Worked example

Amount of transferred losses that can be utilised – application of paragraph 36-17(5)(a)

Description

This example illustrates the application of the restriction in paragraph 36-17(5)(a) of the *Income Tax Assessment Act 1997* (ITAA 1997) to a choice made by a head company to deduct a transferred tax loss against its taxable income.

Note

For more information about:

- loss utilisation and franking offsets → 'Amount of transferred losses that can be utilised – franking offsets', C3-4-415
- the restriction in paragraph 36-17(5)(b) → 'Amount of transferred losses that can be utilised – application of paragraph 36-17(5)(b)', C3-4-417.

Commentary

Amendments to Division 36 of the ITAA 1997 enable corporate tax entities to choose the amount of prior year tax losses they wish to deduct in a later year of income, subject to certain restrictions → section 36-17. Also, a current year tax loss that would otherwise be 'wasted' against franked dividend income can be carried forward to a later year of income. The quantum of the tax loss is determined by reference to the amount of excess franking offsets[1] for the income year → section 36-55.

Where a corporate tax entity chooses to deduct a prior year tax loss against its taxable income of a later income year, the restriction in paragraph 36-17(5)(a) applies. This paragraph states that if a corporate tax entity would have excess franking offsets in the later income year – disregarding the earlier year tax loss and any other tax losses – the entity must choose a nil amount of the tax loss.

This is so regardless of the limit for utilisation of a transferred tax loss as worked out under the available fraction method.

Example

Facts

The head company of a consolidated group is working out its taxable income for the income year ended 30 June 2004.

The group's capital gains for the income year are $1,000. There is a group net capital loss of $200 carried forward from the 2003 income year.

[1] An amount of excess franking offsets is worked out in accordance with subsection 36-55(1).

The group's 'other assessable income' is $1,500. The group incurred allowable deductions of $1,800 in relation to that income.

The other assessable income includes a franked distribution of $630 plus the franking credit on the distribution of $270.[2]

The group's transferred losses are as shown in table 1.

Table 1: Transferred losses and available fractions

Loss bundle	Available fraction	Unused transferred losses
Bundle A	0.500	$300 net capital loss $250 tax loss (not film)

Transferred losses are to be utilised in accordance with the available fraction method.

The head company satisfies the recoupment tests for the utilisation of all losses in the 2004 income year and seeks to utilise losses to the maximum extent possible.

Calculation

A. Apply the three-step available fraction method

Step 1: Work out the categories of group income or gains – subsection 707-310(3)

Table 2: Categories of group income or gains (step 1)

Category of income or gains	Gross amount ($)	*Less*: other allowable deductions/ reductions ($)	*Less*: group/ concessional losses of the relevant sort ($)	*Less*: transferee's grossed-up franking offset amount (applies only for item 6) ($)	Income/gains available for the bundle ($)
Capital gains	1,000	–	200	–	800
Other assessable income	1,500	1,500*	–	Nil**	Nil

*Although allowable deductions are $1,800, only $1,500 needs to be deducted as this reduces the other assessable income category to nil.

**This amount would normally be determined as per paragraph 707-310(3A)(c), i.e. 1/0.3 x $270 = $900. However it is nil in this example as the other assessable income category has been reduced to nil by allowable deductions.

[2] Section 207-20.

Step 2: Calculate the fraction of the income/gains that is attributable to the bundle – subsection 707-310(3)

Table 3: Fraction of income/gains attributable to each bundle (step 2)

Categories of income or gains	Loss bundle	Step 1 amount ($)	*Multiplied by*: available fraction (AF)	AF amount for the bundle ($)
Capital gains	Bundle A	800	0.500	400
Other assessable income	Bundle A	Nil	0.500	Nil

Step 3: Work out a notional taxable income for the bundle – subsection 707-310(2)

Table 4: Net capital gain (step 3)

Capital gains	$	Losses applied	$
Capital gains	400	Transferred net capital loss	300
Total	**400**	**Total**	**300**

The notional net capital gain is $100 ($400 – $300).

Table 5: Taxable income (step 3)

Assessable income	$	Deductions	$
Net capital gain	100	Transferred tax loss (not film)	100
Other assessable income	0		
Total	**100**	**Total**	**100**

The notional taxable income is $0 ($100 – $100).

The limits for utilisation of the transferred losses in bundle A by the head company when it determines its actual taxable income for the 2004 income year are as follows:

- transferred net capital loss $300
- transferred tax loss $100.

B. Determine the head company's actual taxable income

Table 6: Net capital gain

Capital gains	$	Losses applied	$
Capital gains	1,000	Group capital loss	200
		Transferred net capital loss	300
Total	**1,000**	**Total**	**500**

The group's net capital gain is $500 ($1,000 – $500).

Table 7: Taxable income

Assessable income	$	Deductions	$
Net capital gain	500	Deductions	1,800
Other assessable income	1,500	Transferred tax loss (not film)	0*
Total	**2,000**	**Total**	**1,800**

* In step 3 it is determined that the limit for utilisation of the transferred tax loss in bundle A by the head company when it determines its actual taxable income for the 2004 income year is $100. However, paragraph 36-17(5)(a) prevents the head company from deducting any of this amount. This is so because when disregarding the transferred tax loss, the head company would have an amount of excess franking offsets for the income year of $210 (as shown in table 8). Therefore, the head company must choose a nil amount of the transferred tax loss when working out its taxable income for the income year.

The group's taxable income is $200 ($2,000 – $1,800).

The amount of tax payable for the 2004 income year is shown in table 8.

Table 8: Tax payable and excess franking offset

Taxable income ($)	Tax on taxable income (30% corp. tax rate) ($)	*Less*: tax offsets ($)	Tax payable ($)	Excess franking offsets* ($)
200	60	270	Nil	210 (270 – 60)

* In accordance with subsection 36-55(1).

Applying the method statement in subsection 36-55(2), the amount of excess franking offsets – that is, $210 – generates a tax loss of $700, as shown in table 9.

Table 9: Converting excess franking offsets into tax loss

Steps in subsection 36-55(2)	$
Step 1. Work out the amount (if any) that would have been the entity's tax loss for the year under section 36-10 (ignoring net exempt income).	0
Step 2. Divide the amount of excess franking offsets by the corporate tax rate of 30%.	700 (210/0.3)
Step 3. Add the results of steps 1 and 2.	700 (700 + 0)
Step 4. Reduce step 3 result by net exempt income (if any). This is the group tax loss for the 2004 income year.	700 (700 – 0)

Carry-forward losses for the 2004 income year are shown in table 10.

Table 10: Carry-forward losses

Sort	Year incurred	Bundle	$
Group tax loss	2004	–	700
Transferred net capital loss	2003	Bundle A	0 (300 – 300)
Transferred tax loss	2003	Bundle A	250 (250 – 0)

References

Income Tax Assessment Act 1997, section 707-310; as amended by *Taxation Laws Amendment Act (No. 5) 2003* (No. 142 of 2003), Schedule 8

Income Tax Assessment Act 1997, Division 36; as amended by *Taxation Laws Amendment Act (No. 5) 2003* (No. 142 of 2003), Schedule 8:

- section 36-17
- section 36-55

Income Tax Assessment Act 1997, section 207-20

Explanatory Memorandum to Taxation Laws Amendment Bill (No. 5) 2003, Chapter 5

Revision history

Section C3-4-416 first published 10 December 2004.

Proposed changes to consolidation

Proposed changes to consolidation announced by the Government are not incorporated into the *Consolidation reference manual* until they become law. In the interim, information about such changes can be viewed at:

- **http://assistant.treasurer.gov.au** (Assistant Treasurer's press releases)
- **www.treasury.gov.au** (Treasury papers on refinements to the consolidation regime).