Application of the consolidation provisions to cooperative companies

A cooperative company may be eligible to be a member of a consolidatable group. If the group consolidates, its status as a cooperative company, and the associated income tax concessions, may be affected by the operation of the single entity rule. This is because the tests for cooperative company status would be applied to the head company taking into account the objects and activities of all group members.

This section outlines the requirements for a company to qualify for income tax treatment as a cooperative company, and the effects of the consolidation provisions on such a company if it becomes a member of a consolidated group.

Qualifying as a cooperative company

For a company to qualify as a cooperative company and thus claim any concessions it must be established for the purpose of carrying on any business having as its primary object(s) one or more of the objects stated in paragraphs 117(1)(a) to (e) of the *Income Tax Assessment Act* (ITAA) *1936*[1]. These are:

(a) The acquisition of commodities or animals for disposal or distribution among its shareholders.

(b) The acquisition of commodities or animals from its shareholders for disposal or distribution.

(c) The storage, marketing, packing or processing of commodities of its shareholders.

(d) The rendering of services to its shareholders.

(e) The obtaining of funds from its shareholders for the purpose of making loans to its shareholders to enable them to acquire land or buildings to be used for the purpose of residence or of residence and business.

Even when a company qualifies under section 117 it will be deemed not to be a cooperative company in any year in which section 118 applies. This may happen in a year in which the company does not satisfy the requirement to have at least 90% of the value of certain of its dealings with members.

Taxation Ruling TR1999/14 considers the basis on which a company whose business activities include the making of loans to shareholders may qualify as a 'cooperative company'. In deciding whether a company falls within subsection 117(1), two questions need to be asked:

- What *business* or *businesses* is the company carrying on?
- What are the *primary objects* of each business?

[1] Cooperative and mutual companies are dealt with in the ITAA 1936, Part III, Division 9, sections 117 to 121.

Should a company engage in several businesses, *all* must have as their primary object(s) one or more of those listed in paragraphs 117(1)(a) to (e).

Each business carried on by a company may have several primary objects. It is necessary to determine which of the activities of a business can be identified as its core or fundamental activities. Any part of a business that is significant in relation to each of the other parts is a primary object. Secondary objects are those activities that do not impact on the overriding character of the business. They should be no more than occasional or incidental.

In any year in which the company is not or is deemed not to be a cooperative company, the provisions of Division 9 will not apply. This means sections 119 and 120 will not apply in that year to such a company or its shareholders.

Eligibility to consolidate

The table in subsection 703-15(2) of the ITAA 1997 sets out the requirements for entities to be members of a consolidated group.

A cooperative company can be the head company of a consolidated group if it meets all of the requirements in item 1 of the table[2].

Item 2 of the table covers eligibility to be a subsidiary member of a consolidated group. In practice it may be difficult for a company to qualify as both a cooperative company and a subsidiary member of a consolidated or consolidatable group. This is because of a conflict in the ownership requirements for cooperative companies[3] and the requirement for subsidiary members to be wholly-owned subsidiaries of a head company[4]. Under the single entity rule, the objects set out in subsection 117(1) would need to be met by reference to the shareholders in the head company of the consolidated group and not the shareholders in the subsidiary.

Notes

Repeal of exclusion of cooperative companies

Item 4 of the table in subsection 703-20(2) of the ITAA 1997 originally provided that certain cooperative companies could not be members of a consolidated group. Item 4 was repealed with application from 1 July 2002.

For more information on the single entity rule see:

- 'Single entity treatment', C9-1-110
- section 701-1, ITAA 1997
- TR 2004/11.

[2] This is supported by the Explanatory Memorandum to the New Business Tax System (Consolidation, Value Shifting, Demergers and Other Measures) Bill 2002, paragraph 4.7.

[3] Section 117, ITAA 1936.

[4] Item 2 of the table in subsection 703-15(2), ITAA 1997.

Impacts of consolidating

Cooperative groups are often structured with a cooperative company as the parent company. Other activities that have not met the primary objects test in section 117 may have been conducted through wholly-owned subsidiaries of the parent cooperative company.

Once a choice to consolidate is made, the head company and all its subsidiary members are treated as if they are a single entity for income tax purposes. This means the objects, businesses and activities of the subsidiaries are treated as if they are the objects, businesses and activities of the head company. The primary objects of each business must be determined and tested against the requirements of subsection 117(1).

Accordingly, the tests for cooperative company status are applied to the head company (in the manner explained in TR 1999/14) after taking into account all objects, businesses and activities of the head company and its subsidiary members. The tests in section 118 are also applied to the head company (including its subsidiary members).

If after taking into account all the objects, businesses and activities of the head company it no longer qualifies as a cooperative company, Division 9 does not apply and any concessions that would have been available under Division 9 are denied to the head company. Any concession available to members of a cooperative company under Division 9 are also denied to those members in any years in which the head company is not or is deemed not to be a cooperative company.

References

Income Tax Assessment Act 1936, Part III, Division 9, sections 117 to 121

Income Tax Assessment Act 1997:

- section 701-1
- Division 703

Explanatory Memorandum to the New Business Tax System (Consolidation, Value Shifting, Demergers and Other Measures) Bill 2002, paragraph 4.7

Taxation Ruling TR 1999/14: *Income tax: determining the co-operative status of a company which makes loans to shareholders*

Taxation Ruling TR 2004/11: *Income tax: consolidation: the meaning and application of the single entity rule in Part 3-90 of the* Income Tax Assessment Act 1997

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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).