GSTD 2014/D1 - Goods and services tax: in what circumstances is the supply of a credit card GST-free under paragraph (a) of Item 4 in subsection 38-190(1) of the A New Tax System (Goods and Services Tax) Act 1999 (GST Act)?

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This document has been finalised by GSTD 2017/1.

Generated on: 23 November 2026, 12:56:47 AM

Draft Goods and Services Tax Determination

Goods and services tax: in what circumstances is the supply of a credit card GST-free under paragraph (a) of Item 4 in subsection 38-190(1) of the *A New Tax System (Goods and Services Tax) Act 1999* (GST Act)?

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Ruling

1. The supply of a credit card facility is a 'supply made in relation to rights' within paragraph (a) of Item 4 in subsection 38-190(1) of the GST Act (Item 4), as it is a supply of a thing comprising a bundle of rights that derives its value exclusively, or almost exclusively, from those rights.

2. The supply of a credit card facility will be GST-free under Item 4 to the extent it is intended that the cardholder will use the facility to undertake a transaction when they are physically outside Australia, provided the cardholder's location outside Australia is integral to the relevant use of the credit card facility.

3. For card-present transactions when the cardholder is overseas, the cardholder must be physically present to tender the card as payment and make the relevant purchase or receive a cash advance. Therefore, the cardholder's location outside Australia is integral to the relevant use of the credit card facility and to that extent the use of the rights in the credit card facility are outside Australia.

4. For card-not-present transactions, the use of the rights in the credit card facility will only be for use outside Australia in those circumstances where the cardholder enters into the transaction when they are physically outside Australia and the cardholder's presence outside Australia is integral to the relevant use of the credit card facility.

5. For the purposes of this draft Determination:

- The subject matter of the supply is the 'credit card facility'.
- The supplier of the credit card facility will be an Australian Authorised Deposit- taking Institution (ADI) or another Australian credit card issuer. In this Determination, the supplier is referred to as the 'issuer'.
- 'Cardholder' refers to the recipient of the supply and also additional cardholders. For example, if the facility is contractually acquired by a corporate entity which allows an employee to use the facility, the employee as the cardholder will use the facility as agent of the company.
- 'Merchant' refers to an entity that accepts credit cards as a payment option and has access to a credit card payment system via participation in the system.
- A reference to credit card facility in this draft Determination includes a charge card facility.
- The cardholder can use the credit card facility for transactions in the following ways:
  - Card-present transactions refer to those where the cardholder must be physically present at the merchant's location to present the card and may also provide a PIN or signature (depending on the amount of the transaction). For the purposes of this draft Determination a card-present transaction includes cash advances (such as ATM withdrawals or over the counter at a financial institution).
  - Card-not-present transactions[1] refer to those where the merchant doesn't require presentation of the physical card and the cardholder does not need to be present. Examples include online, phone, fax, mail, and periodic payment transactions. In such cases the merchant requires the card number, expiry date and potentially other security information[2], before use of the credit card facility is accepted as payment by the merchant.

6. The application of paragraph (b) of Item 4 and Item 3 in the table in subsection 38-190(1) are not considered in this draft Determination.

[1] Also called a MOTO (Mail Order/Telephone Order) transaction.
[2] For example a Card Verification Value or Card Identification Number printed on the card.

Example

7. Bank Co, an Australian ADI, issues credit cards to its customers. Bank Co is a participant in a credit card payment system which operates in Australia and certain overseas countries and which covers Bank Co's credit cards. Customers may use the credit card facility for card-present transactions both while in Australia and while travelling overseas. Cardholders also use the facility for card-not-present transactions to make purchases from Australian and overseas suppliers, for example via the internet and by phone. When Bank Co makes a supply of a credit card to a new cardholder, it is not practical for it to ascertain whether, or to what extent, customers intend to use the card facility outside Australia.

8. Bank Co is able to ascertain which transactions relate to Australian and overseas merchants. In addition, it conducts market research into usage patterns of cardholders when they are travelling outside Australia. Based on this, it determines some typical transactions where payments are made using the credit card facility and determines if the particular use is outside Australia:

- *Cardholder is at an Australian airport waiting for an overseas flight and books online their first night's accommodation overseas – use is not outside Australia as the cardholder is in Australia.*
- *Cardholder is overseas and books online further overseas accommodation – use is outside Australia, the cardholder is overseas and the cardholder's presence outside Australia is integral to the use of the credit card facility.*
- *Cardholder is overseas and buys books online from US vendor to be delivered to Australia – use is not outside Australia as the cardholder's location is not integral to this transaction.*
- *Cardholder is overseas and a periodic payment of their Australian power bill occurs, via their credit card facility – use is not outside Australia as the cardholder's location is not integral to this transaction.*
- *Cardholder is overseas and purchases a flight to return to Australia from an Australian travel agent online – use is outside Australia, the cardholder is overseas and the cardholder's presence outside Australia is integral to their use of the credit card facility.*

9. Based on these patterns of past usage by cardholders, Bank Co is able to make a reasonable estimate of the extent to which the supply of its credit card facilities are GST-free.

Date of effect

10. When the final Determination is issued, it is proposed to apply both before and after its date of issue. However, the Determination will not apply to taxpayers to the extent that it conflicts with the terms of settlement of a dispute agreed to before the date of issue of the Determination (see paragraphs 75 and 76 of Taxation Ruling TR 2006/10).

Commissioner of Taxation
2 April 2014

Appendix 1 – Explanation

This Appendix is provided as information to help you understand how the Commissioner's preliminary view has been reached. It does not form part of the proposed binding public ruling.

Background

11. The application of Item 4 is considered in Goods and Services Tax Ruling GSTR 2003/8.[3] This draft Determination sets out the Commissioner's views regarding how Item 4 applies to the supply of a credit card facility.

12. This draft Determination does not examine in detail the supply of credit card facilities as a financial supply. A supply of a credit card facility is the supply of a financial interest capable of being an input taxed financial supply if the requirements of subregulation 40-5.09(1) of the A New Tax System (Goods and Services Tax) Regulations 1999 are met.[4]

13. Subsection 9-30(3) of the GST Act contemplates that a supply may be both GST-free and input taxed, and to the extent that a supply would otherwise have the character of both, provides that the supply is to that extent GST-free and not input taxed.[5] Hence, to the extent that the supply of a credit card facility has the character of being both GST-free and input taxed, it will be GST-free.

Supplies in relation to rights that are for use outside Australia

14. Item 4 relevantly provides that 'a supply that is made in relation to rights' is GST-free 'if… the rights are for use outside Australia'.

15. GSTR 2003/8 explains that a supply of a thing is a 'supply that is made in relation to rights' if it fits within one of three categories.[6] These are:

- Category 1 - Supplies identified in paragraph 9-10(2)(e) of the GST Act – that is, the creation, grant, transfer, assignment or surrender of any right.
- Category 2 - Supplies of things comprising a bundle of rights that derive their value exclusively, or almost exclusively from those rights.
- Category 3 – Supplies of services directly connected with rights.

16. The Determination question raises two key sub-issues under Item 4:

- Is the supply of a credit card facility 'a supply made in relation to rights'?; and if so
- To what extent are the rights 'for use' outside Australia?

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[3] GSTR 2003/8 was amended following the High Court decision in *Travelex Ltd v. Commissioner of Taxation* [2010] HCA 33 (*Travelex*).

[4] Although this had long been the Commissioner's view (GSTR 2002/2, Schedule 2), it was confirmed by the Full Federal Court in *Commissioner of Taxation v. American Express Wholesale Currency Services Pty Limited* (2010) 187 FCR 398; [2010] FCAFC 122; 2010 ATC 20-212; (2010) 77 ATR 12 (*Amex*)

[5] Unless the provision under which it is input taxed requires the supplier to have chosen for its supplies of that kind to be input taxed.

[6] Paragraph 27A .

Is the supply of the credit card facility 'a supply made in relation to rights'?

17. When we refer to the 'supply of the credit card facility', we mean the totality of the supply of the credit card facility or account made to the cardholder under the contractual arrangements with the issuer. This includes the use of the physical card and other methods (such as card-not-present transactions) that are made available to access the credit card facility.

18. Consistent with *Amex* at FCAFC 155, the supply of the right to use a credit card is a supply of an interest in or under a credit arrangement or right to credit within the meaning of regulation 40-5.09. Therefore, the supply of the credit card consists of a bundle of rights incorporating the right to credit and the means of accessing that credit.

19. The issuer uses a 'credit card payment system'[7] to provide the credit card facility access methods or payment functionality. When the cardholder uses these access methods it is sending instructions to the card issuer requesting the use of the right to credit. When the merchant receives authorisation from the card issuer by way of operation of the payment system, the merchant will accept the card facility as payment. At this point the cardholder's obligation to the merchant (as a customer) is discharged.[8]

20. Depending on the card issuer and the type of card, there may be other potential supplies such as loyalty program membership, travel insurance, etcetera. Whether these supplies are separate supplies or incidental to the dominant supply under the credit card facility will depend on the facts and is not further dealt with in this draft Determination.[9]

21. Based on the above, a supply of a credit card facility is the supply of something comprising a bundle of rights which derives its value exclusively, or almost exclusively, from those rights and is a Category 2 'supply made in relation to rights' under Item 4 (as explained in paragraph 15 of this determination).

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[7] 'Payment system' is defined in the Dictionary to the GST Regulations to be 'a funds transfer system that facilitates the circulation of money, including any procedures that relate to the system.' In addition to the payment system rules, a series of complementary contractual arrangements provide payment functionality to participating cards as well as settlement of obligations between parties. 'Credit card payment systems' are used not only by credit and charge cards but may provide payment functionality to debit cards and pre-paid cards as well.

[8] *Re Charge Card Services Ltd* [1989] 1 Ch 497 cited with approval in *Visa International Service Association v. Reserve Bank of Australia* [2003] FCA 977 at 265; see also GSTR 2003/12 *Goods and services tax: when consideration is provided and received for various payment instruments and other methods of payment*, at paragraphs 30-31.

[9] Incidental financial supplies are specifically dealt with in regulation 40-5.10, and explained in paragraphs 117 to 143 of GSTR 2002/2. See more generally GSTR 2001/8.

To what extent are the rights 'for use outside Australia'?

22. A supply made in relation to rights will be GST-free under Item 4 to the extent that the rights were intended, at the time they were created, granted, transferred, assigned or surrendered, to be used outside Australia.[10] GSTR 2003/8, in discussing apportionment of supplies that are partly taxable and partly GST-free, at paragraph 125, states:

> 125. You work out the GST payable on a supply that is made in relation to rights that are partly for use outside Australia by apportioning the consideration between the part of the supply that is made in relation to rights for use in Australia and the part that is made in relation to rights for use outside Australia. Apportionment of the consideration for a supply that includes taxable and non-taxable parts[11] is discussed in Goods and Services Tax Ruling GSTR 2001/8.[12]

23. There is no requirement to apportion consideration under Division 9 or section 38-190 of the GST Act when a supply is partly GST-free and partly input taxed, because there is no GST payable on the supply. However, determining the extent that the supply is GST-free will be an important factor in determining the creditable purpose of acquisitions relating to making those supplies. An acquisition will be denied creditable purpose to the extent that it relates to making supplies that would be input taxed.[13]

Determining when the rights are 'for use outside Australia'

24. GSTR 2003/8 states that for the purposes of Item 4, the relevant use is the intended use of the recipient (cardholder) and will depend on the nature of the rights in question. It is not sufficient that the essential characteristics of the rights demonstrate that they may be used outside Australia.[14] GSTR 2003/8 does not set out all the different uses that may arise; but does provide examples of how particular rights are 'for use', such as the intended on-supply of a thing, exploiting the right, or preventing others from exploiting the right,[15] and spending foreign currency as in *Travelex*.[16]

25. There are many ordinary meanings of the word 'use', for example the Macquarie Dictionary[17] defines use, in so far as it is relevant, as:

> 1. to employ for some purpose; put into service; turn to account.
>
> 2. …apply to one's own purposes…
>
> 3. to expend or consume in use…
>
> 11. the act of employing or using…
>
> 22. Law, History a. the enjoyment of property, as by employment, occupation, or exercise of it.

[10] See paragraph 124 of GSTR 2003/8.
[11] A part of a supply that is GST-free is a 'non-taxable part' for the purposes of GSTR 2001/8 (see paragraph 32).
[12] See paragraph 25 of GSTR 2001/8.
[13] Paragraph 11-15(2)(a) of the GST Act.
[14] Paragraph 108A.
[15] Paragraph 117 of GSTR 2003/8.
[16] Paragraph 116A of GSTR 2003/8.
[17] *The Macquarie Dictionary*, [Online], viewed 11 March 2014, www.macquariedictionary.com.au

26. The ordinary meaning set out above illustrates that the word 'use' is a word of wide import and its meaning in any particular case will depend to a great extent upon the context in which it is employed.[18] The uses to which property of any description may be put are manifold and what will constitute 'use' will depend to a great extent upon the purpose for which it has been acquired or created.[19]

Where are the rights in relation to the supply of the credit card facility for use?

27. The credit card facility is a supply that comprises a bundle of rights. Practically, the manner in which the cardholder intends to make use of these rights is reflected by how they intend to use the credit card facility.[20] The broad context and policy of Item 4 (and other Items in section 38-190) is to identify consumption that occurs outside Australia (paragraph 76 of GSTR 2003/8). The right to credit under the supply of the credit card facility is provided by way of an account provided by the Australian issuer. An important feature of the credit card facility is the ability to access the facility in various ways, such as to make a payment to merchants including those located outside Australia. This entails the merchant sending instructions to the issuer requesting the cardholder access their credit. However, as Item 4 concerns the use of the rights by the cardholder, neither the location of the card issuer providing the credit card, nor the merchant's location is determinative of whether the use is outside Australia.

28. Having regard to the ordinary meaning of use described at paragraph 25 such as 'applying', or 'the act of employing or using', when a cardholder initiates a card-present transaction, the use of the credit card facility only occurs when the cardholder is at the merchant's location to undertake the required actions. Therefore, the cardholder's physical location at the time of a card-present transaction is a better reflection of where the cardholder uses the credit card facility and therefore where the rights are for use for Item 4 purposes.

29. However, the credit card facility can also be used for card-not-present transactions, where the actions undertaken by the cardholder to use the credit card facility do not have to occur at the merchant's location (or any other specific location). The cardholder's physical location in such transactions is not relevant to the use of the facility and is not in itself a reflection of where the rights are for use. In such transactions, it is therefore necessary to look at additional factors to determine if the facility is for use outside Australia.

30. In the context of Item 3 in subsection 38-190(1), GSTR 2007/2 indicates that 'effective use or enjoyment outside Australia' of a supply occurs if the supply is provided to an individual that is located outside Australia, provided the individual's presence at that location is integral to, as distinct from being merely coincidental with, the provision of the supply (paragraph 106 & 294 of GSTR 2007/2).

31. This principle is considered relevant to determining whether the rights in the credit card facility are 'for use outside Australia' because it identifies use that is necessarily dependent upon the cardholder's presence outside Australia. Therefore, it can also take into account transactions where the location of the cardholder is irrelevant and which may not reflect where the relevant rights are consumed. Accordingly, in determining if the

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[18] This is illustrated by the discussion of the meaning of 'for use' at paragraphs 108 to 123 of GSTR 2003/8.
[19] *Council of the City of Newcastle* v. *Royal Newcastle Hospital* (1956-1957) 96 C.L.R. 493 at p. 515
[20] Where a supply comprises a bundle of rights the use of the thing supplied may in turn reflect the use of the related rights. See for example paragraph 116A of GSTR 2003/8 and *Travelex* at 35 where the use of the rights in the banknotes is reflected in how the bank notes were for use.

cardholder's physical location is integral to the use of the credit card facility, the guidance set out in paragraph 107 of GSTR 2007/2 is applicable and may be adapted to this context. Relevant indicators may include:

- the need to enter into the credit card transaction arises from the cardholder's presence overseas. This may be relevant for a card-not-present transaction entered into when the cardholder is overseas.
- the presence of the cardholder at that location is integral to the performance of the credit card transaction. For example, a cash advance or card-present transaction that occurs overseas requires the cardholder to be present at that location.

32. An issuer may supply numerous cardholders with credit card facilities where the related rights are intended for use both inside and outside Australia. As it may not be practical to obtain direct evidence of each cardholder's intended use, the issuer will need to determine, on a fair and reasonable basis, the extent the rights are for use inside and outside Australia for supplies of credit card facilities. This could, for example, be based on past usage patterns of other similar cardholders and market research about usage patterns.[21]

[21] GSTR 2003/8, at paragraph 129 provides guidance about forming a judgement as to the extent of the intended use of rights for the purpose of Item 4.

Appendix 2 – Alternative views

This Appendix sets out alternative views and explains why they are not supported by the Commissioner. It does not form part of the proposed binding public ruling.

Alternative views

Location of merchant

33. There is an alternative view about the location of the use of the relevant rights. Under this view, the use of the rights is the place where the cardholder's obligation to the merchant is discharged. This view is based on the following:

- that by using the credit card facility, the cardholder is discharging their obligation, as customer, to the merchant and that this is the use of the rights under the facility;
- the discharge of the cardholder's contractual obligation to the merchant occurs at the location of the merchant (being the location of the jurisdiction governing the contract).

34. The argument is that the right to tender the credit card as payment is the relevant right, and this right is used where the payment obligation is discharged. Under this view, physical location of the cardholder is irrelevant.

35. This view is not preferred because it focuses mainly on the effect of using the credit card facility on the relationship between the cardholder and the merchant, rather than on the customer's use of the rights provided by the issuer under the facility. More specifically, the view focuses on the cardholder and merchant to the exclusion of the use of the right to credit supplied by the issuer of the card, or that these rights are provided by the issuer, not the merchant.

Ongoing use of credit

36. Another alternative view is that the relevant rights that are for use outside Australia are the ongoing use of the right to credit over time, as this reflects the benefit the cardholder obtains by deferring payment. The extent to which the cardholder is outside Australia over the period of time this benefit is enjoyed will determine the extent to which the supply is GST-free. Whilst this view acknowledges the importance of the credit facility, the ongoing enjoyment of the credit arguably does not depend on where the cardholder is subsequently located over the period of time. Therefore, the preferred view is that in considering the bundle of rights that relate to the supply of the credit card facility, use is better reflected by reference to transactions that the cardholder enters into.

Appendix 3 – Your comments

37. You are invited to comment on this draft Determination including the proposed date of effect. Please forward your comments to the contact officer by the due date.

38. A compendium of comments is prepared for the consideration of the relevant Rulings Panel or relevant tax officers. An edited version (names and identifying information removed) of the compendium of comments will also be prepared to:

- provide responses to persons providing comments; and
- be published on the ATO website at www.ato.gov.au.

Please advise if you do not want your comments included in the edited version of the compendium.

Due date:	**2 May 2014**
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References

Previous draft:

Not previously issued as a draft

Related Rulings/Determinations:

TR 2006/10; GSTR 2001/8; GSTR 2002/2; GSTR 2003/8; GSTR 2003/12 GSTR 2007/2

Subject references:

- goods and services tax
- GST debt, loan and credit
- GST financial supplies
- GST free
- rights for use outside Australia

Legislative references:

- ANTS(GST)A 1999 Div 9
- ANTS(GST)A 1999 9-10(2)(e)
- ANTS(GST)A 1999 9-30(3)
- ANTS(GST)A 1999 11-15(2)(a)
- ANTS(GST)A 1999 38-190
- ANTS(GST)A 1999 38-190(1)
- ANTS(GST)R 1999 40-5.09(1)
- ANTS(GST)R 1999 40-5.10

Case references:

- *Commissioner of Taxation v. American Express Wholesale Currency Services Pty Limited* (2010) 187 FCR 398; [2010] FCAFC 122; 2010 ATC 20-212; (2010) 77 ATR 12
- *Council of the City of Newcastle v. Royal Newcastle Hospital* (1956-1957) 96 CLR. 493
- *Travelex Ltd v. Commissioner of Taxation* [2010] HCA 33; 2010 ATC 20-214; (2010) 76 ATR 329
- *Re Charge Card Services Ltd* [1989] 1 Ch 497
- *Visa International Service Association v. Reserve Bank of Australia* [2003] FCA 977; (2003) 131 FCR 300

ATO references

NO:	1-562KAOU
ISSN:	1443-5179
ATOlaw topic:	Goods and Services Tax ~~ International services ~~ supplies of rights

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