LegalTalk Alert

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PRICEWATERHOUSECOOPERS

Indirect tax sharing and funding agreements

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The Australian GST law has recently been amended with effect from 1 July 2010 to allow members of a GST group or participants in a registered GST joint venture to enter into an Indirect Tax Sharing Agreement (ITSA). An ITSA is similar to a tax sharing agreement for income tax consolidated groups, and operates to enable group members or joint venture participants to limit their liability for indirect taxes of the GST group/ joint venture, i.e. GST, Fuel Tax, Wine Equalisation Tax and Luxury Car Tax (Indirect Tax Amounts).

In a GST group/ joint venture, primary liability for Indirect Tax Amounts rests with the group's representative member or joint venture operator, as applicable (Representative). If the Representative fails to pay an Indirect Tax Amount to the Australian Taxation Office (ATO) by the due date for payment, each GST group member/ joint venture participant becomes jointly and severally liable for that Indirect Tax Amount unless there is a valid ITSA in place.

The practical effect of joint and several liability is that the ATO can choose to commence recovery proceedings against any GST group member/ joint venture participant for the entire unpaid amount of the Indirect Tax Amount. A further commercial effect of joint and several liability is that it may result in GST groups/ joint ventures finding it difficult to satisfy banking and debt covenants.

Requirements for an ITSA

An ITSA will apply to a particular tax period provided it is entered into prior to the due date for lodgment of the GST group/ joint venture's Business Activity Statement for that tax period. Accordingly, for GST groups/ joint ventures that remit GST on a monthly basis, the ITSA must be entered into prior to the 21st of the month following the relevant tax period for which the ITSA is intended to apply.

For an ITSA to be valid, and consequently limit joint and several liability, several requirements must be satisfied. The most important requirement is that the ITSA must provide a **reasonable** allocation of the total Indirect Tax Amounts between the GST group members/ joint venture participants (Contribution Amount). A valid ITSA will limit each GST group member / joint venture participant's potential liability to the ATO to its relevant Contribution Amount, other than the Representative who remains liable for the full Indirect Tax Amount.

Clear exit payments

An additional purpose of an ITSA is to allow a GST group member/ joint venture participant to leave the GST group/ joint venture clear of any Indirect Tax Amounts that are due after the date of exit, provided the relevant exit provisions are complied with – namely the exiting GST group member/ joint venture participant making a clear exit payment to the Representative. This is especially important in a mergers and acquisitions context where target entities are acquired out of a GST group/ joint venture.

Indirect tax funding agreements

An ITSA will generally not obligate GST group members/ joint venture participants to make any indirect tax-related payments to other GST group members/ joint venture participants, other than in the case of a clear exit payment.

Accordingly, an indirect tax funding agreement (ITFA) may allow the directors of each GST group member/ joint venture participant to be satisfied that the Representative will be in a position to fund the GST group/ joint venture's indirect tax liabilities as and when they fall due. In the absence of an ITFA, the Representative may have to pay the entire GST group/ joint venture participant's indirect tax liabilities without any formal agreement with the other GST group members/ joint venture participants allowing it to be reimbursed (or paid in advance) by those GST group members/ joint venture participants for their portion of the indirect tax liability. An ITFA may also provide for payments to be made by the Representative to a GST group member/ joint venture participant whose input tax credits reduce the Indirect Tax Amount of the GST group/ joint venture.

We expect that most GST groups/ joint ventures already have either formal or informal funding arrangements in place to

ensure the Representative is in a position to fund the GST group/ joint venture's indirect tax liabilities. However, for GST groups/ joint ventures that are now proposing to enter into an ITSA, it would be an appropriate time to also consider their funding arrangements and formalise them where necessary.

Should you have any queries regarding any of the above issues or would like to enter into an ITSA and/or ITFA, please contact your usual PricewaterhouseCoopers adviser or:

For further information please contact your usual PricewaterhouseCoopers adviser or:

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