



TD 2001/17 - Income tax: capital gains: if a company transferred a net capital loss under Subdivision 170-B of the Income Tax Assessment Act 1997 :(a) when do the adjustments required by section 170-175 or 170-180 to the cost base and reduced cost base of a group company's interest in the loss company or the gain company take effect ; and (b) what happens if a subvention payment (loss company) or a tax benefit (gain company) that would otherwise be taken into account in determining the amount of any adjustment, is no longer reflected in the market value of an interest at the time a CGT event happens to it because the subvention payment or tax benefit has been distributed as a dividend?

 This cover sheet is provided for information only. It does not form part of *TD 2001/17 - Income tax: capital gains: if a company transferred a net capital loss under Subdivision 170-B of the Income Tax Assessment Act 1997 :(a) when do the adjustments required by section 170-175 or 170-180 to the cost base and reduced cost base of a group company's interest in the loss company or the gain company take effect ; and (b) what happens if a subvention payment (loss company) or a tax benefit (gain company) that would otherwise be taken into account in determining the amount of any adjustment, is no longer reflected in the market value of an interest at the time a CGT event happens to it because the subvention payment or tax benefit has been distributed as a dividend?*

 This document has changed over time. This is a consolidated version of the ruling which was published on 4 July 2001

Taxation Determination

Income tax: capital gains: if a company transferred a net capital loss under Subdivision 170-B of the *Income Tax Assessment Act 1997*:

- (a) when do the adjustments required by section 170-175 or 170-180 to the cost base and reduced cost base of a group company's interest in the loss company or the gain company take effect; and
- (b) what happens if a subvention payment (loss company) or a tax benefit (gain company) that would otherwise be taken into account in determining the amount of any adjustment, is no longer reflected in the market value of an interest at the time a CGT event happens to it because the subvention payment or tax benefit has been distributed as a dividend?

Preamble

*The number, subject heading, date of effect and paragraphs 1 and 3 to 12 of this Taxation Determination are a 'public ruling' for the purposes of Part IVAAA of the **Taxation Administration Act 1953** and are legally binding on the Commissioner. The remainder of the Determination is administratively binding on the Commissioner. Taxation Rulings TR 92/1 and TR 97/16 together explain how a Determination is legally or administratively binding.*

Date of Effect

This Determination applies only to net capital losses transferred before 22 February 1999 but may have implications for years commencing both before and after its date of issue. However, this Determination 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).

(a) Time adjustments to cost base and reduced cost base take effect

1. Adjustments to the cost base and reduced cost base (both referred to as ‘relevant cost base’ in this Determination) of a group company’s direct or indirect interest in the loss or gain company after the transfer of a net capital loss take effect (for example for indexation purposes) at the earlier of immediately before a CGT event happens to the interest and the end of the application year (that is, the income year of the gain company for which the amount is transferred: subsection 170-115(1) of the *Income Tax Assessment Act 1997* (‘the 1997 Act’). The fact that the adjustments take effect at this time does not mean they must actually be calculated and made at this time. For example, it will not be possible to determine until immediately before a CGT event happens in respect of an interest in the loss company whether the value of a subvention payment received by the loss company for the transferred net capital loss can be taken into account in calculating the amount of a reduction to the relevant cost base of an interest in the loss company (see paragraph 5 below).

Note 1:

2. Sections 170-175 and 170-180 of the 1997 Act – which applied to transfers of net capital losses within wholly-owned groups of companies before 22 February 1999 – have been repealed and do not apply to net capital losses transferred on or after that date. Subdivision 170-C of the 1997 Act applies to both transfers of tax losses and transfers of net capital losses within wholly-owned groups of companies from 22 February 1999. Reference should be made to the specific provisions of that Subdivision for the adjustment rules that apply in relation to losses transferred from 22 February 1999.

Note 2:

3. No adjustment is required to a group company interest in a loss company if all or part of the transferred net capital loss could not be reflected in a capital loss or capital gain made on the interest. For example, this may be relevant to an interest that did not exist before the end of the application year.

Note 3:

4. As to the transfer limitation in subsections 170-145(2) to 170-145(4) of the 1997 Act for a particular net capital loss transfer, these subsections are applied to the relevant cost base of the share or debt interest before any adjustment required by section 170-175 of the 1997 Act in respect of that transfer takes effect. However, adjustments relating to prior net capital loss transfers (if any) must be taken into account when applying the limitation in respect of that transfer.

(b) Distribution of subvention payment or tax benefit

5. An adjustment made to the relevant cost base may have regard to an amount representing:

- (a) a **subvention payment** in relation to an interest in the loss company (section 170-175 of the 1997 Act); or
- (b) a **tax benefit** arising from the transferred loss in relation to an interest in the gain company (section 170-180 of the 1997 Act);

except (as set out in paragraphs 7 and 8) to the extent that the amount is distributed as a dividend for tax purposes and is no longer reflected in the market value of the interest at the time a CGT event happens to it.

Note 4:

6. If a share is cancelled on dissolution or deregistration of a company, then to the extent the distributed amount referred to in paragraph 5 is included in the capital proceeds for the cancellation,

subsections 118-20(1) and 118-20(1A) of the 1997 Act would reduce any capital gain arising on the cancellation.

7. If:
- (a) a CGT event happens to an interest;
 - (b) a subvention payment or a tax benefit would otherwise be taken into account in determining the amount of an adjustment required by section 170-175 or 170-180 of the 1997 Act; and
 - (c) all or part of the increase in the value of the interest attributable to the subvention payment or tax benefit is not reflected in the market value of the interest at the time of the CGT event because the subvention payment or tax benefit has been previously distributed (in whole or in part) as a dividend;

the distributed amount is not taken into account in making the adjustment.

8. We accept that an amount referable to all or part of a subvention payment or tax benefit has **not** previously been distributed as a dividend, provided the company can do either of the following:

- Demonstrate that the subvention payment or tax benefit (or part thereof) has **not** been distributed as a dividend for tax purposes.
- Point to an amount of undistributed profit in its accounts equal to the whole or part of the subvention payment or tax benefit. If more than one subvention payment has been made (or tax benefit has arisen) then an assertion that more than one amount has not been distributed requires identification of the sum of the relevant amounts. In either case, however, strict tracing of a subvention payment or tax benefit to a particular undistributed amount is not required.

Note 5:

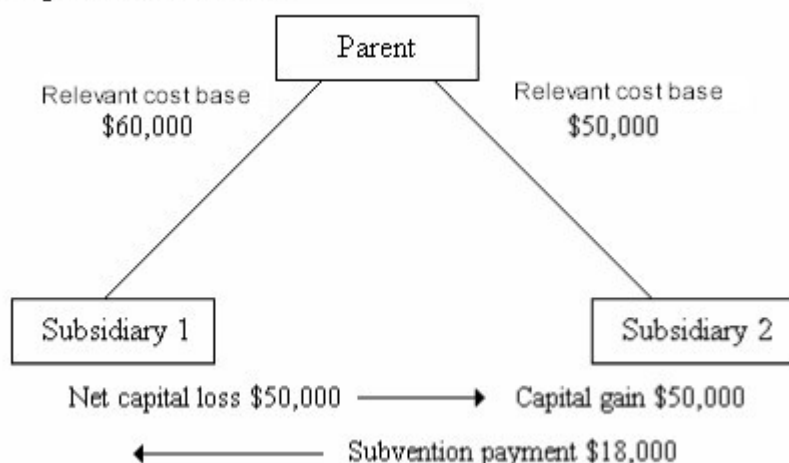
9. Many factors bear on whether a subvention payment can actually be paid as a dividend (for example whether it represents a distributable profit for Corporations Law purposes).

10. Taxpayers may apply the approach set out in this Taxation Determination to adjustments under section 160ZP of the *Income Tax Assessment Act 1936* ('the 1936 Act') subject to the statutory limits in section 170 of the 1936 Act.

11. In this Taxation Determination:

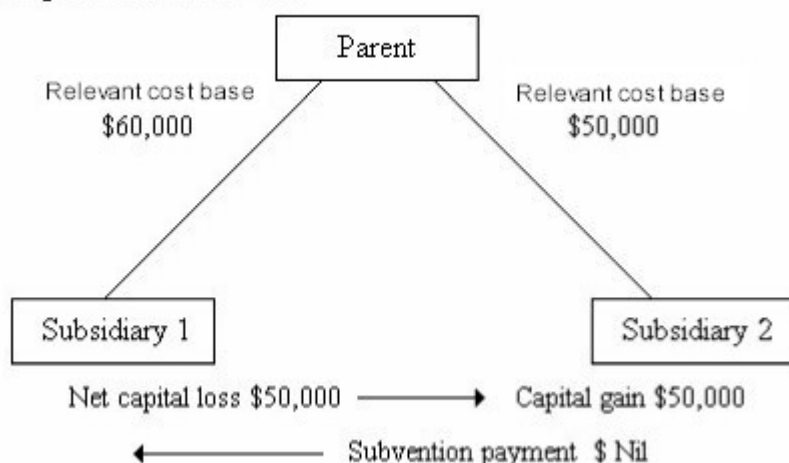
- (a) The term 'subvention payment' refers to a sum paid by a gain company to a loss company for a transfer of a loss.
- (b) The term 'tax benefit' refers to the increase in the market value of the gain company that results from the amount of loss transferred. There is no increase if a subvention payment equal to the tax benefit of the loss transferred is made by the gain company.

12. This Determination replaces Taxation Determination TD 94/90, which is withdrawn from the date of this Determination. To the extent the Determination is more favourable than TD 94/90 it has both a past and future application (subject again to the statutory limits in section 170 of the 1936 Act).

Example 1: section 170 - 175

13. After 19 September 1985, Parent capitalised Subsidiary 1 with \$60,000 and Subsidiary 2 with \$50,000. Subsidiary 1 purchased an asset for \$60,000, which later declined in value and was sold for \$10,000. Subsidiary 1 made a capital loss of \$50,000, which became a net capital loss for the 1997-98 year of income. During that year, Subsidiary 2 made a capital gain of \$50,000 on the sale of an asset and an agreement was made whereby Subsidiary 1 transferred the net capital loss of \$50,000 under Subdivision 170-B to Subsidiary 2. A subvention payment, based on a 36% corporate tax rate, of \$18,000 was made for the net capital loss transferred.

14. Parent later sells its shares in Subsidiary 1 for \$28,000. If Parent can show that, immediately before that time, it has received no dividend from Subsidiary 1 since the loss transfer, or Parent can point to an undistributed profit amount of \$18,000 in Subsidiary 1 (again, immediately before the sale), it would be appropriate to reduce the relevant cost bases of Parent's shares in Subsidiary 1 by \$32,000 (i.e., from \$60,000 to \$28,000). The adjustments would take effect at the end of the application year.

Example 2: section 170 - 180

15. Assume the same facts as for Example 1, except that Subsidiary 2 makes no subvention payment for the transferred net capital loss. If Parent later sells its shares in Subsidiary 2 and, immediately before that time, Parent can show it has received no dividend from Subsidiary 2 since the loss transfer, or can point to \$18,000 undistributed profits in Subsidiary 2, an increase of \$18,000 in the relevant cost bases of its shares in Subsidiary 2 would be appropriate. The increase would take effect at the end of the application year. Indexation, if available, would apply from that time.

16. *If, for example, the entire gain of \$50,000 were distributed before Parent sold its shares in Subsidiary 2, and Subsidiary 2 has no other distributable profits immediately before the shares are sold, no increase to the relevant cost bases of the shares would be made.*

Note 6:

17. *On the facts above, it would also be appropriate in terms of section 170-175 of the 1997 Act for Parent to reduce the relevant cost bases of its shares in Subsidiary 1 by \$50,000 with effect from the end of the application year. The transfer limitation in subsections 170-145(2) to 170-145(4) of the 1997 Act would be applied to the level of relevant cost base before this adjustment assuming there are no outstanding adjustments from previous loss transfers. As the relevant cost base of \$60,000 exceeds the transfer amount of \$50,000, no restriction is imposed by these subsections.*

Commissioner of Taxation4 July 2001

Previously released:

Previously issued as TD 1999/D31 (withdrawn on 2 July 1999) and TD 1999/D33

Related Rulings/Determinations:

TD 2001/16

Subject references:

- cost base
- cost base adjustment
- distribution
- dividend
- gain company
- loss company
- loss transfer
- net capital loss
- reduced cost base
- subvention payment
- tax benefit
- transfer of loss

Legislative references:

- ITAA 1936 160ZP
- ITAA 1936 170
- ITAA 1997 118-20(1)
- ITAA 1997 118-20(1A)
- ITAA 1997 Subdiv 170-B
- ITAA 1997 170-115(1)
- ITAA 1997 170-145(2)
- ITAA 1997 170-145(3)
- ITAA 1997 170-145(4)
- ITAA 1997 170-175
- ITAA 1997 170-180
- ITAA 1997 Subdiv 170-C

ATO references:

NO: 99/8922
FOI: I 1023505
ISSN: 1038-8982