Case note

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ATS PACIFIC: "BEYOND THE FOUR CORNERS" OF A CONTRACT

In the recent decision of *ATS Pacific Pty Ltd v Commissioner of Taxation* [2014] FCAFC 33, the Full Federal Court looked at the GST consequences of arrangements entered into between Australian tour operators, being the taxpayers, and non-resident travel agents. The Full Court's decision affirmed in part the earlier decision of Bennett J of the Federal Court in *ATS Pacific Pty Ltd v Commissioner of Taxation* [2013] FCA 341, but for different reasons.

In reaching its conclusions, the Full Federal Court (comprised of Edmonds, Pagone and Davies JJ) considered in detail the application of the GST-free provisions in s 38-190 of the *A New Tax System (Goods and Services Tax) Act 1999* (Cth) (GST Act) to the arrangements, while also providing some general commentary in relation to the identification and characterisation of supplies. One of the more interesting issues to emerge was the extent to which the nature of supplies can be determined with reference to the terms and conditions of a contract.

While the facts of the case relate specifically to tourism-related supplies, there are lessons to be learned from the judgment for all taxpayers and their advisers. The most significant of these is that when approaching fundamental questions as to the nature and character of a supply, it may be necessary to look "beyond the four corners" of a written contract.[1] A supply may encompass the performance of acts that don't arise as obligations under the express or implied terms of a contract. This outcome, which arises from the breadth of the definition of "supply" under s 9-10 of the GST Act poses challenges for taxpayers and GST compliance aspects, particularly where written contracts are relied on heavily for the identification and characterisation of supplies.

THE FACTS

The taxpayers, including ATS Pacific Pty Ltd (ATS) were inbound tour operators that made supplies to non-resident travel agents (NR Travel Agents).[2] ATS arranged for various tourism products to be provided to the customers of the NR Travel Agents (NR Tourists) by businesses operating in Australia (Australian Providers), including accommodation in hotels and serviced apartments, transport, transfers, car hire, tours, guides and meals (referred to collectively as the Products).[3]

The business of ATS was described by Bennett J in the first instance decision as follows:

> In essence … contracting for and making supplies to NR Travel Agents in relation to Products, which were then provided to NR Tourists by Australian Providers. The NR Travel Agents generally selected these Products through a website and software operated by ATS called Tourplan, and then compiled an itinerary for their NR Tourist clients that included the selected Products. Once the selection was made by the NR Travel Agent using Tourplan, ATS would book the requested Product with the Australian Provider, and charge the NR Travel Agent a fee that included the cost of the Product and a margin (the margin). ATS then paid the Australian Provider for the Product. The Product would be supplied by the Australian Provider to, and consumed by, the NR Tourist.[4]

[1] *ATS Pacific Pty Ltd v Commissioner of Taxation* [2014] FCAFC 33 at [39].

[2] There are two relevant taxpayers that were party to the proceedings, including ATS Pacific Pty Ltd (ATS) which was the relevant taxpayer for the tax periods commencing 1 April 2004 through to 30 June 2007 and Stella Travel Services (Australia) Pty Ltd which was the head of a GST group that included ATS from the tax period commencing 1 July 2007 through to 30 June 2008. The terminology adopted by Bennett J in the first instance decision has been used to denote the relevant parties and terms. "ATS" denotes the relevant taxpayer for all periods.

[3] *ATS Pacific Pty Ltd v Commissioner of Taxation* [2013] FCA 341 at [7].

[4] *ATS Pacific Pty Ltd v Commissioner of Taxation* [2013] FCA 341 at [6]; cited by Edmonds J in *ATS Pacific Pty Ltd v Commissioner of Taxation* [2014] FCAFC 33 at [7].

The dealings and arrangements between ATS and the NR Travel Agents, while primarily occurring by electronic means via the website of ATS Pacific Pty Ltd known as Tourplan, were also carried out, in some cases, by XML link or email.[5]

The agent area of the website contained a link to a web page which included the terms and conditions (Terms and Conditions).[6] ATS relied on the Terms and Conditions, which were available on Tourplan, as representing the terms of the contract between ATS and the NR Travel Agents.[7] The Commissioner argued that the Terms and Conditions did not contain all of the terms of the contract.[8] Relevantly, the contracts did not specify either that ATS would provide the Products itself or that ATS would arrange for those Products to be provided by the Australian Providers.[9]

After confirmation of a booking, passenger information documentation was prepared by ATS or the NR Travel Agent to be given to the NR Tourist before their Australian tour.[10] The agent area of the ATS website listed the details that were required to be included on passenger information documentation.[11] Each tourist was then provided with a unique booking number that was quoted to the Australian Provider, to confirm their identity as the person to be provided with the Products.[12]

The GST in dispute concerned only transactions with those NR Travel Agents which did not have specific written contracts with ATS.[13]

ATS issued tax invoices to the NR Travel Agents in respect of the Products booked and arranged by it under its contracts with the NR Travel Agents.[14] The tax invoices were for a total amount that represented the amount that ATS would be required to pay to the Australian Providers upon their provision of the selected Products to the NR Tourists, plus the margin.[15] The margin was calculated as a percentage of the amounts ATS was liable to pay the Australian Providers.[16] The tax invoices generally stated:

> This invoice covers the cost of supplying the goods and services listed above and our services in arranging these supplies on your behalf.

Once ATS and the NR Travel Agent had agreed on the details of the Products that would be booked, ATS entered into contracts with the relevant Australian Providers. These Australian Providers then provided the Products to the NR Tourist.[17]

The central issue to be decided was whether or not the supplies made by ATS to the NR Travel Agents were GST free under s 38-190 of the GST Act.

THE RELEVANT LEGISLATIVE PROVISIONS

"Supply" is defined in s 9-10 in the widest possible terms. Relevantly, s 9-10(1) states that "[a] ***supply*** is any form of supply whatsoever".

Section 9-25 provides for the circumstances where supplies are connected with Australia in the

[5] *ATS Pacific Pty Ltd v Commissioner of Taxation* [2013] FCA 341 at [18].

[6] *ATS Pacific Pty Ltd v Commissioner of Taxation* [2013] FCA 341 at [22].

[7] *ATS Pacific Pty Ltd v Commissioner of Taxation* [2013] FCA 341 at [72].

[8] *ATS Pacific Pty Ltd v Commissioner of Taxation* [2013] FCA 341 at [72].

[9] *ATS Pacific Pty Ltd v Commissioner of Taxation* [2013] FCA 341 at [80].

[10] *ATS Pacific Pty Ltd v Commissioner of Taxation* [2013] FCA 341 at [23].

[11] *ATS Pacific Pty Ltd v Commissioner of Taxation* [2013] FCA 341 at [23].

[12] *ATS Pacific Pty Ltd v Commissioner of Taxation* [2013] FCA 341 at [23].

[13] *ATS Pacific Pty Ltd v Commissioner of Taxation* [2013] FCA 341 at [29].

[14] *ATS Pacific Pty Ltd v Commissioner of Taxation* [2013] FCA 341 at [36].

[15] *ATS Pacific Pty Ltd v Commissioner of Taxation* [2013] FCA 341 at [36].

[16] *ATS Pacific Pty Ltd v Commissioner of Taxation* [2013] FCA 341 at [36].

[17] *ATS Pacific Pty Ltd v Commissioner of Taxation* [2013] FCA 341 at [33].

following way:

Supplies of goods wholly within Australia

(1) A supply of goods is ***connected with Australia*** if the goods are delivered, or made available, in Australia to the *recipient of the supply.

Supplies of goods from Australia

(2) A supply of goods that involves the goods being removed from Australia is ***connected with Australia***.

Supplies of goods to Australia

(3) A supply of goods that involves the goods being brought to Australia is ***connected with Australia*** if the supplier either:

(a) imports the goods into Australia; or

(b) installs or assembles the goods in Australia.

Supplies of real property

(4) A supply of *real property is ***connected with Australia*** if the real property, or the land to which the real property relates, is in Australia.

Supplies of anything else

(5) A supply of anything other than goods or *real property is ***connected with Australia*** if:

(a) the thing is done in Australia; or

(b) the supplier makes the supply through an *enterprise that the supplier *carries on in Australia; or

(c) all of the following apply:

(i) neither paragraph (a) nor (b) applies in respect of the thing;

(ii) the thing is a right or option to acquire another thing;

(iii) the supply of the other thing would be connected with Australia.

Example: A holiday package for Australia that is supplied overseas might be connected with Australia under paragraph (5)(c).

Section 9-30(1) provides:

GST-free

(1) A supply is ***GST-free*** if:

(a) It is GST-free under Division 38 or under a provision of another Act; or

(b) It is a supply of a right to receive a supply that would be GST-free under paragraph (a).

"Real property" is defined at s 195-1 of the GST Act as follows:

real property includes:

(a) any interest in or right over land; or

(b) a personal right to call for or be granted any interest in or right over land; or

(c) a licence to occupy land or any other contractual right exercisable over or in relation to land.

The relevant section under which ATS contended that any supplies made by it are GST-free is s 38-190, which provides, relevantly, as follows:

Supplies of things, other than goods or real property, for consumption outside Australia

(1) The third column of this table sets out supplies that are ***GST-free*** (except to the extent that they are supplies of goods or *real property):

Supplies of things, other than goods or real property, for consumption outside Australia		
Item	**Topic**	**These supplies are GST–free (except to the extent that they are supplies of goods or *real property)…**
1	…	…

Supplies of things, other than goods or real property, for consumption outside Australia		
Item	**Topic**	**These supplies are GST–free (except to the extent that they are supplies of goods or *real property)…**
2	Supply to *non–resident outside Australia	a supply that is made to a *non–resident who is not in Australia when the thing supplied is done, and: (a) the supply is neither a supply of work physically performed on goods situated in Australia when the work is done nor a supply directly connected with *real property situated in Australia; or (b) the *non–resident acquires the thing in *carrying on the non–resident's *enterprise, but is not *registered or *required to be registered.
3	…	
4	…	
5	…	

(2) However, a supply covered by any of items 1 to 5 in the table in subsection (1) is *not* GST-free if it is the supply of a right or option to acquire something the supply of which would be *connected with Australia and would not be *GST-free.

(2A) A supply covered by any of items 2 to 4 in the table in subsection (1) is *not* *GST-free if the acquisition of the supply relates (whether directly or indirectly, or wholly or partly) to the making of a supply of *real property situated in Australia that would be, wholly or partly, *input taxed under Subdivision 40-B or 40-C.

Note: Subdivision 40-B deals with the supply of premises (including a berth at a marina) by way of lease, hire or licence. Subdivision 40-C deals with the sale of residential premises and the supply of residential premises by way of long term lease.

(3) Without limiting subsection (2) or (2A), a supply covered by item 2 in that table is *not* GST-free if:

(a) it is a supply under an agreement entered into, whether directly or indirectly, with a *non-resident; and

(b) the supply is provided, or the agreement requires it to be provided, to another entity in Australia.

THE SAGA HOLIDAYS CASE

As highlighted by the Full Court, the *ATS Pacific* case was the second case to come before the Full Court involving issues relating to the correct construction and application of the GST law with respect to inbound tour packages.[18] The earlier case, referred to at length in both the primary judgment and on appeal, is *Saga Holidays Ltd v Commissioner of Taxation* (2006) 156 FCR 256 (*Saga Holidays*).[19] In that case, the Full Court considered the correct GST treatment of inbound tour packages from the perspective of a non-resident tour package provider (Saga) making supplies to its non-resident customers of packages that included accommodation and other goods and services provided in Australia.[20]

While Saga was a tour package company incorporated in the United Kingdom, as distinct from the Australian resident taxpayers in the *ATS Pacific* case, the issues that arose in both cases are similar in that they require an examination of the GST provisions as they apply to the way in which inbound

[18] *ATS Pacific Pty Ltd v Commissioner of Taxation* [2014] FCAFC 33 at [1].

[19] This was an appeal from the Federal Court decision of *Saga Holidays Ltd v Commissioner of Taxation* (2005) 149 FCR 41 (Conti J).

[20] *Saga Holidays Ltd v Commissioner of Taxation* (2006) 156 FCR 256 at [2].

tourism is frequently "packaged", both inside and outside Australia.[21] In those circumstances, it is appropriate to recap on the issues resolved in *Saga Holidays*.

The *Saga Holiday* case primarily concerned the proper characterisation of the accommodation component of the Australian holiday packages. The main issues were:

- whether the accommodation component was merely incidental to the overall supply of a right to the performance of the contract as a whole and, therefore, not determinative of the characterisation of the supply for GST purposes;
- whether the accommodation component, if not incidental to the supply of a right to performance of the contract as a whole, included a supply of real property (as defined in the GST Act) and, therefore, connected with Australia under s 9-25(4) and taxable under s 9-5, or whether it was a supply of a right to acquire real property and not connected with Australia;
- if the supply of the accommodation component was a supply of real property that was connected to Australia, whether the supply comprised one taxable supply of real property or a supply of real property and other GST-free supplies, including the various other services and facilities provided alongside the accommodation. The other components "included the use of furniture and facilities within each room, cleaning and linen service, access to common areas and facilities of the hotels such as pools and gymnasiums and various other hotel services such as porterage and concierge".[22]

The supply and the contract as a whole

The Full Court rejected the argument put forward by Saga that the accommodation component was merely incidental to the overall right to execution of the contract (and, in doing so, upheld the decision of the primary judge).[23] Saga had argued that the contract did not involve a supply of real property and that Saga supplied a single right which was the performance of the contract as a whole.[24] Stone J held that the primary judge's conclusion "is entirely consistent with proper contractual analysis taking into account the statutory definitions contained in the GST Act".[25]

In reaching this conclusion, the Full Court referred to the definition of real property in the GST Act, which relevantly includes "a licence to occupy land or any other contractual right exercisable over or in relation to land", which the Full Court viewed as an extension of the ordinary meaning of real property. In this respect, Stone J (who delivered the principal judgment with which Gyles and Young JJ agreed) stated at [36]:

> The definition of "real property" in the GST Act is, however, not confined to interests that would warrant that description under the general law. Indeed the definition goes well beyond even mere proprietary interests and encompasses interests that are purely contractual as well as personal interests which may or may not have arisen under contract; Sterling Guardian at [37]. For instance, s 195-1(c) includes as real property, "a licence to occupy land" or "any other contractual right exercisable over or in relation to land". A licence to occupy land is not proprietary (*Cowell v The Rosehill Racecourse Company Limited* [1937] HCA 17; (1937) 56 CLR 605) although it may be coupled with the grant of a proprietary interest in land (*Australian Softwood Forests Proprietary Limited v Attorney-General (NSW)* [1981] HCA 49; (1981) 148 CLR 121.

Her Honour also placed weight on the fact that the concept of supply in the GST Act is very broad and that the contract was still binding, even though it was an executory contract with the supply of the

[21] *ATS Pacific Pty Ltd v Commissioner of Taxation* [2014] FCAFC 33 at [2].

[22] *ATS Pacific Pty Ltd v Commissioner of Taxation* [2014] FCAFC 33 at [41].

[23] *Saga Holidays Limited v Commissioner of Taxation* [2006] FCAFC 191 [33].

[24] *Saga Holidays Limited v Commissioner of Taxation* [2006] FCAFC 191 [32]-[33].

[25] *Saga Holidays Limited v Commissioner of Taxation* [2006] FCAFC 191 [33].

promised accommodation still to be provided. Stone J held that the contract between Saga and the tourist can be accurately described as including "a contractual right exercisable … in relation to land".[26]

The accommodation component of Saga's supply

Having accepted that the contract between Saga and the tourist involved a contractual right exercisable in relation to land and was, therefore, a supply of real property for the purposes of the GST Act, the second issue to be determined by the Full Court was whether the land in question had a sufficient connection to Australia as set out in s 9-25(4).[27] Even though the land in question had not been allocated at the time of the contract, the court proceeded on the basis that it was clear that the contract required that the land be "in Australia". The court said it was only necessary for there to be a taxable supply if there was a supply within the meaning of s 9-10.[28] Stone J held that the width of the definition of "supply" is enough to show that the contract involved a taxable supply of "real property" connected with Australia.[29]

Accommodation component incidental to other elements of the supply

The Full Court turned its attention to Saga's alternative submission that if the accommodation component was a supply of real property, it was in fact incidental to the actual supply of the tour.[30] Stone J agreed with the primary judge on this issue, in rejecting Saga's contention that s 96-5(4) applied. Stone J observed that s 96-5 is concerned with the supply made under the contract, rather than the purpose of the contract. Thus, in finding that the elements of the supply that Saga agreed to provide to the tourist[31] aside from accommodation were mainly transport and meals, there was no reason to characterise accommodation as subordinate or incidental to these items.[32]

In support of Saga's argument that "where a supply is, from an economic point of view, a single service, it is inappropriate to consider individually the constituent elements of that service",[33] Saga contended that the contract between it and the tourist was comprised of a number of components in addition to the right to occupy a room and, therefore, did not involve the supply of real property.[34] Saga argued that if you looked at the essential, overall character of the provision of a room, it is properly seen as accommodation services and "not the provision of a contractual right exercisable in relation to land".[35]

The Full Court, in line with the decision of the primary judge and the arguments of the Commissioner, agreed "that the accommodation component is a single supply which is properly characterised as a supply of real property".[36] Consequently, the value of the supply of real property did not need to be distinguished for the purpose of calculating supplies that are only partly connected with Australia under s 96-10 of the GST Act.

Prior to the Federal Court decisions having been handed down in *Saga Holidays*, amendments were introduced to the GST Act by the *Tax Laws Amendment (2005 Measures No 1) Act 2005*, which

[26] *Saga Holidays Ltd v Commissioner of Taxation* [2006] FCAFC 191 [37]-[38].

[27] *Saga Holidays Ltd v Commissioner of Taxation* [2006] FCAFC 191 at [45].

[28] *Saga Holidays Ltd v Commissioner of Taxation* [2006] FCAFC 191 at [45].

[29] *Saga Holidays Ltd v Commissioner of Taxation* [2006] FCAFC 191 at [46].

[30] *Saga Holidays Ltd v Commissioner of Taxation* (2006) 156 FCR 256 at [48].

[31] *Saga Holidays Ltd v Commissioner of Taxation* (2006) 156 FCR 256 at [58].

[32] *Saga Holidays Ltd v Commissioner of Taxation* (2006) 156 FCR 256 at [54].

[33] *Saga Holidays Ltd v Commissioner of Taxation* (2006) 156 FCR 256 at [41].

[34] *Saga Holidays Ltd v Commissioner of Taxation* (2006) 156 FCR 256 at [41].

[35] *Saga Holidays Ltd v Commissioner of Taxation* (2006) 156 FCR 256 at [41].

[36] *Saga Holidays Ltd v Commissioner of Taxation* (2006) 156 FCR 256 at [43].

commenced on 29 June 2005.[37] But the *Saga Holidays* case was not a case where subsequent amendments were relied on to clarify the effect of the pre-amendment provisions. The Full Court considered that the same outcome could be arrived at by "entirely conventional analysis".[38]

FIRST INSTANCE DECISION IN ATS PACIFIC

The *ATS Pacific* case involved the proper characterisation of a different step of the way in which inbound tourism is "packaged"[39] to that in *Saga Holidays*. Specifically, the issue was the proper characterisation of the supply by Australian travel agents or tour operators to NR Travel Agents (like Saga) in booking or arranging accommodation, goods and services for the customers of the NR Travel Agents, namely, the NR Tourists.[40]

The question for the primary judge was whether the supply could properly be characterised as the supply of the booking and arranging of Products, the supply of the Products, the supply of a promise of performance, or an assignment of rights.[41]

ATS argued that it only supplied a booking and arranging service, which falls within item 2 of s 38-190(1) of the GST Act, and is therefore a GST-free supply.[42] In support of this argument, ATS stated that the consideration it was paid included "the cost of the services and our fee for arranging those services on your behalf".[43] Those services ATS contended were to book the Australian Providers, as selected by the NR Tourists, which were to provide the Products to the NR Tourists.[44]

The Commissioner relied heavily on the contractual relationship between ATS and the NR Travel Agents in arguing that the "correct characterisation of ATS' supplies to the NR Travel Agents is the supply of the Products themselves".[45]

In determining the nature of the contract entered into between ATS and the NR Travel Agents, Bennett J looked beyond the express terms of the written contract to the broader understanding between the parties. Her Honour found that there was an implied contractual term that ATS would provide, or ensure provision of, the Products to the NR Tourists, consistent with guidance in *BP Refinery (Westernport) Pty Ltd v Shire of Hastings* (1977) 180 CLR 266 at 283 as to when a contractual term should be implied.[46]

Her Honour therefore decided the following at [122]-[123]:

> There was no promise or express condition that ATS would ensure that Products were provided to [NR Tourists] when they came to Australia. Equally there is no explicit support for the obligation of arranging a Product. However, when all of the relevant facts and circumstances are considered, the inference is that there was a promise, relevantly, that ATS would ensure that when the NR Tourists came to Australia and, for example, arrived at a hotel, they would be provided with a room which they believed that they had paid for in advance.
>
> Accordingly, I accept the Commissioner's submission that in order to fulfil its obligations, ATS supplied the NR Travel Agent with a contractual right or promise that the Australian Providers would provide the Products to the NR Tourist. The critical supply was the supply made by ATS to the NR Travel Agent, which was a component of a packaged tour or a right thereto, which also included a contractual promise to the NR Travel Agent that ATS would ensure that the Products were supplied to the [NR Tourists].

[37] *Saga Holidays Ltd v Commissioner of Taxation* (2006) 156 FCR 256 at [7].

[38] *Saga Holidays Ltd v Commissioner of Taxation* (2006) 156 FCR 256 at [32].

[39] *Saga Holidays Ltd v Commissioner of Taxation* (2006) 156 FCR 256 at [2].

[40] *ATS Pacific Pty Ltd v Commissioner of Taxation* [2014] FCAFC 33 at [2].

[41] *ATS Pacific Pty Ltd v Commissioner of Taxation* [2013] FCA 341 at [67].

[42] *ATS Pacific Pty Ltd v Commissioner of Taxation* [2013] FCA 341 at [68]-[69], [131].

[43] *ATS Pacific Pty Ltd v Commissioner of Taxation* [2013] FCA 341 at [69].

[44] *ATS Pacific Pty Ltd v Commissioner of Taxation* [2013] FCA 341 at [69].

[45] *ATS Pacific Pty Ltd v Commissioner of Taxation* [2013] FCA 341 at [79].

[46] *ATS Pacific Pty Ltd v Commissioner of Taxation* [2013] FCA 341 at [84], [89].

Having found that the supply made by ATS was the contractual right or promise that the accommodation would be provided to the NR Tourists by an Australian Provider, and not a supply of the accommodation itself, her Honour then addressed whether the supply characterised as such was a supply of real property. Her Honour found that this was still a supply of real property under the expanded definition in the GST Act, which includes "any contractual right exercisable over or in relation to land". This was consistent with the earlier decision in the *Saga Holidays* case.[47] As supplies of real property are excluded from the application of s 38-190(1), the supplies were found not to be GST-free.

In reaching this conclusion her Honour considered the wording of s 38-190(1) which sets out supplies that are GST-free "except to the extent that they are supplies of goods or real property" and the further exemptions to that section in subsections 38-190(2) and (3).[48]

In relation to the supply of real property, ATS contended that even if it made a promise that it would ensure that Australian Providers provided Products, including rooms, to NR Tourists, as part of its arranging services this did not amount to real property within the scope of s 38-190.[49]

Further, ATS argued that the supply of non-accommodation services was GST-free, as it was not subject to any of the exclusions set out in s 38-190.[50] ATS further argued that if there was a supply by way of a promise that it would provide Products to the NR Tourists, the service was neither a supply of work physically performed on goods situated in Australia when the work was done nor a supply connected with real property in Australia.[51]

The Commissioner, on the other hand, argued that the supply in relation to the accommodation was a supply of real property under the statutory definition and, therefore, s 38-190 could not apply. The other supplies, he argued, could not be GST-free under s 38-190(1) as s 38-190(2) operates so as to make the supply taxable because it is a supply of a right or option to acquire something that would otherwise be taxable and connected to Australia.[52] The Commissioner further argued that the supply by ATS of the arranging of the Products to be provided was incidental to the supply of the Products themselves.

Bennett J went on to find that the other components of the tours and transportation were supplies of goods and services that were not GST-free under s 38-190.[53] However, her Honour disagreed with the Commissioner's argument that both the Products and the arranging services performed by ATS were a single supply. In this respect, her Honour found at [149]-[150]:

> I reject the Commissioner's submissions as to the characterisation of the margin. The contract with the NR Travel Agents makes a distinction between the Products supplied and ATS' fee for arranging for that supply. As such, there were two separate supplies: the Products and the supply of ATS' arranging services. The consideration for the latter was the margin. That fee was not consideration for the supply of the Products. It is clear that ATS charged an independent percentage margin for arranging for the Products. If the Products were not supplied by the Australian Provider, ATS refunded the cost of the Products. It did not refund the margin.
>
> The arranging service supplied by ATS was not merely ancillary or incidental to the supply of the Products. The NR Travel Agents contracted expressly with ATS on the basis that they were obtaining the arranging services supplied by ATS in addition to the Products supplied to their clients. The arranging service constituted an object for the NR Travel Agents and a service for its own sake. It does not contribute to the proper performance of the Products.

[47] *Saga Holidays Ltd v Commissioner of Taxation* [2006] FCAFC 191 at [36].

[48] *ATS Pacific Pty Ltd v Commissioner of Taxation* [2013] FCA 341 at [132].

[49] *ATS Pacific Pty Ltd v Commissioner of Taxation* [2013] FCA 341 at [135].

[50] *ATS Pacific Pty Ltd v Commissioner of Taxation* [2013] FCA 341 at [137].

[51] *ATS Pacific Pty Ltd v Commissioner of Taxation* [2013] FCA 341 at [140].

[52] *ATS Pacific Pty Ltd v Commissioner of Taxation* [2013] FCA 341 at [143].

[53] *ATS Pacific Pty Ltd v Commissioner of Taxation* [2013] FCA 341 at [138]-[139].

Her Honour therefore found that the arranging service, for which the margin charged by ATS to the NR Travel Agents was consideration, was a GST-free supply under s 38-190.[54]

THE FULL FEDERAL COURT'S JUDGMENT IN ATS PACIFIC

ATS appealed the decision of the primary judge to the Full Court, raising on appeal the issue of the proper characterisation of the taxpayer's supplies to the NR Travel Agents for the purposes of s 38-190 of the GST Act. The central issue on the appeal was described by the Full Court as follows:

> In the face of the primary judge's conclusion below, the issue here is whether the primary judge erred, as ATS contends her Honour did, in not characterising the supplies made to the NR Travel Agent as a single GST-free supply of "booking or arranging services" in respect of which the consideration received by ATS was wholly attributed.[55]

The Commissioner cross-appealed, raising the following issue for determination:

> whether the primary judge erred, as the Commissioner contends her Honour did, in finding that ATS made GST-free supplies of booking and arranging services to NR Travel Agents for the separate consideration of the margin.[56]

Identification of a supply and characterisation of that supply

The first step taken by the Full Court was to identify the supply made by ATS to the NR Travel Agents and to determine the correct characterisation of that supply: "Characterisation" sometimes refers to the determination of the GST treatment of a supply; for example, GST-free or taxable. Here, his Honour Edmonds J uses the term "characterisation" in reference to the nature of the supply itself as, for example, a supply of real property or a supply of rights. (The question of whether the supplies were GST-free is discussed further below). The identification of a supply was described by Edmonds J as "a mixed question of fact and law", whereas the characterisation of that supply is "undoubtedly a question of fact".[57]

In characterising the supply from ATS to the NR Travel Agents, the Full Court took a different approach to the primary judge, which nonetheless led to a similar outcome for GST purposes. Specifically, Edmonds J, with whom Pagone and Davies JJ agreed, did not consider it necessary to find an implied term in the contract between the parties in order to find that the supply from ATS to the NR Travel Agents encompassed a promise that ATS would arrange for the Australian Providers to provide the Products to the NR Tourists. This is because the reality of what supply has been made from one party to another, as a matter of fact, is not confined to the written terms of what was agreed under a contract.[58] Edmonds J stated in this regard at [29]:

> The terms and conditions are the instrumentality through which the supply is made, but the text of these terms and conditions is not conclusive of the character of the supply that is made; that will depend as much on the manner of performance of those terms and conditions as the text of the terms and conditions themselves; it will also depend on the commercial or business purposes, discerned objectively, of those who have entered into the relevant contract.

His Honour also pointed out that the present case can be contrasted to cases such as *Federal Commissioner of Taxation v Reliance Carpet Co Pty Ltd* (2008) 236 CLR 342 and *Federal Commissioner of Taxation v Qantas Airways Ltd* (2012) 247 CLR 286 (*Qantas*) where the relevant supply occurred upon entry into the contract. In circumstances where the supply is made pursuant to a standalone executory contract, the terms and conditions will be central to the identification of the

[54] *ATS Pacific Pty Ltd v Commissioner of Taxation* [2013] FCA 341 at [149].

[55] *ATS Pacific Pty Ltd v Commissioner of Taxation* [2014] FCAFC 33 at [9].

[56] *ATS Pacific Pty Ltd v Commissioner of Taxation* [2014] FCAFC 33 at [10].

[57] *ATS Pacific Pty Ltd v Commissioner of Taxation* [2014] FCAFC 33 at [38].

[58] *ATS Pacific Pty Ltd v Commissioner of Taxation* [2014] FCAFC 33 at [32].

supply.[59] In respect of such supplies, Edmonds J stated:

> Undoubtedly, where the supply is made pursuant to the performance of a stand-alone executory contract between B and C which is totally unrelated to any other contract either B or C has entered into, an analysis of the terms and conditions of that contract will shed considerable light on the character of the supply made between B and C.[60]

Here, however, the performance by the Taxpayer of its obligations to the NR Travel Agents involved and was related to other arrangements entered into between ATS and the Australian Providers, between the NR Travel Agents and the NR Tourists and the provision of Products by the Australian Providers to the NR Tourists in Australia. Consequently, a broader view of the arrangements entered into between all these parties was necessary to determine the parameters of the supply.[61]

On the present facts, it was understood between the parties that ATS would ensure provision of the Products to the NR Tourists in Australia, notwithstanding that this aspect of the arrangement was not set out in the terms and conditions of the contract. This was a finding of fact made by the primary judge.[62] The fact of these services having been performed was sufficient for them to constitute a supply. His Honour therefore stated at [39]:

> In determining the character of a supply – what was really supplied? – pursuant to performance of an executory contract, a court is not to be "handcuffed" by the terms embodied in the four corners of the contract, the more so if those terms and conditions do not represent all the terms and conditions of the contract; or where the contract is but one link in a chain of contracts, the performance of each being related to, if not dependent on, performance of the immediately preceding contract; or where, by reference to the factual matrix of the entirety of the arrangements, the commercial or practical reality points to the conferral or provision of a supply which goes beyond the conclusion that might otherwise be drawn from a confined analysis of the terms and conditions of one contract in that chain.

On a related note, his Honour found that there would be significant practical difficulties associated with characterising supplies with reference to what terms can or cannot be implied into a contract, particularly in the GST context. His Honour stated at [33]:

> Secondly, I do not think it is desirable, in the interests of certainty of application of a revenue statute, for the characterisation of a supply made by performance of an executory contract, to depend upon whether or not a term can be implied into the contract, unless it is absolutely essential to give business efficacy to the contract. In this day and age, revenue statutes are inherently complex, and the GST Act is certainly no exception. The concept of a "supply", as defined in s 9-10 of the GST Act, is fundamental to the operation of that Act and has greatly contributed to that uncertainty, both in terms of identifying whether a "taxable supply" has occurred (*Qantas Airways Ltd*), but more importantly, on the premise that a supply has occurred, in determining how that supply is to be characterised (*Travelex Ltd v Federal Commissioner of Taxation* (2010) 241 CLR 510). Resort to jurisprudence in contract law to imply a term into a contract does not contribute to an aspirational hope, let alone a confident expectation, of certainty of application going forward.

On this basis, the Full Court found that it was open to the primary judge to conclude that the supply made by ATS to the NR Travel Agents included the promise that when NR Tourists came to Australia, they would be provided with the relevant Products, notwithstanding that the promise was

[59] *ATS Pacific Pty Ltd v Commissioner of Taxation* [2014] FCAFC 33 at [40].

[60] *ATS Pacific Pty Ltd v Commissioner of Taxation* [2014] FCAFC 33 at [40].

[61] *ATS Pacific Pty Ltd v Commissioner of Taxation* [2014] FCAFC 33 at [40].

[62] *ATS Pacific Pty Ltd v Commissioner of Taxation* [2014] FCAFC 33 at [30].

not specified in the terms and conditions of the contract.[63] ATS led no evidence to contradict this finding, and the Full Court was satisfied that this conclusion was consistent with the "commercial reality" of the transaction.[64]

His Honour Pagone J agreed with the conclusions of Edmonds J, but provided some additional comments, referring to earlier High Court cases that have required a determination of whether a supply is a supply of a right to a thing or a supply of the thing itself, including *Travelex Ltd v Federal Commissioner of Taxation* (2010) 241 CLR 410 (*Travelex*) and the *Qantas* case.

His Honour quoted at [71] from the *Travelex* case at [521], where French CJ and Hayne J concluded in respect of a supply of foreign currency as follows:

> Observing that rights attach to currency, and pass upon negotiation of the currency by delivery, does not constitute any "juristic disaggregation and classification of rights" that fails to reflect "the practical reality of what is in fact supplied". On the contrary, recognising that a sale of foreign currency transfers to the purchaser the rights that attach to the notes does no more than recognise the evident purpose of the transaction. Further classification or identification of the rights that pass, whether as rights against an issuing central bank, or as rights akin to those of the holder of a promissory note, is not necessary. What the Act requires is that there be a supply "in relation to" rights; the operation of the Act does not call for attention to be given to the particular content of the rights.

Further, his Honour cited Heydon J at [524] in the *Travelex* case

> The supply of the currency was a supply in relation to the rights it gave because these rights constituted the pith and substance of the transaction.

Turning to the *Qantas* case, Pagone J observed that the High Court held that what was "at least a promise to use best endeavours to carry the passenger and baggage, having regard to the circumstances of the business operations of the airline" constituted a supply for consideration, notwithstanding that this supply was not expressly stated in the written terms and conditions of the agreement between Qantas and its customers.[65]

These cases supported his Honour's conclusion that the primary judge was not in error in looking beyond the terms and conditions of the contract to identify, from a practical business perspective, the substance of the transaction and the nature and character of the supply.

Other revenue contexts

Edmonds J considered how questions of determination and characterisation have been approached in other revenue law contexts to support his conclusions as to the identification and characterisation of the supply between ATS and the NR Travel Agents. His Honour considered how the "source" of income has been approached in the income tax context in cases such as *Nathan v Federal Commissioner of Taxation* (1918) 25 CLR 183 (*Nathan*) and *Thorpe Nominees Pty Ltd v Federal Commissioner of Taxation* (1988) 19 ATR 1834 at 1846 (*Thorpe Nominees*), stating that although supply is defined in s 9-10 of the GST Act, the word "source" has no technical or precise definition:

> the determination of the characterisation of the supply in a case such as the present is as much a matter of practical or business reality as the determination of the origin of income – where it comes from – in a case of the kind before the Full Court in *Thorpe Nominees*.[66]

Consequently, his Honour cited the following guidance in the *Nathan* case as to the determination of "source":

> The Legislature in using the word "source" meant, not a legal concept, but something which a practical man would regard as a real source of income. Legal concepts must, of course, enter into the question

[63] *ATS Pacific Pty Ltd v Commissioner of Taxation* [2013] FCA 341 at [22]; *ATS Pacific Pty Ltd v Commissioner of Taxation* [2014] FCAFC 33 at [37].

[64] *ATS Pacific Pty Ltd v Commissioner of Taxation* [2014] FCAFC 33 at [37].

[65] *ATS Pacific Pty Ltd v Commissioner of Taxation* [2014] FCAFC 33 at [71].

[66] *ATS Pacific Pty Ltd v Commissioner of Taxation* [2014] FCAFC 33 at [43].

> when we have to consider to whom a given source belongs. But the ascertainment of the actual source of a given income is a practical, hard matter of fact.[67]

The following passage from the *Thorpe Nominees* case was also referred to as guidance in determining the practical or business "reality" of a transaction:

> Practical reality is not a test so much as an attitude of mind in which the court should approach the task of judgment. Reality, like beauty, is often in the eye of the beholder (cf the commens [sic] made by J D Jackson in an article in 51 Mod LR 549 at 557 et seq). What the cases require is that the truth of the matter be sought with an eye focused on practical business affairs, rather than on nice distinctions of the law. For the word "source", in this context, has no precise or technical reference. It expresses only a general conception of origin, leading the mind broadly, by analogy. The true meaning of the word evokes springs in grottos at Delphi, sooner than the incidence of taxes. So the exactness which the lawyer is prone to seek must be consciously set aside; indeed, with respect to a choice between various contributing factors, it cannot be attained. The substance of the matter, metaphorically conveyed when we speak of the source of income, is a large view of the origin of the income – where it came from – as a businessman would perceive it.[68]

Finally, his Honour considered how the High Court has approached characterisation in the context of determining whether an outgoing is on capital or revenue account, citing the following passage from *Hallstroms Pty Ltd v Federal Commissioner of Taxation (Cth)* (1946) 72 CLR 634 at 648:

> What is an outgoing of capital and what is an outgoing on account of revenue depends on what the expenditure is calculated to effect from a practical and business point of view, rather than upon the juristic classification of the legal rights, if any, secured, employed or exhausted in the process.

Consideration of these cases and, in particular, the emphasis on taking into account the practical, business reality of an arrangement or transaction, led his Honour to conclude that there was no error by the primary judge in looking beyond the terms and conditions of the written contract to the broader arrangement between the parties in identifying and characterising the supply.

Policy considerations

Reference is made in the Full Court's decision to policy considerations and the intended outcomes of the provisions as they apply to tourism related supplies. In particular, Edmonds J referred at [2] to the Explanatory Memorandum to the *A New Tax System (Goods and Services Tax) Bill 1998* which, relevantly, stated the following at para 12:

> **Tourists**
>
> Goods and services consumed by tourists in Australia, such as meals and hotel accommodation are subject to GST under the general rules. International air and sea travel is GST-free, as is any domestic air travel purchased overseas by non-residents. Tourists and Australian residents going overseas are able to recover the GST they pay on goods purchased in Australia and taken away with them when they leave. It is proposed that refunds apply to purchases of at least $300 made from any one business within 28 days of departure.

It can be gleaned from this that there was clearly an intention to tax, within Australia, supplies of meals and hotel accommodation, which was the outcome contended for by the Commissioner in this case. The Full Court noted at [47] that the construction of the provisions advanced by ATS, on the other hand:

> would have run counter to the policy design objective of taxing consumption in Australia: if the contention had been accepted, it would have resulted in unintended non-taxation because ATS would have been entitled to recover the GST charged by the Australian Providers without having any corresponding output tax liability. The NR Travel Agent would therefore incur no GST on its purchase and since it would not be required to register, it would not have to account for GST on the supply to the NR Tourist.

[67] *ATS Pacific Pty Ltd v Commissioner of Taxation* [2014] FCAFC 33 at [41].

[68] *ATS Pacific Pty Ltd v Commissioner of Taxation* [2014] FCAFC 33 at [42].

While his Honour remarked that the outcome advocated by the Commissioner was consistent with these policy objectives, he rejected the assertion by ATS that the Commissioner's submissions suggested an a priori rather than purposive approach to construction.[69]

In passing, the Full Court observed at [3] that two GST cases have already arisen in respect of the taxation of package tours in Australia. Their Honours noted as follows:

> The advent of these two cases so early in the life of the GST says something about the difficulty of drafting legislation to give effect to the policy design of the GST, in the factual context of the way in which tours to Australia are packaged and sold to non-resident tourists…

Arguably, this difficulty is reflected in the complexity of s 38-190 of the GST Act (discussed below) and the many voluminous rulings issued by the Commissioner providing guidance as to how, on his view, that provision applies.[70]

The Application of s 38-190 of the GST Act

Having agreed with the primary judge's characterisation of the supply from ATS to the NR Travel agent as "the supply of a promise that it (ATS) would ensure that the Australian Providers would provide the Products to the NR Tourists when they came to Australia", the Full Court then turned to her Honour's conclusions as to the GST treatment of the supply. In doing so, their Honours rejected the approach of the primary judge in drawing a distinction between the arranging services supplied by ATS and the provision of the Products themselves, preferring the primary judge's previous identification and characterisation of the supply of rights, being the promise that those Products would be provided to the NR Tourists.[71] (This is discussed further below in the context of the Commissioner's cross-appeal.)

The first aspect of the supply dealt with by the Full Court was the accommodation component, in order to determine whether this comprised of real property and was therefore not GST-free under s 38-190(1). Section 38-190(1) states (in respect of all items set out in the table) that if the supply is a supply of goods or real property, it will not be GST-free under this provision.

As acknowledged by the Full Court in *Saga Holidays*, "real property" is defined in s 195-1 of the GST Act (extracted above) and is not to be interpreted with reference to its ordinary meaning. Under s 195-1, a supply of real property includes "any contractual right exercisable over or in relation to land".

The Full Court was satisfied that here, ATS did arrange for contractual rights in relation to land to be provided by the Australian Providers to the NR Tourists and that this was sufficient to constitute the promise of a supply "in relation to land" and, therefore, a supply of "real property" for the purposes of s 38-190. Consequently, the accommodation component was not GST-free under s 38-190 of the GST Act.

Turning to the other components of the supply, which were comprised of goods and services, Edmonds J noted that there is no equivalent definition to the definition of real property that applies to goods or services. Consequently, a promise from ATS to the NR Travel Agent that the Australian Provider will provide goods and services to the NR Tourist does not constitute a supply of goods and services for the purposes of s 38-190(1). If they were to fall within an item in the table in s 38-190(1) and not be excluded by virtue of s 38-190(2) or s 38-190(3), those supplies would be GST-free. His Honour then pointed to item 2(b) of the table as the most likely to be applicable, affording GST-free treatment where a supply is made to a non-resident who is not in Australia when the thing supplied is

[69] *ATS Pacific Pty Ltd v Commissioner of Taxation* [2014] FCAFC 33 at [47].

[70] See eg, GSTR 2003/8 Goods and services tax: supply of rights for use outside Australia - subsection 38-190(1), item 4, para (a) and subsection 38-190(2) and GSTR 2005/6 Goods and services tax: the scope of subsection 38-190(3) and its application to supplies of things (other than goods or real property) made to non-residents that are GST-free under item 2 in the table in subsection 38-190(1) of the *A New Tax System (Goods and Services Tax) Act 1999*.

[71] *ATS Pacific Pty Ltd v Commissioner of Taxation* [2014] FCAFC 33 at [61].

done and the non-resident acquires the thing in carrying on the non-resident's enterprise, but is not registered or required to be registered. The question then arose as to whether either of the exclusions applied.

First, his Honour considered the exclusion in s 38-190(3), which applies in circumstances where, (1) the supply is made under an agreement with a non-resident and (2) the supply is provided to another entity in Australia. Here, the Full Court was careful to apply both limbs to the supply as identified by the primary judge, stating at [56]:

> As a matter of statutory construction, it is indisputable that the supply referred to in the second limb is the supply referred to in the first limb. On the premise that the supply in the first limb is ATS' promise to the NR Travel Agents in the terms found by the primary judge, the second limb is not satisfied. In the context of inbound tourism to this country, the exclusion that is s 38-190(3) would seem to be confined to situations where the Australian Provider contracts directly with NR Travel Agents for the supply of Products to their NR Tourist clients in Australia.

In other words, while goods and services were clearly "provided to another entity in Australia", it was not those goods and services that formed the subject matter of the supply for the purposes of s 38-190(3) but, rather, the rights to the provision of those goods and services. As the supply of the rights was not provided to another entity within Australia, the s 38-190(3) exclusion did not apply.

The exclusion in s 38-190(2), however, excludes from GST-free treatment under s 38-190(1) a supply of a right to acquire something, the supply of which would be connected with Australia and not GST-free. His Honour concluded that this exclusion did apply, as the goods were connected with Australia under s 9-25(1) of the GST Act and the services were connected with Australia under s 9-25(5) and neither would be GST-free.

Consequently, the Full Court rejected ATS's appeal against the decision of the primary judge and concluded that none of the supplies made by ATS to the NR Travel Agents were GST-free under s 38-190 of the GST Act.

The cross appeal: single/multiple supply

As noted above, the Full Court disagreed with the primary judge's conclusion that ATS made two supplies to the NR Travel Agents, being the supply of the products (taxable) and the supply of the arranging services, which was GST-free. This was the subject of the Commissioner's cross-appeal.[72] His Honour, Edmonds J, found the primary judge's conclusions in this regard to be inconsistent with her findings as to the character of the supply as a supply of "rights" (not a supply of goods and services and a supply of real property only because rights to real property fall within the statutory definition). In this regard, his Honour stated at [61]:

> Fundamentally, it was not open to the primary judge to find or conclude that there were two supplies from ATS to NR Travel Agents, which her Honour characterised as the Products and the supply of ATS' arranging services, when it was not in dispute, either before her Honour or on appeal, that the Australian Providers supplied the Products, not ATS. Moreover, her Honour had already characterised what her Honour described as "[t]he critical supply" by ATS to the NR Travel Agents as being "a contractual promise to the NR Travel Agent that ATS would ensure that the Products were supplied to the tourists": R [123], and it was for that supply, for that promise, that the NR Travel Agents paid the consideration stipulated in ATS' invoice. In short, the dichotomy of supply arrived at by the primary judge was neither sourced in the respective positions of the parties, nor in her Honour's finding on "[t]he critical supply".

The primary judge might have considered whether other supplies or components of the supplies were ancillary or incidental to the "critical supply". The Full Court said this was a question that should have been approached from a "practical and business point of view: see *Westley Nominees Pty Ltd v Coles Supermarkets Australia Pty Ltd* (2006) FCR 461 at [59], rather than from any separate treatment

[72] *ATS Pacific Pty Ltd v Commissioner of Taxation* [2014] FCAFC 33 at [59].

or quantification in the text of the contract or related tax invoice".[73] In this regard, Edmonds J concluded that there was only one supply, being the supply of the promise. This, his Honour pointed out, was consistent with the policy design as evident in the Explanatory Memorandum.

Application for special leave to appeal to High Court

ATS has applied for special leave to appeal from the decision of the Full Federal Court to the High Court of Australia. The Commissioner has published an Interim Decision Impact Statement setting out his administrative treatment of similar supplies pending the finalisation of the High Court proceedings.[74]

Consequences for taxpayers

Taxpayers, in particular in-house tax managers who are asked to review contracts in isolation, must take care to ensure that they determine and characterise supplies being made with all the necessary facts, including the context of the arrangements. It is not sufficient to rely simply on the terms and conditions of the contract and, in fact, the relevant supply may, such as in the present case, be something that could never be read into the written agreement. As the Full Court did in this case, taxpayers must look beyond the four corners of a contract in order to determine the nature and character of supplies.

[73] *ATS Pacific Pty Ltd v Commissioner of Taxation* [2014] FCAFC 33 at [64].

[74] *Interim Decision Impact Statement ATS Pacific Pty Ltd v Commissioner of Taxation* (2 May 2014).