

## **GST “supply” - the Commissioner’s view**

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After so many GST rulings on so many different topics, the Commissioner has finally issued a ruling on the critical concept of “supply” and its meaning for GST purposes. The new ruling, *GST Ruling GSTR 2006/9*, sets out the Commissioner’s views on what constitutes a “supply” for GST purposes and, in particular, for the purposes of section 9-5 of the GST Act. The recent ruling as issued in final mostly confirms the earlier *Draft GST Ruling GSTR 2005/D8*, with some differences.

### **Introduction**

GST applies when a “taxable *supply*” is made (section 7-1, 9-5 of the GST Act). For there to be a taxable supply, the requirements in section 9-5 have to be met. One such requirement is that a “**supply**” must be made. Accordingly, critical to the need to charge GST on a transaction is the existence of a “supply”; but, surprisingly, only after more than 6 years since the introduction of the tax has the ATO consolidated its thinking on this core concept.

### **Part 1: General meaning of “supply”**

Part 1 of GSTR 2006/9 considers in detail the meaning of the expression “supply” as defined in section 9-10 of the GST Act.

Section 9-10(1) defines a supply as “any form of supply whatsoever.” The breadth of the expression is therefore intended to catch all supplies regardless of whether they concern goods or services or anything else (paragraph 33).

Section 9-10(2) illustrates examples of instances that can amount to a supply.

A supply can have two different aspects, relating either to:

- the thing which passes, such as goods, services, a right or obligation; or
- the means by which it passes, such as its provision, creation, grant, assignment, surrender or release.

Section 9-10(2) does not qualify, nor constrain, section 9-10(1). Accordingly, something that is not listed in section 9-10(2), but which falls within section 9-10(1) will still be a supply (paragraphs 34 to 35).

## **Part 2: Two-party transactions**

Part 2 of the new GST ruling moves from the concept of a “supply” in the context of the GST Act, into its practical application to a given transaction. In particular, 10 propositions are put forward by the Commissioner to analyse a simple two-party transaction and whether a supply arises in such a transaction.

### ***Proposition 1: For every supply there is a ‘supplier’***

Unless a ‘supplier’ makes a supply, there cannot be a supply (*Shaw v Director of Housing and State of Tasmania* (No 2) 2001 ATC 4054; (2001) 46 ATR 213; [2001] TASSC 2).

The term ‘supplier’ is not defined in the GST Act, but whenever the term is used in the GST Act, it refers to the entity that makes the supply or is capable of making a supply (paragraph 52).

***Proposition 2: Generally, for every supply there is a 'recipient' and an 'acquisition'***

In general, for there to be a supply, there will usually be a recipient making an acquisition. Also, for there to be an 'acquisition', there must be a 'recipient' of the supply (paragraph 54). The definition of 'recipient' in section 195-1 suggests that something is passed from the supplier to the recipient. Moreover, the supplier and the 'recipient' of the supply must be different entities, an entity cannot make a supply to itself (paragraph 55).

However, an acquisition and a supply need not occur simultaneously. In particular, in some cases an entity can have something, without actually having made any acquisition of the thing (paragraph 60). GSTR 2006/9 cites the example of an author of an original literary work who does not make an acquisition of a right, since the *Copyright Act 1968* protects the copyright in that work (paragraph 60). This example can be contrasted to the case of an inventor who needs to be granted a patent under the *Patents Act 1990* before being able to exclusively exploit their invention (paragraph 60). It is through the grant of the patent that the inventor acquires their rights to exclusively exploit the invention. Thus, someone who creates an original literary work does not acquire copyright, while someone granted a patent does acquire rights under the patent.

***Proposition 3: A supply may be mixed, composite or neither***

A supply may be a mixed supply, a composite supply or neither.

Where a supply comprises of separately identifiable taxable and non-taxable parts it will be a mixed supply (see also *GST Ruling GSTR 2001/8*). For a mixed supply, the GST treatment of each part depends on the separate parts comprising the mixed supply.

A 'composite supply' is one that contains a dominant part, but also includes something that is integral, ancillary or incidental to that part (paragraph 65). For a composite

supply, the GST treatment of the supply is that which applies to the dominant part of the supply.

Alternatively, a supply may be neither mixed, nor composite, such as where it involves the supply of one thing only, eg a supply of a cake (paragraph 66). Although a cake is made up of mixed ingredients, there are no separately identifiable parts, as only one cake is being supplied.

However, there is no real need to separately identify each part of a supply if all the parts of that supply have the same GST treatment or no GST applies to the supply (paragraph 64).

***Proposition 4: A transaction may amount to 2 or more supplies***

Typically, a supply is made to a recipient who provides consideration in the form of money to the supplier (paragraph 67). However, if the recipient provides consideration in a non-monetary form, the consideration itself is a separate supply since by providing non-monetary consideration, the recipient is also making a supply. Therefore, in a transaction where the consideration is non-monetary, two supplies are made, one going each way (paragraph 68). Thus, each entity to the transaction needs to account for their supply separately.

Accordingly, it follows that providing or making a thing available does not necessarily give rise to a supply (paragraph 69). The thing provided or made available may only be a consequence of the transaction. For instance, a supplier may need to perform services on the recipient's premises. The recipient may agree to allow the supplier to use its computer facilities and stationery in performing those services. Allowing the use of these things is a condition of the contract that goes to defining the supply the supplier makes, rather than being a supply of those things to the supplier by the recipient.

***Proposition 5: To make a supply, an entity must do something***

The Commissioner's view is that some positive act is required to be done by an entity in order for them to make a supply. Therefore, a supply cannot be due entirely to the operation of law, without some positive action by the purported supplier. For example, a judgment creditor makes no supply when a judgment debtor pays off a debt (paragraph 73).

However, if the entity takes positive action to cause a supply to occur, even if compelled by operation of law, this counts as a supply. For instance, a liquidator who makes a disposition pursuant to the operation of law is making a supply (paragraphs 74 to 75).

Also, an owner who acquires a reversionary interest in a lease and tolerates a lessee's occupation subject to the terms of the original lease is making a positive act that counts as a supply (paragraphs 78 to 79).

If the government compulsorily acquires land from a land-owner under operation of law, and offers compensation to the land-owner, there is no supply. The mere fact that the land-owner accepts the compensation without disputing the acquisition does not make the acquisition a supply to the government (paragraph 81).

***Proposition 6: "Supply" usually, but not necessarily, requires something to be passed from one entity to another***

Not all types of supplies require something to be passed from one entity to another. For instance, the creation of a right (section 9-10(2)(e)) does not intrinsically require a passing of the right from one entity to another; yet it still counts as a supply (paragraph 92). The surrender of a right also does not involve the passing of a right from one entity to another.

***Proposition 7: An entity cannot supply to itself***

This proposition flows from proposition 6 (paragraph 95). Division 54 which allows an entity to register its branches separately for GST provides an exception to this proposition (paragraph 96). Section 54-40(2)(c) deems all transfers of anything by the GST branch to its parent entity (including other GST branches of the parent), that would have been supplies made by the branch if it were an entity, to be supplies made by the branch as a separate entity.

***Proposition 8: A supply cannot be made by more than one entity***

Where supplies are made by different suppliers, they cannot be fused together to make a single supply (*C & E Commrs v Wellington Private Hospital Ltd* [1997] BVC 251 at 252).

***Proposition 9: The creation of expectations alone does not result in a supply***

An agreement that does not bind the parties in some way is not sufficient to establish a supply by one party to the other unless there is something else, such as goods or other thing, passing between the parties (paragraph 99). Nevertheless, a supply can be made for consideration in the absence of binding obligations (paragraph 104).

A supply made for consideration constitutes a transaction and implies the existence of binding obligations between the supplier and recipient, irrespectively of whether the obligations are written or oral (paragraph 108).

If a restaurant receives tips from customers, for example, this counts as consideration for the supply of meals for GST purposes. However, if the restaurant passes these tips on to its employees, this merely forms part of the employee's income, and the GST Act will not apply (paragraphs 109 to 112).

***Proposition 10: It is necessary to analyse the actual transaction that occurs, not a hypothetical transaction or earlier or subsequent transaction***

A number of alternative methods may be used by a supplier to achieve an end result. However, in considering what the supply is, no reference should be made to the various alternative approaches to making the supply. Instead, only the manner in which the transaction has actually occurred should be examined (paragraph 112).

### **Part 3: Meaning of “supply” in tripartite transactions**

Although the propositions set out above are relevant to characterizing multi-party arrangements (paragraph 117), closer analysis of such arrangements may reveal a supply made to one entity but provided to another entity, two or more supplies being made, or a supply made and provided to one entity for third party consideration (paragraph 115).

In considering the meaning of “supply” in multi-party transactions, therefore, 6 further propositions have been put forward by the Commissioner. These are considered below.

***Proposition 11: Contract is logical starting point when working out entity making supply and recipient***

The starting point in analysing a given arrangement to determine who is making a supply to whom is to examine the underlying contractual relationships involved (paragraph 119).

***Proposition 12: Transactions that are neither based in an agreement that binds parties in some way, nor involve a supply of goods or some other thing, do not establish a supply***

This proposition reiterates the earlier proposition 9 in that an agreement that does not bind the parties in some way is not sufficient to establish a supply by one party to the

other unless there is something else, such as goods or another thing, passing between the parties (paragraph 123).

***Proposition 13: When A contracts with B for a supply to be provided to C, there is a supply made by B to A (contractual flow) that B provides to C (actual flow)***

The word “made” in proposition 13 takes its meaning from the definition of “recipient” in section 195-1 (paragraph 131). The word “provide” is used in contrast with “made” as it differentiates between the contractual flow of the supply to the recipient (defined as the entity to whom the supply is “made”) and the actual flow of the supply to another entity (i.e. the entity to whom the supply is “provided”) (paragraph 132).

To illustrate this proposition, the Commissioner cites an example of ambulance services supplied to a hospital (paragraphs 157 to 160) where an ambulance service A, enters into an agreement with B, a hospital, which creates a binding obligation for the services by A as and when requested by B and for the payment of those services by B. Under the agreement, A transfers C, a patient, from hospital B to another hospital. The transfer of C is in the course of C’s treatment and B pays A to provide its services to C.

The recipient of A’s supply of ambulance services is hospital B. That is, A’s supply is “made” to B, but “provided” to C.

***Proposition 14: An entity that pays for a supply may not be its recipient***

Consideration for a supply does not have to come from the recipient of the supply (section 9-15(2)). To illustrate this proposition, the Commissioner uses the example of legal services and third party disbursements (paragraphs 205 to 212).

In this example, L, a law firm, is engaged by C, a client, to provide legal services. As part of the service agreement, prior to the provision of the legal services, C deposits money into L’s trust account. This money is treated as an advance for later

disbursements made by L, on behalf of C, and as security for future services made by L. L then advises C to seek the services of a third party, T.

C contracts with this third party directly. L, acting as agent for C, pays for T's services using funds from the trust account. The recipient of the supply of the service by T is C, not L. L is merely paying for a supply on C's behalf.

***Proposition 15: One set of activities may be the basis for making of two (or more) supplies***

To illustrate this proposition, the Commissioner cites the famous UK VAT decision of *Customs and Excise Commissioners v Redrow Group plc* [1999] BVC 96 (*Redrow*) as authority for the principle that one set of actions can constitute two different supplies, or a single course of conduct by one party may constitute two or more supplies to different persons. In particular, in *Redrow's case*, both Redrow and the prospective purchaser contracted for an estate agent's services. Thus, the agent's activities resulted in the agent making a supply of services to both Redrow and the prospective purchaser.

***Proposition 16: The total fact situation will determine the supplier and the recipient***

Proposition 16 is linked to proposition 10. The Commissioner cites an English Court of Appeal decision in *Commissioners for Her Majesty's Revenue and Customs v Debenhams Retail plc* [2005] EWCA 892 (*Debenhams*) to illustrate this proposition.

The issue in *Debenhams' case* concerned the legitimacy of trading terms where, if a customer paid the retailer Debenhams by credit or debit card, 2.5% of the payment was said to be consideration for an exempt supply of card handling services by a separate card issuing company (DCHS).

It was held that there was no separate contract between Debenhams' customers and DCHS for which 2.5% of the sale price was being paid as "the natural interpretation of the course of events and documentation would therefore be that any card handling

(other than that covered by the agreement between the cardholder and his card issuer) was and remained the responsibility of the seller accepting the card in discharge of the price” (*Debenhams* at paragraph 42).

The Court of Appeal took into account the total fact situation and held there was no supply by DCHS to a customer. Debenhams made a supply to the customer for 100% of the payment by credit or debit card.

## **Conclusion**

The meaning of the term “supply” is central to the GST legislation. Most importantly, its meaning determines whether a taxable supply is being made by an entity, requiring the imposition of GST. Although the propositions set out in GSTR 2006/9 are not universal (as there are exceptions to their application), the ruling represents, in certain contexts and for particular transactions, a useful starting point for analysis. It is just a shame that the Commissioner has left it until now to issue a ruling on such a critical concept to the GST legislation.