

GST ISSUES RE SETTLEMENTS AND JUDGMENTS

Gina Lazanas, Partner Balazs Lazanas & Welch LLP ¹

The *A New Tax System (Goods and Services Tax) Act 1999* (Cth) (the **GST Act**) provides that GST is payable on taxable supplies.² Three of the basic conditions for taxability are that there be a supply, that it be made for consideration, and that it be made in the course or furtherance of an enterprise carried on by the supplier.³

It is the first two, and, in particular the requirement that there be a supply, that complicate the application of the GST to settlements and judgments. As will be seen, the complications arise because of the interaction between the breadth of the definitions (of supply and consideration) in the GST Act.

Settlements and judgments involve the payment and/or the provision of property to an aggrieved party, and the question that arises is whether that party will have a GST liability. The basic problem involves identifying what could qualify as a relevant supply and whether the payment and/or provision of property can be said to be consideration *for* that supply.

Definitions

The starting point in the analysis of the issues is the legislative definitions and, more specifically, the concepts of supply and consideration.

Supply

Supply “is defined broadly and is intended to encompass supplies as widely as possible”⁴. The definition is contained in s.9-10 of the GST Act and relevantly provides as follows:

- “(1) A **supply** is any form of supply whatsoever.
- (2) Without limiting subsection (1), **supply** includes any of these: ...
 - (e) a creation, grant, transfer, assignment or surrender of any right;
 - (g) an entry into, or release from, an obligation:
 - (i) to do anything; or
 - (ii) to refrain from an act; or
 - (iii) to tolerate an act or situation.”

Consideration

Consideration in the GST Act is defined to include “any payment, or any act or forbearance, in connection with ..., in response to or for the inducement of a supply of anything”⁵. It “does not matter whether the payment, act or forbearance was voluntary, or whether it was by the recipient of the supply”⁶.

¹ Views expressed and any errors are those of the author. The assistance of Robyn Thomas of Balazs Lazanas & Welch LLP in the preparation of this paper is gratefully acknowledged.

² GST Act, ss.7-1 and 9-40. Unless otherwise stated, all legislative references in this paper are to the GST Act.

³ Section 9-5 of the GST Act. The supply must also be connected with Australia and be made by a supplier who is registered or required to be registered. The supply is not a taxable supply to the extent that it is GST-free or input taxed.

⁴ Parliament of the Commonwealth of Australia, House of Representatives, *Explanatory Memorandum to the A New Tax System (Goods and Services Tax) Bill 1998* (Cth) (*Explanatory Memorandum to the GST Bill*), at para. 3.6.

⁵ Subsection 9-15(1).

⁶ Subsection 9-15(2).

A specific provision dealing, *inter alia*, with settlements and court orders, was inserted in the definition of consideration by the *Indirect Tax and Consequential Amendments Act (No.2) 1999 (Cth)*⁷. It is as follows:

“It does not matter:

- (a) *whether the payment, act or forbearance was in compliance with an order of a court, or of a tribunal or other body that has the power to make orders; or*
- (b) *whether the payment, act or forbearance was in compliance with a settlement relating to proceedings before a court, or before a tribunal or other body that has the power to make orders.*⁸

The Explanatory Memorandum associated with this legislation provided that “[p]ayments, acts or forbearance constituting compensation or damages will be specifically included in the definition of consideration in the GST Act”⁹.

The above specific provision confirms that compulsory contributions are in the GST net. Such payments lie at one end of the broad spectrum of consideration with voluntary contributions at the other end.¹⁰ The inclusion of the provision can be seen as a reaction to certain views expressed in capital gains tax cases about related issues.¹¹

Identifying Relevant Supplies

The first and foremost issue that arises with respect to settlements and judgments is identifying the relevant supplies for GST purposes. This question will be considered initially in the context of settlements. Special considerations concerning judgments will be addressed later in this paper.

Substance and Form in Statutory Interpretation and Characterising Supplies

A plain reading of the definition of ‘supply’ leads one to say that the wording of the GST Act could obviously apply to many aspects of settlements and compromises. Furthermore, when an entity refrains from pursuing a legal action and settles with another, there is “no doubt” that a supply is being made and that the situation “fits neatly into the definition of ‘supply’ for GST purposes – specifically section 9-10(2)(g)(ii)”¹².

An approach which considers whether there is an underlying supply and stops there, without considering whether a surrender of rights can constitute a supply, appears in the Explanatory Memorandum that accompanied the Bill which inserted into the definition of consideration, s.9-15(2A), being the provision concerning settlements and court orders referred to above.¹³ So much appears from the following passages extracted from the relevant Explanatory Memorandum:

⁷ Section 3 and schedule 1, item 1.

⁸ Subsection 9-15(2A).

⁹ Parliament of the Commonwealth of Australia, House of Representatives, *Explanatory Memorandum to the Indirect Tax and Consequential Amendments Bill (No.2) 1999 (Cth)*.

¹⁰ However, one wonders to what extent the fact that a supply must be made “for” consideration to be taxable (s.9-5(a)) incorporates the notion of exchange.

¹¹ See, in particular, *Carborundum Realty Pty Ltd v RAlA Architecture Pt Ltd* (1993) 93 ATC 4418. At 93 ATC 4424 it was stated that “consideration ... has no place where, as here, the plaintiff will obtain the amount of its judgment debt by compulsory exaction from someone who has not agreed to pay it and who will receive nothing as a quid pro quo”. Also, at 93 ATC 4425 it was stated that “[i]n this case, the amount of money which the defendant must pay in order to eliminate the judgment debt will not be received by the plaintiff ‘as a result of or in respect of the disposal’ of that debt. When received, that amount will *effect* the disposal of the judgment debt – and will do so without there being anything received by the defendant (or given by the plaintiff) in return” (emphasis in original). The ATO did not accept this view, as is seen in Taxation Ruling TR 95/35 *Income Tax: Capital Gains: Treatment of Compensation Receipts (TR 95/35)*, paras 117-119.

¹² Hill Peter, “Settlements, Court Orders, and GST”, *GST Today* Issue 17 – April 2000 p8.

¹³ Parliament of the Commonwealth of Australia, House of Representatives, *Explanatory Memorandum to the Indirect Tax and Consequential Amendments Bill (No.2) (Cth)*.

“1.5 Where the consideration relates to an underlying supply that was taxable, the consideration received will be subject to GST. An underlying supply is the subject matter of the claim of compensation or damages. ...

1.7 Consideration in respect of claims of compensation or damages will **only** be subject to GST when the claim relates to a taxable supply of goods or services. For example, money received as a result of a court order for a non-payment of a taxable supply will be regarded as consideration and subject to GST.” (emphasis added)

The first thing to note about s.9-15(2A) is that it primarily deals with the concept of consideration and not supply. More significantly, the use of the word “only” in paragraph 1.7 suggests that there are no GST consequences when there is no underlying supply. However, as discussed above, the GST Act contemplates that a surrender of rights, the entry into an obligation and a forbearance to sue are supplies, as defined. Presumably, such supplies can be taxable supplies where the other building blocks for taxability are satisfied. It is submitted that the purpose of the inclusion of the specific provision was to clarify that consideration can include certain compulsory contributions.

The issue in the case of *Hornsby Shire Council v Commissioner of Taxation* [2008] AATA 1060 was whether the “compulsory acquisition” of a quarry by Hornsby Shire Council (**Council**) from CSR Limited (**CSR**) was a supply for the purposes of s. 9-10 of the GST Act, so that the Council could claim an input tax credit for the GST paid to CSR as part of the compensation for the land. The case canvassed the issue of whether a supply for GST purposes requires a positive act.

In general, a vesting of land in a government authority by way of compulsory acquisition is not treated as a supply, where the original landholder does not voluntarily enter into an arrangement to transfer or surrender the land. This position is set out in **GSTR 2006/9: Supplies**, which states at paragraph 82:

“In cases where land vests in the authority as a result of the authority seeking to acquire the land, and initiating the compulsory acquisition process pursuant to its statutory right, then the owner does not make a supply because it takes no action to cause its legal interest to be transferred or surrendered to the authority.”

However, in the particular circumstances of this case, the compulsory acquisition of the quarry was triggered by the original landholder. Broadly, the background was as follows:

- the quarry was zoned ‘Open Space A (Public Recreation-Local)’ under the *Hornsby Local Environment Plan 1994 (LEP)*;
- under clause 17(5) of the LEP, the Council was required to compulsorily acquire land that was zoned ‘Open Space A (Public Recreation-Local)’, if the landowner made a request in writing;
- CSR made such a request, which the Council resisted, arguing that it was not required to compulsorily acquire the land and refusing to do so;
- after a prolonged dispute between the Council and CSR, culminating in proceedings brought before the Land and Environment Court, the Council finally agreed to and effected the compulsory acquisition;
- The Council paid \$26,508,771 in compensation to CSR for the acquisition, comprising of \$25,000,000 market value of the land, as determined by the Valuer General, \$99,500 loss attributable to the disturbance as determined by the Valuer General and \$1,409,271 in interest under the s. 49 of the *Land Acquisition (Just Terms Compensation) Act*.

Evidently, far from being passive, resisting or opposing in respect of the arrangements, CSR was the party that actively and voluntarily drove the compulsory acquisition. The Council was, in fact, an unwilling acquirer. On this basis, the Council argued that the transfer of the quarry was a supply, as CSR took action to cause its legal interest to be transferred to the Council. Consequently, the Council argued, CSR’s actions amounted to an entry into an obligation for the purposes of s. 9-10(2)(g), or a surrender of real property for the purposes of s. 9-10(d). As the supply was otherwise taxable under

9-5 of the GST Act, the Council argued it was entitled to an input tax credit in respect of the acquisition. The Council therefore claimed an input tax credit of \$2,409,888.

The Commissioner disagreed with the Council's characterisation of the compulsory acquisition as a taxable supply, arguing that the giving of the notice by CSR to the Council was not sufficient to constitute the making of a supply as it was not binding (and therefore did not constitute an entry into an obligation) and gave no legal effect to the vesting of the property.

The Tribunal agreed with the Commissioner's contention that a positive act is required on the part of a party making a supply, notwithstanding the breadth of the definition of 'supply' in s. 9-10 of the GST Act. The Tribunal states at paragraph 70, with reference to the relevant case law:

"It would seem, having regard to the Full Court in [Westley Nominees Pty Ltd & Anor v Coles Supermarkets Australia Pty Ltd & Anor (2006) 152 FCR 461] that the Full Court inclines to the view that some positive action is required. An obiter pronouncement of the Federal Court must be persuasive in relation to a decision by the tribunal..."

However, the Tribunal ultimately agreed with the Council and found that CSR had taken the positive steps necessary to constitute a 'supply'. Specifically, it entered into legal obligations for the purposes of s. 9-10(2)(g) of the GST Act by issuing the written request and taking other actions to cause the compulsory acquisition to take place. Further, the Tribunal found that the quarry was surrendered for the purposes of s. 9-10(2)(d) of the GST Act. Consequently, CSR made a taxable supply of the quarry, and the Council was entitled to claim an input tax credit accordingly. The case amply demonstrates that, even in the context of a compulsory acquisition of property, a supply can be found if there are positive acts by the supplier.

Court Orders

Judgments may, at first instance, appear to raise identical GST/VAT issues as for out-of-court settlements. However, judgments can be more problematic because a plaintiff's claim merges into the judgment when a court makes an order and because of the different role of the plaintiff.

It is on this basis, it is stated, that White J, in *Interchase Corp Ltd v CAN 010087573 Pty Ltd* (Supreme Court of Queensland, 24 June 2000, White J), made some comments, which were *obiter*, concerning the applicability of the GST to the payment of a judgment debt. Her Honour made the following remarks in refusing the plaintiffs an indemnity for the impact of the GST on the judgment:

"It is not easy to see how a court giving judgment or the payment of a judgment sum or the granting of a stay of execution could constitute a 'supply' within the meaning of those expressions.

A taxable supply is made if the supply is made for consideration (s.9-5(a)). Consideration includes matters done pursuant to orders of a court (s.9-15(2A)(a)), but that does not of itself constitute a supply. The receipt of payment by a judgment creditor does not obviously involve the creation, grant, transfer, assignment or surrender of any right or the entry into or release from an obligation (s.9-10(2)(e)(f)). When the judgment is satisfied the debt created by the judgment is thereby extinguished and does not depend on the surrender of any rights or the release of the judgment debtor."¹⁴

The latter paragraph was cited with approval by Underwood J in *Shaw v Director of Housing and State of Tasmania (No.2)*¹⁵ (**Shaw**). In *Shaw* there was a refusal to allow the successful plaintiff in a negligent misrepresentation case to be indemnified for any possible GST liability arising by virtue of the payment of the judgment sum. It was refused because the alleged release of the obligation to pay the judgment sum on payment would not amount to a supply.

¹⁴ Paragraphs [53] and [54] of the judgment. White J had earlier concluded that there was a requirement for the GST component of damages, if one were to exist, to be pleaded, and that there would be associated questions of the remoteness of damages and foreseeability: [50] and [51].

¹⁵ [2001] TASSC 2, at [18].

Underwood J placed heavy emphasis on “the concept that there is a legislative intention not to include in the word ‘supply’ the release of an obligation that occurs independently of the act of the releaser”¹⁶. There was a “legislative intention to impose the tax only on voluntary supplies, not those supplies that occur without any act of the releaser”¹⁷. As “the release of the obligation to pay a judgment sum by the payment of the sum will occur regardless of whether the judgment creditor makes or does any act at all”¹⁸, it could not give rise to a supply.

Barter Transactions

Settlements will often involve non-monetary consideration being provided for the forbearance to sue. This situation may arise particularly where the dispute or litigation between the parties involves counter-claims and mutual releases.

The GST Act clearly contemplates that there can be non-monetary consideration.¹⁹ In these situations, it is likely that what is identified as the consideration for one supply will itself constitute a supply, but it is beyond the scope of this paper to consider the special issues that arise in these circumstances.

Supply in GSTR 2001/4

The Commissioner of Taxation has issued a public GST ruling **GSTR 2001/4: GST consequences of court orders and out-of-court settlements (GSTR 2001/4)** which sets out the GST consequences resulting from court orders and out-of-court settlements. The Commissioner states that supplies that are related to an out-of-court settlement fall within the three categories of supply described below:

- *Earlier supply* – “Where the subject of dispute is an earlier transaction in which a supply was made involving the parties, that supply is referred to in this ruling as an ‘earlier supply’.” [46]
- *Current supply* – “a new supply may be created by the terms of the settlement.” [48]
- *Supply related to discontinuance of action* – “even where there is no earlier or current supply, the very wide range of things that can constitute a ‘supply’ means that one or more new supplies will probably crystallise on an out-of-court settlement being reached. Generally, (it is suggested in most if not all cases), the terms of a settlement in finalising a dispute, will ensure no further legal action in relation to that dispute, provided that the terms of the settlement are complied with. This often takes the form of a plaintiff releasing a defendant from some (or all) of the existing claims and from further claims and obligations in relation to that dispute”. [50-51]

The Commissioner also states the following in terms of conditions of settlement that can create supplies for GST purposes:

“The supplies may be characterised as:

- surrendering a right to pursue further legal action [paragraph 9-10(2)(e)]; or*
- entering into an obligation to refrain from further legal action [paragraph 9-10(2)(g)]; or*
- releasing another party from further obligations in relation to the dispute [paragraph 9-10(2)(g)].*

In this Ruling, we refer to supplies of these kinds as ‘discontinuance supplies’. However, whether discontinuance supply would be a taxable supply would then depend on the requirements of section 9-5 being met in relation to that supply”. [54-55]

Consideration in GSTR 2001/4

¹⁶ [2001] TASSC 2, at [19].

¹⁷ [2001] TASSC 2, at [19].

¹⁸ [2001] TASSC 2, at [19].

¹⁹ S.9-15(1), 9-75(1)(b).

The concept of consideration in GSTR 2001/4 plays the crucial role of determining whether a payment will generate a GST liability. The Commissioner is of the view that a supply in the nature of a discontinuance of a claim will almost always be present in a settlement. However, it is stated that this discontinuance supply will in most cases not have a separately ascribed value.²⁰

GSTR 2001/4 states that no sufficient nexus will exist between a payment and a discontinuance supply where the payment relates to a claim which does not have the character of a supply. Such a claim is described at paragraph 95:

“Where the subject of the dispute is a claim (for example) for property damage, negligence causing loss of profits, wrongful use of trade name, breach of copyright, or personal injury, and payment [is] made in compliance with the settlement or court order that is wholly in relation to this claim, the payment will not be consideration for a supply. This is because the subject of the claim itself does not constitute a supply under section 9-10 of the GST Act.”

The Commissioner distinguishes this from the case where the settlement occurs on the basis that the subject of the dispute is not clearly identified – such as where a settlement occurs with a vexatious litigant. In this case, “such a payment is consideration for a discontinuance supply”.

It is submitted that the Commissioner’s approach provides an unsatisfactory basis for one to determine whether a GST liability should arise. The Commissioner has substituted one difficult question for another, but without suggesting any objective criteria for arriving at an answer. The Commissioner simply lists certain types of claims that do not give rise to a GST liability.

Is the Payment of Judgment Interest Consideration for a Supply?

Judgment interest is an amount of interest payable as, either:

- compensation for being deprived of the use of money prior to the making of a court order (***pre-judgment interest***); or
- compensation for the delay in payment of an amount awarded to a party by a court order (***post-judgment interest***).

In ***GSTD 2003/1***, the Commissioner sets out his view that judgment interest is “separate and distinct” from an underlying supply that is the subject of a cause of action²¹ and is not, therefore, consideration for the underlying supply. As there is an insufficient nexus between the payment and any underlying supply²², and the making of the judgment itself does not constitute a supply made by the court²³, the payment of judgment interest is not consideration for a taxable supply for the purposes of the GST Act.

Further, the Commissioner does not consider the payment of judgment interest to constitute a financial supply, as it does not involve the provision, acquisition or disposal of an interest in or under a debt or credit arrangement for the purposes of reg. 40-5.09(1) of the GST Regulations²⁴. Consequently, following the Commissioner’s view in ***GSTD 2003/1***, the payment of judgment interest does not give rise to any GST consequences.

However, it should be noted that the determination does not apply to the payment of judgment interest in respect of judgments and court orders covered by s. 78-110 of the GST Act; i.e. those which relate to insurance claims and claims for compensation under statutory compensation schemes. In these matters, any payment in compliance with a judgment or court order is considered to be made in

²⁰ GSTR 2001/4, para. 93.

²¹ See paragraphs 13, 14 and 18 of ***GSTD 2003/1***.

²² A payment will constitute consideration for a supply where there is a sufficient nexus between the payment and a supply: see paragraph 68 of GSTR 2001/6 and paragraph 10 of ***GSTD 2003/1***.

²³ See GSTR 2001/4: *GST consequences of court orders and out-of-court settlements*.

²⁴ See paragraphs 24 and 25 of ***GSTD 2003/1***.

settlement of the insurance/statutory compensation claim itself, and the correct GST treatment of the underlying claim will apply.

GST and Recovery of Costs and Costs Assessments

In GSTR 2001/4, the Commissioner states the following at paragraph 149:

“... the payment of court ordered costs or costs negotiated in a settlement in the circumstances described will not be consideration for an earlier or current supply. It does not matter that the payment of the costs order or settled amount is made by an entity other than the unsuccessful party. The costs order or settled amount should take account of any entitlement to an input tax credit of the parties to the original supply.”

In the Commissioner's view, a costs order is essentially the same as a payment of damages, and is intended to compensate a party for legal costs incurred in the course of a dispute. Consequently, there is no GST payable in respect of the payment, as there is no corresponding taxable supply.

However, the GST treatment of the legal costs incurred by the party who has been awarded costs must be taken to account in calculating the amount recoverable. To the extent that the party has been able to claim input tax credits in respect of the GST, the amount recoverable is the GST exclusive amount. To the extent that there was no input tax credit entitlement for the GST paid, the amount recoverable is the GST inclusive amount. Accordingly, a party awarded costs will be compensated only for the actual costs incurred, including GST but net of any associated input tax credit entitlement.

The issue of GST in the context of a costs assessment was recently discussed in the case of *Boyce v McIntyre* [2009] NSWCA 185 by the New South Wales Court of Appeal. The Court of Appeal concluded that a costs assessor does not have the power to determine an amount of GST payable when assessing legal costs.

In that case, Mrs McIntyre was one of approximately 675 sub-lessees of land in Kosciuszko National Park, sub-leased to the parties by Kosciuszko Thredbo Pty Ltd (**KT**). In 2007, Mrs McIntyre and the other sub-lessees agreed with KT to a renewal of the sub-leases. The sub-lessees each agreed to indemnify KT for the costs incurred in renewing the sub-leases, including reasonable legal costs, duties, fees, charges and certain other incidental costs.

Cutler, Hughes and Harris (**CHH**) was the law firm engaged by KT to provide legal services in relation to the renewal of the sub-leases. CHH and KT entered into a costs agreement, pursuant to which CHH would charge a fixed fee of \$3,000 plus GST for each sub-lease, plus certain additional charges. The Court of Appeal noted that this gave rise to a “staggeringly large fee” of more than \$2 million, for what was essentially the review and drawing up of a single form of sub-lease, to be replicated and executed 675 times (para 11).

KT subsequently issued a tax invoice to Mrs McIntyre for \$3,502, comprised of the \$3,000 fee, plus \$202 charged by CHH for disbursements, plus \$300 in GST. Mrs McIntyre took issue with the amount recharged by KT, and as a “third party payer” under s. 302A of the *Legal Profession Act 2004 (LPA)*, was entitled to have the amount reviewed by a costs assessor (see s. 361 of the LPA). The costs assessor determined that a fair and reasonable amount of CHH's costs was \$2,050, less \$1,200 for the cost of the assessment, totaling \$850. As Mrs McIntyre did not dispute the disbursements of \$202, the total amount determined to be payable by Mrs McIntyre to KT was \$1,052.

KT applied for a review of this assessment by the Review Panel under the LPA, but was unsuccessful. CCH appealed to the Supreme Court of New South Wales against the decision of the Review Panel and was unsuccessful before Harrison AsJ. CHH applied to the Court of Appeal for leave to appeal in respect of a number of issues, including whether the costs assessor was empowered to determine the amount of GST payable on legal costs.

Leave to appeal was granted and CHH was successful on this point. The Court of Appeal disagreed with the costs assessor, the Review Panel and Harrison AsJ in finding that the costs assessor could *not* assess the amount of GST payable in respect of the legal costs. Ipp JA stated the following at para 51 (Macfarlan JA and Hoeben J agreed):

“By the Act, a costs assessor is empowered to assess costs that are defined by s 302(1) as including “fees, charges, disbursements, expenses and remuneration”. GST does not fall under any of these categories and does not come within the ambit of legal costs. GST is an Issue in respect of taxation, not legal costs.”

Therefore, the proper GST treatment depends on the operation of the relevant legislation, which governs the proper characterisation of the supplies and the appropriate GST treatment. This cannot be interfered with by a costs assessor, who, in issuing an assessment, is confined to the matters listed in s. 302(1) of the LPA.

GST Implications for Quantum of Damages

In the recent case of *Gagner Pty Ltd trading as Indochine Café v Canturi Corporation Pty Ltd* [2009] NSWCA 413, the NSW Court of Appeal analysed how GST amounts factor into an assessment of the quantum of damages. The decision also sets out helpful commentary in respect of GST and the damages award itself.

The Applicant/Appellant (a restaurant) and the Respondent (a jewellery store) occupied a common building. In 2005, the Applicant's kitchen flooded, causing some damage to the store fit out of the Respondent. As a result of the flooding, the Respondent decided to bring forward certain planned refurbishments to the entirety of the store (not limited to the damaged area).

In the District Court, Gibson DCJ awarded the Respondent a sum of damages representing the amount the Respondent would have paid in order to restore the fit out to its condition prior to the damage caused by the flooding. The amount awarded included a sum of GST that would have been payable on the necessary purchases, notwithstanding that the Respondent was registered for GST and would have been entitled to input tax credits in respect of any GST payable on those purchases.

The Appellant argued that that it was “contrary to the compensatory principle” to award the Respondent an amount for which it would not be out of pocket [134]. In those circumstances, there was no net loss to the Respondent in respect of GST, as any GST paid would give rise to an equal input tax credit entitlement, therefore, the GST should be excluded from the quantum of damages.

The NSW Court of Appeal considered the relevant case law and agreed with the Appellant on this issue, reaching the following conclusion at [151]:

“In summary, as the GST legislation currently stands, if the plaintiff in an action for tort is registered for GST purposes, and stands to receive an input tax credit for any GST payments incurred in making good its damage, and there is no impediment to the plaintiff receiving the full benefit of the input tax credit, that GST amount should be excluded from the quantum of damages recoverable.”

The Court pointed out that this reasoning is consistent with the Tax Office position, as outlined in *Practice Statement Law Administration PS LA 2008/16 The GST implications in the recovery of legal costs (professional fees and disbursements) awarded by courts or settled by agreement between the parties*. Note that this Practice Statement has since been withdrawn and replaced with *Practice Statement Law Administration PS LA 2009/9 Conduct of Tax Office litigation*, which sets out similar principles in respect of legal costs (para 139). Consequently, the quantum of damages was reduced by the GST component.

The judgment also confirms that no GST is payable in respect of the damages award itself, consistent with the Tax Office view. In endorsing the position set out in *GSTR 2001/4 GST consequences of court orders and out-of-court settlements*, the Court states the following at [157]:

“[GSTR 2001/4] states, at para [60], that “a court, giving judgment, does not make a supply for GST purposes”. Nor is there any relevant “taxable supply” involved in the events that led to litigation such as the present.

The Court considered that the ruling “decides for practical purposes the way in which the GST legislation will be administered” [159]. Consequently, the Commissioner’s view in GSTR 2001/4 was upheld.

GST Implications for Quantum Meruit Claim for Services Rendered

In the case of *Peet Limited v Richmond (No 2) [2009] VSC 585*, the Supreme Court of Victoria found that an amount awarded for a claim of *quantum meruit* should, in the circumstances, be grossed up to include an amount of GST. The quantum meruit award related to services that had previously been provided by Peet Limited (**Peet**) to Mrs Richmond.

The Court referred to *GSTR 2001/4 GST consequences of court orders and out-of-court settlements*, which sets out the Commissioner’s view that payment under a court order can constitute consideration for a supply where it bears a sufficient nexus to an “earlier supply”. Hollingworth J formed the view that because the *quantum meruit* award was payment for services previously rendered to Mrs Richmond by Peet, the Commissioner was likely to take the view that the payment was consideration for an earlier taxable supply, thereby giving rise to a GST liability.

At paragraph [80] of the judgment, His Honour states:

“Obviously, this court is not being asked to determine, as between Peet and the Commissioner of Taxation, whether there is in fact a GST liability. It is being asked to make an award which fairly and reasonably reflects a liability which is expected to arise upon payment of the judgment sum.”

Despite the fact that the Court did not purport to determine the GST liability between Peet and the Commissioner, certain administrative steps were prescribed to ensure that the GST amount was actually remitted by Peet, or otherwise returned to Mrs Richmond. These included a requirement that within 30 days of remitting the GST amount to the Commissioner, documentary proof be provided to Mrs Richmond of the amount remitted, as well as a refund of the balance if the amount did not represent the entire GST component.

29 March 2010