


TR 93/4 - Income tax: foreign tax credit system: treatment of worldwide unitary taxes and water's edge unitary taxes

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Taxation Ruling

Income tax: foreign tax credit system: treatment of worldwide unitary taxes and water's edge unitary taxes

other Rulings on this topic

IT 2437 IT 2507

This Ruling, to the extent that it is capable of being a 'public ruling' in terms of Part IVAAA of the Taxation Administration Act 1953, is a public ruling for the purposes of that Part. Taxation Ruling TR 92/1 explains when a Ruling is a public ruling and how it is binding on the Commissioner.

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What this Ruling is about

1. Section 160AF of the *Income Tax Assessment Act 1936* provides, generally, for the granting of a credit against the Australian tax payable on foreign income for the foreign tax paid on that income. Foreign tax is defined in subsection 6AB(2) to exclude, amongst other things, unitary tax. A unitary tax is defined in subsection 6AB(6). This Ruling considers whether the credit for foreign tax paid includes:

- . worldwide unitary tax;
- . water's edge unitary tax; and
- . water's edge election fee.

It also considers whether these taxes or fees are allowable deductions under subsection 51(1). Finally, it explains the records that taxpayers seeking credits or deductions for unitary taxes should retain in support of their claim.

Ruling

2. Subsection 6AB(6) defines a unitary tax as a tax that is:
- . levied under a law of a foreign country on income derived from sources within that country; and
 - . calculated by reference to income, losses, outgoings or assets of the company (or of an associated company that is not a resident company under its law) derived, incurred or situated outside that country.
3. A tax imposed according to the worldwide unitary method falls within the definition of unitary tax in subsection 6AB(6) and is not a

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creditable tax for the purposes of section 160AF. It is not an allowable deduction under subsection 51(1).

4. A water's edge unitary tax is creditable where any factors external to the country levying the tax (foreign income, foreign losses, foreign outgoings and foreign assets) of non-resident companies in the company group are not taken into account in calculating the tax payable.

5. A water's edge election fee is not an income tax and is not creditable. An annual election fee is an allowable deduction under subsection 51(1).

6. Taxpayers who seek a credit or deduction for unitary taxes should retain records of the following in respect of the relevant income tax returns:

- . the precise title of the tax;
- . the country in which it is imposed;
- . the title of the law under which the tax is imposed;
- . whether the tax is levied by a national, state or local authority and the name of the authority; and
- . a description of the nature of the tax and of the way in which the amount of credit has been calculated.

Date of effect

7. This Ruling has both a past and future application (see Taxation Ruling TR 92/20). However, it does not have a past application for a taxpayer who has agreed to a settlement of a dispute to the extent that the Ruling is less favourable than the settlement terms. To the extent that the Ruling is more favourable, it does not have a past application for the taxation years the subject of the settlement.

Explanations

8. Subsection 6AB(2), which specifies the nature of the foreign taxes for which a credit is allowable, specifically excludes a unitary tax.

9. 'Unitary tax' is defined by subsection 6AB(6) to mean a tax that is imposed on a portion of the worldwide income of a company and its associates that is attributed to the taxing State on the basis of the relative level of business activity that occurs in that State. It is not based on the amount of net income derived by the company.

10. The relative level of business activity that occurs in a particular State may be measured as a proportion of the worldwide payroll, property and sales of the company group.

11. Under the worldwide unitary method of taxation, a company's taxable income attributable to a State is determined by allocating to that State a portion of the worldwide income of the company and its commonly controlled affiliates (known as the unitary group). This type of tax is a unitary tax within the meaning of subsection 6AB(6) and a credit is not allowable for that tax.

12. The water's edge method differs from the worldwide unitary method in that it limits the company group to associated companies conducting business in a particular country. In this case, only income, losses, outgoings or assets of the companies within that country are taken into account. The tax does not therefore fall within the definition of unitary tax in subsection 6AB(6). A credit is allowable for that tax.

13. A non-creditable unitary tax is not treated as an allowable deduction under subsection 51(1) as it is not incurred in gaining or producing assessable income or in carrying on a business for the purpose of gaining or producing assessable income.

14. Under the taxation arrangement of some States a company may elect, for a fee, to be taxed in accordance with the water's edge unitary method instead of the worldwide unitary method. The fee as such does not form part of the tax. A 'water's edge election' is made by contract with the Revenue Authorities, generally on the payment of an annual fee. The annual water's edge election fee is deductible under subsection 51(1).

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- ITAA 6AB(2); ITAA 6AB(6); ITAA 160AF