GSTD 2005/6 - Goods and services tax: does a club, association, trade union, society or co-operative ('association') make a supply when it imposes a non-statutory fine or penalty ('fine or penalty') on a member for a breach of the association's membership rules?

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Goods and Services Tax Determination

Goods and services tax: does a club, association, trade union, society or co-operative ('association') make a supply when it imposes a non-statutory fine or penalty ('fine or penalty') on a member for a breach of the association's membership rules?

Preamble

*This document was published prior to 1 July 2010 and was a public ruling for the purposes of former section 37 of the **Taxation Administration Act 1953** and former section 105-60 of Schedule 1 to the **Taxation Administration Act 1953.***

*From 1 July 2010, this document is taken to be a public ruling under Division 358 of Schedule 1 to the **Taxation Administration Act 1953.***

A public ruling is an expression of the Commissioner's opinion about the way in which a relevant provision applies, or would apply, to entities generally or to a class of entities in relation to a particular scheme or a class of schemes.

If you rely on this ruling, the Commissioner must apply the law to you in the way set out in the ruling (unless the Commissioner is satisfied that the ruling is incorrect and disadvantages you, in which case the law may be applied to you in a way that is more favourable for you – provided the Commissioner is not prevented from doing so by a time limit imposed by the law). You will be protected from having to pay any underpaid tax, penalty or interest in respect of the matters covered by this ruling if it turns out that it does not correctly state how the relevant provision applies to you.

*[**Note:** This is a consolidated version of this document. Refer to the Legal Database (http://law.ato.gov.au) to check its currency and to view the details of all changes.]*

1. No. There is no supply made by an association when it imposes a fine or penalty[1] on a member for a breach of its membership rules. The payment of the fine or penalty imposed by the association is not therefore consideration for a supply and a GST liability does not arise for the association.

[1] We consider a non-statutory fine or penalty is a fine or penalty that has not been imposed under a law of the Commonwealth, a State, a Territory or a foreign country. Further, it is a fine or penalty that has not been imposed by a court, upon the conviction of a person for an offence against a law of the Commonwealth, a State, a Territory or a foreign country.

Background

2. A supply of membership by an association to an entity is a taxable supply if all the requirements of section 9-5 of the *A New Tax System (Goods and Services Tax) Act 1999* (GST Act) are met. In return for payment of the membership fee, a member is entitled to the rights and privileges associated with being a member of the association and typically agrees, either explicitly or implicitly, to abide by the rules of the association.

3. If a member refuses or neglects to comply with the rules of membership of an association, or is found guilty of conduct unbecoming a member or prejudicial to the interests of the association, the rules of the association may provide for a fine or penalty to be imposed on that member. The fine or penalty imposed may be either monetary or non-monetary (for example, suspension of rights and privileges) or a combination of both.

When this Determination applies

4. This Determination does not apply to all fines or penalties that may be imposed on an entity. This Determination only applies to a fine or penalty that is imposed by an association on its member in the following circumstances:

- the fine or penalty is imposed, in accordance with the constitution or rules of that association, on a member who has refused or neglected to comply with the rules of membership of the association, or has been found guilty of conduct unbecoming a member or prejudicial to the interests of the association; and
- the fine or penalty is primarily intended as a punishment and/or to act as a deterrent.

Example 1: Sporting association fines a member club

5. *A sporting association fines a club, which is a member of that association, for failing to phone in the results of a game to the association. The association imposes the fine on the club in accordance with the association's rules of membership and the fine is primarily intended as a punishment and/or to act as a deterrent. This Determination applies to determine the GST consequences.*

6. This Determination does not apply if the fine or penalty relates to a supply or is imposed through a commercial contract, including an employment contract. For example, this Determination does not apply if:

- a fine or penalty or liquidated damages is provided for under the terms of a contract such as in the event of a breach of the contract;[2] or
- goods hired for an agreed period are not returned within that period and an additional charge for the extension of the hire period is consideration for a further supply.[3]

[2] GST Rulings relevant to this issue are GSTR 2001/4 Goods and services tax: GST consequences of court orders and out-of-court settlements; and GSTR 2003/11 Goods and services tax: payment on early termination of a lease of goods, in particular paragraphs 70 to 72 which discuss damages.

[3] See paragraph 34 of GSTR 2000/19 Goods and services tax: making adjustments under Division 19 for adjustment events.

Example 2: Hire arrangement

7. *A club has a video hire shop which hires out videos to members for a fee. In accordance with the rules of the club the video shop charges members an extra amount if a video is returned late. As the fine or penalty relates to the hire of a video this Determination does not apply to determine the GST consequences.*

Is there a supply made by the association for which the payment of the fine or penalty is consideration?

8. Typically, a fine or penalty which is imposed by an association on a member for refusing or neglecting to comply with the rules of membership, or on a member who has been found guilty of conduct unbecoming a member or prejudicial to the interests of the association, is intended as a punishment and/or is inflicted as a deterrent.

9. If the true nature of a fine or penalty is as a punishment and/or to act as a deterrent, it does not accord with that nature to suggest that there is a supply to the member in return for its payment.

10. The New Zealand case, *Case S65*,[4] which concerned the prosecution of a solicitor, supports this view of the law. Penalties were imposed on the solicitor and costs and expenses were awarded against him. The solicitor subsequently sought to claim input tax credits on the basis that the costs and expenses awarded against him were subject to GST. In considering whether there had been a service supplied to the solicitor, and whether he was entitled to a 'GST invoice', Willy DJ noted, with respect to the New Zealand GST law, that '[s]ervices are defined very widely as: 'anything which is not goods or money'.[5] He went on to say that '[o]n the face of it the definition of services is so wide that it embraces 'everything' except goods and money'.[6] Against this wide definition Willy DJ stated that:

> …this case produce[s] the curious reasoning that the New Zealand Law Society and the District Law Society supplied to the appellant a service in the nature of a prosecution for breaches of the *Law Practitioners Act*, and a disciplinary hearing to decide whether or not the allegations of the District Society had been made out. For that 'service' the Societies charged the appellant a fee comprising part of their out of pocket expenses. The New Zealand Law Society also imposed a penalty on the appellant payable to it and the District Society. Nobody suggests that can be a charge for the supply of a service, and I say no more about it.
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> This approach to the interpretation is an affront to commonsense and everyday usage. … Indeed one would have thought that to prosecute somebody is the opposite of doing them a service. It is the doing of a disservice.[7]

11. Willy DJ ultimately concluded that what passed between the solicitor and the two Societies did not attract the imposition of GST, that neither Society was obliged to provide the solicitor with a GST invoice and the solicitor was not entitled to claim any input tax credits.[8]

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[4] (1996) 17 NZTC 7408.
[5] *Case S65* (1996) 17 NZTC 7408, at 7410.
[6] *Case S65* (1996) 17 NZTC 7408, at 7410.
[7] *Case S65* (1996) 17 NZTC 7408, at 7411.
[8] *Case S65* (1996) 17 NZTC 7408, at 7411.

12. Further in our view, an association, in accepting the payment of the fine or penalty, does not enter into an obligation with the particular member to tolerate the misconduct but rather is fulfilling its obligation to all members to enforce the rules. The member does not gain rights additional to those which are already enjoyed by virtue of being a member. That is, upon payment of the fine or penalty the member continues to enjoy the same rights and privileges and it follows that the association is required to continue to provide the benefits of membership. In this sense it cannot be said that the association 'makes' a supply where it already has a pre-existing obligation to continue to provide the benefits of membership.

13. This view is supported by the United Kingdom Value Added Tax Tribunal case, *Northamptonshire Football Association* (NFA).[9] This case concerned whether the NFA was entitled to deduct input tax credits which related to income generated by the imposition of fines or penalties. This in turn required consideration of whether the imposition of fines or penalties was part of the business of the NFA. In this context the Tribunal Chairman, Mr Palmer, stated, with respect to the enforcement of the rules by the NFA:

> Is it [the enforcement of the rules] provided in consideration for the payment of the subscriptions to membership? In my view it certainly cannot be said to have been provided in consideration of the fines and penalties imposed. They are the sanctions accepted by the members for the breach of the rules. They are not consideration for the performance of the enforcement activity in any contractual sense. In my judgment the enforcement of the rules is an obligation of the Association undertaken in favour of each of the members in return for their compliance with the rules of the Association including, in particular, the payment of their membership fees and subscriptions.[10]

Example 3: Fine imposed by a sporting club on its member

14. *Northern Sporting Club (NSC) is a member of a national association. NSC is found by the national association to be in breach of the national association's membership rules for playing an ineligible player and is fined $50. NSC pays the fine. NSC does not gain any rights or privileges additional to those which it already enjoys as a member. The national association does not make a supply to NSC. The payment of the fine of $50 by NSC is not consideration for a supply and a GST liability does not arise for the national association.*

15. It may be argued that when a member of an association pays a debt arising from the imposition of a fine or penalty on that member, the extinguishment of the debt results in a supply being made to that member by the association. Consistent with the view that the 'extinguishment of a judgment debt by its payment does not constitute a supply by the judgment creditor for GST purposes',[11] we consider that the extinguishment of a fine or penalty debt through its payment, by the member, does not constitute a supply by the association to the member. The extinguishment of the debt does not depend upon any action on the part of the association. The association cannot be said to 'make' a supply.

16. Further, a question arises as to whether the payment of the fine or penalty gives rise to an adjustment event by reason that payment of the fine or penalty is additional consideration for the supply of membership by the association to the member.

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[9] [1996] BVC 2128.
[10] *Northamptonshire Football Association* (unreported, BVC Tribunal, 1996) 2128. A copy of the judgment is available from the Legal Database on the Tax Office website www.ato.gov.au.
[11] See paragraph 67 of Goods and Services Tax Ruling GSTR 2001/4 Goods and services tax: GST consequences of court orders and out-of-court settlements.

17. The payment of a fine or penalty is not consideration for any supply if it has been imposed because of a breach of the membership rules and is primarily intended as a punishment and/or to act as a deterrent. It is therefore not an additional amount of consideration for the supply of membership by the association to the member.

18. As such, we do not consider that the payment of the fine or penalty gives rise to an adjustment event,[12] for example, an increase in consideration for membership. As discussed above, the nature of the fine or penalty is as a punishment and/or to act as a deterrent. It is not, in our view, related to the consideration paid for membership to the association.

Conclusion

19. In our view, there is no supply made by, or adjustment event arising for, an association if:

- the fine or penalty is imposed by the association on a member because of the member's non-compliant behaviour with the membership rules of the association;
- the fine or penalty is primarily intended as a punishment and/or to act as a deterrent; and
- upon payment of the fine or penalty the member receives no additional rights, benefits or privileges to those rights, benefits or privileges to which the member was already entitled, by virtue of membership of that association, immediately prior to the imposition of the fine or penalty.

Date of Effect

20. This Determination applies [to tax periods commencing] both before and after its date of issue. However, this Determination will not apply to taxpayers to the extent that it conflicts with the terms of a settlement of a dispute agreed to before the date of issue of this Determination (see paragraphs 75 and 76 of Taxation Ruling TR 2006/10).

21. [Omitted.]

Commissioner of Taxation
13 July 2005

Previous draft:

GSTD 2005/D1

Related Rulings/Determinations:

TR 2006/10; GSTR 2000/19; GSTR 2001/4; GSTR 2003/11

Subject references:

- adjustment event
- association
- breach of membership rules
- club
- consideration
- co-operative
- fine or penalty

[12] See Division 19 of the GST Act which is about adjustment events.

- non-statutory fine or penalty
- society
- supply
- taxable supply
- trade union

Legislative references:

- ANTS(GST)A99 9-5
- ANTS(GST)A99 Div 19
- TAA 1953 Sch 1 Div 358

Case references:

- Case S65 (1996) 17 NZTC 7408
- Northamptonshire Football Association [1996] BVC 2128

ATO references

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