Worked example

Amount of transferred losses that can be utilised – franking offsets

Description

This example shows how to determine, under the available fraction method, the limit for utilisation of tax losses transferred to the head company of a consolidated group where the head company is in receipt of a franked distribution for the income year.

Note

For more information about:

- loss bundles and calculating the available fraction → 'Treatment of losses', C3-1; 'Consolidation loss provisions', C3-2-110 (high-level worked example).

Commentary

Amendments to Division 36 of the *Income Tax Assessment Act 1997* (ITAA 1997) enable corporate tax entities to choose the amount of prior year tax losses they wish to deduct in a later year of income, subject to certain limits → section 36-17. Also, a current year tax loss that would otherwise be 'wasted' against franked dividend income can be carried forward to a later year of income. The quantum of the tax loss is determined by reference to the amount of excess franking offsets for the income year → section 36-55.

Consolidation loss rules are designed so that group tax losses and concessional tax losses are used before transferred tax losses[1]. Consequential amendments[2] have been made to section 707-310 to ensure that this principle is maintained in the amended tax loss rules for corporate tax entities.

First, the amount of 'other assessable income' in item 6 in the table in subsection 707-310(3) is calculated by making a reduction for the grossed-up amount of franking offsets[3]. This ensures that any franking offsets are appropriately taken into account in determining the amount of transferred tax losses able to be deducted.

Second, the limit on the amount of transferred tax losses able to be utilised by a consolidated group is set on the assumption that the choice is made to use all available other tax losses without restriction → paragraph 707-310(3A)(a). This prevents a notional choice being made to use a lesser or nil amount of other tax losses in order to increase the transferred tax loss limit.

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[1] There are exceptions to this rule – see C3-4-430.

[2] The amendments discussed in this example apply to an income year that includes 1 July 2002 and later income years.

[3] The meaning of franking offsets is given in paragraph 707-310(3A)(c): franking offsets is the amount of the entitlement to two tax offsets – franking credits and venture capital credits.

Once transferred loss limits have been established under section 707-310, the head company is able to determine its actual taxable income position, incorporating the actual choices made for the deduction of its utilisable tax losses.

Example

Facts

The head company of a consolidated group is working out its taxable income for the income year ended 30 June 2004.

The group's 'other assessable income' is $5,000. The group incurred allowable deductions of $800 in relation to that income.

The other assessable income includes a franked distribution of $1,400 plus the franking credit on the distribution of $600.[4]

There is a group tax loss (not film) of $1,150 carried forward from the 2003 income year.

The group's transferred losses are as shown in table 1.

Table 1: Transferred losses and available fractions

Loss bundle	Available fraction	Unused transferred losses
Bundle A	0.316	$1,450 tax loss (not film)
Bundle B	0.418	$1,825 tax loss (not film)

Transferred losses are to be utilised in accordance with the available fraction method.

The head company satisfies the recoupment tests for the utilisation of all losses in the 2004 income year and chooses to deduct all utilisable losses from its taxable income.

4 Section 207-20.

Calculation

A. Apply the three-step available fraction method

Step 1: Work out the categories of group income or gains – subsection 707-310(3)

Table 2: Categories of group income or gains (step 1)

Category of income or gains	Gross amount ($)	*Less:* other allowable deductions/ reductions ($)	*Less:* group/ concessional losses of the relevant sort ($)	*Less:* transferee's grossed-up franking offset amount (applies only for item 6) ($)	Income/ gains available for the bundle ($)
Other assessable income	5,000	800	1,150	2,000*	1,050

* Determined per paragraph 707-310(3A)(c) as: 1/0.3 X $600

Step 2: Calculate the fraction of the income/gains that is attributable to each bundle – subsection 707-310(3)

Table 3: Fraction of income/gains attributable to each bundle (step 2)

Category of income or gains	Loss bundle	Step 1 amount ($)	*Multiplied by:* available fraction (AF)	AF amount for the bundle ($)
Other assessable income	Bundle A	1,050	0.316	332
	Bundle B	1,050	0.418	439

Step 3(a): Work out a notional taxable income for bundle A – subsection 707-310(2)

Table 4: Taxable income (step 3a)

Assessable income	$	Deductions/losses	$
Other assessable income	332	Transferred tax loss	332
Total	**332**	**Total**	**332**

The (notional) taxable income for bundle A is $0 ($332 – $332).

$332 of the tax loss in bundle A can be utilised by the group when it determines its actual taxable income for the 2004 income year.

Step 3(b): Work out a notional taxable income for bundle B – subsection 707-310(2)

Table 5: Taxable income (step 3b)

Assessable income	$	Deductions/losses	$
Other assessable income	439	Transferred tax loss	439
Total	**439**	**Total**	**439**

The (notional) taxable income for bundle B is $0 ($439 – $439).

$439 of the tax loss in bundle B can be utilised by the group when it determines its actual taxable income for the 2004 income year.

B. Determine the head company's actual taxable income

Table 6: Taxable income

Assessable income	($)	Deductions/losses	($)
Other assessable income	5,000	Deductions	800
		Group tax loss (2003)	1,150
		Transferred tax loss (bundle A)	332
		Transferred tax loss (bundle B)	439
Total	**5,000**		**2,721**

The group's taxable income is $2,279 ($5,000 – $2,721).

Tax payable for the 2004 income year is shown in table 7.

Table 7: Tax payable

Taxable income ($)	Tax on taxable income (30c corp. tax rate)	*Less:* tax offsets ($)	Tax payable ($)
2,279	683.70	600	83.70

The loss bundles as at the start of the 2005 income year will contain the losses shown in table 8.

Table 8: Loss bundles

Bundle	Loss	Available fraction	Sort
A	$1,118 ($1,450 – $332)	0.316	Tax loss (not film)
B	$1,386 ($1,825 – $439)	0.418	Tax loss (not film)

If other assessable income was not reduced by the transferee's grossed-up franking offset amount of $2,000, the transferred tax loss limits for bundle A and bundle B would be inappropriately higher by $1,468[5]. Given a corporate tax entity can deduct tax losses only to the extent that there will not be any amount of excess franking offsets, the head company in this example would have been able to choose to utilise its transferred tax losses ahead of the group tax loss.

References

Income Tax Assessment Act 1997, Section 707-310; as amended by *Taxation Laws Amendment Act (No.5) 2003* (No. 142 of 2003), Schedule 8

Income Tax Assessment Act 1997, Division 36; as amended by *Taxation Laws Amendment Act (No.5) 2003* (No. 142 of 2003), Schedule 8

Income Tax Assessment Act 1997, Section 207-20

Income Tax (Transitional Provisions) Act 1997, Section 707-350

Revised Explanatory Memorandum to Taxation Laws Amendment Bill (No. 5) 2003, paragraphs 5.50–4

Revision history

Section C3-4-415 first published 23 April 2004.

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).

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5 $2,000 x 0.316 plus $2,000 x 0.418 = $1,468.