

Single entity treatment

When a consolidated group is formed, the group is treated as a single entity for income tax purposes.¹ Broadly, this means that on joining a consolidated group the subsidiary members lose their individual income tax identities and are treated as parts of the head company of the consolidated group (rather than as separate entities) for the purposes of determining the head company's income tax liability.

In effect, the consolidated group is treated as if it were a single divisional company. Intragroup assets and liabilities and intragroup transactions have no income tax consequences. The head company is the only entity the income tax law recognises for the purposes of working out the group's income tax liability or losses.

→ Taxation Ruling TR 2004/11

Some of the consequences of the single entity rule for the income tax treatment of consolidated groups are:

- the head company lodges a consolidated income tax return – subsidiary members no longer lodge returns
- the assets and liabilities of subsidiary members are treated as if they were assets and liabilities of the head company
- the actions of subsidiary members in respect of entities outside the group (e.g. acquisition or disposal of assets) are treated as if they had been undertaken by the head company
- intragroup transactions are ignored for income tax purposes
- where an intragroup asset² is sold to an entity outside the group, it is treated in accordance with its economic substance from the point of view of the group as a whole, and
- generally, the income tax law will apply to the head company of the consolidated group (of which subsidiary members are treated as parts) in the same way as to any single company.

The Tax Office has issued the following taxation determinations on various aspects of the single entity rule: TD 2004/43, TD 2004/44, TD 2004/49, TD 2004/51, TD 2004/69.

The following taxation determinations deal with circumstances where the single entity rule does not apply or is not relevant: TD 2004/42, TD 2004/50, TD 2004/68, TD 2004/79.

¹ Section 701-1 ITAA 1997.

² That is, an asset where the rights and obligations are between members of a consolidated group, TR 2004/11, paragraph 8(c).

The following taxation determinations deal with circumstances where the single entity rule does not apply to defeat a clearly intended outcome under provisions outside the consolidation rules: TD 2004/48, TD 2004/81.

This section describes the consequences of single entity treatment for:

- trading stock
- interest paid by a head company for funds on-lent to a subsidiary, and
- the sale of an intragroup asset to a non-member.

Trading stock

In a consolidated group, assets that were previously held by individual members as trading stock may change character in the hands of the head company. This is because the assets of all members of a consolidated group become the assets of the head company and the purpose for which they are held is determined by reference to the economic substance for the group as a whole.

For example, depending on the purpose for which the asset is taken to be held by the head company, the asset could be treated for income tax purposes as a consumable (if the trading stock is held for sale only within the consolidated group), a CGT asset or a depreciating asset.

Deductibility of interest

Where a holding company borrows money to lend to a subsidiary, the basis of deductibility of interest paid by the holding company differs in consolidated and non-consolidated situations, although the result may be the same. In a consolidated group, intragroup transactions have no income tax consequences. The deductibility of interest paid to a non-member is determined by looking at the economic substance for the group as a whole of the purpose of the loan and the use to which it is put – that is, income tax law applies to the interest as if the head company was a single company undertaking the borrowing.

→ 'Single entity treatment – deductibility of interest', C9-5-220 (worked example); Taxation Determination TD 2004/36

Sale of intragroup asset to non-member

A transaction between group members may give rise to an 'intragroup asset', such as an option, interest stream or debt. When an intragroup asset is sold or assigned to an entity outside the consolidated group, there are no income tax consequences from the transaction that gave rise to the intragroup asset but the transaction with the outside party is recognised for the purposes of working out the head company's income tax.

The transaction with the outside party is treated according to its economic substance for the group as a whole, without regard to internal transactions. The asset may therefore be treated (for the purposes of working out the head company's income tax) as something different from its legal form.

→ 'Single entity treatment – sale of intragroup asset to non-member', C9-5-230

The Tax Office has issued Taxation Ruling TR 2004/11 and the following taxation determinations related to this topic: TD 2004/33, TD 2004/34, TD 2004/35, TD 2004/39, TD 2004/45, TD 2004/46, TD 2004/82, TD 2004/83, TD 2004/84, TD 2004/85.

Note

Sale of membership interests

Special rules apply where membership interests in a subsidiary member are sold to a non-member by the head company.

The Tax Office has issued the following taxation determinations related to this issue: TD 2004/37, TD 2004/40, TD 2004/41, TD 2004/47.

Is the head company 'in the business' of the subsidiary?

One result of the single entity rule, and of the consequent ignoring of intragroup transactions, is that businesses undertaken by a subsidiary may not be recognised as being carried on by the head company. Where a subsidiary's business involves solely intragroup activity, it will not be relevant to working out the head company's income tax.

For example, a consolidatable group may include a subsidiary that is a finance company and conducts a business of lending exclusively to other entities in the group.

When the group consolidates, the intragroup lending activity does not have any income tax consequences. The head company of the group is not treated as carrying on the business of a finance company for the purpose of working out its income tax position, and the character of its assets and liabilities held through the finance company is determined from the perspective of the head company.

Note

More information

→ 'Single entity treatment – deductibility of interest', C9-5-220 (worked example)

→ 'Single entity treatment – sale of intragroup asset to non-member', C9-5-230 (worked example)

References

Income Tax Assessment Act 1997 – as amended by *New Business Tax System (Consolidation) Act (No. 1) 2002* (No. 68 of 2002), section 701-1

Explanatory Memorandum to the New Business Tax System (Consolidation) Bill (No. 1) 2002, Chapter 2

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*

Taxation determinations

TD 2004/33 – Income tax: consolidation: capital gains: does a CGT event happen to the head company of a consolidated group if a debt is created within the consolidated group and later transferred to a non-group entity?

TD 2004/34 – Income tax: consolidation: capital gains: does section 104-10 (CGT event A1) of the *Income Tax Assessment Act 1997* apply to the head company of a consolidated group where an option granted within the consolidated group is later transferred to a non-group entity?

TD 2004/35 – Income tax: consolidation and capital gains tax: does section 104-10 (CGT event A1) of the *Income Tax Assessment Act 1997* apply to the head company of a consolidated group where a licence granted within the consolidated group is later transferred to a non-group entity for no capital proceeds?

TD 2004/36 – Income tax: consolidation; can the head company of a consolidated group claim a deduction under section 8-1 of the *Income Tax Assessment Act 1997* for the interest paid on funds borrowed before consolidation and on-lent interest-free to a subsidiary member of the consolidated group?

TD 2004/37 – Income tax: consolidation: are intra-group money lending transactions or dealings taken into account in determining if the head company of a consolidated group is carrying on business as a money lender?

TD 2004/39 – Income tax: consolidation: capital gains: does CGT event A1 in section 104-10 of the *Income Tax Assessment Act 1997* happen to the head company of a consolidated group if an asset is sold by a subsidiary member to an entity outside the group?

TD 2004/40 – Income tax: consolidation: capital gains: does CGT event A1 in section 104-10 of the *Income Tax Assessment Act 1997* happen to the head company of a consolidated group when a contract is made to sell a membership interest in a subsidiary member of the group to a purchaser outside the group?

TD 2004/41 – Income tax: consolidation: capital gains: can membership interests in a subsidiary member of a consolidated group be recognised for the purpose of applying the market value substitution rule in section 116-30 of the *Income Tax Assessment Act 1997* if CGT event A1 happens to the group's head company when a contract is entered into to dispose of the interests?

TD 2004/42 – Income tax: consolidation: capital gains: does the single entity rule in section 701-1 of the *Income Tax Assessment Act 1997* affect the application of CGT event I1 in section 104-160 if a company which is a subsidiary member of a consolidated group stops being an Australian resident?

TD 2004/43 – Income tax: consolidation: capital gains: for the purposes of the capital gains tax provisions in Parts 3-1 and 3-3 of the *Income Tax Assessment Act 1997*, is the head company of a consolidated group taken to have acquired an asset, which a subsidiary member brings to the group, at the same time that the subsidiary member acquired it?

TD 2004/44 – Income tax: consolidation: capital gains: does the transfer of an asset between members of a consolidated group affect the ownership period of the head company for the purposes of applying the small business 15 year exemption in Subdivision 152-B of the *Income Tax Assessment Act 1997*?

TD 2004/45 – Income tax: consolidation: capital gains: how does the controlling individual condition in paragraph 152-110(1)(c) of the *Income Tax Assessment Act 1997* (one of the conditions for the small business 15 year exemption in Subdivision 152-B) apply to the head company of a consolidated group in respect of the sale of an asset brought into the group by a subsidiary member?

TD 2004/46 – Income tax: consolidation: capital gains: is the controlling individual condition in paragraph 152-305(2)(b) of the *Income Tax Assessment Act 1997* (one of the conditions for the small business retirement exemption) applied to the head company of a consolidated group?

TD 2004/47 – Income tax: consolidation: capital gains: does the single entity rule in section 701-1 of the *Income Tax Assessment Act 1997* affect the application of the controlling individual test in paragraph 152-10(2)(a) when a CGT event happens to a share or trust interest that is a membership interest in a subsidiary member (company or trust) of a consolidated group?

TD 2004/48 – Income tax: consolidation: capital gains: for the purposes of Subdivision 125-C of the *Income Tax Assessment Act 1997*, can the head company of a consolidated group meet the requirements of a demerging entity in subsection 125-70(7) where a subsidiary member is demerged from the group?

TD 2004/49 – Income tax: consolidation: capital gains: does the single entity rule in section 701-1 of the *Income Tax Assessment Act 1997* apply in determining whether the consequences in Subdivision 125-C of the *Income Tax Assessment Act 1997* apply to the head company of a consolidated group where one or more subsidiary members hold ownership interests in an entity outside the group that is being demerged?

TD 2004/50 – Income tax: consolidation: capital gains: if a subsidiary member of a consolidated group acquires shares in a company outside the group (the original company) under a scrip for scrip arrangement, is the single entity rule in section 701-1 of the *Income Tax Assessment Act 1997* relevant in determining the eligibility for rollover of shareholders in the original company?

TD 2004/51 – Income tax: consolidation: capital gains: does section 124-784 of the *Income Tax Assessment Act 1997* apply to determine the cost base of equity or debt issued by an acquiring entity to its ultimate holding company as part of a scrip for scrip arrangement if those companies are members of a consolidated group?

TD 2004/68 – Income tax: consolidation: Division 7A: if a private company that is a head company or subsidiary member of a consolidated group makes a payment or a loan, or forgives a debt to a shareholder (or shareholder's associate) external to the consolidated group, does the single entity rule apply to the calculation of the distributable surplus under section 109Y of the *Income Tax Assessment Act 1936*?

TD 2004/69 – Income tax: consolidation: Division 7A: if a private company, as a member of a consolidated group, makes a payment, a loan or forgives a debt to a shareholder (or shareholder's associate), that is also a member of the consolidated group, does the single entity rule in section 701-1 of the *Income Tax Assessment Act 1997* prevent the application of Division 7A of the *Income Tax Assessment Act 1936* to the transaction?

TD 2004/76 – Income tax: consolidation: are the voting interests in a foreign company held by a subsidiary member of a consolidated group treated as being voting interests of the head company of the group when determining whether section 23AJ of the *Income Tax Assessment Act 1936* applies to a dividend paid to the group?

TD 2004/79 – Income tax: consolidation: capital gains: if an entity makes a capital gain prior to becoming a subsidiary member of a consolidated group, can it choose to apply the small business replacement asset roll-over under Subdivision 152-E of the *Income Tax Assessment Act 1997* if it acquires a replacement asset after it has become a member of the group?

TD 2004/81 – Income tax: consolidation: capital gains: does the deregistration of a subsidiary member of a consolidated group cause a 'new event' to happen under paragraph 170-275(1)(a) of the *Income Tax Assessment Act 1997* if, before the subsidiary joined that group, a transfer of shares in it was a 'deferral event' under section 170-255 and the group's head company is the 'originating company' for the deferral event?

TD 2004/82 – Income tax: consolidation: capital gains: can the exemption in section 152-125 of the *Income Tax Assessment Act 1997* apply to a payment made by the head company of a consolidated group to a CGT concession stakeholder of the head company in respect of a capital gain made on the disposal of an asset legally owned by a subsidiary member of the group for which disposal the head company obtained the small business 15 year exemption?

TD 2004/83 – Income tax: can the assignment of an intra-group debt or income stream to an entity that is not a member of the consolidated group give rise to a debt interest for the head company of the group under Division 974 of the *Income Tax Assessment Act 1997*?

TD 2004/84 – Income tax: can Division 16E of Part III of the *Income Tax Assessment Act 1936* apply to a head company of a consolidated group where the principal of an intra-group loan is assigned by a member of the group to a non-member?

TD 2004/85 – Income tax: can Division 16E of Part III of the *Income Tax Assessment Act 1936* apply to a head company of a consolidated group where an intra-group income stream is assigned by a member of the group to a non-member?

TD 2005/3 – Income tax: Income tax: consolidation: will a choice to consolidate under Part 3-90 of the *Income Tax Assessment Act 1997* affect the method of income recognition of the consolidated group?

TD 2005/23 – Income tax consolidation: can the head company of a consolidated group satisfy subsection 25-35(1) of the *Income Tax Assessment Act 1997* in relation to a debt that is written off as bad by a subsidiary member, where the debt is in respect of money lent by the subsidiary in the ordinary course of its business of lending money before it became a member of the consolidated group?

Revision history

Section C9-1-110 first published 3 December 2003.

Further revisions are described below.

Date	Amendment	Reason
14.7.04	Note on proposed changes to consolidation rules.	Proposed legislative amendments.
26.10.05	References to new taxation determinations.	
16.12.05	Revisions to 'Sale of intragroup asset', p. 2.	New tax determinations.

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).