TD 2005/D56 - Income tax: consolidation: when does an injection of capital, as described in paragraph 707-325(4)(a) of the Income Tax Assessment Act 1997, occur where money is received under a publicly listed share offer?

This document has been finalised by TD 2006/18.

Draft Taxation Determination

Income tax: consolidation: when does an injection of capital, as described in paragraph 707-325(4)(a) of the *Income Tax Assessment Act 1997*, occur where money is received under a publicly listed share offer?

Preamble

This document is a draft for industry and professional comment. As such, it represents the preliminary, though considered, views of the Australian Taxation Office. This draft may not be relied on by taxpayers and practitioners as it is not a ruling for the purposes of Part IVAAA of the ***Taxation Administration Act 1953****. It is only final Taxation Determinations that represent authoritative statements by the Australian Taxation Office.*

1. Money received under a publicly listed share offer is considered to be an injection of capital into a company at the time the company issues shares to the applicants. At this time the money is no longer held in trust under section 722 of the *Corporations Act 2001.*

Explanation

2. A publicly listed share offer covers those arrangements whereby there is an issue of shares in a company listed, or to be listed, on a financial market licenced under Part 7.2 of the *Corporations Act 2001*. This Determination covers those publicly listed share offers where additional money is raised, for example by:

- an initial public offering when an existing company is floated and becomes listed on a financial market; or
- an offer of additional shares to existing shareholders of a listed company.

3. The rate of utilisation of losses transferred under Subdivision 707-A of the *Income Tax Assessment Act 1997* (ITAA 1997) to the head company of a consolidated group is limited by reference to the available fraction for the relevant bundle of losses. The initial calculation of an available fraction and its subsequent maintenance can be subject to special rules where there is an event of an injection of capital as described in paragraph 707-325(4)(a) of the ITAA 1997.

4. The timing of an injection of capital event determines when market valuations of a company need to be obtained when applying these special rules in Subdivision 707-C of the ITAA 1997. Specifically:

- An injection of capital prior to joining time may result in a reduction to the modified market value of a joining entity under the rule in subsection 707-325(2) of the ITAA 1997 where that event occurred in the 4 years before that time.[1] In determining the reduction amount (if any), it is necessary to ascertain the increase in the entity's market value immediately after each event because of that event.[2]
- A post-consolidation injection of capital may result in a reduction to existing available fractions for bundles of losses under adjusting event item 4 in the table in subsection 707-320(2) of the ITAA 1997. The market value of the company just before the event must be ascertained as this is a component of the formula in working out the factor to adjust available fractions.

5. Section 722 of the *Corporations Act 2001* applies to certain offers of securities including publicly listed share offers. Under this section, all money received for securities offered under a disclosure document must be held in trust until the issue of securities under the offer or returned to the applicants as soon as practicable. Situations where money may be returned to applicants include where the offer is oversubscribed, or the offer does not proceed for any other reason.

6. Paragraph 12 of Taxation Ruling TR 2004/9: Income tax: consolidation: what is meant by 'injection of capital' in section 707-325 of the Income Tax Assessment Act 1997? states that an injection of capital does not arise until a transaction or act displays all the inter-related characteristics which are listed at paragraph 9 of that Ruling. In the context of a publicly listed share offer, it is considered that these characteristics are present at the issue date which is when the company has use of the funds acquired under the offer. At this time the company will have enhanced net assets, wealth introduced from outside the entity, and its equity accounts will be affected.[3]

7. Where there are multiple offers under a single disclosure document, it is necessary to determine if there is one injection of capital event or multiple events. An initial public offer for example may have one offer for the public and employees and a separate offer for institutional investors. If there is only one issue date in respect of all investors under the offers in the disclosure document, there will be a single injection of capital event. In other cases, there will be multiple events with the timing of each event being dependent on the relevant issue date in respect of that particular class of investors.

---

[1] Subject to section 707-329 of the *Income Tax (Transitional Provisions) Act 1997* which disregards such events where they occur on or before 8 December 2000.

[2] The reduction amount (if any) is worked out under subsection 707-325(3) of the ITAA 1997. It is the lesser of the excess described in paragraph 707-325(2)(b) and the total increase in the market value of the entity that occurred immediately after each event because of the event.

[3] Other characteristics listed in paragraph 9 of TR 2004/9 are also met for a publicly listed share offer, namely the transaction is not related to earnings and profit, capital has been injected by an external party and the transaction is on capital account.

Example

8. *An existing company, Head Co, issued a prospectus in connection with its initial listing on a financial market. The money raised from the issue of shares under this public share offer was used to increase the company's working capital.*

9. *Head Co and its subsidiary members formed a consolidated group on 1 January 2004 and prior year tax losses incurred by Head Co were transferred to itself under Subdivision 707-A of the ITAA 1997. The public share offer was an injection of capital event that occurred within the 4 years before the joining time but after 8 December 2000. It will be taken into account in working out the modified market value of Head Co to derive an available fraction for the bundle of losses under subsection 707-320(1) of the ITAA 1997.*

10. *To ascertain the reduction amount (if any) it will be necessary to establish the time of the event for the purpose of undertaking the market valuation exercise required by paragraph 707-325(3)(b) of the ITAA 1997. The timeline of the offer was as follows:*

15 May 2003	*Public, broker firm and employee offer opens*
29 May 2003	*Institutional offer opens*
18 June 2003	*Public, broker firm and employee offer closes*
25 June 2003	*Institutional offer closes*
2 July 2003	*Final price and basis of allocation of shares announced*
2 July 2003	*Issue of shares to the applicants*
3 July 2003	*First day of trading of shares*
7 July 2003	*Dispatch of refund cheques (shares reduced under allocation)*
10 July 2003	*Dispatch of share statements*

11. *As the issue of shares for institutions and other investors occurred simultaneously under this offer, there was only one injection of capital event. Under section 722 of the Corporations Act 2001, the application money was held in trust until 2 July 2003 when the shares were issued. As this is the day that Head Co obtained access to the trust funds for general use, it will be the time that the injection of capital, as described in paragraph 707-325(4)(a) of the ITAA 1997, will be taken to have occurred. Market valuations will be required in respect of this date to ascertain the increase in market value that occurred because of that event.*

Date of Effect

12. 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 21 and 22 of Taxation Ruling TR 92/20).

Your comments

13. We invite you to comment on this draft Taxation Determination. Please forward your comments to the contact officer by the due date. (Note: The Tax Office prepares a compendium of comments for the consideration of the relevant Rulings Panel. The Tax Office may use a sanitised version (names and identifying information removed) of the compendium in providing its responses to persons providing comments. Please advise if you do not want your comments included in a sanitised compendium.)

Due date:	**3 February 2006**
Contact officer:	**Alan Macpherson**
E-mail address:	**alan.macpherson@ato.gov.au**
Telephone:	**(02) 9374 1826**
Facsimile:	**(02) 9374 1629**
Address:	**Australian Taxation Office** **PO Box 1216** **Hurstville NSW 2220**

Commissioner of Taxation
21 December 2005

Previous draft:
Not previously issued as a draft

Related Rulings/Determinations:
TR 92/20; TR 2004/9

Subject references:
- acquisition of securities
- acquisition of shares
- allotment and issue of securities
- available fraction
- bundle of losses
- capital account
- consolidation
- consolidation – event
- consolidation – losses
- consolidation – market valuations
- consolidation – market value
- corporations law
- injection of capital
- issued capital
- modified market value
- transferred losses
- utilise a loss

Legislative references:
- Corporations Act 2001 722
- Corporations Act 2001 Pt 7.2
- TAA 1953 Pt IVAAA
- ITAA 1997 Subdiv 707-A
- ITAA 1997 Subdiv 707-C
- ITAA 1997 707-320(1)
- ITAA 1997 707-320(2)
- ITAA 1997 707-325(2)
- ITAA 1997 707-325(2)(b)
- ITAA 1997 707-325(3)
- ITAA 1997 707-325(3)(b)
- ITAA 1997 707-325(4)(a)
- IT(TP)A 1997 707-329

ATO references
NO: 2005/16916
ISSN: 1038-8982
ATOlaw topic: Income Tax ~~ Consolidation ~~ losses
Income Tax ~~ Consolidation ~~ market value