

## SMSFs and GST withholding on residential premises

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### Introduction

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The GST withholding regime ('Withholding Regime') was introduced on 1 July 2018 to collect GST from foreign vendors, but has much broader application.

GST is typically a vendor responsibility. However, under the Withholding Regime, purchasers of certain residential property must withhold GST from the amount payable to a vendor and pay that amount direct to the ATO at settlement ('Withholding Obligation').

This article examines key aspects of the Withholding Regime with particular emphasis on how it impacts SMSFs.

All section references are to the *Taxation Administration Act 1953* (Cth) ('TAA') unless otherwise stated.

### What is the GST Withholding Regime?

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A purchaser will have a GST Withholding Obligation if they are a recipient of a taxable supply, by way of sale or long term lease (ie, 50 years or more) of:

- new residential premises that:
  - are not commercial residential premises; or
  - have not been created through substantial renovations of a building; or
- land that could be used to build new residential property, eg, potential residential land that is included in a property subdivision plan and does not contain any building that is in use for a commercial purpose.

If the above requirements are met and there are no applicable exemptions, the purchaser is required to pay the GST withholding amount directly to the ATO at settlement.

Following settlement, the vendor will be entitled to a credit for the amount paid to the ATO, with the credit arising at the time the net amount is assessed on the vendor's GST return.

## What is a taxable supply?

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Note that a purchaser will only have a GST Withholding Obligation where the vendor is making a taxable supply. A supply of new residential premises or potential residential land in Australia will be a taxable supply if the vendor is registered or required to be registered for GST and the supply is:

- made for consideration;
- made in the course or furtherance of an enterprise that is carried on by the vendor;
- the supply is connected with the indirect tax zone (ie, Australia); and
- not a GST-free or input taxed supply — for example, a supply made as part of a GST-free supply of a going concern or a supply of GST-free farmland.

(See s 9-5 *A New Tax System (Goods and Services Tax) Act 1999* (Cth) ('GST Act').)

Accordingly, if a vendor is registered or required to be registered for GST and the supply is made in the course of the vendor's enterprise, GST at settlement may apply.

The next step to analyse is what type of property is being supplied. If new residential premises are being supplied then GST Withholding Obligations arise (subject to the qualifiers above where a withholding obligation does not arise, eg, the property is commercial residential premises or the property is new residential premises due to being created through substantial renovations of a building).

The following scenarios provide several examples where a vendor will not be making a taxable supply:

- the vendor is not registered for GST and the sale is not in the course or furtherance of an enterprise, (eg, where the vendor is constructing a new family home to live in or selling their family home which they have lived in for a considerable period of time);

- the sale of residential premises is input taxed and has been available for residential rental for over 5 years and the real property is no longer new residential premises; or
- the sale is a GST-free supply (eg, the sale of farming, primary production business, land).

## What amount must be withheld and paid to the ATO?

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Typically, when calculating GST on the net GST exclusive amount, GST is broadly calculated as 10% of the GST exclusive amount.

In contrast, under the Withholding Regime, generally 1/11<sup>th</sup> of the contract or sale price must be paid to the ATO, including both monetary and non-monetary consideration, unless:

- the contract is expressed to be a specified amount plus GST; or
- a relevant exception applies — in particular, the amount to be withheld will vary in relation to the following taxable supplies:
  - Where the margin scheme applies — 7% of the purchase price.
  - Where the supply is between 'associates' (as broadly defined) for less than the GST-inclusive market value consideration — 10% of the GST-inclusive market value of the supply.
  - Where the supply is a part taxable supply — a reduced amount that is a proportion of the contract price.
  - Where the supply is to multiple recipients (not including joint proprietors) — for each recipient, the proportion of the taxable supply that is deemed to be made to them in the relevant circumstances.

Note that the margin scheme can, in certain cases, apply to exclude some of the pre-GST value of the land from the GST system as GST was introduced in Australia from 1 July 2000.

## GST withholding obligations for SMSF trustees

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Broadly, an SMSF trustee will be required to register for GST where they are carrying on an enterprise, and their annual GST turnover is or is expected to be \$75,000 or more (s 2-23 of the GST Act). Note that an SMSF trustee may also elect to register voluntarily where the GST turnover is under this amount.

Generally, the investment activities of an SMSF will be subject to input tax without any income tax credit ('ITC') being available to the fund. Also, GST is typically not required to be collected on an SMSF's output (eg, the payment of lump sums and pension benefits). Accordingly, not many SMSFs make taxable supplies.

However, certain transactions undertaken by SMSFs will constitute a taxable supply that is subject to the normal GST rules. For example, an SMSF renting a commercial building to a third party will, subject to the \$75,000 per annum turnover test, have to collect and remit any GST collected on any rent it receives. Conversely, any GST payable by an SMSF on such taxable activities will be capable of being offset against the GST payable to the ATO in relation to that commercial property. That is, the SMSF can claim an ITC for inputs that are related to the taxable supply in question (eg, repairs to the commercial property).

Similarly, an SMSF that is constructing new residential property for sale will typically constitute an enterprise that will give rise to GST obligations. If the SMSF is merely constructing a new residential property for rental purposes then that generally constitutes an input taxed supply unless the property is sold within a 5 year period. GST turnover generally does not include amounts subject to input-tax supplies (eg, financial supplies or income derived from the sale or rental of residential property). However, GST turnover does include:

- rental income from property that is used for commercial purposes; and
- income derived from business assets such as the leasing of plant and equipment to an unrelated party.

In the context of the Withholding Regime, a Withholding Obligation does not arise on the transfer of property that occurs where a change of trustee takes place, nor does it arise where a property is transferred from a custodian entity to an SMSF trustee on the finalisation of a borrowing under a limited recourse borrowing arrangement.

SMSF trustees should be aware of the Withholding Regime when selling or purchasing property whether or not they are registered or required to be registered for GST. Several variables must be considered when selling or purchasing property to determine if a transaction is a taxable supply and if there is a subsequent Withholding Obligation. We recommend that SMSF trustees seek advice to ascertain the correct tax and GST treatment of each property transaction and any potential Withholding Obligations.

## Practical Implications of the Withholding Regime

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Vendors of residential premises or potential residential land are required to notify the purchaser of their Withholding Obligation in writing prior to settlement. This notification obligation applies whether or not the residential property or the potential residential land is 'new'.

There are some exceptions to the vendor's notification obligations. Vendors are not required to provide notice if the transaction is a supply of:

- commercial residential premises; or
- potential residential land where the purchaser is registered for GST and is acquiring the land for a creditable purpose.

The notice must state, among other things, whether or not the purchaser has a Withholding Obligation and the dollar amount that is to be withheld at settlement.

If there is a Withholding Obligation, the purchaser must report the transaction to the ATO before settlement by completing the prescribed ATO forms. At settlement, the purchaser must pay the applicable amount withheld to the ATO. Naturally, the purchaser's property lawyer or conveyancer should guide the purchaser with this process.

## What penalties apply?

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The Withholding Regime places the primary responsibility on the purchaser to pay the GST amount to the ATO and administrative penalties may be imposed if a purchaser fails to comply.

Penalties can also apply to vendors, but as this article demonstrates, the primary obligations fall on the purchaser.

## Conclusion

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SMSF trustees who are planning to dispose of or acquire residential property that is covered by the GST Withholding Regime should take note of the obligations that may arise. While the vendor is broadly obligated to notify the purchaser of the GST obligations, the purchaser is required to pay the GST to the ATO.

Whether an SMSF trustee is a vendor or purchaser in relation to a property transaction, they should seek prior input and ensure they comply with the GST Withholding Regime.

Note that the above commentary is a general summary only and is not intended to be relied on as advice.

## Related articles

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