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A CRITICAL ANALYSIS OF THE SOUTH AFRICAN VAT SINGLE AND COMPOSITE SUPPLY RULES

By

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Declaration

I, **Ngidi Mzwandile**, declare that the work in this research is because of my independent effort. Therefore, all the conclusions and recommendations provided are mine. Where relevant I referred to acknowledge other people's work.

Signature:

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Abstract

The policy developments should consider not only domestic law but also the international cognisance where necessary. The study argues that the current determination of a separate part for VAT purpose is uncertain. The current value-added tax rules do not provide under what circumstances will a taxpayer make a separate supply for VAT purposes. This creates legal uncertainty and compromises certainty and predictability that are undeniably foundation of the tax system. As single or composite supply forms part of the value-added tax system, the absence of clear rules on how to determine a separate supply in SA warrant guidance. To reduce the legal uncertainty, the research argues SARS needs to provide the guidance.

List of Abbreviations and Acronyms

ABBREVIATIONS/ACRONYMS	DESCRIPTION
ATO	Australian Taxation Office
CAN	Canadian, Australian and New Zealand
CRA	Canada Revenue Agency
CSARS	Commissioner for South African Revenue Services
ECJ	European Court of Justice
EU VAT	European Union Value-Added Tax
GST/HST	Goods and Services Tax/Harmonised Sales Tax
OECD	Organisation for Economic Co-operation Development
SARS	South African Revenue Services
VAT	Value-Added Tax

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CHAPTER 1

INTRODUCTION

1.1 RESEARCH PROBLEM

Several countries have had to determine whether several distinct supplies are 'mixed or multiple supply' for value-added tax ('VAT') purposes. South Africa is no exception.[1] The research uses the terms 'single supply or separate part' interchangeable to mean a single supply. To determine for the Value-Added Tax Act 89 of 1991 ('VAT Act') whether a supply is a 'mixed or multiple supply' is paramount. Amongst other reasons, it affects on how the taxpayer must treat entire supply and the value-added tax claimable or payable when acquiring or selling the supplies under the VAT Act. The incorrect treatment of the supply puts the taxpayer at risk since the tax authority may raise reassessments and impose penalties. Therefore, where a supply entails the supply of goods or services or both, it is essential for a vendor to correctly treat the transaction to avoid these repercussions.

Essentially, the research concerns the question of how to determine whether a supply is a 'composite supply', which is not dissociable into separate supplies for the purposes of sections 8(15) and 10(22) of VAT Act, and a 'mixed supply' or 'multiple supply', which is so dissociable.[2]

1.1.1 The concept of composite supplies

The South African VAT Act does not define the term 'composite supply'. Neither the European Union VAT ('EU VAT') and Canadian, Australian and New Zealander approach ('CAN countries or/approach') define the term. The concept of composite supply originates from the supply that entails more than one item supplied together for VAT purposes. In such a supply, one supply is the taxable component and the other part is a non-taxable component.[3]

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1 See *Commissioner South African Revenue Service v British Airways plc* (141/2004) [2005] ZASCA 20 (29 March 2005) ("*British Airways*"). *Purple Parking Ltd, Airparks Services Ltd v the Commissioner of Her Majesty's Revenue Service* (ECJ 2012) (Case C-117/11) ("*Purple Parking*").

2 Sec 8(15) regulate the composite supply consists of a part that is taxable at the standard rate and the other part at zero-rate, while sec 10 deals with the composite supply that entails a taxable component, and the other component is a non-taxable supply.

3 *Virgin Atlantic Airways Ltd v Customs and Excise Commissioners, Canadian Airlines International Ltd v Customs & Excise Commissioners* [1995] BVC 93. In this matter, the air-carrier company sold aeroplane tickets to its

Each jurisdiction has a unique legislative context. However, there appears to be a consensus on the meaning of the composite supply concept. The understanding is that the composite supply is a supply with more than one component partially taxable and partly non-taxable.[4] Because of the absence of the universally and internationally accepted composite supply definition, for this research the composite supply refers to supply comprises two or more taxable or non-taxable supplies whether of goods or services or both supplied together by the same registered vendor to a recipient. The supply might attract VAT at a different rate, such as the standard, zero and exempt rates. It is instructive to consider how the South African rules deal with the composite supply.

1.1.2 The principal-agent relationship in the composite supply

Another interrelated issue that arises frequently in the composite supply is that of a principal-agent relationship.[5] To determine whether a supplier is a principal or agent will influence whether a supply in question is a single or composite supply. Therefore, this study intends to examine this issue considering *Commissioner South African Revenue Service v British Airways* matter.

1.2 METHOD-LEGAL COMPARISON

The study analyses the South African case law, relevant legislative provisions to develop more determinate rules that govern the determination of separate part or composite supplies. It also undertakes a comparative analysis to consider how the EU VAT and CAN countries treat the composite supply.

The comparative analysis explores how other legal systems may inform domestic law and official guidance. Put differently, the international analysis is useful to gain a better understanding of the meaning of the separate part is in South African law. As a result, the dissertation will rely on foreign authorities such as the legislation, case law, and policy statement to mention a few as a mechanism to develop the determinate rules for South Africa. Ultimately, the study endeavours to

customers. The services involved were amongst other services, the aeroplane ticket (which was zero-rated) as well as a limousine service (which was standard rated).

4 O Henkow "Defining the tax object in composite supplies in European VAT" (2013) 2 *World Journal of VAT/GST Law* 182-202 189; *Auckland Institute of Studies Ltd v CIR* (2002) 20 NZTC 17,685; *College of Estate Management v Customs and Excise Commissioners* [2005] BVC 704; *Commissioner of Taxation v Luxottica Retail Australia Pty Ltd* [2011] FCAFC 20.

5 *British Airways*; *Bookit Ltd v Revenue and Customs Commissioners* (Case C-607/14) [2016] BVC 21.

bring light to the legislature and South African Revenue Service ("SARS") that the need exists to develop the VAT legislation. It will be clear that SARS should provide more guidelines to lessen the legal uncertainty currently arise when determining if a supply is a separate part of the composite supply.

The justification for selecting the EU and CAN countries is as follows. In the EU VAT system, the European Court of Justice ("ECJ") has adjudicated several cases that deal with the composite supply. This resulted in the guiding principles which help to decide if several distinct supplies are separate parts or composite supply. In *Card Protection Plan Limited v Customs & Excise Commissioner*, ("*CPP*" case),[6] the ECJ developed the three-stage approach to apply when deciding if several distinct supplies are separate parts or composite supply. These principles form the foundation of the ECJ decisions, and CAN countries have also incorporated them into their domestic law.

South Africa and CAN countries have the modern value-added tax system.[7] Effectively these countries have similar value-added tax rules and principles to a certain extent. The CAN countries have similar legislative provision substantively. Intuitively, it is appropriate to consider the CAN approach on the treatment of the composite supply.

Canada

The Canadian Goods and Services Tax ("GST") system contains three sections that deal with the composite supply. These sections are 138, 139 and 169 of the Excise Tax Act 1985 ("ETA"). The Canada Revenue Agency ("CRA") has supplemented these sections by issuing the GST/HST Policy Statement P-077R2 ("GST P-077R2") as a guide to the treatment of composite supply.[8] It is instructive to contrast these provisions with the South African approach.

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6 *Card Protection Plan Limited v Customs & Excise Commissioner* [2001] 2 All ER 149 (HL) para 29-30. '*CPP* case').

7 S Poddar "Consumption taxes: The role of the value-added tax" in P Honohan *et al*., *Taxation of financial intermediation; Theory and practice for emerging economies* (2003) at 7. L Ebrill & M Keen *et al*., *The modern VAT* (2001). See also ML van Oordt "A qualitative measurement of policy options to inform value-added tax reform in South Africa" PhD Thesis, University of Pretoria, 2015 at 68-79. Retrievable online: https://repository.up.ac.za/handle/2263/53009 [accessed 27 May 2019].

8 Canada Revenue Agency "Single and Multiple Supplies: GST/HST Policy Statement P-077R2" (26 April 2004). Retrievable online: https://www.canada.ca/en/revenue-agency/services/forms-publications/publications/p-077r2/p-077r2-single-multiple-supplies.html [accessed 23 March 2020].

Australia

Section 9-75 and 9-80 of the New Tax System, Goods and Services Tax Act 55 of 1999 ('GST Act') deals with the composite supplies.[9] In 2007, the Australian Administrative Appeals Tribunal delivered an important decision regarding the principles applicable to the composite supply.[10] These principles were further analysed and confirmed by the Federal Court of Australia ("FCA") in the *Luxottica Retail Australia Pty Ltd* ("*Luxottica*"),[11]. These principles still form the foundation of the Australian approach to the composite supply. Post the *Luxottica Retail Australia* case, the Australian Taxation Office ("ATO") amended the rulings that govern the composite to reflect the guidelines provided by the court.[12]

Therefore, it is intuitive to consider these principles for the lesson for South Africa.

New Zealand

In the New Zealander, section 5(14) of the Goods and Services Act 141 of 1985 ("NZ GSA Act") regulates the composite supply transaction. The judgment of the High Court in *Auckland Institute of Studies Ltd v CIR*,[13] led the tax authority to issue the Inland Revenue *Interpretation Statement* IS 18/04 ("IS 18/04"), [14] which the taxpayer can use to determine if the supply made is single or composite.

It seems significant to contrast the South African composite supply rules to those of the foreign jurisdictions so to get any lesson so to reduce uncertainty in the county.

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9 Secs 9-75 & 9-80 of the GST Act.

10 *Tribunal in Re Food Supplier and FCT* [2007] AATA 1550; 2007 ATC 157; (2007) 66 ATR 938.

11 *Commissioner of Taxation v Luxottica Retail Australia Pty Ltd* [2011] FCAFC 20 (23 February 2011).

12 Goods and Services Tax Ruling 2001/8: "Goods & services tax: apportioning the consideration for a supply that includes taxable and non-taxable parts". Retrievable online: https://www.ato.gov.au/law/view/document?docid=GST/GSTR20018A3/NAT/ATO/00001&PiT=20120411000001 [accessed 29 October 2019].

13 (2002) 20 NZTC 17,685.

14 Inland Revenue, Interpretation Statement: IS 18/04 — Good and Services Tax— Single Supply or Multiple Supplies (2018). Retrievable online: https://www.classic.ird.gov.nz/technical-tax/interpretations/2018/interpretations-2018-is1804.html [accessed 25 march 2020].

1.3 RESEARCH OBJECTIVE AND MOTIVATION

The motivation for this study is that the current determination of the separate part for VAT purposes creates legal uncertainty.[15] The study will also show that the current case law that deals with this issue offers little guidance (if any) to lessen the uncertainty. It is further argued that the lack of guidance by SARS amplifies the legal uncertainty on how to determine the separate part in SA. Therefore, there is little official guidance on how to determine the separate part, especially in composite supplies. There are no other studies that discuss the treatment of composite supplies.

1.4 STUDY STRUCTURE

In analysing the determination of a separate part in South Africa, the research structure is:

C*hapter 1* provides an introduction and set out research problems.

Chapter 2 discusses the treatment of single and composite supply rules in South African VAT.

Chapter 3 analyses the single and composite supply rules in foreign jurisdictions VAT.

Chapter 4 provides the shortcomings of the South African approach to single and composite supply and set out recommendations.

[15] M van Oordt & R Krever "Legal Uncertainty in the South African VAT" in C Evans & R Franzen *et al*., *Tax Simplification: An African Perspective* (2019) 160-61 Chapter 7.

CHAPTER 2

THE SINGLE AND COMPOSITE SUPPLY RULES IN SOUTH AFRICA

2.1 Introduction

This chapter discusses how the current South African VAT rules deal with single or composite supplies. The discourse analyses the relevant South African authorities (i.e., VAT Act, and case law).

2.2 Single and composite supplies under the VAT

The above notes that even though the South African VAT Act does not define the term "*separate part or composite supply*", but there are relevant sections which regulate composite supplies. The analysis will now discuss these sections.

2.2.1 Section 8(15) of the VAT Act

This subsection states that:

> For the purposes of this Act, where a single supply of goods or services or goods and services would if separate considerations had been payable, have been charged with tax in part at the rate applicable under section 7(1)(a) and in part at the rate applicable under section 11, *each part of the supply* concerned shall be deemed to be a separate supply […].[16]

This subsection deals with a composite supply comprises separate parts which are supplied together. Each of these parts would if supplied individually attract the value-added tax at standard and zero rates. In such a case, the section deems each part of the supply as a separate part from other parts. This means that 15 per cent will apply on the supply that represents a standard rate supply, while a 0 per cent will apply on the part that represents a zero-rate supply.[17]

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16 Sec 8(15) of the VAT Act. (Emphasis added).

17 V Moodaley & G Badenhorst "Splitting hairs… VAT Case 1558" (2019) *Tax & Exchange Control Alert* 2-7 2. Available online: https://www.cliffedekkerhofmeyr.com/export/sites/cdh/en/news/publications/2019/Tax/downloads/Tax-Exchange-Control-Alert-7-June-2019.pdf [accessed 19 March 2020].

It seems it is irrelevant whether, from a consumer's perspective, such supplies ought to constitute a composite supply. Arguably, this section will deem each part in the composite supply to be a separate part. The below discussion outlines the South African courts' approach or interpretation to section 8(15).

2.2.2 The legal interpretation of section 8(15) of the VAT Act

The South African Supreme Court of Appeal ("SCA") has had to decide on the meaning and interpretation of section 8(15). The *Diageo South Africa (Pty) v CSARS* ("*Diageo SA*"),[18] is the relevant authority.

In casu, a South African resident supplied a non-resident with advertising and promotional services. As per the service contract, the taxpayer had an exclusive right (i.e. trademarks, intellectual property, equipment, packages, and labels) to market, distribute and promote the non-resident's alcoholic products in South Africa. As part of the agreement the taxpayer integrated and synergetic marketing strategy, the taxpayer supplied the promotional products to the customers to enhance the services,[19] distributed and consumed in South Africa. The entire service was a zero-rated supply as it constituted an exported service that is zero-rated for VAT purposes. The tax commissioner argued promotional products made up a separate supply that must be taxable at the standard rate. The question was whether the taxpayer supplied a composite service or two independent supplies (i.e. advertising and promotional services and promotional goods).

The SCA held the supply constituted two separate supplies since the taxpayer distributed promotional goods in the Republic, whereas the advertising and promotional service were zero-rated as exported services supplied to the non-resident, not present in the country at the time the services were rendered, and not related to movables in the Republic.[20]

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[18] *Diageo South Africa (Pty) v Commissioner for South African Revenue Services* (330/2019) [2020] ZASCA 34 (03 April 2020).

[19] The term promotional products refer to goods given away free of charge by the SA resident in the Republic as the means to build and maintain the brand image of the non-resident. These products include alcoholic products for sampling and branded giveaways items such as glasses, optics, towels, beer mats, lanyards, keyrings, T-shirts, aprons, caps and the like.

[20] Sec 11(2)(l) of the VAT Act.

The importance of the *Diageo SA* decision is that the SCA sets out the jurisdictional requirements must be present before section 8(15) applies. According to the court, this means that if the supply complies with all the jurisdictional requirements, each part of the composite supply will be deemed to have been supplied separately. The section 8(15) jurisdictional requirements are:[21]

a) there must be a 'single supply' of two or more types of goods or services or a combination of goods and services;

b) one consideration must be payable, as only a single supply is made; and

c) the circumstances must be such that if the supply of the goods or services or both had been charged for separately, part of the supply would have been standard rated, and part zero-rated.

The jurisdiction requirements listed in *b* and *c* appear to be clear. However, it is unclear what constitutes '*single supply'* for jurisdictional requirements. The SCA did not define the meaning and intention of '*single supply'*. Arguably this may further perpetuate the legal uncertainty embedded in the VAT system when determining a separate part in composite supply. Therefore, it remains unclear what qualifies as "*single supply*" where the taxpayer supplies composite supply.

The SCA found that all these requirements were present in the *Diageo SA* case. As a result, the promotional goods made up a separate part which ought to be taxable. To determine if the taxpayer supplied a separate part, the question is whether a part of the composite supply falls within the ambit of the deeming provisions in section 8(15).[22] If the part of the composite supply falls within section 8(15), the next step is to apply the jurisdictional requirements. The SCA enunciated the significance of this section as follows.

> The section only apportions the value-added tax rate levied under section 7 at which the vendor must pay when supplied different goods or services as a composite whole.[23]

Section 7(1) of the VAT Act, known as the imposition clause, allows the imposition of the VAT on the supply of goods, services, and importation. Section 7(1) accordingly considers each supply as a separate part.

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21 *Diageo SA* para 13.
22 *Diageo SA* para 17.
23 *British Airways* para 13.

As per *Diageo SA* case, the enquiry is whether a taxpayer has supplied a separate part, even though combined into a single supply. It appears therefore that South Africa does not concern itself with the question of the composite supply per se. The question seems to be whether the part of the composite supply is a separate supply or not. Section 8(15) regards the part of the composite supply as a separate part if such part meets all the jurisdictional requirements.

2.2.3 The economic or commercial substance test under section 8(15)

Eventually, it will be clear that foreign jurisdictions (such as CAN countries) apply the so-called economic or commercial substance test in determining if a supply is a mixed or multiple part. This test requires that several formally distinct supplies must be considered to be a single transaction when they are not independent if such approach accords with the economic or commercial reality.[24]

Consequently, the question is whether South Africa follows the 'economic substance test' when determining composite supplies, especially under section 8(15)? In *Diageo SA*, the court expressly rejected the application of the economic substance test. The SCA held as follows;

> "Section 8(15) then deemed these independent supplies to be separate supplies, each carrying its own VAT treatment. The purpose of the section was thus not the creation of *an economically, or commercially unreal outcome*, but rather the avoidance of one. Therefore, the section did not deem single supplies to be separate when they were dissociable."[25]

The court continued to state that expressions such "economically not dissociable', 'the supply not being an end in itself' and the question of 'principal and ancillary supplies", which are found in foreign authorities, play no role in the interpretation and application of section 8(15).[26] from the above SCA's remark, it is clear that South Africa does not apply the economic or commercial substance test. According to the court, section 8(15) intends to avoid any tax avoidance may ensue. Although this is correct, however, it may be argued that not all economic or commercial reality intend to achieve tax benefits. Hence the guidance in warranted in this regard.

[24] Henkow 187.
[25] *Diageo SA* para 10. (Emphasis added).
[26] *Diageo SA* para 16.

2.2.4 Section 10(22) of the VAT Act

This section deals with a supply that is partly taxable at the standard rate and taxable at zero-rate. It states that:

> Where a taxable supply is not the only matter to which a consideration relates, the supply shall be deemed to be *for such part* of the consideration as is properly attributable to it.[27]

According to the section, if a taxpayer supplies a taxable supply together with other non-taxable supplies, section 10(22) deems the supply partially taxable and non-taxable. This suggests that the value-added tax is payable on the taxable component.

2.2.5 The legal interpretation of section 10(22) of the VAT Act

There has been little written (or reported) about this section. However, the *Taxpayer v Commissioner for South African Revenue Service*[28] guides how subsection 22 should apply. The facts of the matter are that the taxpayer supplied *amongst other supplies*, money-transfer services within Africa, mobile phone credit and bureau de change services. In furtherance of the enterprise, the taxpayer makes both taxable and exempt supplies for value-added tax purposes.

One should note that the dispute before the court was not whether the taxpayer supplied a separate part. The dispute relates to the apportionment method, and whether the method should apply retroactively or retrospectively to the composite supply of the taxpayer. The facts illustrate one instance where section 10(22) applies. Section 10(22) applies to the supply with a taxable and non-taxable supply.

As for this case, one submits the court correctly ruled that value-added tax was properly payable on the taxable consideration. It is submitted that where a supply is partly taxable and exempt, section 10(22) will treat each part accordingly. The taxable part appears to constitute a separate part which qualifies to be '*for such part*'

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[27] Sec 10(22) of the VAT Act. (Emphasis added).

[28] *Taxpayer v Commissioner for the South African Revenue Services* (VAT 2063) [2019] ZATC (15 November 2019).

2.3 The meaning of '*each part of the supply*' and '*for such part*'

It is unclear what constitutes '*each part of supply*' and '*for such part*' as required by section 8(15) and 10(22), respectively. The absence of the meaning of these terms/phrases arguably causes legal uncertainty in determining the separate part for VAT purposes. The discussed court cases do not provide the meaning of these crucial terms. Arguably, it becomes a challenge for the vendors who make a composite supply of goods or services to determine a separate part. In the event where several distinct supplies are unidentifiable or inseparable, it seems unclear which part of the supply constitutes '*each part of supply*' and '*for such part*' as required by the Act.

Van Oordt and Krever correctly submit that the VAT legal uncertainty causes significant compliance costs for taxpayers.[29] The authors argue that this is so since legal uncertainty requires taxpayers to interpret the legislative provision, "with the risk of penalties if their interpretation proves incorrect".[30] One can argue that under the single and composite supply, taxpayers are likely to incur high compliance costs in pursuant of the correct meaning of '*each part of supply*' and '*for such part*' in the composite supply. Arguably this may be burdensome on the taxpayers, since to get the accurate meaning and avoid the penalties may be substantial.[31]

The submission is that SARS should provide a clear explanation and guidance to clarity under what circumstance would the taxpayer make a separate supply in the composite supply context. Without guidance, as to the meaning and intention underlying these phrases, the courts will likely to more disputes.

2.4 Principal-agent relationship in determine the single or composite supply

Sometimes, it possible that the nature of the relationship between the supplier and taxpayer could aid in assessing whether the taxpayer makes a separate part. This is so in the *CSARS v British Airways plc* case.

In the *British Airways* case, the taxpayer is an international carrier service provider who supplies its customers with the international transport service (ITS). ITS is taxable as a zero-rated service

[29] Van Oordt & Krever 161.
[30] Van Oordt & Krever 161.
[31] Van Oordt & Krever 161.

under the value-added tax. ITS included amongst other charges, the airport charges,[32] that Airport Company Ltd ('AC Ltd') (i.e. the airport operator) charges British Airways ('BA') for using the airport.

The fee that British Airways charges its passengers is the aggregate of various airport charges that separately reflected on the passenger ticket. The fee comprises an amount designed to recover BA operating costs and profit. This matter concerns one of those airport charges that go to make up the composite fee.

SARS contended BA was liable to pay value-added tax at the ordinary rate (as it was then 14%) on the airport charge of its composite fee that constitutes the recovery of the passenger service charge levied by AC Ltd. Put differently, SARS argued the airport charge formed a separate supply, thus taxable individually from ITS supply. BA contended the airport charge was part of its composite fee for the supply of ITS, the whole of which was zero-rated under section 11 of the Act.

The question was whether BA is liable to pay VAT at the ordinary rate on the element of its composite fare that constitutes the recovery of the passenger service charge levied on it by AC Ltd? The SCA found the ITS and the airport charges not to form part of a zero-rated composite supply, since BA merely recovered the airport charges as part of its operating costs.[33] As per the SCA conclusion, BA did not supply the passenger services in respect of which the airport charges were received.[34] Hence, the apportionment rule under section 8(15) did not apply to tax the element of its composite fare at the standard rate.

2.4.1.1 The implication of judgment on single or composite supply

The question is whether AC Ltd is a principal or an agent of BA? The general principle that governs the principal-agent relationship is that the principal retains all the rights and obligations derive

[32] Airport charges include, landing charge upon British Airways' aircraft, aircraft parking charges, baggage handling facilities, waiting for lounges and check-in counters offered to British Airways customers.
[33] *British Airways* para 14.
[34] *British Airways* para 14.

from the contract.[35] The principal, not the agent, makes the supply.[36] Since the principal makes the supply, the normal value-added tax consequences arise in that he must account for tax on the supply made.[37]

In *the British Airways* case, the court found that AC Ltd made the airport service supply.[38] This implies that AC Ltd acted as the principal of the airport service, not an agent of BA. This means that even though the BA acquired various supplies in furtherance of its ITS, AC Ltd remained the principal of such supplies which must account to SARS for any VAT payable. According, various supplies remained the separate parts because BA did not supply them. It is unclear whether the court would have reached the same conclusion had it found that BA was the supplier these supplies.

It is noteworthy that whether the party acts as the principal or an agent will largely depend on the facts and circumstances of each case. As per the *British Airways* case, the supply of this nature will probably be a composite supply, thus no separate part made.

2.5 Conclusion

To surmise, the key issue is the meaning of '*single supply'* under case law, and '*each part of the supply'* and '*for such part*' in terms of section 8(15) and 10(22), respectively. Even though the *Diageo SA* court seems to show when the taxpayer makes a separate part. However, the guidance does not reduce legal uncertainty. Hence, SARS should reduce legal uncertainty by issuing tax interpretation notes.

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[35] VAT guide (VAT Notice 700) The guide to Value Added Tax (VAT) about the rules and procedures (17 December 2014) para 22.2. Retrievable online: https://www.gov.uk/guidance/vat-guide-notice-700#contents [accessed 16 March 2020].

[36] Reed Elsevier UK Ltd Agency (2015) 277 Chapter 34. Retrievable online: http://www.tolleytaxtutor.co.uk/taxtutor/files/subscriber/business-tax/value-added-tax/lectures/2c34.pdf [accessed 16 March 2020].

[37] Sec 54(1) of the VAT Act provides that where a supply is made by the vendor acting as the agent on behalf of the principal, such supply is deemed to have been made to the principal, not the agent.

[38] *British Airways* paras 13-14.

CHAPTER 3

THE SINGLE AND COMPOSITE SUPPLY RULES IN THE EU AND CAN JURISDICTIONS

3.1 Introduction

This chapter provides how foreign jurisdictions determine if a taxpayer makes the separate part or composite supply in terms of indirect tax. The discussion further compares the South African approach with the international community VAT system in determining if a supply is separate part or not. It is important to note that foreign countries also known the composite supply as "*incidental, combined* or *mixed*"[39] supply. Therefore, where necessary references will also be made to these terms to the respective jurisdiction.

3.2 The EU VAT System

3.2.1 Legislative context

Article 2(1) of the Sixth VAT Council Directive, 77/388/EEC of 17 May 1977 on the harmonization of the laws of the Member States relating to turnover taxes — Common system of a value-added tax: uniform basis of assessment ("Sixth VAT Directive" as amended) provides the relevant legislative provision. The provision provides that:

> "The following shall be subject to value-added tax:
>
> The supply of goods or services effected for consideration within the territory of the country of by a taxable person acting as such;
>
> The importation of goods."[40]

In several cases, ECJ had held that as per article 2(1) each supply of goods, services or importation of goods is separate and independent. ECJ states:

> "In this respect, taking into account, first, that it follows from Article 2(1) of the Sixth Directive that every supply of a service must normally be regarded as distinct and independent

[39] E.g. sec 138 of the Canadian Excise Tax Act 1985 ("ETA") refers to as "incidental" supply, sec 139 refers to "mixed" supply, sec 168(8)(a) refers to as "combined supply", while the Australian GST Ruling 2001/8 refers to as "mixed or composite" supply.

[40] Article 2(1) of the Sixth VAT Directive.

> and, second, that a supply which comprises a single service from an economic point of view should not be artificially split, so as not to distort the functioning of the VAT system, the essential features of the transaction must be ascertained to determine whether the taxable person is supplying the customer, being a typical consumer, with several distinct principal services or with a single service."[41]

3.2.2 Discussion

The EU VAT system has a long-standing history on the treatment of the composite supply transactions. Dating back to 1979 in the decision of *Nederlandse Spoorwegen v Staatssecretaris van Financiën*,[42] the question before the ECJ was whether the "cash-on-delivery price charged by the carrier to deliver the customers" goods to the consignee made up an ancillary fee to the transport service price collected on the delivery of goods. Here, the cash-on-delivery fee was taxable whereas the VAT legislation exempted transport service price. The court developed and applied the principle of *accessorium sequitur*. The *accessorium sequitur* principle states that an accessory thing does not lead to rather accedes to the principal thing to which it is accessory.[43] The ECJ found that the cash-on-delivery fee was ancillary or integral to a single price of the transport service price. According to the court, the cash-on-delivery fee was an accessory closely connected to the principal service, which was a transport service fee. As a result, the cash-on-delivery acquired the tax consequences of the principal service that was exempted under VAT. Since then, the EU VAT system constantly applied this principle in cases dealing with the composite supply.[44]

The point of departure in every matter that deals with supply for VAT purposes, whether it is a single or composite supply, is article 2(1) of the Sixth VAT Directive.[45] Article 2(1) as noted allows the imposition of VAT on the supply of goods or service or importation payable by the vendor. The ECJ has held that the provision deems every supply as supplied independently,[46]

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41 *CPP* para 29. *Commissioners of Customs and Excise v Madgett and Baldwin* [1998] ECR I-6229, (Joined Cases C-308/96 and C-94/97) para 24.

42 *Nederlandse Spoorwegen v Staatssecretaris van Financiën* 126/78 [1979] ECR 02041.

43 Henkow 196.

44 Henkow 189.

45 *Airtours Holidays Transport Limited v Commissioners for Her Majesty's Revenue and Customs* [2016] UKSC 21 paras 13; 19.

46 *Purple Parking* paras 26–31; *Field Fisher Waterhouse LLP v Revenue & Customs Commissioners* (Case C-392/11) [2012] BVC 292 paras 14–19.

unless the exceptions as discussed in *Card Protection Plan Limited v Customs & Excise Commissioner* exist.[47]

In the *CPP Ltd* case, the question was whether the supply comprises several parts made up a composite supply or several supplies. *In casu*, a taxpayer supplied its customers with an insurance policy cover. The insurance policy covered the customers against the financial loss, inconvenience resulting from the loss or theft of their cards or loss of items such as car keys, passports and insurance documents (exempt supply) and maintenance of the holder's card registration number (taxable supply). Since 1983, the tax authorities have been exempting the entire insurance policy supply under VAT. Notably, in 1990, the revenue authority applied a standard rate in the supply of insurance policies. The tax authority argued that CPP Ltd supplied two distinct supplies that ought to be apportioned by applying a standard rate on the taxable supply portion.

The ECJ had to decide if CPP Ltd supplied a composite supply or two distinct supplies. In deciding if a taxpayer supplies a composite or several distinct supplies, the court sets out the test as follows;[48]

a) every supply of service must normally be regarded as distinct and independent;

b) however, a supply which comprises a single service from an economic point of view should not be artificially split, so as not to distort the functioning of the VAT system; and

c) essential features of the supply must be considered in determining if the vendor supplies a typical customer with several distinct principal services or with a single service.

Kapteyn J further showed the circumstances which will most likely point towards a composite supply. The composite supply is when one or more goods or services serve as a principal component while the other goods or services serve as an ancillary component which shares the tax consequences of the principal component.[49] The court described an ancillary component as that part of the composite supply that is not an aim itself, rather enhances the enjoyment of the principal component.[50] In this circumstance, a single price paid by the customers is not a decisive factor. However, in some circumstances, there may be multiple components supplied for a single price.

47 *CPP* para 30-31.
48 *CPP* par 29.
49 *CPP* par 30.
50 *CPP* par 30.

In such cases, the single price may point to toward the composite supply. Sometimes, a customer may pay a single price for several distinct supplies. However, if the facts dictate that the customer intended to pay for several distinct supplies, then it will be necessary to identify that part of the supply which will remain exempt.[51]

The ECJ has applied the *CPP* test in several subsequent cases when dealing with the composite supply. For instance, in the *Purple Parking* case.[52] In this matter, the taxpayer supplied its customers with the 'off-airport park-and-ride' service where the customers could park their cars at a safe parking operation and board a bus or mini-bus provided by Purple Parking to the airport. The question before the court was whether the supply of the 'off-airport park-and-ride' service and transport service to and from the airport made up a composite service or two distinct services.

The court applied the *CPP Ltd* criteria and concluded that the two services formed a composite service for VAT purposes. Amongst other reasons, the court noted the taxpayer charged a single price for the parking service. More so, the taxpayer only charged the customers based on the duration or length of the time parked (some customers could park their cars for several days on average),[53] as opposed to the number of customers transported to and from the airport.[54] According to the court, additional transport service to and from the airport was an inevitable supply since the parking was at a distance from the parking operation. The transport service was just a completion of the supply of the principal parking service.[55] In *Finanzamt Burgdorf v Manfred Bog*,[56] the ECJ had to decide if the supply of beverages (taxable supply) supplied together with the food or meals prepared for an immediate consumption taxable at a reduced rate made up a composite supply or two independent supplies.[57] The court applied the *CPP Ltd* test to conclude that from the consumer's standpoint, this supply made up a composite supply.

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[51] See the apportionment method in this regard, *ECJ, Joined Cases C-308/96 & C-94/97, Commissioners of Customs and Excise V T.P. Madgett, R.M. and the Howden Court Hotel* [1998] ECR I-6229 paras 45-46.

[52] *Purple Parking; Město Žamberk v Finanční Ředitelství v Hradci Králové ECJ*, Case C-18/12, [2013] ECR I-0000.

[53] *Purple Parking* paras 33-36.

[54] *Purple Parking* par 34.

[55] *Purple Parking* paras 12-22.

[56] *Finanzamt Burgdorf v Manfred Bog; CinemaxX Entertainment GmbH & Co. KG v Finanzamt Hamburg-Barmbek-Uhlenhorst; Lothar Lohmeyer v Finanzamt Minden and Fleischerei Nier GmbH & Co. KG v Finanzamt Detmold* (Joined Cases C-497/09, C-499/09, C-501/09 & C-502/09) [2011] ECR I-01457 (thereafter '*Bog & Others*').

[57] *Manfred Bog* & *Other* paras 23-24.

Notably, the EU Member States have also adopted these principles. The EU Member States apply the principles when facing the question of composite supply. The former EU Member State, the United Kingdom ('UK') courts, have applied the test consistently in several cases. For example, in the *British Airways* case,[58] the Court of Appeal found that the provision of in-flight catering was, in substance and reality, an integral part of the supply of air transportation.[59]

Therefore, the above proves that this test forms a foundation of the EU VAT system in determining if a supply comprises a composite supply or several individual supplies. In what follows is the demonstration of how CAN countries treat the composite supply.

3.3 Canadian System

3.3.1 General comments

As per the Canada Revenue Agency ('CRA'), the issue is whether a transaction comprising several elements is a single supply or two or more supplies.[60] The distinction is important where the taxpayer supplied a combination of elements, some of which would be taxable 7% or 15% and some of which would be zero-rated or exempt from GST/HST if supplied separately.[61]

To determine if a supply is a single supply or multiple supplies, CRA uses the following general principles:[62]

a) every supply should be regarded as distinct and independent;

b) a supply that is a single supply from an economic point of view should not be artificially split; and

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58 *British Airways plc v. Customs and Excise Commissioners* (1990) 5 BVC 97.

59 *British Airways* (1990) paras 102-103 notes that '…Catering facilities are part of and integral to the transportation in that degree of comfort which British Airways have decided is commercially appropriate and indeed necessary to attract passengers.

60 Single and Multiple Supplies. Retrievable online: https://www.canada.ca/en/revenue-agency/services/forms-publications/publications/p-077r2/p-077r2-single-multiple-supplies.html [accessed 09 November 2020].

61 Canada Revenue Agency 'Single and Multiple Supplies: GST/HST Policy Statement P-077R2' (26 April 2004), https://www.canada.ca/en/revenue-agency/services/forms-publications/publications/p-077r2/p-077r2-single-multiple-supplies.html [accessed 23 March 2020].

62 See also *FCA, Hidden Valley Golf Resort Assn. v. R.* [2000] G.S.T.C. 42 paras 20, 28-29; *TCC, Camp Mini-Yo-We Inc. v. R.* [2006] G.S.T.C. 154 paras 6-11; *TCC, Great Canadian Trophy Hunts Inc. v. R.* [2005] TCC 612 para 25.

c) there is a single supply where one or more elements constitute the supply and remaining elements serve only to enhance the supply.

3.3.2 The meaning of '*single supplies and multiple supplies'*

The CRA Policy Statement P-077R2 defines multiple supplies as "when one or more of the elements can sensibly or realistically be broken out."[63] Conversely, two or more elements are of a single supply when:

- "the elements are integral components;
- the elements are inextricably bound up with each other;
- the elements are so intertwined and interdependent that they must be supplied together; *or*
- one element of the transaction is so dominated by another element that the first element has lost any identity for fiscal purposes."[64]

CRA also stresses that when conducting the determination, it is important that one confines the analysis to the transaction at issue, rather than referring to other transactions resemble similar element.[65] Therefore, whether the supply is single supply or multiple supplies depends on the subjective analysis of each fact.

3.3.3 Incidental supply

If the above analysis concludes that there are multiple supplies, it is then necessary to determine whether one of those supplies is incidental to another and whether it may consequently be deemed to form part of a single supply according to section 138 of the Canadian Excise Tax Act.[66]

This section states that:

> *A particular property or service is supplied together with any other property or service for a single consideration*, and it *may reasonably* be regarded that the provision of the other property

[63] Single and Multiple Supplies: GST/HST Policy Statement P-077R2. Revised first in April 1998 second on March 1999.
[64] Single and Multiple Supplies: GST/HST Policy Statement P-077R2.
[65] Single and Multiple Supplies: GST/HST Policy Statement P-077R2; S Conese "The EU VAT treatment of composite supplies: evolution trends and critical points" LLM Thesis, University of Tilburg (2017) 58.
[66] Single and Multiple Supplies: GST/HST Policy Statement P-077R2.

> or service is *incidental* to the provision of the particular property or service, the other property or service shall be deemed to form part of the particular property or service so supplied.[67]

It appears from this section that an ancillary component forms part of the principal supply if it is reasonable and incidental thereto. But what do we mean by "*a particular property or service is supplied together with any other property or service for a single consideration*" and "*reasonably and incidental*"?

3.3.4 Meaning of the "*where a particular property or service is supplied together with any other property or service*"

The reliance upon section 138 requires that one proves element is the incidental supply. The analysis must further prove that more than one property or service are supplied together. The policy statement explicitly requires that one establish that the number of supplies being made is part of a particular transaction.[68] Section 138 may apply in three instances, namely;[69]

- "where it reasonably be determined that at least two supplies are being made together;
- where more than two supplies are being made. This may be the case where a supplier makes a primary supply together with more than one secondary incidental supply;
- where more than one primary supply and one or more secondary supplies are made. In this regard, it will be necessary to evaluate each secondary supply concerning its respective primary supply."

Therefore, if it is determined that only one supply is being made, section 138 will not apply to the particular transaction. It is submitted that where more than two supplies are made together, each supply will have to be analysed in relation to each other supply to if the provision of one property or service may be regarded as incidental to the provision of another supply.

3.3.5 Meaning of the "*reasonably regarded as incidental*"[70]

CRA states the arrangements, contracts, and all other circumstances that exist between the supplier and recipient regarding transaction or series of transactions, should inform the meaning "reasonable regarded as incidental". Also, the meaning thereof must consider the context of design and purpose of section 138. According to the Policy Statement P-077R2, the purpose of the section

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67 Excise Tax Act R.S.C.,1985, c. E-15 (thereafter 'ETA'). (Emphasis added).
68 Single and Multiple Supplies: GST/HST Policy Statement P-077R2.
69 Single and Multiple Supplies: GST/HST Policy Statement P-077R2.
70 Single and Multiple Supplies: GST/HST Policy Statement P-077R2.

is to deal with recurring commercial transactions where an allocation of the purchase price between two or more elements provided together would be administratively cumbersome for the supplier particularly where the value of the property or services is small.

Definitions of '*incidental'* often use word and phrase such as[71]

- Minor role
- Not essential
- Subordinate
- Depending upon
- Pertaining to

Based on these words or phrases, one can surmise the relationship that must exist between the properties and/or services being provided for one to be regarded as incidental to the other. Policy Statement continues to state that the provision of the incidental supply would have to be insignificant, or of little importance relative to the provision of the other. Arguably, the provision of the incidental supply should only play a minor role in relation to the principal supply. Where the incidental supply plays an essential role by itself in a particular transaction, it is unlikely to be reasonably regarded as incidental supply.[72]

Therefore, separate part ought to play a relatively minor role to the provision of the other supply. CRA affirms this that section 138 will not apply to transactions where its application would have significant tax revenue implications.[73] Therefore, it can be argued that where the separate part imposes little revenue losses, it will probably be reasonably regarded as incidental supply. Thus, there will be no separate part supplied. Conversely, if the separate part will cause significant tax revenue losses, it will not be reasonably regarded as an incidental part. That incidental supply will make up an independent part for GST/HST purposes.

[71] Single and Multiple Supplies: GST/HST Policy Statement P-077R2.
[72] Single and Multiple Supplies: GST/HST Policy Statement P-077R2.
[73] Single and Multiple Supplies: GST/HST Policy Statement P-077R2.

3.3.6 Mixed supply: financial service

Section 139 of the ETA specifically deals with financial services supplied together with other supplies. It states that:

> "(a) one or more financial services are supplied together with one or more other services that are not financial services, or with properties that are not capital properties of the supplier, for a single consideration,
>
> (b) the financial services are related to the other services or the properties, as the case may be,
>
> (c) it is the usual practice of the supplier to supply those or similar services, or those or similar properties and services, together in the ordinary course of the business of the supplier, and
>
> (d) the total of all amounts, each of which would be the consideration for a financial service so supplied if that financial service had been supplied separately, is greater than 50% of the total of all amounts, each of which would be the consideration for a service or property so supplied if that service or property had been supplied separately, the supply of each of the services and properties shall be deemed to be a supply of financial service."

Whether the transaction is a mixed supply is a question of fact. As noted, one will conduct the subject analysis to determine if a supply is mixed or not. Therefore, to classify financial service transaction as a mixed supply, it must comply with all the requirements listed in section 139(*a*)-(*d*). Conversely, failing to meet one or more of these requirements, the financial service transaction may not be considered as a mixed supply for GST/HST purposes.

3.3.7 Combination supply

Section 168(8) of ETA which states that:

> "where a supply of any combination of service, personal property or real property (each of which is in this subsection referred to as an "element") is made and the consideration for each element is *not separately identified*,
>
> (i) where the value of a particular element *can reasonably be regarded as exceeding the value of each of the other elements*, the supply of all the elements shall be deemed to supply only of the particular element; and
>
> (ii) in any other cases, the supply of all the elements shall be deemed
>
> *(a)* where one of the elements is real property, to be the supply only of real property; and
>
> *(b)* in any other case, to supply only of service."

Butcher submits one should conduct the subjective analysis to determine if an element is "*not separately identified*" or if its "*value can reasonably be regarded as exceeding the other element*".[74] Subsection 168(8) establishes rules for determining the nature of supply to determine when tax is payable. These rules apply where the supply comprises any combination of service, personal property or real property (each of which is referred to as an element) and the consideration for each element is not separately identified (i.e., "there is a single all-inclusive price").[75] The policy statement notes these rules operate to ensure that tax on the entire consideration for the combined supply is payable one day. For example, where the supply comprises personal property (e.g., a sale of a dishwasher) as part of a supply and-install contract and the value of the dishwasher is greater than the installation service.[76] In this circumstance, GST/HST will be payable according to the timing rules in relation to supplies through sale of tangible personal property.[77]

Section 168(8) also applies to the supply comprises the sale of real property and service, where one cannot reasonably determine which element is of greater value. For example, the sale and subsequent renovation of a house. In terms of the policy statement, CRA will regard the supply as a supply of real property.[78] Subsequently, the tax on the combined supply (including the renovation after the sale of the house) becomes payable.

It is submitted that where an element is "*separately identified*" or its *value can reasonably be regarded as exceeding the other element*", that element is likely to constitute a separate part and vice versa.

3.4 Australian System

On the 1st of July 2010, the Australian Taxation Office ('ATO') has issued an amended tax ruling, the GSTR 2001/8,[79] which deals with a supply that includes a taxable and non-taxable part under

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74 R Butcher *Value-added taxation in Canada: GST, HST and QST* (2009) 57.

75 CRA, Combined Supplies (GST 300-6-16). Retrievable online: https://www.canada.ca/en/revenue-agency/services/forms-publications/publcations/g300-6-16/combined-supplies-gst-300-6-16.html [accessed 10 November 2020].

76 CRA, Combined Supplies (GST 300-6-16).

77 CRA, Combined Supplies (GST 300-6-16).

78 CRA, Combined Supplies (GST 300-6-16).

79 Goods and Services Tax Ruling 2001/8: "Goods & services tax: apportioning the consideration for a supply that includes taxable and non-taxable parts" (thereafter 'GSTR 2001/8'), Available https://www.ato.gov.au/law/view/document?docid=GST/GSTR20018A3/NAT/ATO/00001&PiT=20120411000001 [accessed 29 October 2019].

A New Tax System (Goods and Services Tax) Act 1999, (thereafter 'GST Act'). Notably, the GSTR uses the terms '*mixed supply*' and '*composite supply'* which the GST Act makes no reference to. However, these terms are used to identify whether a supply has taxable and non-taxable components which informs the extent to which a supply may be a taxable supply.

Section 9-75 of the GST Act deals with the value of entirely or fully taxable supplies. Section 9-80, deals with the supplies which are partly taxable and partly either GST- free or input taxed.[80] In essence, the sections provide formulas that guide the extent to which the GST is payable in the making of the '*mixed or composite'* supply.

3.4.1 Mixed supply

At paragraph 43, GSTR 2001/8 defines a "*mixed supply*" as;

> a single supply made up of *separately identifiable parts*, where one or more of the parts is taxable and one or more of the parts is non-taxable, and these parts are not integral, ancillary or incidental in relation to a dominant part of the supply.

Paragraphs 45 to 54C of the GSTR 2001/8 explain how to identify whether a supply has separately identifiable parts. At paragraphs 45 and 52, it states that;

> "45. In many circumstances, it will be a matter of fact and degree whether the parts of a supply are separately identifiable, and retain their own identity.
>
> [..]
>
> 52. The Commissioner's view is that a supply has separately identifiable parts where the parts require individual recognition and retention as separate parts, due to their relative significance in the supply. This view applies where the supply comprises a mix of separate things, such as various combinations of goods and services, including the provision of advice."

Accordingly, whether a supply is separately identifiable is a matter of "facts and degree" and the ability to "retain its own identity". The Commissioner retains the power to determine if a taxpayer makes the separately identifiable part.

3.4.2 Composite supply

A "*composite supply*" is described as;

[80] Input-taxed refers to the supply that is not subject to output tax, but the taxpayer is also not entitled to an input tax credit for tax on any acquisitions to the extent that the acquisition relates to the making of input taxed supplies. this is equivalent to the exempt supplies in SA. E.g., the rendering of the financial supplies.

> "a single supply made up of one *dominant part* and other parts that are not treated as having a separate identity as they are *integral, ancillary, or incidental* to the dominant part of the supply."[81]

The GSTR 2001/8 treats the composite supply as a "supply of a single thing".[82] Paragraphs 55 to 63 explain what integral, ancillary or incidental parts are.

3.4.2.1 Integral, ancillary, or incidental parts

GSTR 2001/8 provides that some supplies include parts that do not need to be separately recognised for GST purposes. These supplies are referred to as parts of a supply as being integral, ancillary, or incidental. In a composite supply, the dominant part of the supply has subordinate parts that complement the dominant part.[83] If such a supply is analysed in a "common-sense way", it can be seen that the supply is essentially the provision of one thing. It need not be broken down, unbundled or dissected any further.[84] For this reason, a composite supply "may appear, at first, to have more than one part, but is treated as if it is the supply of one thing."[85]

It is noteworthy that no single factor (by itself) will provide the sole test one uses to determine whether a part of a supply is *integral, ancillary, or incidental* to the dominant part of the supply.[86] Having regard to all the circumstances, and taking a common-sense and practical approach, indicators that a part may be integral, ancillary or incidental include where:

- "you would reasonably conclude that it is a means of better enjoying the dominant thing supplied, rather than constituting for customers an aim in itself; or
- it represents a marginal proportion of the total value of the package compared to the dominant part; or
- it is necessary or contributes to the supply as a whole, but cannot be identified as the dominant part of the supply; or
- it contributes to the proper performance of the contract to supply the dominant part."[87]

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81 GSTR 2001/8 11 para 43. (Emphasis added).
82 GSTR 2001/8 5 para 17.
83 GSTR 2001/8 55 para 15.
84 GSTR 2001/8 55 para 15.
85 GSTR 2001/8 55. para 15.
86 See Lord Hope of Craighead in *Customs and Excise Commissioners v. British Telecommunications plc* [1999] BVC 306 at 314. GSTR 2001/8 59 para 17.
87 GSTR 2001/8 59 para 17.

To determine whether a supplier is making a mixed or composite supply, the key question is whether the supply should be regarded as having more than one separately identifiable part, or whether it is essentially a supply of one dominant part with one or more integral, ancillary or incidental parts.[88]

3.4.3 Case law

Australian courts have in several cases called to determine whether the supply with several distinct supplies makes up a mixed or composite supply. For instance, in *Saga Holidays v Commissioner of Taxation*,[89] the court had to determine if a portion of the accommodation element that related to accommodation provided in Australia and sold as a package made up a mixed or composite supply. Stone J concentrated on the 'social and economic reality' of the supply. The court found that the accommodation component that included several parts in addition to the right to occupy a room was a single supply which was properly characterised as a supply of real property, it was a composite supply.[90] In *Commissioner of Taxation v Luxottica Retail Australia Pty Ltd*,[91] the Federal Court of Australia ('FCA') had to determine if the supply comprised the prescription lenses fitted into frames for glasses and sunglasses (i.e. the frame and a pair of lenses) was a mixed or composite supply.

The FCA noted the supply entailed the sunglasses and lenses prescription, which may be purchased as separate items. However, a common-sense approach comfortable with the 'practical business tax'[92] the outcome requires the supply be to regard a composite supply of the pair of spectacles.[93] Last, in *Re Food Supplier and Commissioner of Taxation (Food Supplier)*,[94] the court

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88 GSTR 2001/8 11 para 44.

89 *Saga Holidays v Commissioner of Taxation* 2006 ATC 4841 (thereafter '*Saga Holidays'*).

90 *Saga Holidays* para 43.

91 *Commissioner of Taxation v Luxottica Retail Australia Pty Ltd* [2011] FCAFC 20 (thereafter '*Luxottica*').

92 The GST is classified as a 'practical business tax' since according to several cases, the supplier as opposed to the consumer the collection of the tax. The tax is collected by the suppliers at the various stage of the supply chain. Last, in exceptional cases, where it is practicable to "quarantine business" from the ultimate tax burden, the supplier bears the full burden of the GST. See generally *HP Mercantile Pty Ltd V Commissioner of Taxation* (2005) 143 FCR 553 para 66; *Sterling Guardian Pty Ltd v Commissioner of Taxation* (2005) 220 ALR 550 para 39; *Saga Holidays* para 30. *ACP Publishing Pty Ltd v Commissioner of Taxation* [2005] FCAFC para 2.

93 *Luxottica* paras 13-15.

94 *Re Food Supplier and Commissioner of Taxation* (2007) 66 ATR 938.

found that the supply of the promotional items supplied together with food such a jar of coffee (main item) and a mug (promotional item) made up a mixed supply each part taxable individually.

The Australian system appears to focus on the element of the supply combined or disaggregated to alter the nature of the supply from taxable or non-taxable or vice visa.[95] In deciding whether a supply comprises several distinct supplies or composite supply, the common-sense approach is adopted.[96]

3.5 New Zealand System

New Zealand Goods and Services Act 141 of 1985 (thereafter 'NZ GST Act') regulate the imposition of goods and services tax. The relevant provision is section 5(14) of the NZ GST Act states:

> If a supply charged with a tax under section 8 [standard rate], but sections 11, 11A, 11B, 11AB, 11B or 11C [zero rates] requires part of the supply to be charged at the rate of 0%, that part of the supply is treated as being separate supply.

As per section 5(14) of the GST Act, where a supply comprises several distinct supplies, one taxable as the standard rate supply and the other as a zero-rate supply, the section treats each part as a separate supply. The standard and zero rates apply to different parts accordingly.

Also, the Inland Revenue ('IR') has provided an Interpretation Statement that is detailed on the '*single supply'* or '*multiple supplies*'.[97] According to IS 18/04, first, is to consider if the so-called 'boundary issues' arise or not when dealing with the composite supply. Boundary issues primarily arise where some supplies in the composite supply are subject to VAT at different GST rates (i.e. exempt, standard, zero rates or not subject to GST).[98] Boundary issues mean one should first consider if the entire composite supply falls within the specific deeming provisions of the GST Act. Essentially, if the supply falls within one of these specific provisions, irrespective of how the

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95 A Schenk & V Thuronyi *et al*., *Value added tax: a comparative approach* (2015) 129.

96 GSTR 2001/8 6 paras 20.

97 Inland Revenue, Interpretation Statement: IS 18/04 — Good and Services Tax— Single Supply or Multiple Supplies (2018), (thereafter 'IS 18/04'), https://www.classic.ird.gov.nz/technical-tax/interpretations/2018/interpretations-2018-is1804.html [accessed 25 March 2020].

98 IS 18/04 5 para 14.

composite supply may be treated under the ordinary principles, the specific provision overrides ordinary rules.[99] The specific provisions are as follows;[100]

a) Section 5(14B) — for rights embedded in shares;

b) Section 5(20) — for warranty services provided to a non-resident warrantor; and

c) Section 5(15) — for supplies, including residences.

If the composite supply does not fall within one of the specific inclusions, then the inquiry continues to consider the crucial test of the single or multiple supplies. In New Zealand, the High Court judgment in *Auckland Institute of Studies Ltd v CIR*[101] sets out the principles that must apply in determining whether there are single or multiple supplies. The IR issued the supplementary guidelines based on these principles. As the Canadian guidelines, the IR's guidelines mirror the *CPP Ltd* criteria as discussed in the following paragraphs.

3.5.1 The true and substantial nature test

The essential question is, what is the true and substantial nature of what the taxpayer supplies the recipient? The Revenue Commissioner considers the phrase 'the true and substantial nature' as the consideration given to the consumer perspective. The analysis must give consideration to what the recipient paid for, and the supply that has received for the consideration paid. This consideration is what the taxpayer provides the typical consumer based on the objective assessment of all the facts.[102]

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99 IS 18/04 6 para 20.

100 IS 18/04 paras 19-20. Sec 5(14B) requires that if part of a supply of a share in the supply of a right to receive supplies of goods and services that are not exempt supplies, the supply of the right is treated as being a separate supply; sec (20) also requires the supply of goods and services to the final consumer to be treated as the service of remedying a defect to the non-resident warrantor. Sec 5(15) further deems a supply that includes a principal place of residence to be a separate supply from the supply of any other property included in the supply. Sec 5(15) applies to a dwelling that has been rented out by the vendor exclusively for accommodation for at least the preceding five years. For example, when a farm (which includes the farmer's house and its surrounding curtilage) is sold, sec 5(15) provides that the vendor's supply of the farmer's house and curtilage is a separate supply from the supply of the remainder of the farm. The GST treatment of each supply is determined separately.

101 *Auckland Institute of Studies Ltd v CIR* (2002) 20 NZTC 17,685 (thereafter '*Auckland Institute'*).

102 *Wilson & Horton Ltd v C of IR* (1995) 17 NZTC 12,325; *British Airways plc Customs & Excise Commissioner* [1990] STC 643 (CA); *Auckland Institute* paras 44-45.

3.5.2 The relationship between the elements supplied test

The question is, the relationship between the elements supplied. The relationship refers to whether a part that is supplied is an integral part of ancillary or incidental to the essential elements of the entire supply. This is largely depending on the facts of each case.[103] In the *Auckland Institute case*, the court had to determine if the supply of the pre-arrival services were ancillary or incidental to the principal supply of tuition services? Hansen J ruled that the pre-arrival services made up the ancillary parts to the supply of tuition services. The court held that this was so because the pre-arrival services facilitated the students undertaking a course of study.[104]

College of Estate Management v Customs and Excise Commissioners stated that the mere fact that the supply of the printed materials could not be described as an ancillary did not mean that it was to be regarded as a separate supply for tax purposes.[105] The question was whether, for tax purposes, these were to be treated as separate supplies or merely as elements in some over-arching supply.[106] *Metropolitan International School v Revenue and Customs Commissioners* succinctly explained the significance of the ancillary.[107] The court held that an element, not an end itself, ranked as an ancillary, and which contribute to the better enjoyment of the principal element.[108] Accordingly, an ancillary part does not constitute a supply itself. Hence it acquires the tax consequences of a principal part.

3.5.3 Whether it Reasonable to supply the element separately test

Is it reasonable to serve the element into separate supplies? According to the IS 18/04, this test requires taking an overall view without over-zealous dissection and considering the essential (or dominant) purpose of the supply.[109] As pointed out in the *CPP* case, similarly in the *Auckland*

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103 *Customs and Excise Commissioners v United Biscuits (UK) Limited* [1992] STC 325; *Customs and Excise Commissioners v Wellington Private Hospital Ltd [*1997] STC 445 (EWCA) 462; *College of Estate Management v Customs and Excise Commissioners* [2005] UKHL 62.

104 *Auckland Institute* paras 52; 59.

105 *College of Estate Management* para 62.

106 *College of Estate Management* para 12.

107 *Metropolitan International School v Revenue and Customs Commissioners* [2015] UKFTT 517 (TC) (thereafter '*Metropolitan International School*').

108 *Metropolitan International School* para 66.

109 IS 18/04 13 paras 55.

Institute case, the court stated that the supply that comprises a composite service from an economic point of view should not be artificially split.[110]

The court cited the judgment of *Customs and Excise Commissioners v British Telecommunication plc* in that:

> … it is clear that the fact that one 'package price' is charged without separate charge for individual supplies being specified does not prevent there being two separate supplies for VAT purposes. In my opinion, the fact that separate charges are identified in a contract or on an invoice does not on a consideration of all the circumstances necessarily prevent the various supplies from constituting one composite transaction nor does it prevent one supply from being ancillary to another supply which for VAT purposes is the dominant supply…[111]

It follows, therefore, that at the end of the inquiry if one found the supply to be multiple supplies, different VAT rates apply to each part in question. Conversely, if the supply is a composite supply, the IS 18/04 states that the last step is to consider if the entire composite supply falls within the below sections:[112]

a) Some supplies of land must be zero-rated—section 11(1) (mb) of the GST Act;
b) Other supplies may be partly zero-rated—section 11, 11A, 11AB and 11B.[113]

If these partly zero-rated sections do not apply, the GST treatment of that supply will follow the dominant element of the supply. Importantly, if no dominant component is identifiable, meaning the several equally essential elements make up the composite supply, the GST treatment will be determined by the overall characteristics of composite supply.[114]

Last, the IS 18/04 states that where multiple components are supplied with potentially different VAT treatments, a supplier must determine if he made a single or composite supply.[115] The supplier must inform the IR whether the supply with several parts makes up a single or composite supply.

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110 *CIR v Smiths City Group Ltd* (1992) 14 NZTC 9 140 (HC) 144.
111 *British Telecommunication plc* [1999] BTC 5, 273.
112 IS 18/04 14 paras 63-67.
113 While these sections provide that some taxable supplies must be zero-rated. According to the IS 18/04, while all zero-rating provisions use 'apply' some provisions indicate that part of the supply can be zero-rated by using the phrase 'to the extent that' or other equivalent wording.
114 IS 18/04 15 para 68.
115 IS 18/04 5 para 15.

While noting the different legislative context, however, a reasonable conclusion is that normally each supply is regarded as separate and distinct, a supply that is a composite supply from the economic standpoint (supplier or consumer's point of view) should not be an artificial split, and last, there is a composite supply if one or more parts make up the dominant part and the remaining ones enhance the enjoyment of the supply.

3.6 Comparative overview in determining a separate or composite supply

Table A below outlines the principles that South Africa and foreign countries to determine if a supply is a single or composite supply.

APPROACH	**JURISDICTION**		
	RSA	**CAN**	**EU**
Approach to composite supply	there must be a 'single supply' of two or more types of goods or services or a combination of goods and services.	every supply should be regarded as distinct and independent.	every supply should be regarded as distinct and independent.
	one consideration must be payable, as only a single supply is made.	a supply that is a single supply from an economic point of view should not be artificially split.	a supply that is a single supply from an economic point of view should not be artificially split.
	the circumstances must be such that if the supply of the goods or services or both had been charged for separately, part of the supply would have been standard rated, and part zero-rated.	there is a single supply where one or more elements constitute the supply and remaining elements serve only to enhance the supply.	there is a single supply where one or more elements constitute the supply and remaining elements serve only to enhance the supply.
Supplementary Rule (i.e. Ruling, Policy Statement)	N/A	Y/A	N/A
Legal Precedent	Y/A	Y/A	Y/A
Legislative framework	Y/A	Y/A	Y/A

Table A: Comparative overview of the country's perspective to composite supply

Source: Author's compilation

N/A: *Not Adopted*

Y/A: *Yes Adopted*

South African approach is that several distinct parts which constitute a composite supply must be viewed or deemed as supplied separately in terms of section 8(15) or 10(22). It seems, regarding the composite supplies, the South African taxpayer must determine if part of the supply is "*separate part*", "*each part of supply"* and "*for such part*" as required by the VAT Act. However, what constitutes these terms is arguably unclear or legally uncertainty. It is submitted that the absence of the meaning of "*separate part*", "*each part of supply*" and "*for such part*" causes the legal uncertainty. The taxpayers who make composite supplies do not have clear guidance in determining a separate part as required by the VAT Act.

On the other hand, foreign jurisdictions appear to have proper guidance in dealing with single or composite supplies. The CAN jurisdictions have widely accepted and adopted the ECJ principles set out in *CPP* case. Foreign countries have adopted these principles in a manner that suite the needs of the domestic taxpayers in address the single or composite supplies. Also, countries have a policy statement or interpretation notes that provide the taxpayer with guidance when deciding on a separate part or composite supply. For example, tax guidance provides amongst other things, the meaning of '*mixed, composite, single or multiples* supply', the *integral, ancillary or incidental,* and the test and factors must one should apply in determining if one or more parts fall under these terms. The guidance can reduce the legal uncertainty that may arise in this analysis.

To lessen the uncertainties, the ECJ had developed guiding principles set out in *CPP* case. Since the inception of these principles, ECJ has constantly and consistently applied the principles in every matter that deals with the determination of separate or composite supply. As noted, the EU VAT does not have interpretation notes, these principles have been arguably a robust tool in determining if the taxpayer makes a separate or composite supply under the EU VAT system.

It is argued that South Africa's problem lies amongst other things, the legislative wording. Researchers correctly identify this issue as the "readability of the law in terms of the types of words used in the tax Act."[116] The absence of the meaning of "*separate part*", "*each part of supply*" and "*for such part*" for VAT purposes cause the legal uncertainty. The VAT vendors who make composite supplies do not have clear guidance in determining a separate part as required by the

[116] Van Oordt & Krever 161.

VAT Act. Van and Krever rightly put that under the readability, "longer, but well-drafted law that provides detailed guidance may simplify compliance risk."[117] Moreover, the use of specialised terms which reduce readability that the laypersons might easily understand, and provide clear explanations to, the commercial taxpayers" may lessen the legal uncertainty.

Notably, not all taxpayers are acquainted with the reading of tax legislation. This is so because these taxpayers rely on tax authority to discern the intention behind a particular section.[118] With this in mind, it is clear that the taxpayers rely on SARS for the intention and the meaning behind the composite supply provisions. Therefore, SARS must provide a clear explanation and guidance in determining if part of the composite supply is separate or not.

117 Van Oordt & Krever 161.
118 Van Oordt & Krever 161.

CHAPTER 4

CONCLUSIONS AND RECOMMENDATIONS

4.1 Conclusion

With an exception to the South African approach, the study identified the following as the foundational principles in determining a separate part of the supply. That;

i) every supply should be regarded as distinct and independent;

ii) a supply that is a single supply from an economic point of view should not be artificially split; and

iii) there is a single supply where one or more elements constitute the supply and remaining elements serve only to enhance the supply.

4.2 The shortcomings of the South African approach to composite supply

It is argued that South Africa's uncertainty lies amongst other things, the legislative wording. An empirical research rightly points it out as the "readability" of the law under which certain types of words are used in the tax Act.[119] The absence of the meaning of "*separate part*", "*each part of supply*" and "*for such part*" for VAT purposes cause the legal uncertainty. The VAT vendors who make composite supplies do not have clear guidance in determining the "*separate part, each part of supply or for such part*" as required by the VAT Act.

Van and Krever rightly put that under the readability "longer, but well-drafted law that provides detailed guidance may simplify compliance risk."[120] Using specialised terms which reduce readability, that laypersons easily understood, might reduce the legal uncertainty.[121] The specialised terminologies can minimise the uncertainty by providing a clear and comprehensive explanation to the commercial taxpayers.

119 Van Oordt & Krever 161.
120 Van Oordt & Krever 161.
121 Van Oordt & Krever 161.

Notably, not all taxpayers are acquainted with the reading of tax legislation. This is so because these taxpayers rely on tax authority to discern the intention behind a particular section.[122] With this in mind, it is clear that the taxpayers rely on SARS to provide the intention and meaning of these terms. Therefore, clear explanation and guidance is needed to clarify the meaning of "*separate part, each part of supply or for such part*" in composite supply context. It is submitted that guidance may enhance tax system certainty and reduce the compliance costs the taxpayers are likely to incur when establishing the intention and meaning of these terminologies.

4.3 Recommendations

To address the identified issues and improve the South African VAT system efficacy, the research suggests the recommendations. These are namely, SARS interpretation notes, legal precedent certainty, and additional composite supply rule. The discussion will now provide these recommendations.

4.3.1 Issuance of Interpretation Note

SARS notes that '… certainty and predictability are undeniably important in the tax arena.'[123] To enhance certainty in the tax system, SARS may supplement the existing single or composite supply rules with guidelines. This rule will clarify the SARS position in determining the separate part. As clear in the CAN countries, SARS may provide the taxpayers with step-by-step guidance on how to determine if the taxpayer makes a separate part in composite supply context.

4.3.2 Legal Precedent Certainty

Although policymaking or legislative decisions ought to be left to the relevant bodies, such as the executive authority,[124] however, in exceptional cases, the courts may exercise its power to reduce legal uncertainty.[125]. This is because the nature of these decisions typically involves several economic and political considerations which the courts have less knowledge thereof.[126]

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122 Van Oordt & Krever 161.

123 SARS *Discussion paper on tax avoidance and section 103 of the Income Tax Act 58 of 1962* (2005) 46.

124 *Union of India v. Azadi Bachao Andolan (*2004) 10 SCC 1. K Benedict "The Australian GST regime and financial services: How did we get here and where are we going?" (2011) 9(2) *eJournal of Tax Research* 174-193 174.

125 See *Mazibuko & Another v S* (8774/09) [2009] ZAKZPHC 2010 (1) SACR 433 (KZP) (19 November 2009) para 13. Exceptional circumstances refer to any factors which the opinion of the court should be considered.

126 *Union of India v. Azadi Bachao Andolan (*2004) 10 SCC 1.

In *Canada Trustco,* court correctly stated that one *must*[127] interpret the tax rules in a manner that permits constancy, predictability, and fairness to enable the taxpayer to manage their affairs "intelligently". As noted in the EU VAT system that ECJ plays a crucial role to reduce any legal uncertainty arise in determining the separate part. It may be argued that South African courts have a role to play. The courts may develop robust and consistent principles which may be applied in determining if the separate part is made or not. Importantly, this may be done on a case-by-case approach, considering the circumstances of the supply.

4.3.3 Additional Composite Supply Rule

South Africa may also supplement or expand the current single or composite supply rules with new robust rules — which provide a detailed approach/guidance. The rule will allow courts to effectively consider the determination of a separate part. While ensuring a proper determination of the separate part, the rule ought to prevent tax avoidances. It is submitted this can be achieved by crafting a clause in a manner that is open-ended or none-exhaustive.

127 *Canada Trustco Mortgage Company v The Queen* [2003] CTC 2009 para 12.

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