

Worked example

Transfer testing where ownership or control failed – single joining time and pre-1 July 1999 year loss case

Description This example shows how the relevant recoupment test (modified as required) is applied in a situation where an entity fails the ownership test prior to joining a consolidated group and incurs a loss prior to 1 July 1999.

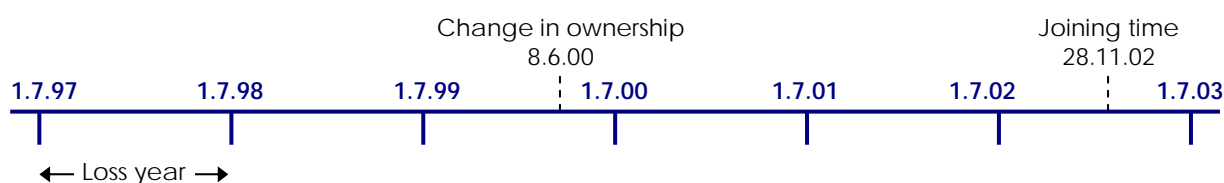
Commentary An entity that joins a consolidated group transfers any unutilised losses on hand at the joining time to the head company. It is necessary to apply the relevant recoupment test (modified as required) to ascertain the basis on which a loss is transferred to a head company.

Section 707-120 requires a loss to be tested as if the joining entity was in a position to utilise the loss itself in the context of the trial year and had sufficient income or gains to do so. To the extent that the loss could be so utilised, it is transferred as at the joining time.

Example

Facts A subsidiary member of a group that consolidates on 28 November 2002 has worked out that it has an unutilised 1998 tax loss of \$1,500 as at the joining time. There was an ownership failure on 8 June 2000.

Figure 1: Joining entity timeline



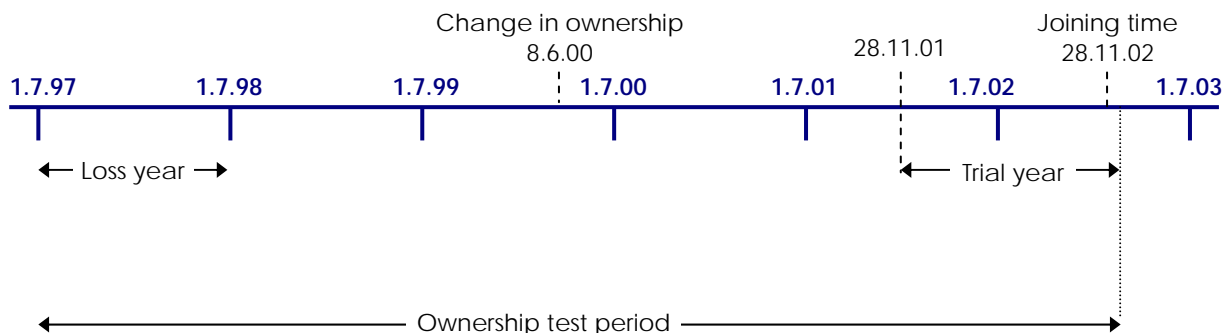
Calculation **Step 1: Apply the ownership and control transfer tests**

Sections 165-12 and 165-15 require the company to test for same owners and same control respectively throughout the ownership test period: from the start of the loss year to the end of the income year. In this case:

- the loss year is the 1998 income year, and
- the income year is represented by the trial year: 28 November 2001 to just after 28 November 2002.

In this case there has been an ownership failure within the ownership test period 1 July 1997 to just after 28 November 2002.

Figure 2: Ownership test period

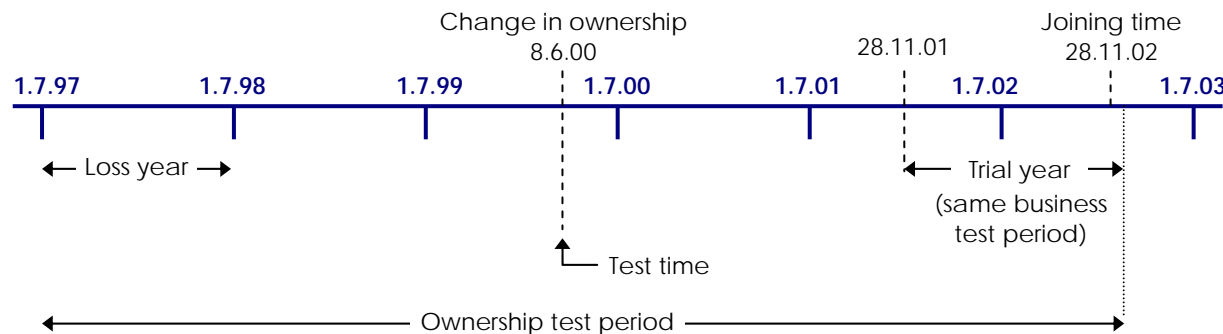


Section 165-10 provides an alternative qualifying test that requires the company to meet the conditions about carrying on the same business.

Step 2: Identify same business test points

Under section 165-13, the company must satisfy the same business test (section 165-210) for the income year (the *same business test period*). That test must be applied to the business that the company carried on immediately before the test time, which in this example is 8 June 2000, when the ownership test is failed. As the trial year is the later income year for transfer testing purposes, it is the same business test period.

Figure 3: Same business test points



Outcome

If the testing process concludes that the same business test was met in respect of these relevant times, the loss is transferred to the head company.

As the loss transfer occurred because the entity from which the loss was transferred carried on during a particular period the same business as it carried on at a particular time, the loss is 'tagged' as a loss that will always be subject to the additional test if transferred again. → section 707-135

If it cannot be transferred, its utilisation will be restricted in accordance with section 707-150 – that is, it cannot be used by any entity for the 2003 and later income years.

References

Income Tax Assessment Act 1997, sections 165-12, 165-15, 165-210

Income Tax Assessment Act 1997 – as amended by:

- *New Business Tax System (Consolidation) Act (No.1) 2002* (No. 68 of 2002), Schedule 1:
 - paragraph 707-110(2)(a)
 - section 707-115
 - subsection 707-120(3)
 - paragraph 707-120(1)(b)
 - sections 707-135, 707-150
- *Taxation Laws Amendment Act (No. 5) 2003* (No. 142 of 2003):
 - sections 165-10, 165-13

Explanatory Memorandum to the New Business Tax System (Consolidation) Bill (No. 1) 2002, Chapter 6

Revision history

Section C3-3-220 first published (excluding drafts) 2 December 2002.

Further revisions are described below.

Date	Amendment	Reason
5.4.04	Modify description of same business test points.	Reflect changes in <i>Taxation Laws Amendment Act (No. 5) 2003</i> (No. 142 of 2003).

Proposed changes to consolidation

Proposed changes to consolidation announced by the Government are not incorporated into the *Consolidation reference manual* until they become law. In the interim, information about such changes can be viewed at:

- <http://assistant.treasurer.gov.au> (Assistant Treasurer's press releases)
- www.treasury.gov.au (Treasury papers on refinements to the consolidation regime).