TD 2003/20 - Income tax: is a deduction allowable to a reward provider under section 8-1 of the Income Tax Assessment Act 1997 ('ITAA 1997') when points are credited to a member under a 'consumer loyalty program'?

This cover sheet is provided for information only. It does not form part of *TD 2003/20 - Income tax: is a deduction allowable to a reward provider under section 8-1 of the Income Tax Assessment Act 1997 ('ITAA 1997') when points are credited to a member under a 'consumer loyalty program'?*

This Ruling has been reviewed by the ATO and does not require any updates as at 31 March 2017.

Taxation Determination
TD 2003/20

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Preamble

The number, subject heading, date of effect and paragraph 1 to 11 of this Taxation Determination are a 'public ruling' for the purposes of Part IVAAA of the ***Taxation Administration Act 1953*** *and are legally binding on the Commissioner. The remainder of the Determination is administratively binding on the Commissioner. Taxation Rulings TR 92/1 and TR 97/16 together explain how a Determination is legally or administratively binding.*

1. No.

2. A 'consumer loyalty program' is defined in paragraph 3 of Taxation Ruling TR 1999/6 'Income tax and fringe benefits tax: flight rewards received under frequent flyer and other similar consumer loyalty programs'.

3. Under a consumer loyalty program, customers are credited with points at a time when goods or services are supplied. Those points may, within the terms and conditions of the particular program, result in the customer being able to redeem points for certain rewards. When points are awarded under a consumer loyalty program, the reward provider may make a provision in its accounts for the estimated future liability. The actual expenses associated with the rewards would not normally be realised until the goods or services are actually supplied.

4. To qualify for deduction under section 8-1 of the ITAA 1997, a loss or outgoing must have been 'incurred'. The word 'incurred' is discussed in Taxation Ruling TR 97/7: 'Income tax: subsection 51(1) – meaning of 'incurred' – timing of deductions'.

5. For a loss or outgoing to be incurred there needs to be a presently existing liability of a pecuniary character – *Nilsen Development Laboratories Pty Ltd v. FC of T* 144 CLR 616 at 624. At the time the points are credited to the member there is no presently existing liability to actually provide a reward. When the points are credited to the member, the reward provider has not completely subjected itself to the future liability so as to have incurred a deductible expense under section 8-1 of the ITAA 1997. Any future liability is subject to contingencies as an actual entitlement to a reward may not arise until a certain

number of points are accrued. Even at that time there is no certainty that a reward will be redeemed or what reward will be redeemed. It is not therefore a presently existing liability – refer *FC of T v. James Flood Pty Ltd* (1953) 88 CLR 492 at 506; *Nilsen Development Laboratories* (CLR at 624); *Merrill Lynch International (Australia) Ltd v. FC of T* [2001] FCA 1127; 47 ATR 611; 2001 ATC 4541.

6. Even where a member has sufficient points to redeem a reward, a liability in respect of the points will not arise until such time as the reward is actually redeemed and supplied. To be deductible, the liability must be 'more than impending, threatened or expected' – refer *New Zealand Flax Investments Ltd v. FC of T* (1938) 61 CLR 179 at 207.

Example 1

7. A merchant commences business on 1 January and at the same time it sets up a customer loyalty program. It awards points to members of the program based on the amount spent by the member in each calendar month. The points are accumulated and, subject to meeting the terms and conditions of the program, the rewards are taken in the form of free flights or other goods or services provided by the merchant. Points are awarded at the end of each month and a provision is raised in its accounts for the estimated future liability arising from the points credited. As at 30 June, the end of the first year of income, no rewards have been claimed.

8. *No deduction is available to the merchant for the points awarded. No 'presently existing liability' has arisen by reason of the fact that points have been awarded to customers.*

Example 2

9. In the course of carrying on its business, a merchant purchases consumer loyalty program points from an arm's length reward provider. At the end of each month, the reward provider bills the merchant for the points purchased. The merchant claims a deduction for the amounts billed in relation to the costs of the points, at the time the liability arises for payment to the reward provider. Points purchased by the merchant are awarded to customers on the same basis as in example 1. When sufficient points have been accumulated, the customer can claim a reward from the reward provider.

10. The reward provider creates a provision in its accounts for the estimated future liability it may incur arising from the points sold to the merchant. The reward provider will not be entitled to claim a deduction for the provision it created, because as in example 1, there is no 'presently existing liability' by reason of the creation of a provision for a future liability.

Date of effect

11. This Determination applies to years commencing both before and after its date of issue. However, this Determination does not apply to taxpayers to the extent that it conflicts with the terms of settlement of a dispute agreed to before the date of the Determination (see paragraphs 21 and 22 of Taxation Ruling TR 92/20).

Commissioner of Taxation
30 July 2003

Previous Draft:
TD 2003/D6

Related Rulings/Determinations:
TR 92/1; TR 92/20; TR 97/7; TR 97/16; TR 1999/6

Subject references:
- frequent flyer benefits
- deductions
- non-cash benefits

Legislative references:
- ITAA 1997 8-1
- ITAA 1936 51(1)
- TAA 1953 Pt IVAAA

Case references:
- FC of T v. James Flood Pty Ltd (1953) 88 CLR 492; [1953] ALR 903; 5 AITR 579; 10 ATD 240
- Nilsen Development Laboratories Pty Ltd v. FC of T (1981) 144 CLR 616; 11 ATR 505; 81 ATC 4031
- New Zealand Flax Investments Ltd v. FC of T (1938) 61 CLR 179; [1939] ALR 1; (1938) 5 ATD 36
- Merrill Lynch International (Australia) Ltd v. FC of T [2001] FCA 1127; 47 ATR 611; 2001 ATC 4541

ATO references
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