Privy Council Appeal No. 39 of 1989

The Commissioner of Inland Revenue *Appellant*

v.

Databank Systems Limited *Respondent*

FROM

THE COURT OF APPEAL OF NEW ZEALAND

JUDGMENT OF THE LORDS OF THE JUDICIAL COMMITTEE OF THE PRIVY COUNCIL, DELIVERED THE 23RD JULY 1990

Present at the hearing:-

THE LORD CHANCELLOR
(LORD MACKAY OF CLASHFERN)
LORD BRANDON OF OAKBROOK
LORD TEMPLEMAN
LORD ACKNER
LORD LOWRY

*[Majority Judgment delivered by **Lord Templeman**]*

By an Agreement dated 17th July 1969 and made between the respondent, Databank Systems Limited, ("Databank") and five clearing banks, Databank agreed:-

> "To provide for each of the Member Banks a General Bank Accounting and Record Package Service (commonly known as the 'C.I.F. Package' ...) consisting of the basic services mentioned in the Schedule hereto as the same may be varied or extended from time to time by agreement ..."

The initials C.I.F. mean customer information file. The list of basic services of the C.I.F. Package as set out in the Schedule were as follows:-

> "1. Full range of payment services.
>
> 2. Full customer static information.
>
> 3. Full customer accounting records, including:-
>
> (a) Statements
> (b) Control Reports
> (c) Interest and charges
> (d) Asset records
> (e) Collateral
> (f) History and Analysis

4. Full branch general ledger, including:-

(a) Account records
(b) Control reports
(c) Budget limits
(d) History and Analysis."

By paragraph 2 of the Agreement it was provided that:-

"... Databank will arrange to collect each business day from each of the Member Banks (or Branches thereof respectively) at designated pick-up points ... all vouchers maintenance and other forms which the said respective Member Banks may require to have processed by Databank at its computer centres in connection with the C.I.F. Package ..."

By paragraph 4 Databank agreed to process promptly after receipt "all input items such as cheques deposits credits debits maintenance and other forms". Databank disclaimed liability "for or on account of incorrect encoding mispostings incorrect recording or other errors in the processing or recording of data received from Member Banks". By paragraph 5 Databank agreed to return all outputs from the relevant computer centre to the designated pick-up points of the respective Member Banks. By paragraph 9 Databank agreed to give priority to the Member Banks for their respective servicing requirements over other users of Databank's computer processing services and agreed that "all Member Banks will receive uniform fair and equitable treatment from Databank in the servicing of their respective processing requirements in terms of this Agreement". By paragraph 7 each bank agreed to pay the charges for the C.I.F. Package services to be provided by Databank "separately determined having regard to the time required for the processing of each function within the C.I.F. Package". In the course of the present proceedings a brief of evidence was submitted by Mr. Shaw who was the manager of the bank customer group of Databank. He explained that:-

"Databank undertakes four major activities for the Banks:

(a) Providing a financial clearing system covering various types of transactions (and forming part of the settlement process).

(b) The posting of transactions to customer accounts, and maintenance of computer files of customer accounts.

(c) Network management.

(d) Software support and development."

The question is whether the services supplied by Databank pursuant to the Agreement dated 17th July 1969 are financial services exempt from the Goods and Services Tax ("G.S.T."). The provisions of the Agreement appear to provide computer services consistently with the first three objects of Databank set out in its Memorandum of Association as follows:-

> "(a) To provide electronic data processing facilities and services for members of the Company and other persons;
>
> (b) To purchase take on lease or otherwise acquire and to install operate and maintain machines computers apparatus equipment and facilities of all kinds for the sorting processing calculating collating storing and recording by electronic electrical mechanical or photographical means or by any other means whatsoever of accounts records data and information of every description and for all purposes;
>
> (c) To collect collate prepare record process and circulate statistical information of every description and for all purposes;"

Davison C.J. and the majority of the Court of Appeal (Cooke P., Somers and Casey JJ., Richardson and McMullin JJ. dissenting) have held that Databank provides financial services. The Commissioner of Inland Revenue appeals to the Board.

Section 8(1) of the Goods and Services Tax Act 1985 imposes G.S.T. at the rate of 10%:-

> "... on the supply (but not including an exempt supply) in New Zealand of goods and services ... by a registered person in the course or furtherance of a taxable activity carried on by that person, by reference to the value of that supply."

By section 6(1) a taxable activity means:-

> "(a) Any activity which is carried on ... by any person, ... and involves ..., in whole or in part, the supply of goods and services to any other person for a consideration; and includes any such activity carried on in the form of a business, ..."

By section 6(3):-

> "Notwithstanding anything in subsections (1) and (2) of this section, for the purposes of this Act the term 'taxable activity' shall not include, in relation to any person, -
>
> ...
>
> (d) Any activity to the extent to which the activity involves the making of exempt supplies."

Section 2 defines services as meaning anything which is not goods or money; a supplier in relation to any supply of goods and services means the person making the supply, and a recipient in relation to any supply of goods and services, means the person receiving the supply.

By section 10(2):-

> "... the value of a supply of goods and services shall be such amount as, with the addition of the tax charged, is equal to ... to the extent that the consideration for the supply is consideration in money, the amount of the money;"

Databank is a registered person. Databank carries on an activity in the course of a business which involves the supply of services to the banks for a money consideration pursuant to the terms of the Agreement between Databank and the banks dated 17th July 1969. G.S.T. is therefore payable unless Databank makes exempt services. Section 14 provides that:-

> "The following supplies of goods and services shall be exempt from tax:
>
> (a) The supply of any financial services ..."

If the services supplied by Databank, pursuant to the Agreement dated 17th July 1969, are financial services then the charges paid by the banks to Databank under the Agreement are not liable to G.S.T. But if those services are not financial services then G.S.T. must be paid.

By section 3:-

> "(1) For the purposes of this Act, the term 'financial services' means any one or more of the following activities:
>
> (a) The exchange of currency (whether effected by the exchange of bank notes or coin, by crediting or debiting accounts, or otherwise):"

"Currency" is defined as any bank note or other currency of any country. Databank in performing its contractual duties under the Agreement produces no bank notes or coins for the purposes of exchange. It is the banks which exchange currency.

> "(b) The issue, payment, collection, or transfer of ownership of a cheque or letter of credit:"

A "cheque" is defined as:-

> "A cheque for the purposes of the Bills of Exchange Act 1908, ... a postal note, a money order, a traveller's cheque, or any order or authorisation (whether in writing, by electronic means, or otherwise) to a financial institution to credit or debit any account."

Databank does not issue cheques or transfer the ownership of a cheque or a letter of credit. Databank claims that its activities include the payment and collection of cheques. But a cheque does not order or authorise Databank to pay or collect money. A cheque orders or authorises a bank to pay or collect money. Databank is not a financial institution. Databank has no money which it can pay and no depository for any collection. Databank is a moneyless machine transmitting instructions and recording the payment and collection of cheques by banks.

Sub-paragraphs (c) to (k) inclusive of section 3(1) describe other activities including dealing in debts, shares, guarantees, life insurance and superannuation schemes. These activities are far removed from the activities performed by Databank under the Agreement.

Sub-paragraph (ka) is in these terms:-

> "(ka) The payment or collection of any amount of interest, principal, dividend, or other amount whatever in respect of any debt security, equity security, participatory security, credit contract, contract of life insurance, superannuation scheme, or futures contract:"

This makes it clear that section 3(1) is dealing with the payment and collection of money and not with the transmission of instructions to pay or collect money.

Finally section 3(1)(l) includes in the term "financial services" the activity of:-

> "(l) Agreeing to do, or arranging any of the activities specified in paragraph (a) to (ka) of this sub-section, other than advising thereon."

Databank claims that by the Agreement it agrees or arranges the payment and collection of cheques. But while a bank may agree to pay and collect cheques, Databank cannot do so and does not do so. Databank records the effect of any agreements or arrangements made by the banks for the specified activities.

There are two separate contracts, the contract between a bank and its customers, whereunder the bank supplies financial services, and the contract by a bank with Databank whereunder Databank provides computer services.

A bank contracts to pay a customer's cheques (if he is not overdrawn), and to collect cheques in his favour. When a customer writes a cheque he instructs the bank to pay the cheque in accordance with the contract. When a customer pays in a cheque to his bank, he instructs the bank to collect the monies due on the cheque. By the terms of his contract with the Bank, the customer agrees that the difference from time to

time between cheques paid and cheques collected shall remain as a debt from the bank to the customer repayable on demand by cheque. By the contract between the bank and the customer, the bank supplies financial services so any bank charges for such services are exempt from G.S.T. Before computers were invented, the clerical work of carrying out the instructions of customers and banks with regard to cheques drawn by customers on the same bank, or drawn by customers on different banks and of recording the state of the accounts between each customer and each bank, and the state of the accounts between different banks was performed by clerks and couriers. In this computer age almost all the clerical work formerly carried on by clerks and couriers can now be carried out by a computer which mechanically and automatically obeys instructions from the banks programmed into the computer. A cheque is not paid until a bank reduces its indebtedness to a customer's account and a cheque is not collected until a bank increases its indebtedness to a customer.

Under the Agreement Databank provides a computer and programmes the computer so that the computer responds to the instructions of the bank with regard to the payment and collection of cheques, and records these transactions just as the clerks and couriers responded to the instructions of the bank manager. Databank supplies the bank with the services of a computer which replaces the services of the banks' employees. Databank also supplies employees who collect the written instruments which constitute cheques, then the information on these instruments in writing is, pursuant to the instructions of the bank, fed into the computer. In the context of the Act of 1985 the collection of a cheque does not mean the mere taking of possession of the instrument in writing. The collection of a cheque means collection of the money for which the cheque is authority. Similarly payment of a cheque is the payment of money which the written instrument instructs to be paid.

There is nothing in the Agreement dated 17th July 1969 and no evidence was produced to indicate that Databank carries on any of the activities specified in section 3(1) of the Act or possesses the resources or the authority or the desire to do so. By the Agreement Databank is a supplier of computer services to banks and not a supplier of financial services to banks or customers. Databank has no money to pay and collects no money. A customer of a bank pays money into a bank and draws money out of a bank. The customer does not pay money to Databank or collect money from Databank. A customer may not know or care whether Databank supplies to the banks machinery, which transmits instructions and requests by and between banks and by and between banks and customers, and gathers information and keeps records in

accordance with the programmed instructions of the banks. Banks provide financial services and computer companies provide computer services.

Mr. Kentridge, who appeared for Databank, with his habitual and forceful powers of persuasion adopted and presented the views of each of the judges who found in favour of Databank.

Davison C.J., in reaching his decision, said that:-

> "I apply the test of whether Databank is involved in any activities which result in any of the various matters set out in section 3 - for example, whether in terms of section 3(1)(a) they result in the 'exchange of currency' or in terms of section 3(1)(b) they result in 'the issue, payment, collection, or transfer of ownership of a cheque or letter of credit'."

Databank carries on a business activity which involves Databank in the supply of services to the banks for a consideration and that activity is therefore within the scope of section 6. Databank being involved in the requisite activity, the supply of services by Databank is by section 8 chargeable to G.S.T. unless the supply is an exempt supply of financial services as provided by section 14 and defined by section 3. Exemption is not afforded to "a person" who is "involved" in "an activity" which "results in" the supply of financial services; such an exemption, (which would present great difficulties of definition and application) is nowhere to be found in the wording of the Act. Databank is involved in the supply of financial services by the banks to their customers; such a supply by the banks to the customers is exempt by the express words of the Act. Databank neither supplies services to a customer recipient nor charges the customer. Databank is the supplier of services which are not financial services to the banks under and by virtue of the Agreement dated 17th July 1969 for a consideration paid by the recipient of those services.

Cooke P. supported the views of Davison C.J. and also relied on section 60 of the Act. Section 60(1) deals with the relationship of principal and agent supplying goods and services on the one hand and the recipient of those goods and services on the other hand. Section 60(1) is in these terms:-

> "(1) Subject to this section, for the purposes of the Act, where an agent makes a supply of goods and services for and on behalf of any other person who is the principal of that agent, that supply shall be deemed to be made by that principal and not by that agent:
>
> Provided that, where that supply is a taxable supply, that agent, being a registered person,

> may, notwithstanding anything in this Act, issue a tax invoice or a credit note or a debit note in relation to that supply as if that agent had made a taxable supply, and to the extent that that tax invoice or credit note or debit note relates to that supply, that principal shall not also issue, as the case may be, a tax invoice or a credit note or a debit note."

Section 60(2) contains corresponding provisions dealing with the supply of goods and services by a supplier on the one hand and agent and principal recipients of those goods and services on the other hand. Section 60(3) deals with the records to be kept by agents. Section 60(4) and (5) deal with the special case of auctioneers. Section 60(5) deals with and gives options with respect to supplies to a New Zealand agent acting for a foreign principal. Section 60 prevents confusion and confers options where an agent is employed to supply or receive goods and services on behalf of a principal. Section 60 does not deal with the agency services supplied by an agent to a principal for a consideration. Section 60, which applies whether financial services or non-exempt services are supplied, does not create a favoured class of agents whose services are exempt from G.S.T.

The President concluded that:-

> "The services performed by Databank as agents for the trading banks are part of the financial services provided by those banks to their customers, and accordingly exempt from tax."

The services provided by Databank enable the banks to supply financial services to their customers for an exempt consideration. Databank does not supply services of any kind to the customer for a consideration. Databank supplies computer services to the banks for a taxable consideration and there is nothing in section 60 or elsewhere to exempt that supply from G.S.T.

The services supplied by Databank to the banks enable the banks to provide financial services to their customers. Services provided by Databank to the banks constitute the most modern and efficient machinery yet devised for the purposes of enabling the banks to provide financial services to their customers. Databank supplies the machinery, in the form of computers, hardware, software and operators. The banks make use of the machinery supplied by Databank in order that the supply of financial services by the banks to the customer may be efficient and speedy. The supply of machinery is not the supply of financial services.

Somers J. held that:-

> "... what is collectively provided to customers by the banks and Databank are financial services."

If Databank and the banks formed a partnership to supply financial services, those services would be collectively supplied. But under the Agreement there are no collective supplies. Databank provides computer services to the banks and the banks provide financial services to their customers. Somers J. also held that what is done by Databank can be described as "supply to the customer". Databank does not supply anything to the customer save such information and records as the banks may decide and pay for. Casey J. rejected the view that "the nature of the supply of services by Databank is no more than the computing and other banking tasks described in detail in the evidence". He held that:-

> "... Databank's functions are an integral part of the various activities going to make up the definition of 'financial services' in section 3(1), and as such can be regarded as an extension of the trading bank's normal functions, constituting an important part thereof."

In the old days the functions of clerks were an integral part of the various activities required by the banks in order that the banks might supply financial services. Now the computer and other services provided by Databank replace the clerks and form an integral part of the supply by the banks of financial services to their customers. But there are two supplies. Databank is the supplier of computer services, the banks are the recipients of computer services, charges are made for computer services and G.S.T. is leviable in respect of the charges so made. The banks, making use of the computer services supplied by Databank, supply financial services to the customers, and those services are exempt from G.S.T.

Since the Agreement dated 17th July 1969, Databank has improved and developed the services which it supplies. The most spectacular development illustrates the operation of the Act of 1985. Under the EFTPOS system (Electronic Funds Transfer - Point of Sale) the purchaser for example of petrol from a garage tenders his bank card as a means of completing the contract between the garage and the purchaser for the sale and purchase of petrol. The bank card and the details of the petrol supplied are presented to the computer and constitute a cheque as defined by the Act of 1985. If the computer has been instructed by the bank that the bank is willing to honour that cheque, the computer debits the price of the petrol to the customer's bank account and credits the price to the bank account of the garage with any of the banks which are parties to the Agreement, thus completing the contract between

the purchaser and the garage for the sale and purchase of petrol. The computer may also provide a receipt for the purchaser and adjust the records of the sales and stocks of petrol of the garage.

In these circumstances there are three separate activities, three (at least) separate contracts and three separate supplies for three separate considerations. The activity of the garage is the supply of goods, namely petrol; GST is payable by reference to the price of the petrol unless the supply of petrol is by the Act of 1985 exempt or zero rated. The activity of the bank is the supply of financial services, namely the payment of the cheque for the price of the petrol; GST is not payable on the charges (if any) made by the bank for the services. The activity of Databank is the supply of computer services to the bank and to the garage; GST is payable by reference to the charges made by Databank for its services. The cost of Databank services is passed on to the purchaser (and other customers of the garage) who purchase taxable petrol and are supplied with non-taxable financial services. The supply of petrol by the garage and the supply of computer services by Databank do not attract the exemption afforded to the supply of financial services by the bank. The supply of financial services by the bank does not lose its exemption because the bank's activities take place simultaneously with other non-exempt activities or because the exempt activity of the bank makes use of the non-exempt activity of Databank for the purpose of completing the non-exempt activity of the garage. The activity of the bank is a separate activity. The activity of Databank is the instrument whereby the bank implements its contract with its customer. The activities of Databank and the supply of computer services by Databank do not form part, important or integral or otherwise of the separate activity and supply of financial services by the bank or part of the separate activity and supply of petrol by the garage. Three activities are simultaneous and interdependent but they are separate. There is nothing in the Act which infects separate activity with the exempt or non-exempt status of another separate activity.

Davison C.J. and the President were influenced by the belief that Parliament intended that the services provided by Databank and other persons whose activities assisted the banks to provide financial services should be exempt from tax. Davison C.J. said that:-

> "If the services of Databank in carrying out parts of those activities are to be taxed with G.S.T. then such tax will be passed on by the Banks to their customers and the intentions of Parliament will be frustrated. That would be the effect of regarding Databank as supplying only administrative services as the Commissioner claims is the case."

Their Lordships have been unable to find anything in the Act which indicates that Parliament intended to exempt anything other than the supply of financial services or that Parliament intended that all or any of the costs incurred by the banks in supplying financial services should be exempt from G.S.T. The exemption is restricted to the consideration paid by a recipient of financial services for the supply of financial services. The only recipients of financial services are the customers and the consideration which they pay to the banks is exempt.

By section 20 of the Act of 1985 a supplier must account to the Revenue at the end of every taxable period for the difference between input tax suffered by him and output tax charged by him during the period. By section 2 input tax in relation to a registered person means tax charged under section 8(1) of the Act on the supply of goods and services to that person. Correspondingly output tax in relation to a registered person means tax charged pursuant to section 8(1) of the Act in respect of the supply of goods and services made by that person. The Act does not provide that in calculating the difference between input and output tax a supplier shall be entitled to deduct input tax suffered by him in respect of a non-exempt supply made to him in the course of or for the purpose of enabling him to supply exempt services.

The provisions relating to input and output tax are inconsistent with any intention of Parliament to grant an exemption not only for financial services supplied by the bank but also in respect of taxable services supplied to the bank.

In 1989 Parliament passed an amending Act which negatived for the future the construction of the Act which had found favour with the majority of the Court of Appeal. Although the 1989 Act cannot be employed to construe the Act of 1985, it appears from the 1989 Act that in 1989, at any rate, Parliament was unwilling to allow a wider exemption than that for which the minority contended.

Their Lordships agree with the minority judgments and with the analysis of Richardson J. who stated that in his opinion Databank:-

> "... provides its customer trading banks with computing and other services which enable those banks to provide financial services to their customers."

Before the Board reliance was placed on the provisions of the 1989 Act, namely the Goods and Services Tax Amendment (No. 2) Act 1989. Parliament may expressly amend an earlier enactment. Parliament may also resolve an ambiguity in an earlier enactment for example by a provision "for the avoidance of

doubt". By such an expression Parliament may resolve an ambiguity by declaring that a provision in an earlier enactment shall bear a particular meaning. When Parliament passes an amending enactment, the amendment is, save in exceptional circumstances, never given retrospective effect. Where Parliament resolves an ambiguity the meaning attributed by Parliament to the earlier enactment takes effect as if the earlier enactment had not been ambiguous. But if Parliament has not amended the enactment or removed an ambiguity the enactment must be construed in the sense pronounced by the courts, in this case the Court of Appeal, unless and until the decision of the Court of Appeal has been reversed whereupon the enactment must be construed in the sense advised by the Board. Databank can only rely on the Act of 1989 if and so far as the Act amends the Act of 1985 or resolves an ambiguity.

The Act of 1989 received the Royal assent on 19th December 1989 some eight months after the decision of the Court of Appeal in favour of Databank and some four months after the Commissioner of Inland Revenue received final leave to appeal to the Board. The decision of the Commissioner to appeal to the Board must have been known to and approved by the Government which introduced and commended and persuaded Parliament to enact the Act of 1989.

Section 3(1) of the Act of 1989 amends section 3(2) of the Act of 1985 by inserting a definition of "General Accounting and Record Package Services". That definition includes all the services supplied by Databank pursuant to the agreement dated 17th July 1969. Section 3(2) of the Act of 1989 amends section 3 of the Act of 1985 by adding the following sub-section:-

> "(5) Notwithstanding anything in this section, where any person supplies goods and services (being the supply of general accounting and record package services) to any person who is a supplier of financial services, or to a customer of a person who is a supplier of financial services, that supply shall, for the purposes of this Act be deemed not to be a supply of financial services."

Section 3(3) of the Act of 1989 provides as follows:-

> "This section shall come into force on the day on which this Act receives the Royal assent and shall apply to supplies made on or after that date."

The Act of 1989 is of no assistance on this appeal. The Court of Appeal having decided that the services supplied by Databank under the agreement were financial services, Parliament could only alter the law as laid down by the Court of Appeal and Parliament has

done so. Parliament has not made that alteration retrospective. If the Board reverses the Court of Appeal, then Databank will be liable for G.S.T. for supplies before 19th December 1989 by virtue of the Act of 1985 as construed by the Board and for supplies on and after 19th December 1989 by virtue of the Act of 1985 as amended by the Act of 1989. When Parliament passed the Act of 1989 Parliament did not know whether the appeal of the Commissioner to the Board would succeed or when the advice of the Board would be given. The amendments to the Act of 1985 made by the Act of 1989 cannot assist Databank in construing the Act of 1985 prior to its amendment. The 1989 amendments only show that Parliament wished to make sure that the majority decision of the Court of Appeal in the present case would not apply to supplies of services in the future, leaving the Commissioner and the Government free to determine whether the effect of the decision of the Court of Appeal on supplies made in the past justified the continued prosecution of the present appeal. The Commissioner continued to prosecute his appeal.

Reliance was also placed on behalf of Databank on section 8 of the Act of 1989 which amended section 14 of the Act of 1985. As with section 3 of the Act of 1989 which only amended section 3 of the Act of 1985 after 19th December 1989, section 8(1) of the Act of 1989 which amended section 14 of the Act of 1985 was directed to come into force when the Act of 1989 received the Royal assent and to apply only to supplies made on or after that date.

Section 14 of the Act of 1985 as amended by the Act of 1989 provides that an exempt supply shall include:-

> "(a) The supply of any financial services (together with the supply of any other goods and services, supplied by the supplier of those financial services, which are reasonably incidental and necessary to that supply of financial services), not being -
>
> ...
>
> (ii) A supply of goods and services which (although being part of a supply of goods and services which, but for this sub-paragraph, would be an exempt supply under this paragraph) is not in itself, as between the supplier of that first mentioned supply and the recipient, a supply of financial services in respect of which this paragraph applies."

The wording of that amendment makes it clear that as from the passing of the Act of 1989 the supply by Databank of services which are part of a supply of exempt services and held by the Court of Appeal to be exempt shall no longer be exempt.

At the date when the Act of 1989 was passed, Parliament could not foresee whether the Board would uphold the Court of Appeal or reverse their decision. In the meantime Parliament was bound to proceed on the basis that the decision of the Court of Appeal correctly represented the effect of the Act of 1985. If the Board upheld the Court of Appeal then the reference in sub-paragraph (ii) to a supply of goods and services "which, but for this sub-paragraph would be an exempt supply under this paragraph" would be and remain wholly accurate and necessary. If the Board reversed the Court of Appeal then sub-paragraph (ii) would cease to be necessary. Parliament cannot have intended by sub-paragraph (ii) to approve the construction put upon the Act of 1985 by the majority of the Court of Appeal so as to indicate to the Commissioner that he must abandon his appeal or to indicate to the Board that the appeal should be dismissed. The arguments of Databank in reliance on the Act of 1989 are wholly untenable.

In the result their Lordships will humbly advise Her Majesty that this appeal should be allowed. Databank must pay the costs of the Commissioner before the Board and before the courts of New Zealand.

Dissenting Judgment delivered by
Lord Ackner

The question, whether the charges made by Databank for its services to the trading banks are exempt from the payment of Goods and Services Tax ("G.S.T."), depends upon the true construction of the relevant sections of the Goods and Services Tax Act 1985 and the application of that interpretation to the relevant facts. The resolution of this question has, however, been made more difficult by the change of attitude adopted by the appellant, the Commissioner of Inland Revenue, both before issue was joined and during the course of this litigation.

The history of this dispute begins in June 1986 before Databank claimed that the majority of the services which it supplied to the trading banks were "financial services" within the meaning of section 3(1) of the Act and thus "exempt supplies" which are not subject to assessment for G.S.T. by reason of the provisions of section 14 of the Act. It is apparent from the Commissioner's letter of 27th June 1986 that there had been a meeting with his Department on 9th June with representatives of the N.Z. Bankers' Association to discuss a list, which the latter had prepared, of the services provided by banks and the

status of these services for G.S.T. purposes. In the letter of 27th June it was maintained on behalf of the Commissioner that to fall within the definition of "financial services" in section 3 of the Act the test was:-

> "... whether the specific service described is reasonably incidental to any supply described in paragraphs (a) to (l) of the definitions of financial services. If this test is met ... that service constitutes part of the activity of providing that financial service and is therefore exempt."

In a subsequent letter dated 28th August in relation to nominee companies it was asserted on behalf of the Commissioner that "if the nominee company supplies financial services as defined in section 3 of the GST Act then the services supplied are exempt".

Shortly after the conclusion of this correspondence, by a letter dated 3rd September, the banks took up the question of the status of a number of services provided by Databank to trader banks. Having identified certain of these activities the letter continued:-

> "We refer to your letter of 27 June 1986 in which you expressed the view that the proper interpretation of section 3(1) is to apply a 'reasonably incidental' test. We are actually of the view that the test is whether a service is an integral part of a financial service."

The banks then contended that, applying either interpretation, the activities which they specified in the letters were exempt for the purposes of GST. The banks however conceded that in the case of payroll services and management timesharing facilities the banks did not believe that these were financial services nor was the provision of head office accounting and status reports.

Whether or not the Commissioner or the banks were conscious of the English decisions on analogous, but by no means identical, legislation, the test of "integral", in the sense of services normally performed by a bank as an integral part of its banking activities or "reasonably incidental" in the sense that it was reasonable to expect a bank to provide that service in the course of undertaking any supply described in the definition of financial services, was consistent with the English Value Added Tax Tribunal decisions in *Williams and Glyns Bank Limited v. Commissioners of Customs and Excise* [1974] V.A.T.T.R. 262 and *Barclays Bank PLC v. The Commissioners of Customs and Excise* [1988] V.A.T.T.R. 23.

The banks had to wait five weeks before they received a reply to their letter. There now followed a change of tack. None of the services provided by

Databank to the banks were considered to be financial services and the three reasons for this opinion were summarised by Davison C.J. in his judgment as follows:-

"1. For an activity within the categories set out in s.3 to be exempt, all aspects of that service must be carried out by the Banks.

2. Databank does no more than record crediting and debiting of accounts with appropriate calculations and ancillary services on behalf of the Banks.

3. Databank should be treated in the same way as any third party which supplies goods and services to the Banks."

Davison C.J. dealt with these three reasons one by one. In regard to the contention that all aspects of the service must be carried out by the banks he said:-

"The first comment I make on that argument is that nothing in s.3 or in the statute as a whole requires that all aspects of the service must be so carried out by the Banks or by any single person.

The next comment is that if for reasons of policy, 'financial services' are to be exempt from Goods and Services Tax then what does it matter if those financial services are furnished by one person or by two or more persons provided that each of those persons takes part in the specified activity and the end result is the supply of the relevant 'financial services' to the customer?

If the intention of the Legislature is, as I interpret it to be, to exempt the activities set out in s.3(1) from liability for Goods and Services Tax then the whole of the activities should be so exempt whether the activities are performed by the individual Banks themselves or whether part of the activities are undertaken for the Banks by Databank. If the services of Databank in carrying out parts of those activities are to be taxed with Goods and Services Tax then such tax will be passed on by the Banks to their customers and the intentions of Parliament will be frustrated. That would be the effect of regarding Databank as supplying only administrative services as the Commissioner claims is the case. It is the supply of financial services that is exempt and it appears to me that it matters not who performs those services.

Finally, my view of this matter finds support from s.6(3)(d) where there is excluded from the definition of 'taxable activity' -

'Any activity to the extent to which the activity involves the making of exempt supplies.'

> The activities of Databank are activities involved in the making or provision of exempt supplies, namely, financial services and even though what Databank does may not extend to the whole of the financial services, to the extent to which it does so the supply of those services is exempt from Goods and Services Tax."

When Mr. Andrew Park Q.C. referred in the course of his submissions on behalf of the Commissioner to the three reasons, as summarised by Davison C.J. in his judgment, he was asked in terms whether he still relied on the first reason. He unequivocally said he no longer relied on that ground. This was a very significant concession, since this first ground appeared to go to the very heart of the contentions urged before the Court of Appeal. In his judgment Cooke P., having recorded "it is argued that it would be inconsistent with the structure and purpose of the Act for parts of either goods or services to be treated as such for G.S.T. purposes", then referred in terms to the written submissions made by Mr. Jenkin Q.C. on behalf of the Commissioner in response to the section 60 point (to which more detailed reference will be made later) which ended with the following summary which he quoted:-

> "That both the agreement and the evidence clearly point to Databank's services forming part of the integrated supply of services made by the bank to its customer. Virtually nothing done by Databank is of value to the customer on its own. What is needed, in varying degrees, is either the approval of the bank or decision-making by the bank before the service can be complete.
>
> It is only if a complete service can be seen to be provided by Databank to the customers that Databank could be seen to be the alter ego of the bank and section 60(1) could apply. That is demonstrably not the case on the evidence before the Court."

The President, having dealt with the analogy of an engine supplied in parts relied upon by Mr. Jenkin, then observed:-

> "The services provided by Databank are in themselves and without modification or adaptation part of or necessarily incidental to the very services provided by the bank to its customer. There is no 'change of character' as the Commissioner contends. The Databank services are of value to the customer, though not separately charged to the customer. It is true that they can be said to not be of value to the customer on their own, in the sense that some authority from the bank is always needed - and in some services (e.g. cheque clearing) action by the bank also. But I am unable to accept that s.60(1) applies only if a complete service is provided by Databank to the customers. On the Commissioner's

argument it would seem that s.60(1) would not apply to any case where the agent had to obtain authority from his principal; which would go far to nullify the statutory provision."

He added towards the end of his judgment:-

"Such significant parts of the banks' services are provided by Databank that I find compelling force in Davison C.J's opinion that to deny exemption would be to frustrate the intention of the legislature."

Somers J. dealt with the first reason for the Commissioner's decision in this way:-

"The argument for the Commissioner is illustrated by reference to the clearance of cheques and runs as follows. It is evident that a very substantial part of the process of the collection of a cheque is handled by Databank but the whole collection process is not undertaken by it. Accordingly, Databank does not undertake for the banks the collection of a cheque from which it follows that Databank does not supply to the banks the service of collection of cheques - it assists the banks in clearance, it is involved in the payment and collection, but that is not sufficient. The argument on the next two major activities, the posting and maintenance of customer accounts and network accounts, is similarly put. It was conceded that the relevant parts of the supply of software must follow the treatment of the other three services.

In respect of the matters in issue, I am of opinion that what is collectively provided to customers by the banks and Databank are financial services. That is what the bank is required to provide its customers and what the customer receives from the bank. The service is provided in part by the bank's own activities and in part by what the bank procures Databank to do for it. The same result is reached by reference to exclusion from taxable activity provided by s.6(3)(d) - any activity to the extent to which the activity involves the making of exempt supplies. The exclusion may well cover cases of a composite supply by one person only, part chargeable to tax and part exempt. But I think it also embraces activities by two or more which together comprise a supply to a third person. Put in another way, that which is done by Databank, in the case of the clearance of cheques for example, is part of a financial service provided by a bank to its customers and to that extent is an activity involving the making of an exempt supply by the Bank."

Mr. Andrew Park, understandably, relied heavily upon the dissenting judgment of Richardson J. and accepted that the pith of the judgment is to be found on one page. Earlier in his judgment, Richardson J. set out what he considered to be the rival contentions of the parties as to the test of whether supplies are exempt from tax. He said:-

> "For the Commissioner it was submitted that the determinative question is what is the nature of the supply of services provided by the supplier to the recipient? For Databank it was in effect what is the nature of the activity carried on by the supplier?"

He then stated that he was satisfied:-

> "... that the test of whether supplies are exempt from tax must be expressed in terms of the nature of the supply by the supplier to the recipient in the particular case."

He then said:-

> "It is common ground that if the matter is approached in this way, and subject to the agency point, the Commissioner must succeed."

Unless interpreted in the manner respectfully suggested hereafter, this was a most surprising observation. The judgments of the Court of Appeal were reserved judgments and Richardson J. would have read the judgment *inter alios* of Somers J. where he said:-

> "In the High Court Davison CJ tested the matter by asking whether Databank was involved in any activities which result in any of the matters set out in s.3, that is to say any of the matters which constitute financial services as defined. It was an enquiry as to the nature of the activity carried on or undertaken by the supplier, Databank. That approach was supported by Databank in this Court. For the Revenue, Mr. Jenkin submitted that the true question was the nature of the supply of services provided by Databank to the banks. The difference between the two was said by Mr. Jenkin to be that the approach of the Commissioner looks to the nature of the service supplied in the context of supplier and recipient, that of Databank to the nature of the activity divorced from that context.
>
> I doubt whether these two ways of putting the matter pose a real anthithesis. There must be a supply of services before there is a charge to tax. The supply of services will in most, if not all, cases involve some activity. Because not all activities are taxable their nature must be examined. If, and to the extent, they involve the making of exempt supplies, that is to say they involve the supply of any financial services, the activity, and hence its supply is, by reason of s.6(3)(d), not chargeable to tax."

Immediately after the short quotation above, Richardson J. continued:-

> "The required focus is on the nature of the services supplied by Databank to the trading bank. As provided in the agreement of 17 July 1969 and in the expanded scope of the activities presently undertaken by Databank, the company provides its customer trading banks with computing and other services which enable those banks to provide financial services to their customers. Because the factual result is common ground it is not necessary to review and compare the services provided by Databank to the trading banks with the services provided by the trading banks to their customers."

In his judgment on this particular aspect of the appeal, Casey J. stated:-

> "For the Commissioner, Mr. Jenkin submitted that in arriving at this result the Chief Justice had overlooked the Act's fundamental concern with the nature of the supply of services, and had concentrated on the character of the activities comprising those services. While it is true that s.3 defines 'financial services' in terms of the listed activities, s.14 exempts the supply of such services. It was his contention that Databank does not supply any of its services to the trading banks in a way that enables it to be treated as a supplier of financial services under the Act. What it does is to supply specialised ministerial and administrative services in terms of its contract with the banks to enable the latter to supply the defined financial services to their own customers.
>
> This submission is unanswerable if one assumes that the nature of the supply of services by Databank is no more than the computing and other banking tasks described in detail in the evidence. The Chief Justice rejected this approach, characterising it as too simplistic a description of Databank's services. I agree.
>
> There was ample evidence demonstrating that Databank's functions are an integral part of the various activities going to make up the definition of 'financial services' in s.3(1), and as such can be regarded as an extension of the trading bank's normal functions, constituting an important part thereof. The Commissioner's approach was to look at each part of the work done by Databank in isolation, like the individual pieces of a jig-saw puzzle. But put together in the broad categories identified in the evidence and looked at in the round, they constitute sufficiently clear - although incomplete - pictures of its various functions to bring them fairly within the respective categories listed in s.3(1). This, I think, is essentially the reason behind the Chief Justice's conclusion and I concur with it.

> The expert banking evidence on which he relied supported such a view of the nature of the services supplied by Databank, and I think that view also accords with the commercial reality of their relationship."

The above excerpts from the judgments of Somers J. and Casey J. have been set out at some length in order to demonstrate that it could not have been common ground that if the test whether supplies are exempt from tax is expressed in terms of the nature of the supply by the supplier to the recipient in the particular case, the Commissioner must succeed unless there is read into that observation that all aspects of the supply of that activity must be provided by Databank to the customers. It is only on that basis that it could be said to have been common ground that, approached in that way and subject to the agency point, the Commissioner must succeed. Accordingly, it seems abundantly clear that, if the same concession that was made and rightly made to their Lordships had been made to the Court of Appeal, the basis for the dissent would not have existed. As Davison C.J. observed, having heard the evidence which fully justified this conclusion, Databank "performs the greater part of the activities listed in section 3(1) as being 'financial services'".

There is nothing in the legislation to suggest that the identity of the supplier of the goods is of any relevance in determining whether the supplies are exempt supplies other than that, pursuant to section 8(1), he must be a "registered person". Section 2 defines "recipient" in relation to any supply of goods and services as meaning "the person receiving the supply", and therefore whether the bank or the customer is to be treated as the recipient is of no relevance. It is to be noted that section 6 does not state that the consideration has to move from the recipient. Accordingly if what is supplied to the bank were financial services, then such supply of services is exempt and this of course is wholly consistent with the opinion expressed on behalf of the Commissioner in the letter of 28th August relative to services provided by nominee companies quoted above. As regards section 60, this appears only to have become relevant because of the Commissioner's contention that all aspects of the service must be carried out by the banks. Were that contention to be correct, and in my judgment it is not, then I would agree with the views expressed by the President in the following excerpts from his judgment:-

> "It is true of course that, like any other agent, Databank supplies services to its employer. The employer in this case is a trading bank. But at the same time Databank is acting as the alter ego of the bank concerned by supplying the services to the customer. In some services Databank is in direct contact with the customer (e.g. ATMs; EFTPOS). In

> others it is not (e.g. cheque clearing; procedures incidental to the keeping of current accounts) but even then it is performing, with the authority of the bank, part of the very services which the bank has undertaken to provide to the customer. So, as I see the matter, Databank is necessarily supplying services not only to the bank but also, on behalf of the bank, to the bank's customers; and s.60 governs the treatment of such a case for G.S.T. purposes. ...
>
> The position is simply that the services are provided to the customer in the name of his bank, which is a position by no means uncommon when a principal supplies services through an agent. Similarly it is of course usual, indeed almost invariable, for the agent's remuneration from the principal to differ from any consideration moving from the third party to the principal."

And with his conclusion that:-

> "... the services performed by Databank as agents for the trading banks are part of the financial services provided by those banks to their customers, and accordingly exempt from tax."

For these reasons I would have humbly advised Her Majesty that this appeal ought to be dismissed.