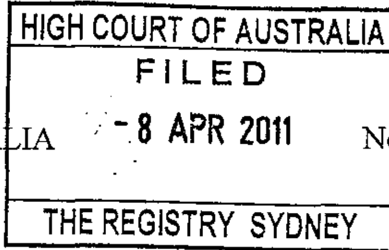
HIGH COURT OF AUSTRALIA
FILED
- 8 APR 2011
THE REGISTRY SYDNEY

10 IN THE HIGH COURT OF AUSTRALIA SYDNEY REGISTRY No. S238 and S239 of 2010

BETWEEN:

S238/2010	S239/2010
AMERICAN EXPRESS WHOLESALE CURRENCY SERVICES PTY LTD Applicant	AMERICAN EXPRESS INTERNATIONAL INC Applicant
and	and
COMMISSIONER OF TAXATION Respondent	COMMISSIONER OF TAXATION Respondent

APPLICANTS' SUBMISSIONS IN REPLY

20 **Part I: Certification for publication**

The following submissions in reply are in a form suitable for publication on the internet.

Part II: Reply

1. *Re Respondent's Submissions paragraphs 4(c) and 40(a) and (b)* ("**RS [4(c)], [40(a) and (b)]**"). The applicants have not argued, nor is it necessary for them to establish, that "all supplies made by Amex ... were made in or under a 'payment system' within the meaning of Reg 40-5.12 of the GST Regulations". Rather, the applicants contend that:

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   (a) Amex makes the supplies identified in paragraph 28 of the applicants' submissions ("**AS [28]**");

   (b) Amex supplies to cardholders "something", namely a "payment system" as defined, or "an interest in or under" a payment system (whether or not it makes other supplies[1]);

   (c) by reason of r 40-5.12, that supply is not a financial supply;

40 (d) Amex did not supply a relevant property interest which can be properly be described as "a credit arrangement or right to credit" for which the default fees were consideration (or from which the applicant derived the default fees as

[1] The applicants acknowledge at AS [24] that Amex makes a financial supply to a credit cardholder who chooses to defer payment.

Filed on behalf of the Applicants
Date of filing: 8 April 2011

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10 revenue); accordingly there was no financial supply within the meaning of r 40-5.09 to which those default fees relate;

(e) if (contrary to the applicants' submission), there was a financial supply which fell within the meaning of r 40-5.09 to which the default fees were related, there was nevertheless no financial supply by reason of the tie-breaking operation of r 40-5.08, because there was also a supply of "something", namely a "payment system", or "an interest in or under" it.

2. Accordingly, the default fees are not revenue *from*, nor consideration *for*, an input
20 taxed supply.

3. *Re RS [8(e)].* The respondent's assertion that 'revenue' in the numerator of the formula meant 'consideration' had its origin in the applicants' returns is incorrect. The applicants' returns simply set out its net amounts in numerical form (at __AB___). As set out in AS [62], the Respondent's Compliance Activity Report issued on 13 April 2006 together with the assessments in dispute, made the positive assertion that the default fees were consideration for an input taxed financial supply by Amex and so should be treated accordingly in the apportionment calculations. However the real issue is that both parties treated the words "revenue from" in the
30 numerator as meaning "consideration for". As is explained in the applicants' submissions that is consistent with the scheme of the GST Act.

4. *Re RS [17].* Contrary to the respondent's assertion, the applicant does contest, and has done so at all times, that there was a relevant supply of a "credit arrangement or right to credit". The relevant supplies are as identified in AS [28] and do not involve the supply of a "credit arrangement or right to credit" (except in the case of a credit cardholder who chooses to defer payment).

5. *Re RS [24], [28], [41(a)].* Until now, the respondent has not argued that for the
40 purpose of determining the apportionment of input credits, the debt which becomes payable by a cardholder to Amex gives rise to the making of a financial supply. Indeed, as Dowsett J observed at FC [46], the case on appeal was not conducted on that basis. The majority did not consider whether or not there had been an "acquisition supply" because no such contention was advanced. There is no application by the respondent to this Court seeking to raise this new argument belatedly on appeal.

6. In any event, this new assertion that the acquisition of the debt due by the cardholder to Amex is the relevant financial supply simply emphasizes that the artificial division
50 of the card system into a "payment system" in so far as the relationship with merchants is concerned but not in so far as the relationship with cardholders is concerned is flawed. The "acquisition" of a debt due by the cardholder to Amex when the cardholder uses a card to acquire goods or services from a merchant is so intricately connected with the emerging obligation of Amex to pay the merchant that they cannot be divided into two unrelated relationships. The consideration due by Amex when the cardholder purchases goods or services and incurs a debt to Amex does not flow to the cardholder but to the merchant. In these circumstances it would be inconsistent to treat the relationship with the merchant as being part of a payment system but not to do so in respect of the relationship with the cardholder. It is this

10 inconsistent treatment of the merchant fees as consideration for taxable supplies while treating the default fees as connected with input taxed supplies which leads to the inappropriate denial of input credits.

7. Further the default fees are only paid when a cardholder fails to pay the outstanding balance or minimum amount (whichever is the case) in accordance with the cardholder's contractual obligations. The default fees are not consideration ***for*** or revenue ***from*** a debt created when the purchase was made, less still from an acquisition of any such debt. The respondent impermissibly seeks to substitute a "but for" test in establishing the relevant connection between the default fees and the

20 acquisition of the debt by Amex. This is highlighted by the fact that default fees are not paid where a cardholder complies with the relevant obligations. While it is true that the default fees may not have accrued if the relevant purchase had not taken place, this "but for" test does not tell one what the default fee is ***for***. As set out at AS [13] and [14], the default fees simply compensate Amex for its loss arising from a cardholder's default. The default fees are truly liquidated damages.[2]

8. Further, even if there is an "acquisition supply" it must be for consideration if it is to be a financial supply. The respondent does not identify what consideration is provided for this "acquisition supply". The debt and the cardholder's obligation to pay Amex

30 are one and the same thing. Consequently the acquisition of the debt is not for consideration unless the relevant consideration is the obligation to pay the merchant under what is admitted by the respondent to be a payment system.[3] If the acquisition of the debt by Amex is not a financial supply, it has no bearing on the outcome of this case. If the relevant consideration is the obligation to pay the merchant, this demonstrates that the relationship with the cardholder is part of the payment system.

9. *Re RS [27].* The respondent's contention that the default fees were derived from the supply of the "right to present the card in satisfaction of the purchase price of goods and services" is incorrect. Once again the respondent substitutes a "but for" test. The

40 default fees are payable by reason of breach by the cardholder of its contractual obligation to pay the amount required by the relevant date. The fact that the default fees would not be payable if the card was not issued in the first place tells one nothing about what the default fees were for.

10. *Re RS [29].* RS [29] fails to appreciate that a financial supply must be "for consideration". As set out in AS [19], the scheme of the GST Act is that all acquisitions by registered entities are creditable unless the acquisition relates to making an input taxed supply. A financial supply is input taxed; however, a supply cannot be a financial supply unless it is of a property interest and made "for

50 consideration".[4] If a particular receipt is not consideration for a financial supply, it cannot result in a reduction of input tax credits which are otherwise allowable. By ignoring that a financial supply must be for consideration, the assertion in the last sentence of RS [29] proposes that input tax credits must be denied for any entity that makes a financial supply even if the relevant revenue was derived from (or was consideration for) a taxable supply and only had a secondary relationship to the

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[2] *Dunlop Pneumatic Tyre Co v New Garage and Motor Co* [1915] AC 79 at 86.

[3] Regulation 40-5.09(1)(a)(i).

[4] Regulation 50-5.09(1)(a)(i).

10 financial supply. Such a proposition does not arise from the words of the legislation, does not meet any identifiable statutory object and should be rejected.

11. The reference in footnote 50 to the judgment of this Court in *Reliance Carpet*[5] is misplaced. The passage cited went to the determination of whether or not a particular payment was consideration for a supply, and in circumstances where there was a specific statutory regime[6] dealing with forfeited deposits, so as to generate a liability for GST output tax. It has no relevance to the determination of whether a receipt should be treated as being derived from a particular source for the purposes of apportioning input tax credits.

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12. *Re RS [34]*. The respondent misunderstands and incorrectly records the applicants' argument, apparently in terrorem. The applicants do not suggest that all supplies involving transfers of funds into or out of bank accounts are not input taxed financial supplies, nor is that the consequence of the submissions advanced by the applicants. If it be the case that some of the examples in Parts 1 and 2 of Schedule 7 are "meaningless", the statute itself expressly contemplates that the examples might be inconsistent with the regulation and thus necessarily erroneous. The important difference between the holder of an Amex card and a person with a savings account is that the Amex card is used, and intended to be used, to make a payment to a merchant

30 via a system whereby the cardholder incurs a debt to Amex and Amex becomes indebted to the merchant. The Amex card system is so far removed from the relationship under a typical bank savings account as to not bear comparison.

13. *Re RS [37 – 39]*. The respondent's contention that the applicants' argument before the Full Court necessarily meant that card fees are taxable is irrelevant and incorrect. That question has never been put in issue by the respondent and was not a basis on which he ran his case below. As it happens, the reason that this has never been an issue below is that such an argument by the respondent is foreclosed to him by reason of him having issued a binding ruling(s) to the effect that Amex (and others in similar

40 positions to it) are not required to pay GST on the annual fees derived from cardholders[7]. These rulings are not in evidence because the respondent has not until now made this assertion. In the absence of such a binding ruling Amex could have sought to recover the GST on the annual fees from cardholders. In view of these binding rulings it is entirely appropriate that Amex comply with them.

14. The matters raised in footnote 73 are irrelevant. Unlike the ruling referred to in the previous paragraph which is binding on the respondent, the reference in this ruling to what is and what is not a "payment system" is not binding on Amex. It is merely a statement of opinion on the interpretation of the relevant taxing statute. Further, the

50 irrelevant implication in footnote 73 that the GST liability that might be payable if annual fees were, in the absence of the respondent's binding ruling, consideration for a taxable supply (a question which is beyond the scope of this case) would completely offset the additional input tax credits if the applicants are successful is not sustainable. If card fees were consideration for a taxable supply, those fees would be included in both the numerator and denominator in the formula, resulting in a significant increase

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[5] *FCT v Reliance Carpet Co Pty Ltd* (2008) 236 CLR 342.

[6] cf: s 49(2) of the *Property Law Act 1958* (Vic).

[7] See public ruling *GSTR 2002/2 Goods and Services Tax: GST Treatment of Financial Supplies and Related Supplies and Acquisitions*; Schedule 2; Line B41 and a private ruling issued to Amex dated 20 March 2000.

10 in the applicants' entitlement to input tax credits. It is not possible to determine whether the additional input tax credits from such an increase in the applicants' extent of creditable purpose would offset the additional output tax payable. Further, such GST would be borne by the consumer.

15. *Re RS [43 – 51].* Contrary to the respondent's submission, the respondent's "new argument" did raise questions of fact and not merely questions of construction. The trial would have been conducted by reference to further and different factual matters as recorded in the judgment of Dowsett J at FC [72].[8] It is not necessary to adduce the evidence which would have been adduced in order to establish prejudice for the
20 purpose of declining an application for leave to amend.

16. The objections were framed by reference to the respondent's reasoning process, exposed in the Compliance Activity Reports issued with the assessments. The respondent's reasoning hinged upon and decided that the default fees were not "consideration for an input taxed supply". The respondent thus sought, and was granted leave, to argue on appeal for the first time a basis for issuing the assessments which had never been put before and which the applicants have never had the opportunity to meet by evidence.

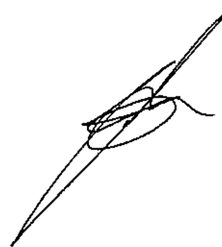
30 17. The majority erred in the exercise of their discretion by:

(a) erroneously concluding (at FC [189]) that the application to amend only raised an issue of statutory construction and not matters of fact;

(b) erroneously concluding (at FC [195]) that the applicants would not have been granted leave to amend their grounds of objection if the respondent had sought to change the fundamental basis upon which he had issued the assessments;

(c) failing to take into account the identification by the applicants of how the trial
40 would have proceeded differently and by reference to further evidence had the respondent advanced, as he should have, his "new argument" at trial.

Dated: 8 April 2011



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