

GFS/gst-ritc-it-agreements -



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ATO expectations on how you support your reduced input tax credit claims on complex information technology outsourcing agreements

Our commitment to you

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Purpose of this document

This document outlines ATO expectations to support your reduced input tax credit (RITC) claims on complex information technology (IT) outsourcing agreements acquired partly or wholly in making of input taxed supplies.

One area of focus under the ATO's GST Financial Services and Insurance strategy is ensuring that taxpayers have controls in place to correctly:

- identify the extent to which an acquisition is a reduced credit acquisition (RCA), and
- distinguish between mixed and composite acquisitions as required when claiming RITCs.

These issues can particularly arise in determining the application of table item 2 of subsection 70-5.02(1) of the *A New Tax System (Goods and Services Tax) Regulations 2019* (table item 2) to acquisitions made under a complex IT outsourcing agreement.

This document highlights the types of questions we will ask when reviewing your RITC claims in relation to these acquisitions, to ensure compliance with the ATO's view in Goods and Services Tax Ruling [GSTR 2004/1](#) *Goods and services tax: reduced credit acquisitions*.

Determining your entitlement to RITCs in relation to IT outsourcing agreements is highly factual and dependent on your specific circumstances. In this regard, we encourage you to review your arrangements to prepare for a review.

This document is intended to provide practical guidance to assist you in undertaking such a review and determining your entitlements in accordance with:

- GSTR 2004/1 – which sets out the application of table item 2 (see paragraphs 73 to 190 of the Ruling)
- Goods and Services Tax Ruling GSTR 2002/2 *Goods and Services Tax: GST treatment of financial supplies and related supplies and acquisitions* – which sets out the GST treatment of financial supplies and related supplies and acquisitions, and
- Goods and Services Tax Ruling GSTR 2006/3 *Goods and services tax: determining the extent of creditable purpose for providers of financial supplies* – which sets out the ATO's view in determining the extent of creditable purpose for providers of financial supplies.

Understanding the IT outsourcing agreement

When we are reviewing an IT outsourcing agreement, we want to ensure we understand:

- the framework of the outsourcing arrangement and any separate agreements for specific services (or services provided by other providers), and
- how the services are identified, accounted for and invoiced, as well as any other relevant circumstances around the agreement.

In the context of table item 2, 'processing services' means services performed by an entity that have the character of being steps or actions directed towards achieving a specific processing outcome in relation to account information for an account provider.

The threshold issue is to confirm whether the acquisition is of processing services rather than IT capacity. As set out in paragraph 83 of GSTR 2004/1, the term 'processing services' is to be read as a single term. This can be distinguished from an acquisition of processing capacity, which is not within the ambit of table item 2 which contemplates the acquisition of processing services rather than the mere acquisition of processing or processing capability (refer to paragraph 87 of GSTR 2004/1). In this regard, we will look to understand what the outsourced provider is responsible for and controls under the agreement, and whether they are responsible for and control a processing function in relation to account information for you as the account provider.

Determining which parts of the acquisition fall within the scope of table item 2

Following this, we need to consider whether you have correctly identified which of the acquisitions under the IT outsourcing agreement fall within the scope of table item 2 or other RCA items in the *A New Tax System (Goods and Services Tax) Regulations 2019* (GST Regulations) (for example, table items 5 or 7 of subsection 70-5.02). Specifically, in relation to table item 2 this involves considering whether the services acquired are directed towards a specific processing outcome in relation to account information.

Paragraph 113 of GSTR 2004/1 makes clear that, in the context of table item 2 of subsection 70-5.02 of the GST Regulations, the expression 'in relation to':

... is not intended to convey the widest possible connection between processing services and account information. Rather, the processing service and the account information are related, for the purposes of item 2, where there is an identifiable (as opposed to general) association between them. ... Item 2 ... is seeking only to link very specific *processing services* to *account information* ...

Applications or services that perform operational functions

Some applications and services under an IT outsourcing agreement may fall within the scope of table item 2 because:

- they perform an operational function that involves processing of account information, or they are integral to such a function, and
- the outsourced provider is responsible for, and in control, of the processing functions that process transactions on an account.

However, an application that serves an operational function that does not directly involve processing in relation to account information, and is not integral to applications that process such information, will not fall within the scope of table item 2.

Practical examples of services or applications that generally would not fall within the scope of table item 2 include:

- Workplace services or applications that provide tools such as Microsoft Word or Outlook, or printing services for bank staff, as these do not have the identifiable relationship to account information that is required to be within scope for table item 2. They are too far removed in their association to account information – the relationship is only a general association to account information; for instance, their use in obtaining, storing or conveying client information, which may include account information.
- Applications that are used for marketing or sales purposes by the bank that references an existing customer base (including their account information) and other data that would have a general association with that pre-existing account information, as this could be used to inform a marketing or sales strategy. The purpose, or specific processing outcome, of this application is to generate potential sale leads for future supplies of products by the bank (which may or may not result in an account being created) and this does not have a sufficient relationship to account information. The use of existing account information is merely an input used by the application that only has a general association with the processing outcome of producing sales leads, and it would not qualify as an RITC.

Processing services to support operational functions or which are related to the general IT environment

Some services or applications acquired under an IT outsourcing agreement may not serve an operational function themselves but instead are supportive of the general IT environment that the outsourced provider is responsible for or controls.

An example may be anti-virus software or the incident reporting or help desk functions that relate to handling disruptions in the IT environment. These types of services and applications are capable of being integral to a table item 2 processing function to an extent. An example of this could be the acquisition of a password management function that is used across a number of bank systems, which partly relates to allowing staff to access processing functions for account information.

We would expect you to apportion these expenses on a fair and reasonable basis, between RCAs (including table item 2 processing services) and other acquisitions, to determine your entitlement to RITCs.¹

However, if instead you have retained responsibility for and control over the part of the IT environment that these services or applications support, the services and applications in relation to that part of the IT environment will not be within the scope of table item 2. This links back to the threshold issue that these services are not processing services in relation to account information; they are services that facilitate you performing a corporate IT function (that is not an RCA) over which you have retained responsibility and control.

Apportionment methodology

Where what is acquired is partly an RCA and partly not, we will seek to understand how your apportionment methodology estimates the extent of your entitlement to RITCs to seek assurance that it is fair and reasonable.

¹ See paragraph 98 of GSTR 2004/1.

We expect that any RITC apportionment analysis will be supported by detailed evidence as to how you determined the extent to which what you have acquired is a listed RCA. In doing so, we would expect you to be able to identify robust data that can be used to allocate IT costs across different functions to determine any apportionment rate to be applied. For instance, in relation to workplace services for bank staff, you could use transactional or system data that breaks down the time spent by staff on the systems that perform processing services in relation to account information.

We would expect you to have documented processes in place to periodically review your apportionment methodology or to review it if there are material changes (for example, changes to the underlying agreements) that may impact on your apportionment methodology.

In some circumstances, it may be appropriate to use staff surveys to obtain information as to time spent on certain applications or processes. For example, this may be appropriate where workplace desktop services are provided that allow staff to initiate RCA processing functions that are the responsibility of the provider. However, we need to ensure that the methodology used is fair and reasonable.

Some issues to consider in deciding to rely on survey results are:

- Is there an alternative objective way in which to undertake an apportionment analysis drawing on data available in your business or could there be complementary data available to sense check the results of a survey?
- Are surveys across a large enough sample size to accurately reflect time spent on applications that relate to processing account information?
- Are surveys undertaken regularly to reflect changes in business processes?
- Do the staff selected for the survey have the appropriate background and knowledge to accurately provide the information sought by the survey? For instance, survey results are more robust when completed by the staff doing the work, rather than their managers.
- What are the questions that are asked of staff in the survey and how are the answers to these questions determinative in concluding a fair and reasonable extent of RCAs?
- Are there any assumptions that are applied in conducting the surveys and can these assumptions be tested or validated separately to the survey?

Determination of overall input tax recovery

In our reviews, we will also seek to understand how you have calculated the overall input tax recovery on the IT outsourcing agreement using the formula in Division 70 of the GST Regulations (that is, the interaction between how you determined your entitlement under Division 11 of the *A New Tax System (Goods and Services Tax) Act 1999* and Division 70 of the GST Regulations). This will include understanding the extent of creditable purpose rate under Division 11 and how you have used this rate to calculate your overall input tax recovery.

References

Related Rulings or Determinations:

GSTR 2002/2; GSTR 2004/1; GSTR 2006/3

- ANTS(GST)R 2019 70-5.02
- ANTS(GST)A 1999 Div 11

Legislative references:

- ANTS(GST)R 2019 Div 70
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ATO references

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