


***TD 2005/48 - Income tax: consolidation: in applying the formula in subsection 707-325(3) of the Income Tax (Transitional Provisions) Act 1997 to more than one real loss-maker in relation to the same value donor, does the amount of the 'value donor's modified market value at initial transfer time' remain unchanged?***

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## Taxation Determination

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Income tax: consolidation: in applying the formula in subsection 707-325(3) of the *Income Tax (Transitional Provisions) Act 1997* to more than one real loss-maker in relation to the same value donor, does the amount of the 'value donor's modified market value at initial transfer time' remain unchanged?

### **Preamble**

The number, subject heading, date of effect and paragraph 1 of this document are a 'public ruling' for the purposes of Part IVAAA of the **Taxation Administration Act 1953** and are legally binding on the Commissioner.

1. Yes. In applying the formula in subsection 707-325(3) of the *Income Tax (Transitional Provisions) Act 1997* (IT(TP)A 1997) to more than one real loss-maker in relation to the same value donor, the value donor's modified market value<sup>1</sup> at the initial transfer time remains unchanged.
2. Subdivision 707-C of the IT(TP)A 1997 contains the value donor rules. These rules allow the available fraction<sup>2</sup> for a bundle of losses<sup>3</sup> transferred from an entity ('the real loss-maker'), under Subdivision 707-A of the *Income Tax Assessment Act 1997* (ITAA 1997), to be worked out as if an amount of the modified market value of another entity ('the value donor') were added to the modified market value of the real loss-maker.

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<sup>1</sup> Within the meaning of section 707-325 of the ITAA 1997.

<sup>2</sup> Within the meaning of section 707-320 of the ITAA 1997.

<sup>3</sup> Within the meaning of section 707-315 of the ITAA 1997.

3. Subsection 707-325(3) of the IT(TP)A 1997 states:

Work out the available fraction for the bundle of losses as if there were added to the modified market value of the real loss-maker at the initial transfer time the amount worked out using the formula:

$$\text{Value donor's modified market value at initial transfer time} \times \text{Percentage chosen by transferee} \times \frac{\text{Total of real loss-maker's Division 170 losses in bundle}}{\text{Total of real loss-maker's non-foreign losses in bundle}}$$

**Note:** The amount worked out using the formula will be nil if the value donor's modified market value at the initial transfer time is nil. Even if the amount is nil, section 707-327 may treat losses transferred by the value donor to the transferee as if they were included in the bundle of losses transferred by the real loss-maker to the transferee.

4. The first element of the formula in subsection 707-325(3) of the IT(TP)A 1997 is the value donor's modified market value at the initial transfer time. Paragraph 707-325(1)(b) of the IT(TP)A 1997 provides that one of the conditions to be satisfied in respect of a 'value donation' is that both the real loss-maker and the value donor became members of the consolidated group at the time that the consolidated group was formed – this is the initial transfer time in respect of the bundle of losses that was transferred from the real loss-maker.<sup>4</sup> The initial transfer time, as mentioned in the formula, is therefore the time that the bundle of losses (transferred from the real loss-maker) came into existence (which is also the time that the consolidated group was formed).

5. Subsection 707-325(5) of the IT(TP)A 1997 provides that the transferee<sup>5</sup> may choose to use a fixed percentage (that is, the second element of the formula in subsection 707-325(3) of the IT(TP)A 1997) of the value donor's modified market value to work out the available fraction in respect of the bundle of losses transferred from the real loss-maker. The percentage chosen must be greater than 0% but cannot exceed 100%.

6. Further, subsection 707-325(7) of the IT(TP)A 1997 provides that if subsection 707-325(3) of the IT(TP)A 1997 applies more than once in relation to the same value donor but in respect of different real loss-makers, the sum of the amounts of modified market value taken to be 'donated' (as a result of the separate applications of the formula) cannot exceed the modified market value of the value donor at the initial transfer time.

7. Subsection 707-325(8) of the IT(TP)A 1997 provides that in working out the available fraction in respect of a bundle of losses transferred from the value donor, the modified market value of the value donor is reduced by the amount worked out under subsection 707-325(3) of the IT(TP)A 1997.

8. Where the formula in subsection 707-325(3) of the IT(TP)A 1997 is applied more than once in relation to the same value donor, the first element of the formula will be the value donor's modified market value at the initial transfer time and this amount will remain unchanged.

<sup>4</sup> Within the meaning of subsection 707-315(1) of the ITAA 1997.

<sup>5</sup> The transferee mentioned in subsection 707-325(1) of the IT(TP)A 1997 will generally be the head company of a consolidated or MEC (multiple entry consolidated) group.

9. If the first element in the formula in subsection 707-325(3) of the IT(TP)A 1997 was to be reduced after each application of the formula in relation to the same value donor, then subsections 707-325(7) and 707-325(8) of the IT(TP)A 1997 would be unnecessary. As subsection 707-325(5) of the IT(TP)A 1997 provides that the fixed percentage chosen cannot exceed 100%, it would not be possible for the sum of the amounts of modified market value 'donated', as a result of applications of the formula, to exceed the value donor's modified market value at the initial transfer time (which is what is prohibited by subsection 707-325(7)). Also, there would be no need for subsection 707-325(8) if the modified market value of a value donor was decreased by applications of the formula in subsection 707-325(3).

10. Accordingly, when the formula in subsection 707-325(3) of the IT(TP)A 1997 is applied more than once to different real loss-makers in relation to the same value donor, the first element of the formula remains unchanged.

### **Example**

11. *Head Co forms a consolidated group on 1 July 2003. Loss Co and Donor Co are both subsidiary members at the time that the consolidated group is formed.*

12. *Losses are transferred, under Subdivision 707-A of the ITAA 1997, from Head Co and Loss Co to Head Co (as the head company of the consolidated group) at the time the group forms (the initial transfer time). Head Co chooses (as the remaining conditions in subsections 707-325(1) and 707-325(2) of the IT(TP)A 1997 are satisfied) for Donor Co to be a value donor in respect of working out the available fractions for both the bundle of losses transferred from Head Co and the bundle of losses transferred from Loss Co.*

13. *The details of the bundles of losses transferred from Head Co and Loss Co are as follows:*

<i>Loss Transferred from</i>	<i>Details of Loss transferred</i>	<i>Division 170 loss<sup>6</sup> in respect of Donor Co?</i>	<i>Total of non-foreign losses<sup>7</sup> in bundle</i>
<i>Head Co</i>	<i>Tax loss \$1,000 2000-2001 income year</i>	<i>No</i>	
<i>Head Co</i>	<i>Tax loss \$1,000 2001-2002 income year</i>	<i>Yes</i>	<i>\$2,000 (i.e. \$1,000 + \$1,000)</i>
<i>Loss Co</i>	<i>Tax loss \$500 2000-2001 income year</i>	<i>No</i>	
<i>Loss Co</i>	<i>Tax loss \$500 2001-2002 income year</i>	<i>Yes</i>	<i>\$1,000 (i.e. \$500 + \$500)</i>

<sup>6</sup> Within the meaning of subsection 707-325(4) of the IT(TP)A 1997.

<sup>7</sup> Within the meaning of subsection 707-325(4) of the IT(TP)A 1997.

14. Donor Co's modified market value at the initial transfer time is \$8,000. In applying the formula in subsection 707-325(3) of the IT(TP)A 1997 to Head Co and Loss Co in relation to Donor Co, Head Co chooses (within the limitations prescribed by subsection 707-325(5) of the IT(TP)A 1997):

- to use a fixed percentage of 100% in respect of the available fraction for the bundle of losses transferred from Head Co; and
- to use a fixed percentage of 100% in respect of the available fraction for the bundle of losses transferred from Loss Co.

15. As a result of applying the formula in subsection 707-325(3) of the IT(TP)A 1997, the available fraction for 'bundle Head Co' will be worked out as if there were added to the modified market value of Head Co, the following amount of Donor Co's modified market value:

$$\$8,000 \times 100\% \times 1,000/2,000 = \$4,000$$

16. As a result of applying the formula in subsection 707-325(3) of the IT(TP)A 1997, the available fraction for 'bundle Loss Co' will be worked out as if there were added to the modified market value of Loss Co, the following amount of Donor Co's modified market value:

$$\$8,000 \times 100\% \times 500/1,000 = \$4,000$$

**Outcome if the first element was reduced – when the formula in subsection 707-325(3) of the IT(TP)A 1997 is applied to more than one real loss-maker in relation to the same value donor**

17. If the first element of the formula in subsection 707-325(3) of the IT(TP)A 1997 was to be reduced where there was more than one application of the formula in relation to the same value donor, then the first element of the formula in respect of Loss Co would be \$4,000 (that is, \$8,000 - \$4,000).<sup>8</sup>

18. Therefore, as a result of applying the formula in subsection 707-325(3) of the IT(TP)A 1997, the available fraction for 'bundle Loss Co' would be worked out as if there were added to the modified market value of Loss Co, the following amount of Donor Co's modified market value:

$$\$4,000 \times 100\% \times 500/1,000 = \$2,000$$

19. This would mean that the total amount of modified market value that would be added to the modified market value of Head Co and Loss Co would only be \$6,000 (that is, \$4,000 + \$2,000 respectively).

**Date of effect**

20. This Determination applies to years commencing both before and after its date of issue. However, it does not apply to taxpayers to the extent that it conflicts with the terms of settlement of a dispute agreed to before the date of the Determination (see paragraphs 21 and 22 of Taxation Ruling TR 92/20).

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<sup>8</sup> Which is Donor Co's modified market value at the initial transfer time less the amount 'donated' with respect to 'bundle Head Co'.

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**Commissioner of Taxation**30 November 2005

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*Previous draft:*

TD 2005/D13

*Related Rulings/Determinations:*

TR 92/1

*Subject references:*

- available fraction
- bundle of losses
- consolidation - formation
- consolidation - losses
- head company
- head company of a MEC group
- real loss-maker
- transferred losses
- utilise a loss
- value donor

*Legislative references:*

- ITAA 1997 Subdiv 707-A
- ITAA 1997 707-315
- ITAA 1997 707-315(1)
- ITAA 1997 707-320
- ITAA 1997 707-325
- IT(TP)A 1997 Subdiv 707-C
- IT(TP)A 1997 707-325(1)
- IT(TP)A 1997 707-325(1)(b)
- IT(TP)A 1997 707-325(2)
- IT(TP)A 1997 707-325(3)
- IT(TP)A 1997 707-325(4)
- IT(TP)A 1997 707-325(5)
- IT(TP)A 1997 707-325(7)
- IT(TP)A 1997 707-325(8)
- IT(TP)A 1997 707-327
- TAA 1953 Pt IVA

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*ATO references*

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