

PS LA 2004/4 (GA) - Income tax and fringe benefits tax - rewards received under consumer loyalty programs.

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This Practice Statement is issued under the authority of the Commissioner and must be read in conjunction with Law Administration Practice Statement PS LA 1998/1. It must be followed by ATO officers unless doing so creates unintended consequences. Where this occurs ATO officers must follow their Business Line's escalation process for significant issues.

SUBJECT: Income tax and fringe benefits tax - rewards received under consumer loyalty programs.

PURPOSE: Where rewards are received under a consumer loyalty program that results from points accrued from business expenditure, the rewards *may* be subject to income tax or fringe benefits tax.

This Law Administration Practice Statement provides guidance in deciding when cases should be referred to a senior technical leader for review.

BACKGROUND

1. This Law Administration Practice Statement follows on from:
 - the decision in *Payne v FC of T* (1996) 66 FCR 299, 96 ATC 4407, (1996) 32 ATR 516 ('*Payne's Case*'),
 - Taxation Ruling TR1999/6 - Income tax and fringe benefits tax: flight rewards received under frequent flyer and other similar consumer loyalty programs, and
 - Taxation Determination TD1999/34 – Income tax: is a reward received under a 'consumer loyalty program' that results from private expenditure assessable?
2. It is recognised that there may be some cases where a reward received from a consumer loyalty program will fall outside the guidelines contained in TR1999/6 and TD1999/34. In circumstances where the facts materially differ from those considered in *Payne's Case*, fine distinctions at law can arise, which potentially alter the assessability of rewards.
3. One area which may require careful consideration is the nature of the various business relationships that exist. For instance a taxpayer's relationship with a bank as a credit provider, where the taxpayer is a sole trader or conducting business through a private company or other structure may give rise to different taxation

consequences to those stated in *Payne's Case*. This practice statement provides guidelines in those instances where a reward is possibly subject to tax as it is considered to be outside the circumstances covered in TR1999/6 and TD1999/34.

4. It is recognised that there may be significant compliance costs to taxpayers and to the Tax Office in ensuring a high level of compliance in relation to the tax treatment of rewards received under consumer loyalty programs given the fine distinctions that can exist at law. As a recognition of those compliance costs, administrative action will not be considered warranted unless factors described in paragraph 7 are present. This practice statement advises when such cases should be referred to a senior technical leader.
5. For the purposes of this practice statement, 'consumer loyalty program' and 'flight reward' have the same meaning as in TR 1999/6.

STATEMENT

6. In determining whether a reward received under a consumer loyalty program is a fringe benefit or assessable income, officers are required to apply the principles set out in TR1999/6 and TD1999/34.
7. Cases should be referred to a senior technical leader for review where, on consideration of those principles and this practice statement, a reward that is received under a consumer loyalty program is considered to be assessable income or a fringe benefit because:
 - the arrangement is so contrived and artificial that it has no commercial purpose other than to allow the recipient to receive the rewards to which they become entitled, and/or
 - the nature of the arrangements suggest that the rewards are being received in substitution for income which would otherwise be earned, and/or
 - the points accumulated from a business relationship or business expenditure exceed 250 000 points per annum.

Administrative action is only considered warranted in cases that meet the above stated criteria.

EXPLANATION

Flight rewards received under consumer loyalty programs

8. The taxation consequences of flight rewards received under a consumer loyalty program were considered by the Federal Court in *Payne's Case*.
9. The Court held that the benefits received by Mrs Payne did not form part of her assessable income because:
 - the rewards did not constitute income according to ordinary concepts - the flight reward was not 'money' or 'money's worth', and
 - the rewards did not fall within section 26(e) of the *Income Tax Assessment Act 1936* (the ITAA 1936). If there was a benefit given, it was given as a result of a personal contract between the taxpayer and the consumer loyalty program provider, notwithstanding the benefit arose as a 'consequence' of employment.

10. In view of the issues and the facts of *Payne's Case*, it was not necessary for the Court to consider whether section 21A of the ITAA 1936 applied, nor whether the 'arranger' provisions in the *Fringe Benefits Tax Assessment Act 1986* (the FBTA) applied.
11. Given the range of consumer loyalty programs in the market place, the differing circumstances of the participants in them and the wide variety of arrangements that may be entered into, circumstances may arise where the assessability of rewards cannot be determined by reference to the decision in *Payne's Case* or from the guidance provided in TR1999/6 and TD1999/34.

Taxation Ruling TR 1999/6 and Taxation Determination TD 1999/34

12. TR1999/6 and TD 1999/34 were issued following the decision in *Payne's Case*.
13. The assessability of 'flight rewards' received under consumer loyalty programs are considered in TR1999/6, which states that flight rewards received under frequent flyer and other similar consumer loyalty programs are generally not subject to tax.
14. However it is noted in TR1999/6 that there are situations where flight rewards would be taxable:
 - Flight rewards may be subject to FBT in the following situations. Firstly, where the person with the personal contract is also an employer and provides the 'flight reward' received to an employee (who is a family member) in respect of the employment. That is, under the conditions of the flight reward program, FBT only applies where the employer and employee have a family relationship and the flight reward is received in connection with the employment. A second exception is where, in respect of employment of an employee, a flight reward is provided to an employee, or the employee's associate, under an 'arrangement' for the purposes of the FBTA, that results from business expenditure. (TR1999/6, paragraph 7).
 - Flight rewards that are received by an individual who renders a service or has received the flight reward as a result of business expenditure where the person renders a service on the basis that an entitlement to a flight reward will arise (e.g., a person enters into a secretarial service contract with an understanding that a flight reward will be received) or, in a business context, where the activities associated with the obtaining of the benefits amount in themselves to a business activity (TR1999/6, paragraph 9).
15. An addendum to TR1999/6 issued at the same time as this practice statement. That addendum amended paragraph 7 of TR1999/6 (which is reflected in the preceding paragraph of this practice statement) to make it clear that there may be situations where 'flight rewards' are received under an arrangement for the purposes of the FBTA and that a liability to fringe benefits tax may arise.
16. TD 1999/34 discusses the assessability of rewards received under consumer loyalty programs arising from *private expenditure* and states that those rewards are not subject to tax.

Rewards received from consumer loyalty programs

Income Earning Activity

17. Rewards received under consumer loyalty programs will be taxable in circumstances where the facts demonstrate that the reward is received as part of an income earning activity and
 - there is a business relationship between the recipient of the reward and the reward provider; and
 - the benefit is convertible directly or indirectly to money's worth; or
 - the taxpayer is carrying on a business, and section 21A of the ITAA 1936 operates to include the reasonable value of the non-cash business benefit in the taxpayer's assessable income.
18. Similarly, where the activities associated with the obtaining of a reward amount to a business or commercial activity and the reward is a non-cash business benefit in terms of section 21A of the ITAA 1936 the reward will be assessable.

Arrangement between Employee and Employer

19. A reward received by an employee under a consumer loyalty program may be a fringe benefit for the purposes of the FBTAA where the facts demonstrate that there is an arrangement between the employee and employer so that the provision of the reward has a sufficient and material connection to employment. That is, the reward takes on the character of being a benefit received 'in respect of employment' (see *Smith v FC of T* (1987) 164 CLR 513; 87 ATC 4883; (1987) 19 ATR 274; and *J & G Knowles & Associates Pty Ltd v Commissioner of Taxation* 2000 ATC 4151; (2000) 44 ATR 22; [2000] FCA 196; (2000) 96 FCR 402).
20. An employer might enter into an arrangement with an employee which allows the employee to use a credit card to pay the employer's costs which are subsequently reimbursed. By doing this, the employee accrues loyalty program points which can be redeemed for substantial personal benefit. In this situation, FBT may apply to any rewards obtained – refer example 4.
21. However, where the expenses are incurred on behalf of the employer for legitimate business reasons, FBT would not apply – refer example 3.
22. Where an employee enters into an arrangement with an employer on the basis that an entitlement to a reward will arise as a result of services rendered and the employee receives a reward, in substitution for income, the employee may incur an income tax liability in respect of that reward – refer example 5.

Rewards or Points - the taxing point

23. In TR1999/6, the tax implications of flight rewards received from consumer loyalty programs was considered. It is the receipt of a reward which is the taxing point and the value of that reward may be subject to tax. The receipt of points would not be a taxing point in accordance with the views expressed in TR1999/6.
24. Further where points received under a consumer loyalty program are substituted for points in another consumer loyalty program, that is, the points are transferred between programs, the transfer is not considered to be the receipt of a reward.

EXAMPLES

Example 1:

1. Pamela is a sole trader operating a painting and wallpapering business, and she buys her paint from a paint wholesaler. The wholesaler has a loyalty program that entitles her to points which can be redeemed for shopping vouchers. There is a business relationship between Pamela and the paint wholesaler and it is this relationship that makes Pamela eligible to receive possible benefits.
2. Pamela redeems her points for vouchers worth \$2 500. Pamela uses the vouchers to acquire clothing for herself and her children.
3. The redemption of points in return for the vouchers valued at \$2 500 was as a result of business purchases of paint. The value of vouchers, \$2 500, is assessable under section 21A of the ITAA 1936 as the benefit flows from the business relationship Pamela has with the paint supplier. The vouchers are assessable income at the time of receipt. Pamela is required to return \$2 500 in her assessable income.

Example 2:

4. Pamela is also a member of a credit card loyalty program and she uses her credit card for all her business and personal expenses. The rewards flowing from the redemption of the credit card loyalty program points arise from her relationship with the credit card loyalty program provider, and may be assessable as the relationship has both a personal and business aspect.
5. It is arguable that Pamela has a business relationship with the financier:
 - she pays fees for the service
 - where business expenditure is incurred the credit card provider is extending credit to her business, so that
 - the rewards she receives under the program in relation to her business expenses are arguably assessable under section 21A of the ITAA 1936.
6. However in the absence of the features listed in paragraph 7 of this practice statement, referral to a senior technical leader would not be required, and further administrative action would not be warranted.

Example 3:

7. Paula frequently travels interstate on business. Paula is provided with a corporate credit card by her employer so that Paula can pay for her business related accommodation, meals, taxis, hire cars, etc. There is a fee for operating the corporate card but the savings in administration costs far outweigh the fee charged. The credit card company has a loyalty program and Paula joins.
8. The arrangements between Paula and her employer exist because of the administrative benefits to her employer. Accordingly there is unlikely to be a sufficiently material connection with her employment for any rewards received from the consumer loyalty program to be in respect of employment.

9. In the absence of the features listed in paragraph 7 of this practice statement, referral to a senior technical leader would not be required, and further action is not warranted.

Example 4:

10. John is an employee of XYZ Company. John uses his personal credit card for private expenditure. Under an arrangement (which can be explicit or tacit) between John's employer and John, John is able to place all of the business expenditure of the company on his personal credit card. The company reimburses him for the expenditure he has paid on its behalf. Under the arrangement John's points entitlement from the business expenditure is significant and exceeds 250 000 points per annum.
11. FBT may apply in this case. Any reward that arises from the redemption of the points has accrued in respect of significant business expenditure. The reward may have been provided under an arrangement, and may be in respect of employment.
12. This is an arrangement falling within the parameters set out in paragraph 7 of this practice statement. Such a case should be referred to a senior technical leader for review.

Example 5:

13. Sam is employed by James' Wholesale Stationery Company. Rather than paying Sam a Christmas bonus, the employer and Sam agree to an arrangement by which Sam will accrue points in a consumer loyalty program which he can redeem for significant rewards. Sam will pay a significant portion of the company's business expenses on his credit card each October, and the company will reimburse Sam when the payment on his card falls due.
14. This arrangement has no apparent purpose other than to enable Sam to receive significant rewards, from the redemption of points accumulated from business expenditure, in substitution of income he would otherwise have been expected to receive.
15. This is an arrangement falling within the parameters set out in paragraph 7 of this practice statement. Such a case should be referred to a senior technical leader for review.

Amendment history

Date of amendment	Part	Comment
14 May 2013	Contact details	Updated
6 August 2008	Contact details	Updated
September 2006	Throughout	Reference to 25(1) of the ITAA 1936 deleted

<i>subject references:</i>	fringe benefits income non-cash benefits
<i>legislative references:</i>	<i>Fringe Benefits Tax Assessment Act 1986</i> <i>Income Tax Assessment Act 1936 section 21A</i> <i>Income Tax Assessment Act 1997 section 6-5</i> <i>Income Tax Assessment Act 1997 section 6-10</i> <i>Income Tax Assessment Act 1997 section 6-25</i>
<i>related public rulings:</i>	Taxation Ruling TR1999/6 Taxation Determination TD1999/34
<i>case references:</i>	<i>Payne v FC of T</i> (1996) 66 FCR 299, 96 ATC 4407, (1996) 32 ATR 516 <i>Smith v FC of T</i> (1987) 164 CLR 513; 87 ATC 4883; (1987) 19 ATR 274 <i>J & G Knowles & Associates Pty Ltd v Commissioner of Taxation</i> 2000 ATC 4151; (2000) 44 ATR 22; [2000] FCA 196; (2000) 96 FCR 402
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