

GST and Loyalty Programs

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GST and Loyalty Programs

The Australian Taxation Office (ATO) has released a draft GST ruling GSTR 2011/D3 outlining its preliminary views on the GST treatment of transactions which commonly take place as part of the operation of a loyalty program. This draft ruling represents the ATO's first major public expression of views on the GST treatment of loyalty program transactions since the then Commissioner's Media Release 2000/14 which broadly stated that there would be no GST on loyalty.

Loyalty programs are now common place in commerce. Nevertheless, they continue to pose difficulties from a GST perspective as they can give rise to significant GST inefficiency and GST cost if not structured correctly.

Whilst this draft ruling highlights some of the key issues to consider from a compliance perspective, there are many further issues to consider when structuring your loyalty program to ensure that GST does not represent an irrecoverable cost to your business.

Summary

The ruling, once finalised, will apply to most existing loyalty programs, which typically involve a loyalty program operator, members of the program and, in many circumstances, program partners.

Based on our experience in working with loyalty programs, the draft ruling does not contain any major surprises other than the change of view relating to payments by a program partner into a trust.

In general, the ATO has taken pragmatic or commercial view of the GST treatment of loyalty program transactions, and this should be well received by taxpayers.

The draft ruling sets out the GST treatment of transactions between the relevant parties, as follows:

- On the 'earn' transaction, the allocation of loyalty points to a member is not a supply to the member for consideration. No payment by a program member is therefore attributable to the points allocated to the member as part of the earn transaction. Rather, all of the payment is for the goods and services supplied in the 'earn' transaction.
- Under a participation arrangement entered into between the program operator and a program partner:
 - points allocated to members represent a supply of 'rights' by the operator to the partner
 - although supplied to the partner, the rights are provided to the members
 - 'points fees' charged by the operator to the partner represent consideration for the supply of the rights by the operator to the partner
 - to the extent that the points would be redeemed for GST-free or input-taxed supplies by a member, the points fee will not be subject to GST in the hands of the operator
 - the expected redemption of points for taxable, GST-free and input-taxed supplies should be determined on a fair and reasonable basis to determine the extent to which the points fee will be subject to GST

- an example of a fair and reasonable basis would be historic redemption rates, omitting from the calculation points that will never be redeemed
- no adjustment will be required to the GST remitted in respect of the points fee where actual redemptions are found to differ from the estimate
- input tax credits can be claimed by a partner to the extent that the supply made by the operator is a taxable supply and the creditable acquisition rules are otherwise met
- where a trust funds the provision of rewards to members, a payment of a points fee by a partner to the trustee represents consideration for a supply by the operator to the partner (which is either taxable, GST-free or input-taxed, as determined above) -we note that this is a change to the views previously held by the ATO, and
- where a partner provides goods or services to a member as a reward on redemption of points accumulated by the member in accordance with a participation arrangement entered into with the operator:
 - the partner makes a supply to the operator of the underlying reward provided to members, e.g. hotel accommodation, goods, etc
 - a supply of the reward is also made to the member
 - a payment from the operator to the partner is consideration for the supply of the reward

- input tax credits can be claimed by the operator to the extent that the supply by the partner is a taxable supply and the creditable acquisition rules are otherwise satisfied
- the redemption of points is the exercise of a contractual right by the member and not consideration for the supply of rewards to the member
- the supply to the member is not a taxable supply unless additional consideration is provided by the member
- under a 'points plus pay' arrangement, there are two supplies that may be subject to GST, to the extent points are redeemed as 'payment' for the reward - the supply of the reward by the partner to the operator and, to the extent the member provides additional consideration – the supply of the reward by the partner to the member, and
- where the reward provided to a member is a gift card, the supply of the gift card by the partner to the operator is not a taxable supply.

Implications

Where a private binding ruling is already held in relation to transactions under an existing loyalty program, it may be overridden by this public ruling, once it is finalised by the ATO.

Existing private rulings should therefore be reviewed to identify any differences to the views expressed in this draft public ruling to assess potential impact.

Loyalty program operators should consider the extent to which points supplied to program partners would be redeemed for GST-free and input-taxed supplies and formulate a methodology for assessing this on a fair and reasonable basis.

Any agreements with program partners pertaining to supplies under a loyalty program should be reviewed, with particular consideration given to agreements based on GST-inclusive pricing which do not contain a GST gross-up clause.

Where your current GST treatment of supplies under an existing or proposed loyalty program contractual arrangement differs from the treatment suggested by the Commissioner in this ruling, the commercial implications of the change in GST treatment should be considered and factored into any contract negotiations.

Businesses participating in loyalty programs should consider the need to seek transitional relief from the ATO with regard to any existing agreements where the GST treatment of supplies is not in line with the ATO's views expressed in this public ruling. A strategy should be devised for engaging with the ATO in this regard.

Comments on the draft ruling are due by 7 October 2011.

Further information

To have a deeper discussion about what the above means for your business, please contact your usual PwC contact or:

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