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## Draft Taxation Determination

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Income tax: consolidation: under subitem 50(5) of Part 4 of Schedule 3 to the *Tax Laws Amendment (2012 Measures No.2) Act 2012*, does the original 2002 law only apply to the particulars that form part of a head company's assessment for an income year in respect of a joining entity if the latest notice of assessment for that income year, which relates to subsection 701-55(6) of the original 2002 law in respect of that joining entity, is served on the head company before 12 May 2010?

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**Ruling**

1. Yes. Subitem 50(5) of Part 4 of Schedule 3 to the *Tax Laws Amendment (2012 Measures No.2) Act 2012*<sup>1</sup> only operates to apply the original 2002 law<sup>2</sup> to the particulars that form part of a head company's assessment for an income year in respect of the joining entity, if the head company's latest notice of assessment for the income year, which relates to the application of subsection 701-55(6) of the original 2002 law in respect of the joining entity, was served *before* 12 May 2010. That is, the conditions precedent to the operation of subitem 50(5) cannot be met where the head company's notice of assessment was served on or after that date.
2. Once the conditions in subitem 50(5) are satisfied, the original 2002 law applies in respect of the income year covered by the latest notice of assessment which invoked subitem 50(5) and applies to an 'assessment' of the head company for *that* income year (subitems 50(1) and 50(5)).<sup>3</sup> That is, under subitem 50(5), the original 2002 law does not automatically apply to assessments for subsequent income years.
3. Only particulars (relating to the joining entity) which form part of an 'assessment' of the head company for the relevant income year fall within the ambit of subitem 50(5) (therefore it is only these particulars which are, under subitem 50(5), subject to the original 2002 law). A particular, in this context, means a specific or definite constituent element in the assessment of the taxable income (or that there is no taxable income) or tax payable thereon (or that there is no tax payable).<sup>4</sup>
4. A net capital gain (and, consequently, the constituent elements which comprise that net capital gain) that has been included in assessable income, and therefore forms part of an assessment, for the relevant income year pursuant to subsection 102-5(1) of the *Income Tax Assessment Act 1997* (ITAA 1997), constitutes a particular in the assessment for that income year and therefore may attract the operation of subitem 50(5).
5. However, the mere process of working out a tax cost setting amount for an asset under the original 2002 law during the relevant income year is not in itself sufficient to obtain the treatment afforded by subitem 50(5).
6. Where the conditions in subitem 50(5) are not satisfied, the pre rules<sup>5</sup> or interim rules<sup>6</sup> may have application.

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<sup>1</sup> All legislative references are to Schedule 3 to the *Tax Laws Amendment (2012 Measures No.2) Act 2012* unless otherwise indicated.

<sup>2</sup> The *Income Tax Assessment Act 1997* disregarding amendments to that Act made by Division 1 of Part 1 and Division 2 of Part 11 of Schedule 5 to the *Tax Laws Amendment (2010 Measures No.1) Act 2010* and by Schedule 3: item 49.

<sup>3</sup> Note: if a tax loss was calculated for that income year and the assessment that was served on the head company for that income year was a nil assessment, then regard should be had to the effect of the Commissioner's preliminary view provided in Draft Taxation Determination TD 2014/D3. This scenario is not addressed in this Draft Taxation Determination.

<sup>4</sup> This is the meaning of particular in the context of section 14ZV of the *Taxation Administration Act 1953*: refer to paragraphs 156 to 162 of Taxation Ruling TR 2011/5: *Income tax: objections against income tax assessments*. This Draft Taxation Determination adopts that meaning of particular.

<sup>5</sup> The amendments made by Part 1 of Schedule 3: item 49.

<sup>6</sup> The amendments made by Parts 1 and 2 of Schedule 3: item 49.

## Examples

*Note: The following examples are provided for the purposes of illustrating the Commissioner's view about the way in which subitem 50(5) applies and do not provide a view about the application of the original 2002 law, the pre rules or sections 8-1, 102-5 and 104-25 of the ITAA 1997.*

***Example 1: tax cost setting amount for asset worked out at the joining time in accordance with the original 2002 law is (in effect) preserved by subitem 50(5)***

7. Cleaning Co became a subsidiary member of a consolidated group (whose head company was Head Co) on 1 July 2008 (the joining time). At the joining time, Cleaning Co has Asset X and is also a party to a contract (here a CGT asset) giving it the right to clean a client's offices for a pre-determined fee for a period of five years ('the cleaning contract').

8. A tax cost setting amount for each of these assets was worked out at the joining time under the original 2002 law.

9. On 1 January 2009, the cleaning contract was disposed of for consideration by Cleaning Co. Head Co used the cleaning contract's tax cost setting amount calculated (and subsequently used, having regard to subsection 701-55(5) of the ITAA 1997), as the cost base when working out its capital gain on the contract's disposal.

10. A notice of assessment for the income year ended 30 June 2009 was served on Head Co on 15 December 2009. In this assessment:

- a deduction was claimed under section 8-1 of the ITAA 1997 by applying subsection 701-55(6) of the original 2002 law in relation to Asset X; and
- a net capital gain, (which included the capital gain that was made on the disposal of the cleaning contract), was included in assessable income for the income year pursuant to subsection 102-5(1) of the ITAA 1997.

11. In the absence of subitem 50(5), the pre rules would apply for the 2009 income year because Cleaning Co joined the consolidated group before 12 May 2010. In this instance however, the conditions in subitem 50(5) are met because:

- the latest notice of assessment for the 2009 income year was served before 12 May 2010; and
- there was an application of subsection 701-55(6) of the original 2002 law in respect of Cleaning Co for that income year.

12. This means that the relevant particulars that comprise that assessment are worked out on the basis of the original 2002 law.

13. That is, subitem 50(5) applies to preserve the application of the original 2002 law to the particulars in Head Co's assessment for the income year ended 30 June 2009 (in so far as they relate to Cleaning Co). The net capital gain for the income year is a particular in that assessment. Therefore, the cost base of the contract which was used to calculate the capital gain (and ultimately, the net capital gain) is (in effect) preserved by subitem 50(5).

***Example 2: tax cost setting amount for asset worked out at the joining time under the original 2002 law is not (in effect) preserved by subitem 50(5)***

14. Assume the same facts as in Example 1. In addition:

- at the joining time, Cleaning Co was also party to another contract ('the general maintenance contract'), providing it with the right to clean and undertake general maintenance on another client's business premises for a fixed term (of three and a half years) for a pre-determined fee;
- at the joining time, the tax cost setting amount of this asset was worked out under the original 2002 law;
- the general maintenance contract ended on 30 December 2011;
- Head Co made a capital gain for the year ended 30 June 2012 from the sale of Asset Y (an asset that had previously been directly acquired by Head Co);
- if the general maintenance contract's tax cost setting amount is taken into account in working out the capital gain or loss on its ending, there will be a capital loss that would reduce the capital gain from Asset Y (noting that the quantum of that loss would not be greater than the capital gain made from the disposal of Asset Y); and
- Head Co makes no other capital gains or capital losses for the income year ended 30 June 2012.

15. The conditions in subitem 50(5) are not met in this example. Only particulars which form part of an assessment of Head Co for an income year covered by a notice of assessment which invokes subitem 50(5) (here the income year ended 30 June 2009) can fall within the ambit of subitem 50(5). The process of working out the tax cost setting amount for the general maintenance contract at the joining time under the original 2002 law did not result in the tax cost setting amount being used to calculate a particular in Head Co's assessment for the income year ended 30 June 2009.

16. Head Co's notice of assessment for the income year ended 30 June 2012 does not satisfy the conditions in subitem 50(5) as that notice does not relate to the application of subsection 701-55(6) of the original 2002 law in respect of the joining entity; and it will not be served on Head Co before 12 May 2010.

17. The pre rules apply for the income year ended 30 June 2012 because Cleaning Co joined the consolidated group before 12 May 2010 (refer subitem 50(2)). Under the pre rules, the general maintenance contract will be treated as a non-deductible right to future income and consequently an asset forming part of goodwill under subsection 701-63(2) in conjunction with paragraph 701-63(3)(c) of the pre rules.

18. Therefore, the tax cost setting amount worked out for the general maintenance contract at the joining time, under the original 2002 law is not (in effect) preserved by subitem 50(5). Consequently, Head Co will not make a capital loss, as a result of the general maintenance contract coming to an end, in the income year ended 30 June 2012.

**Date of effect**

19. When the final Determination is issued, it is proposed to apply both before and after its date of issue. However, the Determination will not apply to taxpayers to the extent that it conflicts with the terms of settlement of a dispute agreed to before the date of issue of the Determination (see paragraphs 75 to 76 of Taxation Ruling TR 2006/10).

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**Commissioner of Taxation**

15 January 2014

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## **Appendix 1 – Explanation**

**1 This Appendix is provided as information to help you understand how the Commissioner's preliminary view has been reached. It does not form part of the proposed binding public ruling.**

### **Explanation**

20. The Application rules in Part 4 of Schedule 3 are relevant to ascertaining whether the pre rules, interim rules or prospective rules<sup>7</sup> apply in relation to an assessment of the head company of a consolidated group or multiple entry consolidated (MEC) group in respect of an entity (the 'joining entity') when that entity joins the group.

21. Subitem 50(1) provides:

The pre rules, interim rules or prospective rules apply to an assessment of the head company of a consolidated group or MEC group for an income year in respect of an entity (the joining entity) that becomes a member of the group at a time (the joining time), in accordance with subitems (2), (3), (4) and (5).

22. Subitem 50(2) provides that the pre rules will apply to an assessment of the head company for an income year in respect of a joining entity if the entity joined the group before 12 May 2010 (or where the arrangement under which the entity joined the group commenced before 10 February 2010).

23. There are two exceptions to the pre rules, namely the interim rules as provided for in subitem 50(3) and the original 2002 law as provided for in subitem 50(5).

24. Relevant to this Draft Tax Determination, subitem 50(5) states:

Despite subitems (2) and (3), the original 2002 law applies, for the income year in respect of the joining entity, if the head company's latest notice of assessment, for the income year, that relates to the application of subsection 701-55(6) of the original 2002 law in respect of the joining entity, was served on the head company by the Commissioner before 12 May 2010.

25. Subitem 50(5) operates where the head company's latest notice of assessment for an income year, which relates to the application of subsection 701-55(6) of the original 2002 law in respect of a joining entity, was served before 12 May 2010. That is, the conditions precedent to the operation of subitem 50(5) cannot be met where the head company's notice of assessment was served on or after that date.

26. Once the conditions in subitem 50(5) are met, the original 2002 law applies in respect of the income year covered by the latest notice of assessment referred to in that subitem. This can be inferred from the phrase 'the income year' in subitem 50(5) (subitem 50(5) provides 'the original 2002 law applies, for **the** income year...if the head company's latest notice of assessment, for **the** income year, that relates to the application of subsection 701-55(6)...') [emphasis added]. Since the conditions precedent to the operation of subitem 50(5) cannot be satisfied where the head company's notice of assessment is served on or after 12 May 2010, it follows that the original 2002 law cannot apply in respect of income years that end after that date.

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<sup>7</sup> The amendments made by Parts 1, 2 and 3 of Schedule 3: item 49.

27. The original 2002 law applies to an assessment of the head company in respect of a joining entity for the income year covered by the latest notice of assessment which invokes subitem 50(5) (subitem 50(1) in conjunction with subitem 50(5)). An assessment is made up of elements or particulars. Therefore, only particulars in respect of that joining entity, which form part of the head company's assessment for the relevant income year fall within the scope of subitem 50(5) and thus, it is only these particulars which are subject to the original 2002 law.<sup>8</sup> This can be discerned when subitem 50(5) is considered in the context of subitems 50(1) and (2).

28. To form part of an assessment for the relevant income year, the particular must be a constituent element in the taxable income calculation for that income year. This follows from the meaning of the term assessment.

29. The term 'assessment' in relation to an income tax liability is defined by subsection 6(1) of the *Income Tax Assessment Act 1936*. Paragraph (a) of the definition provides that 'assessment' means the ascertainment of:

- the amount of taxable income (or that there is no taxable income); and
- the tax payable on that taxable income (or that there is no tax payable); and....

30. The cost base of a CGT asset does not form part of an assessment until a CGT event occurs in relation to the asset and the resulting capital gain or loss is taken into account in calculating the net capital gain of the taxpayer under subsection 102-5(1) of the ITAA 1997. This is because a capital gain or loss is not made unless and until a CGT event happens (see section 102-20 of the ITAA 1997). Once a CGT event happens, subsection 102-5(1), which includes net capital gains in assessable income, provides the (only) mechanism by which the resultant capital gain or loss is included in assessable income and used to work out taxable income (consequently, this is the only means by which a capital gain or loss can form part of an assessment).

31. This means, for example, that the tax cost setting amount of an asset, worked out under the original 2002 law, which has been used to calculate a capital loss made but not applied in a relevant income year (that is, an income year to which subitem 50(5) refers) is not in effect preserved by subitem 50(5). Also, for example, subitem 50(5) does not in effect preserve the tax cost setting amount for an asset (for the purposes of a future CGT event) where it is merely worked out under the original 2002 law during the relevant income year. The process of working out the tax cost setting amount for a joining entity's asset at the joining time does not in itself result in the tax cost setting amount being used to calculate a particular in an assessment (for example, a net capital gain that is included in assessable income pursuant to subsection 102-5(1) of the ITAA 1997) for that income year.

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<sup>8</sup> These particulars must include a claim that relates to the application of subsection 701-55(6) of the original 2002 law in order for the original 2002 law to apply to the assessment.

## Appendix 2 – Your comments

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32. You are invited to comment on this draft Determination including the proposed date of effect. Please forward your comments to the contact officer by the due date.

33. A compendium of comments is prepared for the consideration of the relevant Rulings Panel or relevant tax officers. An edited version (names and identifying information removed) of the compendium of comments will also be prepared to:

- provide responses to persons providing comments; and
- be published on the ATO website at [www.ato.gov.au](http://www.ato.gov.au).

Please advise if you do not want your comments included in the edited version of the compendium.

**Due date:** **21 February 2014**

**Contact officer:** **Melissa Bird**

**Email address:** **[melissa.bird@ato.gov.au](mailto:melissa.bird@ato.gov.au)**

**Telephone:** **(02) 6058 7735**

**Facsimile:** **(02) 6058 7661**

**Address:** **Australian Taxation Office  
GPO Box 9977  
Albury NSW 2640**

## References

*Previous draft:*

Not previously issued as a draft

*Related Rulings/Determinations:*

TR 2006/10; TR 2011/5; TD 2014/D3;  
TD 2014/D4; TD 2014/D5; TD 2014/D6

*Subject references:*

- calculation of the allocable cost amount
- CGT cost base
- consolidation
- goodwill
- tax assessments
- tax cost setting amount

*Legislative references:*

- ITAA 1936 6(1)
- ITAA 1997 8-1
- ITAA 1997 102-5
- ITAA 1997 102-5(1)
- ITAA 1997 102-20
- ITAA 1997 104-25
- ITAA 1997 701-55(5)
- ITAA 1997 701-55(6) disregarding amendments to that Act made by Division 1 of Part 1 and Division 2 of Part 11 of Schedule 5 to the Tax Laws

Amendment (2010 Measures No. 1)  
Act 2010 and by Schedule 3 to Tax Laws  
Amendment (2012 Measures No. 2)  
Act 2012

- ITAA 1997 701-63(2) as amended by Part 1 of Schedule 3 to Tax Laws  
Amendment (2012 Measures No. 2)  
Act 2012
- ITAA 1997 701-63(3)(c) as amended by Part 1 of Schedule 3 to Tax Laws  
Amendment (2012 Measures No. 2)  
Act 2012
- TAA 1953 14ZV
- Tax Laws Amendment (2012 Measures No.2) Act 2012 Sch 3 Pt 4 Item 49
- Tax Laws Amendment (2012 Measures No.2) Act 2012 Sch 3 Pt 4 Subitem 50(1)
- Tax Laws Amendment (2012 Measures No.2) Act 2012 Sch 3 Pt 4 Subitem 50(2)
- Tax Laws Amendment (2012 Measures No.2) Act 2012 Sch 3 Pt 4 Subitem 50(3)
- Tax Laws Amendment (2012 Measures No.2) Act 2012 Sch 3 Pt 4 Subitem 50(4)
- Tax Laws Amendment (2012 Measures No.2) Act 2012 Sch 3 Pt 4 Subitem 50(5)

ATO references

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|---------------|---|
| NO:           | 1-52MHROE   |
| ISSN:         | 1038-8982   |
| ATOlaw topic: | Income Tax ~~ Consolidation ~~ assets<br>Income Tax ~~ Consolidation ~~ capital gains tax<br>Income Tax ~~ Consolidation ~~ tax cost setting amount |

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