Worked example

Transfer of attribution surpluses

Description

This example shows how attribution account surpluses relating to interests in controlled foreign companies (CFCs), foreign investment funds (FIFs) and foreign life assurance policies (FLPs) are transferred from a joining company to a head company at the joining time and from a head company to a leaving company at the leaving time.

Commentary

The transfer of attribution account surpluses from a joining company to a head company ensures that distributions from CFCs, FIFs and FLPs are not taxed to the head company where the joining company has already been taxed on the attributed income. The same rationale applies when a company leaves a group.

Where a company that holds interests in a CFC, FIF or FLP becomes a subsidiary member of a consolidated group, any surplus in the relevant attribution account at the joining time is transferred to the head company. This applies with respect to surpluses in attribution accounts, attributed tax accounts, FIF attribution accounts and FIF attributed tax accounts.

If the company leaves the consolidated group and takes interests in a CFC, FIF or FLP with it, the head company transfers to the leaving company at the leaving time a proportion of the surplus in the relevant attribution account kept by the head company.

Example: joining company

Facts

HCo is the head company of a consolidated group. On 1 January 2006 HCo acquires all the shares in another company, ACo. Both companies have an income year of 1 July to 30 June.

At the joining time HCo has FIF interests in FIF1, which has a notional accounting period of 1 July to 30 June. At that time the FIF attribution account for FIF1 has a surplus of $50.

Table 1: ACo's FIF interests at the joining time

	Notional accounting period	Attribution account balance as at 30.06.05
FIF1	1 July to 30 June	$75 surplus
FIF2	1 January to 31 December*	$100 surplus
FIF3	1 January to 31 December*	$150 surplus

* ACo made an election under subsection 486(3) of the *Income Tax Assessment Act 1936* (ITAA 1936) that the notional accounting period for FIF2 and FIF3 is the period for which the FIFs' accounts are prepared.

ACo has held these interests for the two years prior to the joining time, neither acquiring nor disposing of any interests during that period. ACo used the market value method to calculate the FIF income accruing to the FIF interests.

Section 529 in Part XI of the ITAA 1936 requires a taxpayer that holds an interest in a FIF at the end of the taxpayer's income year to include in their assessable income any FIF income that accrues to that FIF interest for the notional accounting period of the FIF that ends in the taxpayer's income year.

A non-membership period is treated as if it were an income year → former section 701-30, *Income Tax (Transitional Provisions) Act 1997*. This means ACo must determine the FIF income or loss that accrued in relation to its FIF interests for the non-membership period 1 July 2005 to 31 December 2005.

Calculation

For the purpose of calculating the FIF income assessable to ACo, FIF1's notional accounting period is taken to end earlier than it actually does. Ending the notional accounting period of FIF1 immediately before the joining time ensures that ACo is assessed on the FIF income that accrues to its FIF1 interest for the non-membership period before the joining time, and that HCo is assessed on any FIF income that accrues to its FIF1 interests (which include ACo's interests) during the period of consolidation. HCo determines the FIF income as if it has acquired the FIF interests at the joining time. If HCo chooses to use the market value method, the consideration taken to be given at the joining time is the market value of those interests immediately before the joining time.

The notional accounting periods of FIF2 and FIF3 both end at the joining time. Therefore, for the purpose of calculating its assessable income in the non-membership period, ACo must determine in relation to each FIF the FIF income or loss that accrued for the whole of the notional accounting period.

The FIF income/loss for each of ACo's FIF interests determined for the purposes of ACo's assessable income for the non-membership period before the joining time is shown in table 2.

Table 2: FIF income/loss of ACo FIF interests for non-membership period

	Period in which FIF income accrued	FIF income
FIF1	1 July 2005 to 31 December 2005	$200
FIF2	1 January 2005 to 31 December 2005	($100)
FIF3	1 January 2005 to 31 December 2005	$300

The FIF loss in relation to FIF2 can be claimed as a deduction against ACo's other assessable income → section 532, ITAA 1936. ACo can claim the deduction only to the extent of the surplus in the attribution account of FIF2. The deduction gives rise to an attribution account debit to the extent of the loss or the surplus, whichever is less. ACo includes the FIF income for FIF3 for the whole of the notional accounting period in its assessable income.

The FIF income included in ACo's assessable income gives rise to an attribution account credit immediately before the joining time.

The attribution account surplus transferred by ACo for each of the three FIFs is shown in table 3.

Table 3: Attribution account surplus transferred by ACo

	FIF1		FIF2		FIF3	
	Credit	Debit	Credit	Debit	Credit	Debit
Balance brought forward as at 1.7.05	$75		$100		$150	
Credit/debit as at 31.12.05	$200			$100	$300	
Balance as at 31.12.05	**$275**		**NIL**		**$450**	

Had the FIF loss in relation to ACo's interest in FIF2 exceeded the attribution account surplus, that excess would not have been allowable as a deduction. Instead the entry history rule would make the remaining FIF loss available to HCo to offset against FIF income accruing in later income years for interests in FIF2 held by the group.

The attribution account surpluses transferred by ACo are pooled with those of HCo as head company of the group. As HCo also held interests in FIF1 and had a surplus of $50 in the attribution account that it kept for its interest in FIF1, the attribution accounts kept by HCo immediately following the joining time are as shown in Table 4.

Table 4: HCo's attribution accounts immediately following joining time

	FIF1		FIF2		FIF3	
	Credit	Debit	Credit	Debit	Credit	Debit
Balance at joining time	$50		N/A	N/A	N/A	N/A
Surplus from ACo	$275		NIL		$450	
Balance post joining time	**$325**		**NIL**		**$450**	

Example: leaving company

Facts

On 1 July 2006 HCo sells all its shares in ACo to a company outside the group. ACo takes 50% of the group's interests in FIF1 with it. FIF1's attribution account was in surplus to the extent of $350.

The proportion of the attribution account surplus to be transferred to ACo is determined using the following formula:

$$\frac{\text{Leaving company's attribution account percentage in relation to the attribution account entity at the leaving time}}{\text{Head company's attribution account percentage in relation to the attribution account entity just before the leaving time}} \times \text{Attribution surplus for the attribution account entity in relation to the head company just before the leaving time}$$

Calculation

ACo's attribution account percentage in FIF1 at the leaving time is 50% of HCo's attribution account percentage in FIF1 just before the leaving time. The proportion of the attribution account surplus transferred to ACo at the leaving time will therefore be $175, i.e. 50/100 x $350.

The attribution account surplus taken by ACo ensures that it will not be assessed on distributions it receives from FIF1 in relation to the interests it holds to the extent of the surplus.

References

Income Tax Assessment Act 1936, sections 532 and 529 and subsection 486(3)

Income Tax Assessment Act 1997, Division 717, Subdivisions 717-D and 717-E; as amended by *New Business Tax System (Consolidation, Value Shifting, Demergers and Other Measures) Act 2002* (No. 90 of 2002), Schedule 6

Income Tax (Transitional Provisions) Act 1997, former section 701-30; as amended by *New Business Tax System (Consolidation, Value Shifting, Demergers and Other Measures) Act 2002* (No. 90 of 2002), Schedule 7

Explanatory Memorandum to the New Business Tax System (Consolidation, Value Shifting, Demergers and Other Measures) Bill 2002, Chapter 2

Tax Laws Amendment (Repeal of Inoperative Provisions) Act 2006 (No. 101 of 2006), which repealed section 701-30 of the *Income Tax (Transitional Provisions) Act 1997*

Revision history

Section C6-2-210 first published (excluding drafts) 2 December 2002.

Further revisions are described below.

Date	Amendment	Reason
15.11.06	Updated references to inoperative provisions.	Legislative amendment.

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).