



***TD 2004/67 - Income tax: consolidation: capital gains: does the determination of a capital loss under section 104-530 (CGT event L7) of the Income Tax Assessment Act 1997 require a full reconstruction of the allocable cost amount in relation to the relevant liability?***

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 This document has changed over time. This is a consolidated version of the ruling which was published on 22 June 2011



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## Taxation Determination

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Income tax: consolidation: capital gains: does the determination of a capital loss under section 104-530 (CGT event L7) of the *Income Tax Assessment Act 1997* require a full reconstruction of the allocable cost amount in relation to the relevant liability?

### **Preamble**

*The number, subject heading, date of effect and paragraphs 1 to 9 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.*

**[Note:** *This is a consolidated version of this document. Refer to the ATO Legal Database (<http://law.ato.gov.au>) to check its currency and to view the details of all changes.*]

1. Yes. In order to determine a capital loss under section 104-530 (CGT event L7) of the *Income Tax Assessment Act 1997* (ITAA 1997), a full reconstruction of the allocable cost amount (ACA) is required. This ensures that the full impact of the discharged amount of a liability is reflected in working out the amount of any capital loss.
2. For CGT event L7 to happen to the head company of a consolidated group, the conditions specified in subsection 104-530(3) of the ITAA 1997 must be satisfied for a liability.
3. Paragraphs 104-530(3)(a) and (b) of the ITAA 1997 require that the amount of a liability that was taken into account in working out the ACA for an entity at the time it becomes a member of the consolidated group (the original ACA), is later discharged for a different amount (the realised amount).
4. Further, paragraph 104-530(3)(c) of the ITAA 1997 requires the original ACA to be different to what it would have been (referred to as the true ACA) if the realised amount had been taken into account in working out the ACA. A capital loss will arise if the ACA would have been greater had the realised amount been taken into account in working it out.
5. Paragraph 104-530(3)(c) of the ITAA 1997 does not set out how to determine the true ACA. The existence of the condition in this paragraph however indicates the need for a full reconstruction to arrive at the true ACA. This involves going beyond merely working out the difference in ACA that flows from using the realised amount rather than the amount of the liability taken into account in the original ACA. The true ACA is worked out by substituting the realised amount of the liability for the amount used in the original ACA and

taking into account the changes that would flow from this. This will involve a notional recasting of the statement of financial position.

6. These changes could affect step 2 of the ACA calculation (see sections 705-70 to 705-85 of the ITAA 1997) and subsequent ACA steps (see sections 705-90 to 705-115 of the ITAA 1997). An example is where the realised amount is more than the amount of the liability reflected in the original ACA and there would have been a decrease in the tax payable because of a decrease in the taxable income arising from an increase in the liability. In this case, the reconstructed step 2 amount should reflect the realised amount of the liability and a reduction in the liability to income tax.

7. As well, discharged liabilities, such as provisions for employee entitlements, that are subject to section 705-75 and/or section 705-80 of the ITAA 1997 at the joining time, would be subjected to these provisions again under a full reconstruction in order to work out the true ACA and the capital loss under CGT event L7.

8. The way in which subsections 104-530(4) and 104-530(5) of the ITAA 1997 apply also supports the full reconstruction view. In order to work out the capital loss under CGT event L7, these subsections require the head company to work out the difference between the original ACA and the true ACA, as opposed to merely working out the difference between the amount of the liability taken into account in the original ACA and the realised amount of the liability.

9. In addition, the Explanatory Memorandum to the New Business Tax System (Consolidation and Other Measures) Bill (No. 2) 2002 (the EM) supports the view that a full reconstruction is necessary. This is illustrated by examples 5.4 and 5.5 in paragraphs 5.40 and 5.41 respectively. In both examples, even though no workings are shown, a reconstruction of the step 2 amount, (including the corresponding impact on step 5 and step 6 of the ACA calculation), is required to arrive at the true ACA figures shown. There is also an inference in paragraph 5.41 of the EM that a full reconstruction of the ACA is required. This paragraph notes that the change in the amount of a liability may not affect the amount of the ACA because the ACA calculation '...factors in future tax effects for the liability and, taking those into account, there may be no net change in the ACA'.

10. *[Omitted.]*

## **Date of Effect**

11. This Determination applies to a capital loss under CGT event L7 that arises on or after 1 July 2002 and before 10 February 2010. 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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## **Commissioner of Taxation**

3 November 2004

### *Previous draft:*

TD 2004/D29

### *Related Rulings/Determinations:*

TR 92/20

### *Subject references:*

- accounting liabilities
- CGT event L7
- CGT events
- consolidation
- consolidation – capital gains tax
- consolidation – liabilities

- discharge of liabilities

*Legislative references:*

- TAA 1953 Pt IVAAA
- ITAA 1997 104-530
- ITAA 1997 104-530(3)
- ITAA 1997 104-530(3)(a)
- ITAA 1997 104-530(3)(b)
- ITAA 1997 104-530(3)(c)
- ITAA 1997 104-530(4)
- ITAA 1997 104-530(5)
- ITAA 1997 705-70
- ITAA 1997 705-75
- ITAA 1997 705-75(1)
- ITAA 1997 705-80

- ITAA 1997 705-85
- ITAA 1997 705-90
- ITAA 1997 705-93
- ITAA 1997 705-95
- ITAA 1997 705-100
- ITAA 1997 705-105
- ITAA 1997 705-110
- ITAA 1997 705-115

*Other references:*

- Explanatory Memorandum to the New Business Tax System (Consolidation and Other Measures) Bill (No. 2) 2002

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*ATO references*

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