

Transfer of tax losses under Subdivision 170-A – consolidation part-way through the head company's income year

Note

Date on which existing grouping provisions cease to operate

Subdivision 170-A of the ITAA 1997 provides for tax losses to be transferred within wholly-owned groups of companies. Access to Subdivision 170-A generally ceases on 1 July 2003. However:

- groups that consolidate before 1 July 2003 are entitled to transfer tax losses only until the date of consolidation, and
- head companies with a substituted accounting period (SAP) that consolidate their group on the first day of their next income year after 1 July 2003 are entitled to transfer tax losses until the date of consolidation.

For further discussion of the removal of the grouping provisions → 'Substituted accounting period (SAP)', C9-4-110.

Background

As part of the introduction of the consolidation regime, the existing grouping rules applicable to wholly-owned groups of companies have only limited operation. The provisions of Subdivision 170-A of the *Income Tax Assessment Act 1997* (ITAA 1997), which allow tax losses to be transferred within wholly-owned groups of companies, have been significantly modified. Generally, from 1 July 2003 tax loss transfers are allowed only where one of the parties to the transaction is an Australian branch of a foreign bank.

The date at which the amendments to Subdivision 170-A of the ITAA 1997 apply, and the amount of transfers allowable for the income year prior to the amendments applying, is determined by the application provisions contained in Schedule 3, Items 37 to 39 of the *New Business Tax System (Consolidation) Act (No. 1) 2002*.

Items 37 and 38 determine the year in which the amendments to Subdivision 170-A apply. In summary, these amendments apply to a company – and therefore supersede the existing Subdivision 170-A provisions – for:

- income years starting on or after the date of consolidation if the company joins a consolidated group on its formation and the date of consolidation is either:
 - before 1 July 2003, or
 - the first day of the head company's next income year starting after 30 June 2003 (and before 1 July 2004), and
- income years starting after 30 June 2003 in other cases, including where the company does not join a consolidated group.

Tax loss transfers in the final year

Item 39 operates to determine the amount of transfers allowable under Subdivision 170-A for the final income year before the amendments to Subdivision 170-A apply. The amount transferable is determined by reference to the 'apportioning day', which is either 1 July 2003 or the date of consolidation, depending on whether item 37 or 38 applies to the company. The object of item 39 is to ensure that the company can either:

- transfer a loss it makes for the final year only so far as the loss is attributable to the period in the final year elapsing before the apportioning day, or
- utilise a loss transferred to it to reduce income or gains for the final year only so far as the income or gains are attributable to the period in the final year elapsing before the apportioning day.

Formulas provided in item 39 give effect to these objects.

Item 39 does not reduce the tax loss transfer allowable under Subdivision 170-A where consolidation occurs on the first day of the head company's income year¹. In these situations the tax loss limit and the income limit are not apportioned – the group members have 'full access' to tax loss transfers in the final year before the amendments to Subdivision 170-A apply.

Item 39 may operate to reduce the amount transferable² where consolidation takes place part-way through the head company's income year. In these 'part-year' situations, item 39 applies only to *certain* transfers of tax losses.

In part-year situations, the following tax loss transfers can be made:

- a non-membership period tax loss of a subsidiary member may be transferred to another eligible subsidiary member with sufficient income in its non-membership period
- a prior year tax loss of a subsidiary member may be transferred to another eligible subsidiary member with sufficient income in its non-membership period, and
- the portion of a group tax loss of the head company referable to the period in the income year prior to consolidation may be transferred to an eligible subsidiary member with sufficient income in its non-membership period.

In part-year situations it is not possible to transfer a prior year tax loss of a head company to an eligible subsidiary, nor is it possible for a subsidiary to transfer either a non-membership period or a prior year tax loss to the head company under Subdivision 170-A.

The limited application of item 39 in part-year situations is a product of the dissimilar treatment of subsidiary members and head companies in the year of

¹ Provided all subsidiary members have the same balancing date as the head company.

² As determined by Subdivision 170-A of the ITAA 1997.

consolidation. Specific provisions divide the consolidation year of subsidiary members into non-membership and membership periods. This 'rule-off' ensures income and tax loss amounts are calculated for the pre-consolidation period. Transfers of tax losses can be undertaken between subsidiary members for this pre-consolidation period and any surplus tax losses are then transferred to the head company at the joining time³.

Conversely, head companies are *not* permitted to rule-off. Surplus tax loss amounts in the wholly-owned company group must be transferred under Subdivision 707-A of the ITAA 1997 to the head company at the joining time. In part-year situations, transfers take place before the end of the final year of the head company and hence restrict the operation of item 39. Losses that have been transferred to the head company under Subdivision 707-A must subsequently be utilised under the provisions contained in Subdivision 707-C (i.e. essentially subject to the available fraction method).

Similarly, at the joining time the head company must transfer to itself any prior year tax losses it has incurred. These head company tax losses (transferred to itself part-way through its income year) cannot be transferred to an eligible subsidiary member under Subdivision 170-A.

A group tax loss incurred in the year of consolidation can be transferred to an eligible subsidiary member in respect of its pre-consolidation income as it is a tax loss made in the final year and is able to be apportioned under item 39 based on the number of days pre and post consolidation.

→ worked examples C3-5-110, C3-5-120

Revision history

Section C3-5 first published 2 October 2003.

³ Provided transfer tests are satisfied.