any new rate agreed will not be greater than 15%.[8]

37. NZ accepted a rate of 10% which was a compromise between the (then) UK rate of 15% and the 5% rate arrived at through empirical testing undertaken in the field.

38. As international precedent suggests that a set-rate method is acceptable to most industry participants and also suggests that a maximum rate of 15% is appropriate, the Commissioner therefore considers that 15% is a reasonable percentage to apply in determining the extent of creditable purpose for Division 11 under a disclosed hire purchase agreement.

39. Notwithstanding this view, for a tax period up to and including a tax period ending on 31 March 2008, the Commissioner will accept the application of a revenue-based method of apportionment (incorporating consistent values to values for both financial supplies and non-financial supplies) to determine the extent of creditable purpose for partly creditable acquisitions. The Commissioner takes this approach in view of the particular circumstances which have surrounded the implementation of GST to disclosed hire purchase agreement transactions.

40. However, for the BAS periods mentioned in paragraph 39 of this Practice Statement, a taxpayer will be at a risk of audit in circumstances where they have applied a revenue-based formula incorporating bailment payouts or gross revenues for non-financial supplies and net revenues for financial supplies. This is due to the ATO view on such practices being clearly outlined in GST public rulings.[9]

41. For a tax period ending on or after 1 April 2008, the Commissioner will accept an apportionment method (including a set-rate method) that achieves an extent of creditable purpose for partly creditable acquisitions of less than or equal to 15%.

42. Taxpayers who consider a proper application of the law to their circumstances warrants a higher percentage may, if they wish, seek a private ruling and are encouraged to do so prior to applying a higher rate.

The use of the revenue method for products other than disclosed hire purchase agreements

43. Notwithstanding that the Commissioner considers that the revenue-based method is inappropriate in typical cases, it is open for a taxpayer to apply a revenue-based method of apportionment to their circumstances where the use of such an approach achieves an accurate reflection of the ITCs available for acquisitions acquired in carrying on the taxpayer's enterprise. Accordingly, while it is open for a taxpayer to adopt a revenue-based approach to apportionment, the decision to do so must be based on fair and reasonable principles[10] rather than a belief that resorting to such a method is available on a default basis (where no other method is available or practical).

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[8] The Commissioner notes the decision in the UK Value Added Tax (VAT) Tribunal case *The Royal Bank of Scotland Group PLC v Revenue and Customs* [2007] UKVAT V19983 (where HM Revenue & Customs argued for a 0% rate). The unique features of this case make it unreliable as a precedent for Australian GST purposes. For example, conflicting evidence in the way in which the case was presented ultimately led to the VAT Tribunal adopting the application of a 'transaction count' apportionment method, which we consider provides a doubtful proxy for the measurement of use to which expenditure is applied in these arrangements. Additionally, the VAT Tribunal provided little in the way of clarification as to why this method was considered fair and reasonable.

[9] See GST issues registers – Financial services – questions and answers and paragraph 109 of GSTR 2006/3.

[10] As stated in paragraph 73 of GSTR 2006/3.

EXAMPLES

Partly creditable acquisition – no entitlement to RITCs

Tax periods up to and including the tax period ending 31 March 2008

44. Under subsection 11-30(3), the amount of the ITC for a partly creditable acquisition that does not give rise to RITCs is calculated by applying the formula:

full ITC × revenue formula%[11] × extent of consideration[12]

Where:

- revenue formula includes:

$$\frac{\text{GST-exclusive value of gross disclosed hire purchase principal receipts}}{\text{GST-exclusive value of total gross disclosed hire purchase receipts}} \times \frac{100}{1}$$

Example 1 – acquisition of overheads on or before 31 March 2008

45. *EasyCredit Financial Services (EasyCredit) carries on an enterprise of providing motor vehicle finance to customers on disclosed hire purchase terms. In the September 2006 tax period, EasyCredit is invoiced for 'overheads' worth $55,000 (inclusive of $5,000 GST). To determine its entitlement to ITCs, EasyCredit applies a revenue-based formula. This formula uses the previous month's gross receipts from the hire purchase activities as follows: the GST-exclusive value of principal repayments ($830,000) is divided by the total GST-exclusive value of both principal and interest repayments ($1,000,000) and multiplied by 100.*

46. *Using this formula, EasyCredit determines an extent of creditable purpose of 83% for its overhead acquisitions. The ITC amount is $4,150 ($5,000 × 83%).*

47. *In this circumstance, based on the application of this methodology, the Commissioner will accept the ITC claim determined by EasyCredit.*

Tax periods from 1 April 2008

48. Under subsection 11-30(3), the amount of the ITC for a partly creditable acquisition that does not give rise to RITCs is calculated by applying the formula:

full ITC × 15%[13] × extent of consideration[14]

Example 2 – acquisition of overheads on or after 1 April 2008

49. *In the November 2008 tax period, EasyCredit is invoiced for overheads to the value of $66,000 (inclusive of $6,000 GST). To determine its entitlement to*

[11] As required by subsection 11-30(3), in this circumstance the extent of creditable purpose percentage is determined by application of the revenue-based formula approach outlined in paragraph 9 of this Practice Statement.

[12] In each of the associated examples, the assumption has been made that the extent of consideration is 100% (and has therefore not been depicted).

[13] As required by subsection 11-30(3), in this circumstance the extent of creditable purpose percentage is determined by application of the 15% set-rate approach (or such other percentage agreed to with the Commissioner) outlined in paragraph 11 of this Practice Statement.

[14] In each of the associated examples, the assumption has been made that the extent of consideration is 100% (and has therefore not been depicted).

ITCs, EasyCredit applies the 15% set rate. The amount of ITC for its overhead acquisitions is $900 ($6,000 × 15%).

50. *In this circumstance, based on the application of the 15% set-rate method, the Commissioner will accept the ITC claim determined by EasyCredit.*

Partly creditable acquisition – entitlement to reduced ITCs

Tax periods up to and including the tax period ending 31 March 2008

51. Subsection 11-30(3) is modified by applying the formula set out in subsection 70-20(2) in relation to the 'extent of creditable purpose' component. The amount of ITC for a partly creditable acquisition that includes an entitlement to RITCs is calculated by applying the formula:

extent of creditable purpose + [extent of Division 70 creditable purpose × percentage credit reduction]

Where:

- *extent of creditable purpose* is calculated as follows:

  full ITC × revenue formula%[15] × extent of consideration[16]

  – where the revenue formula includes:

  $$\frac{\text{GST-exclusive value of gross disclosed hire purchase principal receipts}}{\text{GST-exclusive value of total gross disclosed hire purchase receipts}} \times \frac{100}{1}$$

- extent of Division 70 creditable purpose is the extent expressed as a percentage, to which the purpose for which the entity makes the acquisition was a creditable purpose, because of Division 70
- percentage credit reduction is 75%.[17]

Example 3 – acquisition of introductory services on or before 31 March 2008

52. *In the June 2006 tax period, Hybrid Motor Vehicle Dealerships (Hybrid) invoices EasyCredit for introductory services to the value of $82,500 (inclusive of $7,500 GST). These services are reduced credit acquisitions under table item 18 of subsection 70-5.02(1) of the GST Regulations. EasyCredit calculates its extent of creditable purpose using the revenue-based formula described in Example 1 of this Practice Statement (83%). It then applies this in the subsection 70-20(2) formula as follows: extent of creditable purpose (83%) plus (the extent of Division 70 creditable purpose (17%) times the percentage credit reduction (75%)). That is, 83% plus 12.75%, giving an extent of creditable purpose of 95.75%. The amount of ITC for the acquisition of introductory services is $7,181 ($7,500 × 95.75%).*

53. *In this situation, based on the application of this methodology, the Commissioner will accept the ITC claim determined by EasyCredit.*

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[15] As required by subsection 11-30(3), in this circumstance the extent of creditable purpose percentage is determined by application of the revenue-based formula approach outlined in paragraph 9 of this Practice Statement.

[16] In each of the associated examples, the assumption has been made that the extent of consideration is 100% (and has therefore not been depicted).

[17] See paragraph 23 of this Practice Statement.

Tax periods from 1 April 2008

54. Subsection 11-30(3) is modified by applying the formula set out in subsection 70-20(2) in relation to the extent of creditable purpose component. The amount of ITC for a partly creditable acquisition that includes an entitlement to RITCs is calculated by applying the formula:

extent of creditable purpose + [extent of Division 70 creditable purpose × percentage credit reduction]

Where:

- *extent of creditable purpose* is 15%
- *extent of Division 70 creditable purpose* is 85%
- *percentage credit reduction* is 75%

Example 4 – acquisition of introductory services on or after 1 April 2008

55. *In the April 2008 tax period, Hybrid invoices EasyCredit for introductory services to the value of $124,875 (inclusive of $11,352 GST). These services are reduced credit acquisitions under table item 18 of subsection 70-5.02(1) of the GST Regulations. Using the 15% set rate in the subsection 70-20(2) formula, EasyCredit determines the extent of creditable purpose for the acquisition of introductory services from Hybrid as follows: 15% + (85% × 75%) giving an extent of creditable purpose of 78.75%. The amount of ITC for the acquisition of introductory services is $8,939 ($11,352 × 78.75%).*

56. *In this situation, based on the application of the 15% set-rate method, the Commissioner will accept the ITC claim determined by EasyCredit.*

Partly creditable acquisition – no entitlement to RITCs (acquisition allocated to a dedicated asset finance cost centre – no floor plan finance activities)

Tax periods up to and including the tax period ending 31 March 2008

57. A taxpayer that has a dedicated asset finance cost centre or apportions expenses at an overall enterprise level, and provides only retail finance products (that is, no floor plan wholesale finance products) can calculate the extent of creditable purpose under subsection 11-30(3) for partly creditable overheads using the formula:

full ITC × revenue formula%[18] × extent of consideration[19]

Where:

- the revenue formula includes gross (GST-exclusive) revenues for non-financial supplies in both the numerator and the denominator, and gross revenues for financial supplies in the denominator of the formula.

[18] As required by subsection 11-30(3), in this circumstance the extent of creditable purpose percentage is determined by application of the revenue-based formula approach outlined in paragraph 9 of this Practice Statement.

[19] In each of the associated examples, the assumption has been made that the extent of consideration is 100% (and has therefore not been depicted).

Example 5 – acquisition of overheads on or before 31 March 2008

58. *CarFinance Financial Services (CarFinance) supplies a range of asset finance products to customers, including finance and operating leases, chattel mortgages and disclosed hire purchase agreements. In carrying on its enterprise, CarFinance allocates its overhead acquisitions to a central cost centre which services all of its asset finance activities and applies a revenue-based formula to determine the extent of creditable purpose for these acquisitions. The revenue-based formula applied by CarFinance uses:*

- *gross (GST-exclusive) finance and operating lease revenue – this product represents 25% of active contracts and historically generates gross annual revenue of $77 million*
- *gross chattel mortgage revenue (including principal and interest repayments) – this product represents 25% of active contracts and historically generates gross annual revenue of $77 million ($66 million principal repayments and $11 million interest repayments and credit charges), and*
- *gross (GST-exclusive) disclosed hire purchase revenue (including both principal and interest repayments) – this product represents 50% of the active contracts and historically generates gross annual revenue of $193 million ($165 million principal repayments and $28 million interest repayments and credit charges).*

59. *Using the gross annual revenues, CarFinance determines that its overhead acquisitions are made 69% for a creditable purpose as follows: $242 million (which is made up of $165 million disclosed hire purchase principal repayments and $77 million leasing payments) divided by $347 million (calculated by adding $193 million disclosed hire purchase repayments, $77 million leasing payments and $77 million chattel mortgage principal and interest repayments) and multiplied by 100.*

60. *In the September 2007 tax period, CarFinance is invoiced for overheads worth $1.1 million (inclusive of $100,000 GST). By application of the 69% extent of creditable purpose, CarFinance calculates that the amount of ITC entitlement for these acquisitions is $69,000 ($100,000 × 69%).*

61. *In this Example, based on the application of this methodology, the Commissioner will accept the ITC claim determined by CarFinance for its overhead acquisitions.*

Example 6 – acquisition of overheads on or before 31 March 2008

62. *Mobile Financial Solutions (Mobile) supplies a range of asset finance products to customers, including finance and operating leases, chattel mortgages and disclosed hire purchase agreements. Mobile allocates its overhead acquisitions to a central cost centre which services all of its asset finance activities. Mobile also uses a revenue-based formula to determine the extent of creditable purpose for its overhead acquisitions. However, the revenue-based formula applied by Mobile uses:*

- *gross (GST-exclusive) finance and operating lease revenue – this product represents 20% of active contracts and historically generates gross annual revenue of $50 million*
- *net chattel mortgage interest revenue – this product represents 30% of active contracts and historically generates net annual revenue of $3 million; this net figure is calculated as $18 million gross interest*

repayments and credit charges minus $15 million, being the annual cost of funding the chattel mortgages – gross annual principal repayments are not included in the calculation but generate $89 million, and

- *gross (GST-exclusive) disclosed hire purchase principal repayments and net disclosed hire purchase interest revenue – this product represents 50% of active contracts and historically generates $165 million in gross annual principal repayments and $6 million net annual interest revenue This is calculated as $28 million gross interest repayments and credit charges minus $22 million, being the annual cost of funding the disclosed hire purchase products.*

63. *Using the gross revenues, Mobile determines that its overhead acquisitions are made 95.99% for a creditable purpose as follows: $215 million (which is made up of $165 million disclosed hire purchase principal repayments and $50 million leasing revenue) divided by $224 million (calculated by adding $165 million disclosed hire purchase principal repayments, $6 million net disclosed hire purchase interest revenue, $50 million leasing revenue and $3 million net chattel mortgage interest revenue) and multiplied by 100.*

64. *In the November 2006 tax period, Mobile is invoiced for overheads worth $1.1 million (inclusive of $100,000 GST). Using 95.99% extent of creditable purpose, Mobile calculates that the amount of ITC entitlement for these acquisitions is $95,990 ($100,000 × 95.99%).*

65. *Mobile has applied a revenue-based formula to work out the extent of creditable purposes for overhead acquisitions that are attributable to a tax period which ends on or before 31 March 2008.*

66. *However, in this circumstance, the Commissioner is likely to challenge the ITCs determined by Mobile for its overhead acquisitions, because the revenue-based formula applied incorporates inconsistent values for input-taxed and non-input taxed activities.*

67. *Had Mobile included gross (GST-exclusive) revenues for non-financial supplies in both the numerator and the denominator, and gross revenues for financial supplies in the denominator of the formula, the Commissioner would have accepted the amount of ITCs determined on that basis.*[20]

Example 7 – acceptable use of a revenue-based formula

68. *Using Mobile's gross revenues, the extent of creditable purpose is 61% as follows: $215 million (made up of $50 million gross leasing revenue and $165 million gross disclosed hire purchase principal revenue) divided by $350 million (calculated by adding $50 million gross leasing revenue, $165 million gross disclosed hire purchase principal revenue, $28 million gross disclosed hire purchase interest revenue, $89 million gross chattel mortgage principal revenue and $18 million gross chattel mortgage interest and credit charges revenue) and multiplied by 100.*

69. *Had Mobile used the 61% extent of creditable purpose figure, its ITC entitlement for its acquisition of overheads would be $61,000 ($100,000 × 61%). This calculation of the entitlement to ITCs would have been accepted by the Commissioner.*

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[20] Equally, the Commissioner would have accepted the amount of ITCs calculated by use of a revenue-based formula inclusive wholly of net values for both financial supplies and non-financial supplies.

Tax periods from 1 April 2008

70. A taxpayer that has a dedicated asset finance cost centre or apportions expenses at an overall enterprise level and provides only retail finance products (that is, no floor plan wholesale finance products) can calculate the extent of creditable purpose under subsection 11-30(3) for partly creditable overheads in the following manner:

Step 1 By a fair and reasonable method, determine the ratio of each retail finance product (for example, disclosed hire purchase agreements, chattel mortgages, finance lease and operating leases) to all retail finance products.

Step 2 Allocate overheads to each retail finance product according to the ratio of that product to all retail finance products.

Step 3 Overheads allocated to finance and operating lease products are acquired solely for a creditable purpose

Overheads allocated to chattel mortgage products are acquired not at all for a creditable purpose.

For overheads allocated to disclosed hire purchase products, go to Step 4.

Step 4 Apply the formula

full ITC × 15%[21] × extent of consideration[22]

Example 8 – acquisition of overheads on or after 1 April 2008

71. *In the June 2008 tax period, CarFinance acquires overheads for $2.2 million (inclusive of $200,000 GST). In determining its entitlement to ITCs, CarFinance uses:*

- *gross (GST-exclusive) finance and operating lease revenue – this product represents 25% of active contracts and historically generates gross annual revenue of $77 million*
- *gross chattel mortgage revenue (including principal and interest repayments) – this product represents 25% of active contracts and, historically generates gross annual revenue of $77 million ($66 million principal repayments and $11 million interest repayments and credit charges), and*
- *gross (GST-exclusive) disclosed hire purchase revenue (including both principal and interest repayments) – this product represents 50% of the active contracts and historically generates gross annual revenue of $193 million ($165 million principal repayments and $28 million interest repayments and credit charges).*

[21] As required by subsection 11-30(3), in this circumstance the extent of creditable purpose percentage is determined by application of the 15% set-rate approach (or such other percentage agreed to with the Commissioner) outlined in paragraph 11 of this Practice Statement.

[22] In each of the associated examples, the assumption has been made that the extent of consideration is 100% (and has therefore not been depicted).

72. *CarFinance adopts the following approach:*

Step 1 *CarFinance uses 'active contracts'*[23] *to determine the ratio of each retail finance product to all finance products. Using historical benchmarks, the ratios are:*

Leasing (finance and operating)	-	*25%*
Chattel mortgages	-	*25%*
Disclosed hire purchase	-	*50%*

Step 2 *CarFinance allocates the GST component of the $2.2 million overheads ($200,000) to each retail finance product according to the ratio worked out in Step 1; that is:*

Leasing	*$50,000 ($200,000 × 25%)*
Chattel mortgages	*$50,000 ($200,000 × 25%)*
Disclosed hire purchase	*$100,000 ($200,000 × 50%)*

Step 3 *For overheads allocated to each retail finance product, CarFinance determines that:*

- *overheads allocated to leasing products are wholly for a creditable purpose, giving an ITC entitlement of $50,000*
- *overheads allocated to chattel mortgage products are not at all for a creditable purpose and do not give rise to any ITCs, and*
- *overheads allocated to disclosed hire purchase products are partly for a creditable purpose, with the amount of ITC determined by applying the formula set out in Step 4.*

Step 4 *CarFinance determines the amount of ITC for overheads allocated to disclosed hire purchase products by applying the formula:*

$100,000 × 15% = $15,000.

73. *By adding the results from Steps 3 and 4, CarFinance determines that it is entitled to an ITC of $65,000 (that is, $50,000 relating to leasing activities plus $15,000 determined to relate to the taxable supplies made under disclosed hire purchase agreements).*

74. *In this circumstance, based on the application of this approach, the Commissioner would accept the ITC claim determined by CarFinance.*

Partly creditable acquisition – no entitlement to RITCs (acquisition allocated to a dedicated asset finance cost centre – floor plan finance activities)

Tax periods up to and including the tax period ending 31 March 2008

75. A taxpayer that has a dedicated asset finance cost centre or apportions expenses at an overall enterprise level and provides both floor plan wholesale finance products and retail finance products can calculate the extent of

[23] The use of 'active contracts' for 'portfolio' apportionment purposes is intended to be illustrative and is not prescriptive of the way in which 'portfolio' apportionment is to be carried out in all circumstances. The Commissioner will accept the use of other methods of portfolio apportionment, providing that the method selected delivers a fair and reasonable outcome.

creditable purpose under subsection 11-30(3) for partly creditable overheads in the following manner:

full ITC × revenue formula%[24] × extent of consideration[25]

Where:

- revenue formula
  - excludes the value of floor plan payouts[26] as non-financial supply revenue in both the numerator and denominator of the formula, or
  - includes gross (GST-exclusive) revenues for non-financial supplies in both the numerator and the denominator and gross revenues for financial supplies in the denominator of the formula.

Example 9 – acquisition of overheads on or before 31 March 2008

76. *Mendarosa Financial Services (Mendarosa) is the wholly owned (non-GST grouped) finance arm of Mendarosa Motors. Mendarosa provides both wholesale (floor plan finance) and retail finance products (finance and operating leases, chattel mortgages and disclosed hire purchase agreements) to customers. Mendarosa allocates its overhead acquisitions to a central cost centre which services all of its wholesale and retail asset finance activities. Mendarosa uses a revenue-based formula to determine the extent of creditable purpose for its overhead acquisitions. The revenue-based formula applied by Mendarosa includes:*

- *the (GST-exclusive) value of floor plan payouts – historically, the annual amount of floor plan payouts is $750 million*
- *the (GST-exclusive) value of floor plan fees – historically, floor plan fees generate $15 million in annual gross revenue*
- *gross (GST-exclusive) finance and operating lease revenue – these products represent 30% of active contracts and historically generates annual gross revenue of $118 million*
- *net chattel mortgage interest revenue – this product represents 30% of active contracts and historically generates annual net revenue of $3 million ($18 million gross interest repayments and credit charges minus $15 million annual cost of funding the chattel mortgages); gross principal repayments are not included but generate $100 million annually, and*
- *gross (GST-exclusive) disclosed hire purchase principal repayments and net disclosed hire purchase interest revenue – this product represents 40% of active contracts and historically generates $135 million in annual gross principal repayments and $7 million annual net interest revenue ($22 million gross interest repayments and credit charges minus $15 million annual cost of funding the disclosed hire purchase products).*

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[24] As required by subsection 11-30(3), in this circumstance the extent of creditable purpose percentage is determined by application of the revenue-based formula approach outlined in paragraph 9 of this Practice Statement.

[25] In each of the associated examples, the assumption has been made that the extent of consideration is 100% (and has therefore not been depicted).

[26] 'Floor plan payout' is the consideration received by the 'floor plan financier' for the supply of goods to the wholesaler or retailer, when the wholesaler or retailer sells the goods.

77. *Using these historical revenues, Mendarosa determines that its overhead acquisitions are made 99.02% for a creditable purpose as follows: $1,018 million (made up of $750 million floor plan payouts plus $15 million floor plan fees plus $135 million disclosed hire purchase principal repayments plus $118 million leasing revenue) divided by $1,028 million (calculated by adding $750 million floor plan payouts, $15 million floor plan fees, $135 million disclosed hire purchase principal repayments, $118 million leasing revenue, $7 million net disclosed hire purchase interest revenue and $3 million net chattel mortgage interest revenue) and multiplied by 100.*

78. *In the November 2006 tax period, Mendarosa acquires overheads for $3.3 million (including GST). Applying 99.02% extent of creditable purpose, Mendarosa calculates that the amount of ITC entitlement for these acquisitions is $297,060 ($300,000 × 99.02%).*

79. *Mendarosa has applied a revenue-based formula to work out the extent of creditable purpose for overhead acquisitions that are attributable to a tax period which ends on or before 31 March 2008.*

80. *However, in this circumstance, the Commissioner is likely to challenge the ITCs determined by Mendarosa for its overhead acquisitions, because the revenue-based formula applied incorporates floor plan payout amounts and inconsistent values for input-taxed and non-input taxed activities.*

81. *Had Mendarosa excluded the value of floor plan payouts and included gross revenues for non-financial supplies in both the numerator and the denominator, and gross revenues for financial supplies in the denominator of the formula, the Commissioner would have accepted the amount of ITCs determined on that basis.*

Example 10 – acceptable use of a revenue-based formula

82. *Using Mendarosa's gross revenues, the extent of creditable purpose is 65.68% as follows: $268 million (made up of $15 million floor plan finance fees plus $135 million gross disclosed hire purchase principal revenue plus $118 million gross leasing revenue) divided by $408 million (calculated by adding $15 million floor plan finance fees, $135 million gross disclosed hire purchase principal revenue, $118 million gross leasing revenue, $22 million gross disclosed hire purchase interest revenue, $100 million gross chattel mortgage principal revenue and $18 million gross chattel mortgage interest and credit charges revenue) and multiplied by 100.*

83. *Had Mendarosa used the 65.68% extent of creditable purpose figure, its ITC entitlement for its overheads would be $197,040 ($300,000 × 65.68%). This calculation of the entitlement to ITCs for the overhead acquisitions would have been accepted by the Commissioner.*

Tax periods from 1 April 2008

84. A taxpayer that has a dedicated asset finance cost centre or apportions expenses at an overall enterprise level and provides both floor plan wholesale finance products and retail finance products can calculate the extent of creditable purpose under subsection 11-30(3) for partly creditable overheads in the following manner:

Step 1 By a fair and reasonable method, apportion overhead acquisitions between wholesale and 'retail' finance products.

Overheads allocated to wholesale finance products are acquired wholly for a creditable purpose.

For overheads allocated to retail finance products, go to Step 2.

Step 2 By a fair and reasonable method, determine the ratio of each retail finance product (for example, disclosed hire purchase agreements, chattel mortgages, finance and operating leases) to all retail finance products.

Step 3 Allocate overheads to each retail finance product according to the ratio of that product to all retail finance products.

Step 4 Overheads allocated to finance and operating lease products are acquired solely for a creditable purpose.

Overheads allocated to chattel mortgage products are acquired not at all for a creditable purpose.

For overheads allocated to disclosed hire purchase products, go to Step 5.

Step 5 Apply the formula:

full ITC × 15% × extent of consideration

Example 11 – acquisition of overheads on or after 1 April 2008

85. *In the April 2008 tax period, Mendarosa acquires overheads for $2.2 million (inclusive of $200,000 GST). In determining its entitlement to ITCs, Mendarosa uses:*

- *the (GST-exclusive) value of floor plan payouts – historically, the annual amount of floor plan payouts is $750 million*
- *the (GST-exclusive) value of floor plan fees – historically, floor plan fees generate $15 million in annual gross revenue*
- *gross (GST-exclusive) finance and operating lease revenue – these* products represent 30% of active contracts and historically generates *annual gross revenue of $118 million*
- *net chattel mortgage interest revenue – this product represents 30% of active contracts and, historically, annual net revenue of $3 million ($18 million gross interest repayments and credit charges minus $15 million annual cost of funding the chattel mortgages); gross principal repayments are not included but generate $100 million annually, and*
- *gross (GST-exclusive) disclosed hire purchase principal repayments and net disclosed hire purchase interest revenue – this product represents 40% of active contracts and historically generates $135 million in annual gross principal repayments and $7 million annual net interest revenue ($22 million gross interest repayments and credit charges minus $15 million annual cost of funding the disclosed hire purchase products).*

86. *Mendarosa adopts the following approach:*

Step 1 Mendarosa allocates the GST component of the $2.2 million overheads ($200,000) between its wholesale and retail finance products. It does this by applying the ratio of gross wholesale product revenue (excluding floor plan payouts) to total asset finance product

revenue (including gross wholesale and retail product revenue but excluding floor plan payouts) to the $200,000 amount.

Using historical benchmarks, Mendarosa determines that 3.67% (calculated as $15 million annual gross floor plan fees divided by $408 million total annual gross asset finance revenues multiplied by 100) of the $200,000 should be allocated to its taxable wholesale finance products.

The acquisition of the overheads allocated to Mendarosa's wholesale finance products is solely for a creditable purpose, giving an ITC entitlement of $7,340 ($200,000 × 3.67%).

Step 2 *Mendarosa uses active contracts to determine the ratio of each retail finance product to all finance products. Using historical benchmarks, the ratios are:*

Leasing (finance and operating)	*-*	*30%*
Chattel mortgages	*-*	*30%*
Disclosed hire purchase	*-*	*40%*

Step 3 *Mendarosa allocates the remaining overheads ($192,660) to each retail finance product according to the ratio worked out in Step 2; that is:*

Leasing	*$57,798 ($192,660 × 30%)*
Chattel mortgages	*$57,798 ($192,660 × 30%)*
Disclosed hire purchase	*$77,064 ($192,660 × 40%)*

Step 4 *For overheads allocated to each retail finance product, Mendarosa determines that:*

overheads allocated to leasing products are solely for a creditable purpose and give rise to an ITC entitlement of $57,798

overheads allocated to chattel mortgage products are not at all for a creditable purpose and do not give rise to any ITCs

overheads allocated to disclosed hire purchase products are partly for a creditable purpose. The amount of ITC is determined by applying the formula set out in Step 5.

Step 5 *Mendarosa determines the amount of ITCs for overheads allocated to disclosed hire purchase products by application of the formula:*

$77,064 × 15% = $11,559

87. *By adding the results from Steps 1, 4 and 5, Mendarosa determines that it is entitled to an ITC of $76,697 (that is, $7,340 relating to wholesale finance activities plus $57,798 relating to leasing activities plus $11,559 determined to relate to the taxable supplies made under disclosed hire purchase agreements).*

88. *In this circumstance, based on the application of this approach, the Commissioner would accept the ITC claim determined by Mendarosa.*

Amendment history

18 July 2024

Part	Comment
All	Updated in line with current ATO style and accessibility requirements.
Paragraph 2	Amended paragraph numbering from 1A to 2, for consistency with the rest of the Practice Statement. Updated subsequent paragraph references to new paragraph numbers.

4 July 2019

Part	Comment
Paragraph 15	Updated to correct paragraph references in relation to GSTR 2000/29.

7 June 2013

Part	Comment
Contact details	Updated.

1 November 2012

Part	Comment
Subject (title)	Change in title – added date to reflect the scope of arrangements the Practice Statement applies to.
Table of contents	Updated to include new paragraphs 13 to 16.
Paragraphs 3 and 17	Updated to reflect scope of Practice Statement.
Paragraph 24	Minor update.
Footnotes 2 and 3	Minor update.
Paragraphs 13 to 16	Inserted paragraphs – our approach to arrangements from 1 July 2012 as a result of law change.
Footnotes 4 to 7	Inserted new footnotes to support new paragraphs.
References	Updated to add or remove legislative references, related public rulings, case references and contact details.
Contact details	Updated.

References

Legislative references	ANTS(GST)A 1999 Div 11 ANTS(GST)A 1999 11-15 ANTS(GST)A 1999 11-30(1) ANTS(GST)A 1999 11-30(3) ANTS(GST)A 1999 29-25 ANTS(GST)A 1999 Div 70 ANTS(GST)A 1999 70-20(2) ANTS(GST)R 1999 ANTS(GST)R 2019 40-5.12 ANTS(GST)R 2019 40-5.09(1) ANTS(GST)R 2019 70-5.02(1) ANTS(GST)R 2019 70-5.03 New Tax System (Goods and Services Tax) Amendment Regulation 2012 (No. 1) TAA 1953 105-50 of Schedule 1
Related public rulings	GSTR 2000/29 GSTR 2002/2 GSTR 2006/3
Case references	The Royal Bank of Scotland Group PLC v Revenue & Customs [2007] UKVAT V19983
Other references	GST issues registers – Financial services – questions and answers
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