

GSTD 2013/1 - Goods and services tax: when a payment for a supply fails, is a failed payment fee charged by the supplier consideration for a supply?

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! This Ruling contains references to provisions of the *A New Tax System (Goods and Services Tax) Regulations 1999*, which have been replaced by the *A New Tax System (Goods and Services Tax) Regulations 2019*. This Ruling continues to have effect in relation to the remade Regulations.

Paragraph 32 of [TR 2006/10](#) provides further guidance on the status and binding effect of public rulings where the law has been repealed and rewritten.


A [comparison table](#) which provides the replacement provisions in the *A New Tax System (Goods and Services Tax) Regulations 2019* for regulations which are referenced in this Ruling is available.

! This document has changed over time. This is a consolidated version of the ruling which was published on *15 October 2014*



Goods and Services Tax Determination

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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.]

Ruling

1. The payment of a failed payment fee is not consideration¹ for a supply in the circumstances covered by this Determination.

¹ As defined in section 195-1 of the *A New Tax System (Goods and Services Tax) Act 1999* (GST Act). All further legislative references are to the GST Act unless specified otherwise.

GSTD 2013/1

2. This Determination applies where:

- there is an attempt to make a payment for the underlying supply by way of the supplier presenting a cheque or the supplier attempting a direct debit on the recipient's bank account² in accordance with the authority it has from the recipient;
- the attempted payment is dishonoured or declined and the supplier's financial institution imposes an 'inward dishonour fee' on the supplier;
- the supplier and recipient have agreed or would be taken to have agreed that in utilising direct debit or cheque payment methods the recipient will have available funds to make the payment of the initial consideration amount for the underlying supply (we accept that this would be the case in the absence of contrary arrangements between the supplier and recipient);
- the supplier and the recipient have agreed that if the payment fails the recipient will be liable to pay a fee ('failed payment fee'). The obligation to pay the failed payment fee may be included in the agreement or contract for the underlying supply, or in the terms of the Direct Debit Authority for a direct debit, or because the supplier's ability to charge a failed payment fee is specified by statute;
- the failed payment fee arises because the recipient of the underlying supply has not fulfilled its obligation to ensure funds were available to honour a cheque, or meet a direct debit request;
- the recipient's failure to fulfil its payment obligations causes the supplier to incur additional costs, such as the inward dishonour fee charged by the supplier's financier, or to suffer other loss, such that the failed payment fee is characterised as compensatory for the additional costs or loss incurred; and
- there is nothing in the agreement between supplier and recipient that describes the failed payment fee as part of the consideration for anything supplied by the supplier.

3. In the circumstances described in paragraph 2 of this Determination, payment of a failed payment fee is not consideration for either a financial supply or another supply (for example, a supply of administrative services).³

4. However, the characterisation of a payment for GST purposes is dependent upon the facts in each case. It follows that in other circumstances not covered by this Determination, it may be possible for the payment of a failed payment fee to have a sufficient nexus with the underlying supply for the failed payment fee to form part of the consideration for that supply. This Determination is limited to the circumstances set out in paragraph 2.

5. In this Determination, a 'failed payment' means a dishonoured cheque or a declined direct debit request. 'Underlying supply' means the supply in respect of which the payment failed. References to 'supplier' and 'recipient' are references to the supplier and recipient of the underlying supply. A fee charged by the supplier to the recipient in respect of the failed payment is described as a 'failed payment fee'.

² Bank account refers to any account with an Authorised Deposit-taking Institution (ADI) such as a bank, credit union or building society where a cheque facility is offered or direct debit can be used.

³ Alternative views to this conclusion are discussed in Appendix 2 to this Determination.

Example – Attempted payment for taxable supply where a direct debit is declined

6. *Ziffnet makes taxable supplies of internet services (the underlying supply). Ziffnet's internet plans are offered on a monthly basis and are invoiced in advance on the first day of the month. Ziffnet offers customers the option of making monthly payments via direct debit. To pay by this method the customer enters into a Direct Debit Authorisation agreement with Ziffnet. Under the terms of this agreement, the customer agrees that sufficient funds will be available in their account and that Ziffnet is entitled to levy a failed payment fee of \$10 if the customer's financial institution rejects the direct debit request initiated by Ziffnet. Whilst it is not specified in documentation provided to customers, Ziffnet has calculated the \$10 fee on the basis of a pre-estimate of loss, being the costs Ziffnet will incur from its financial institution when a declined direct debit payment occurs.*

7. *Polina acquires internet services from Ziffnet. Ziffnet attempts to debit Polina's account for \$40 on 1 February for that month's internet access. Polina's account has insufficient cleared funds available and the direct debit request is declined. Ziffnet contacts Polina advising that the direct debit has failed and Polina will need to ensure sufficient cleared funds are available for Ziffnet to reprocess the direct debit request, or make alternative payment within 14 days. In addition, Ziffnet advises Polina that a \$10 failed payment fee will be charged as part of the next month's billing cycle. Polina transfers funds into the account and advises Ziffnet. Ziffnet successfully reprocesses the direct debit request and debits Polina's account for \$40.*

8. *When Ziffnet initiates a direct debit on 1 March for the March internet access, the total direct debit is \$50 as this includes the additional amount of \$10 for the failed payment fee.*

9. *As the failed payment fee arises from Polina not abiding by the terms of the Direct Debit Authorisation agreement to have funds available, and the calculation of the fee is based on Ziffnet's expected loss, the \$10 is merely compensatory, it does not have a sufficient connection to any supply to be consideration for a supply. Accordingly, as the failed payment fee is not consideration for any supply made by Ziffnet, Ziffnet only makes a taxable supply of internet access and the consideration for this supply is \$40 per month. There is no GST payable in relation to the \$10 failed payment fee.*

Date of effect

10. This Determination applies 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).

11. Goods and Services Tax Advice GSTA TPP 065, which described a failed payment fee as consideration for an input taxed financial supply, is withdrawn with effect from the date of the issue of this Determination. You can choose to apply the GST treatment stated in this Determination to past transactions despite having previously relied on GSTA TPP 065 if your circumstances are consistent with those described in this Determination.⁴ This may increase the extent to which certain acquisitions you have made are treated as being for a creditable purpose.

⁴Section 105-55 of Schedule 1 to the *Taxation Administration Act 1953* (TAA) and Division 93 of the GST Act will need to be considered if adopting this treatment gives rise to additional input tax credits.

GSTD 2013/1

12. If, in the circumstances set out at paragraph 2, you have treated a failed payment fee as consideration for a taxable supply before the date of issue of this Determination, and the fee is not consideration for a supply under the views expressed in this Determination, you may be entitled to a refund. However, you would need to consider relevant time limits and the restriction on refunds of overpaid GST (see Miscellaneous Taxation Ruling MT 2010/1 *Miscellaneous tax: restrictions on GST refunds under section 105-65 of Schedule 1 to the Taxation Administration Act 1953*) including potential reimbursement of unregistered recipients.^{4A}

12A Changes made to this Determination by the Addendum that issued on 15 October 2014 have been incorporated into this version of the Determination. Refer to the Addendum to see how the Addendum amends this Determination.

Commissioner of Taxation

27 February 2013

^{4A} Section 105-65 of Schedule 1 to the TAA applies to tax periods starting on or before 30 May 2014. For tax periods starting after this date, Division 142 of the GST Act applies to deny refunds of excess GST.

Appendix 1 – Explanation

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

Background

13. When compared to other payment methods, cheque and direct debit payments have an inherent risk of being dishonoured (when a cheque is presented) or being declined (when a direct debit request is processed). This is because a successful payment using either method is contingent upon the recipient having sufficient available funds in their bank account at that time.

14. The circumstances covered by this Determination arise where there is an attempt to make a payment for the underlying supply by the supplier presenting a cheque or attempting a direct debit on the recipient's bank account in accordance with the authority it has from the recipient. The attempted payment is dishonoured or declined and the supplier's financial institution imposes an 'inward dishonour fee' on the supplier.⁵ This Determination does not address supplies associated with the 'dishonour fee' charged by financial institutions to their account holders, as these dishonour fees are part of the consideration for the supply of the bank account.⁶

15. The parties agree that if the payment fails the recipient will be liable to pay a fee which we refer to as a 'failed payment fee'. The obligation to pay the fee may be included in the agreement or contract for the underlying supply, or in the terms of the Direct Debit Authority for a direct debit, or the supplier's ability to charge a failed payment fee may be specified by statute.

16. A failed payment fee can be calculated in a number of ways. For example, an agreement may specify that the supplier will pass on the cost of the 'dishonour fee' charged to the supplier by its financial institution and may also allow for the inclusion of the supplier's internal costs of managing the dishonour, such as staff costs for additional processing, or the agreement may provide for a flat fee. The agreement may not specify how the fee is calculated.

17. When a dishonour or decline occurs, the supplier will notify the recipient that they are liable to pay the failed payment fee. For example, that fee may appear as an additional amount on the next periodic invoice for the underlying supply.

Consideration for a supply

18. Consideration is defined in section 195-1 as:

consideration, for a supply or acquisition, means any consideration, within the meaning given by section 9-15, in connection with the supply or acquisition.

⁵ The recipient's financial institution may impose a similar fee (described as an 'outward dishonour fee') upon the recipient. However, this type of fee is not directly relevant to the circumstances in this Determination and is not considered further.

⁶ Items A17 and A29 of Schedule 2 to GSTR 2002/2 respectively indicate that dishonoured direct debit and dishonoured cheque fees are consideration for a financial interest mentioned in item 1 in the table in subregulation 40-5.09(3) of the GST Regulations and therefore consideration for input taxed financial supplies made by an Australian ADI.

19. Paragraphs 9-15(1)(a) and (b) provide that a payment will be consideration for a supply if the payment is in connection with a supply, or it is in response to or for the inducement of a supply. Thus, there must be a sufficient nexus between a supply and a payment for that supply, for there to be a supply for consideration.

20. In other GST rulings the Commissioner discusses the requisite link between supply and consideration for the purposes of the GST Act. In determining whether a payment is consideration under section 9-15, and whether there is a 'supply for consideration', those rulings take the view that:

- the test whether there is a sufficient nexus between the supply and the payment made is an objective one;
- regard needs to be had to the true character of the transaction; and
- an arrangement between parties will be characterised not merely by the description that the parties give to the arrangement, but by looking at all of the transactions entered into and the circumstances of the transactions.⁷

Determining whether a failed payment fee is consideration

21. In the circumstances covered by this Determination, the failed payment fee does not have sufficient nexus to any supply. The following matters, in combination, are relevant to this conclusion:

- (a) The failed payment fee relates to losses suffered by the supplier when the recipient fails to meet its obligations to have funds available.
- (b) The failed payment fee is not an intended consequence of the underlying supply, but arises because the recipient failed to have sufficient funds available.
- (c) There is nothing in addition to the underlying supply that the failed payment fee could be described as 'for', even within the broader definition of 'for consideration'.

22. The *mere* fact that an amount can have the character of damages, a penalty or compensation, does not mean it cannot be in connection with a supply. The fundamental question to be answered is whether the amount is consideration for a supply.⁸

23. This is consistent with the AAT case, *Vidler v. Commissioner of Taxation (Vidler)*⁹ in which the Tribunal commented that:

It is not sufficient to establish a relationship or an association of some kind between a payment and some act, activity or event that is not a taxable supply, or perhaps not a supply at all, and argue from that position that the payment is not consideration for a supply...

24. Nevertheless, in this case there is insufficient connection between a failed payment fee and anything supplied by the supplier.

⁷ *Marac Finance Ltd v. Virtue* [1981] 1 NZLR 586

⁸ Refer to paragraphs 64 & 65 of GSTR 2009/3.

⁹ [2009] AATA 395; 2009 ATC 10-093; (2009) 72 ATR 832.

25. This may be contrasted with circumstances where a compensatory payment is linked to a further supply. An example is the fact scenario in *Vidler*. In that case, a payment described as compensatory was a condition of a contract for the sale of land, and was found to be consideration for that supply. Here, the payment of the failed payment fee cannot be properly construed as part of the consideration for future supplies, or part of the payment of consideration for a periodic or progressive supply between the parties.

26. The circumstances of the imposition of a failed payment fee can also be distinguished from those relating to the imposition of a late payment fee.

27. The failed payment fee is not a conditional or contingent part of the agreed price. This can be contrasted with a credit card surcharge, where the supplier and recipient agree that credit card is an acceptable means of payment, and that the surcharge is payable if the recipient uses that agreed method of payment. The surcharge therefore forms part of the total consideration payable for the underlying supply.

28. In summary, taking into account all the circumstances discussed in this Determination, there is an insufficient nexus between the payment of the failed payment fee and the underlying supply.

29. However, due to the broad range of circumstances that can arise between a supplier and a recipient, it is possible that the payment of a failed payment fee in circumstances other than described in this Determination could have sufficient nexus with the underlying supply and could form part of the consideration for that supply. For that reason, it should be noted that the protection provided by this Determination only applies in the circumstances set out in paragraph 2.

Appendix 2 – Alternative views

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

Failed payment fees: consideration for a financial ‘interest’

30. An alternative view which was previously set out in Goods and Services Tax Advice (GSTA) TPP 065 (withdrawn) was that the fee was consideration for the supply of a financial ‘interest’ under item 2 in the table in subregulation 40-5.09(3) of the A New Tax System (Goods and Services Tax) Regulation 1999 (GST Regulations).¹⁰ Item 2 concerns a debt, credit arrangement, or right to credit.

31. Accordingly, such a transaction was regarded as a financial supply for the purposes of subsection 40-5(2) to the extent that the further requirements of subregulation 40-5.09(1) of the GST Regulations were met.

32. A typical transaction involves the supplier providing goods or services to the customer and in return the customer owes a debt to the supplier. When payment is made by the customer by tendering a cheque or through the activation of a direct debit instruction, the debt remains the property of the supplier until the cheque or direct debit has cleared at which time the debt is extinguished.

33. When the cheque or direct debit is dishonoured the debt remains outstanding. When considering whether an ‘interest’ in a financial supply is provided or created under GST law in this context, the Commissioner considers that the better view is that the supplier has not received any property in a debt or a new debt from the customer. That is, the original debt never ceased to exist and remained the property of the supplier.

34. Accordingly, the payment of a failed payment fee by the recipient cannot be consideration for the supply of an interest in a debt.

Failed payment fees: consideration for another supply

35. Another alternative view is that when a failed payment occurs, notifying the customer of the dishonour event and requesting a payment, or reprocessing a direct debit instruction are activities performed by the supplier that constitute an additional supply to the recipient. It would then follow that the failed payment fee is consideration for that supply.

36. The Commissioner considers that although there may be other things supplied to the recipient, such as entry into contractual rights, and things done that facilitate the underlying supply, the failed payment fee does not have a sufficient connection with such supplies.

37. Whilst a failed payment may result in the supplier having to undertake additional actions these are not services that are supplied to the recipient; they are simply a necessary part of the supplier ensuring it receives payments for amounts owed.

¹⁰ Item 2 mentions an interest in, or under, a debt, credit arrangement or right to credit.

References

Previous draft:

Not previously issued as a draft

*Related Rulings/Determinations:*GSTR 2002/2; GSTR 2009/3
MT 2010/1; TR 2006/10*Previous Rulings/Determinations:*

GSTA TPP 065

Subject references:

- GST
- GST supplies & acquisitions
- GST consideration
- direct debits
- cheques

Legislative references:

- TAA 1953
- TAA 1953 Sch 1 105-55

- TAA 1953 Sch 1 105-65
- ANTS(GST)A 1999 9-15
- ANTS(GST)A 1999 9-15(1)(a)
- ANTS(GST)A 1999 9-15(1)(b)
- ANTS(GST)A 1999 40-5(2)
- ANTS(GST)A 1999 Div 93
- ANTS(GST)A 1999 Div 142
- ANTS(GST)A 1999 195-1
- ANTS(GST)R 1999 40-5.09(1)
- ANTS(GST)R 1999 40-5.09(3)

Case references:

- *Marac Finance Ltd v. Virtue* [1981] 1 NZLR 586
- *Vidler v. Commissioner of Taxation* [2009] AATA 395; 2009 ATC 10-093; (2009) 72 ATR 832

ATO references

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