TD 2005/D24 - Income tax: consolidation: for the purposes of working out step 1 of a consolidated group's exit allocable cost amount in the leaving entity under section 711-25 of the Income Tax Assessment Act 1997, is the terminating value for a CGT asset determined under Subdivision 110-A for assets that have their tax cost set under subsection 701-10(4)?

This document has been finalised by TD 2006/19.

Draft Taxation Determination

Income tax: consolidation: for the purposes of working out step 1 of a consolidated group's exit allocable cost amount in the leaving entity under section 711-25 of the *Income Tax Assessment Act 1997,* is the terminating value for a CGT asset determined under Subdivision 110-A for assets that have their tax cost set under subsection 701-10(4)?

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. Yes. Subsection 711-30(2) of the *Income Tax Assessment Act 1997* (ITAA 1997) requires the terminating value of a CGT asset of a leaving entity for the purposes of section 711-25 of the ITAA 1997 to be worked out in accordance with subsection 705-30(4) of the ITAA 1997. The terminating value of a CGT asset of a leaving entity is equal to the asset's cost base or reduced cost base just before the leaving time.

2. The CGT asset's cost base or reduced cost base is worked out under Subdivisions 110-A and 110-B of the ITAA 1997 respectively. The tax cost that was set for the CGT asset under subsection 701-10(4) when the subsidiary member joined the consolidated group, is what would be the asset's cost base under section 110-25 or the asset's reduced cost base under section 110-55 if a cost base or reduced cost base was worked out at that time.

3. The terminating value of a CGT asset of a leaving entity that had its tax cost set at the joining time under subsection 701-10(4) of the ITAA 1997 will therefore consist of the cost set at the joining time and reflect any adjustments that are made to the cost base or reduced cost base in accordance with Subdivision 110-A or Subdivision 110-B respectively, as well as other related provisions that make adjustments to the cost base or reduced cost base, until just before the asset leaves the consolidated group.

Explanation

4. Where a subsidiary leaves a consolidated group, the tax cost setting amount (TCSA) is worked out under Division 711 of the ITAA 1997. The TCSA for each membership interest in the leaving entity that members of the consolidated group held is worked out under section 711-15.

5. Paragraph 711-15(1)(a) provides that the consolidated group's allocable cost amount (ACA) for the leaving entity is worked out in accordance with section 711-20. In working out the consolidated group's exit ACA (referred to in the provisions as the *'old group's'* ACA) there are a series of steps under section 711-20 which need to be followed.

6. Step 1 of a consolidated group's exit ACA for the leaving entity is worked out under section 711-25 of the ITAA 1997. Subsection 711-25(1) provides:

> For the purposes of step 1 in the table in subsection 711-20(1), the step 1 amount is worked out by adding up the *head company's *terminating values of all the assets that the head company holds at the leaving time because the leaving entity is taken by subsection 701-1(1) (the single entity rule) to be part of the head company.

7. The meaning to be given to terminating value of an asset held by a head company is addressed in section 711-30 of the ITAA 1997. Specifically, subsection 711-30(2) provides that the terminating value of an asset at the leaving time is worked out in a corresponding way to the terminating value calculation under section 705-30 for an asset that the joining entity holds at the joining time.

8. By adapting subsection 705-30(4) of the ITAA 1997 in the required way, the law provides that if an asset of the leaving entity is a CGT asset that is not covered by any of the earlier subsections in section 705-30, the leaving entity's terminating value for the asset will be equal to the asset's cost base just before the leaving time.

9. The meaning of the term 'cost base' in subsection 705-30(4) of the ITAA 1997 is the same as in the CGT cost base rules in Subdivision 110-A. Subsection 711-20(2) extends the reference to the term 'cost base' to include the reduced cost base worked out under Subdivision 110-B of the ITAA 1997:

> If it is necessary to work out whether the *head company makes a capital loss for a *CGT event that happens at or after the leaving time in relation to any of the *membership interests, the old group's allocable cost amount for the leaving entity is instead worked out as if the head company's *terminating value for any asset covered by subsection 705-30(4) (as if it applies for the purposes of section 711-30) were instead equal to the asset's *reduced cost base just before the leaving time.

Therefore, the cost base or reduced cost base of an asset to which subsection 705-30(4) applies will be calculated according to the appropriate Subdivision. The asset's cost base or reduced cost base, and hence its terminating value, will reflect any changes to it in accordance with the provisions that make adjustments to the cost base or reduced cost base as from the joining time.

10. Subsection 110-25(12) of the ITAA 1997 provides that in circumstances where no CGT event happens but it is necessary to work out the cost base:

> …assume, for the purpose only of working out the cost base at the particular time, that such an event [i.e. CGT event] does happen in relation to the asset at or just after that time.

Note 2 of subsection 110-25(12) provides, *inter alia*:

> The assumption that a CGT event happens does not have any consequence beyond that stated.

Example

11. *Sub X is leaving the consolidated group with various assets. It is assumed there will be a capital gain to the head company on disposal of its membership interests.*

12. *One of the assets is land with a commercial building on it, which Sub X owned before joining the consolidated group. The TCSA for the asset at the joining time is $400,000.*

13. *The land is a CGT asset under section 108-5 of the ITAA 1997*.

14. *Head Co incurs legal expenses of $6,000 in order to defend the title to the land in Year 3. These expenses will comprise the fifth element of the cost base under subsection 110-25(6) of the ITAA 1997.*

15. *The cost base of the land is calculated at the leaving time as follows:*

$400,000

$6,000 + cost base is increased under subsection 110-25(6) of the ITAA 1997

$406,000

16. *The cost base as calculated under Subdivision 110-A of the ITAA 1997 is $406,000. Therefore, the terminating value of the asset under subsection 705-30(4) of the ITAA 1997 and Step 1 of the exit ACA under subsection 711-25 of the ITAA 1997 is $406,000.*

Date of effect

17. 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

18. We invite you to comment on this draft Taxation Determination. Please forward your comments to the contact officer by the due date.

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Commissioner of Taxation
20 July 2005

Previous draft:

Not previously issued as a draft

Related Rulings/Determinations:

TR 92/20

Subject references:

- capital gains tax
- CGT cost base
- consolidation
- consolidation – assets
- consolidation – CGT
- consolidation exiting

Legislative references:

- TAA 1953 Pt IVAAA
- ITAA 1997 108-5
- ITAA 1997 Subdiv 110-A
- ITAA 1997 110-25
- ITAA 1997 110-25(6)
- ITAA 1997 110-25(12)
- ITAA 1997 Subdiv 110-B
- ITAA 1997 110-55
- ITAA 1997 701-1(1)
- ITAA 1997 701-10(4)
- ITAA 1997 705-30
- ITAA 1997 705-30(4)
- ITAA 1997 Div 711
- ITAA 1997 711-15
- ITAA 1997 711-15(1)(a)
- ITAA 1997 711-20
- ITAA 1997 711-20(1)
- ITAA 1997 711-20(2)
- ITAA 1997 711-25
- ITAA 1997 711-25(1)
- ITAA 1997 711-30
- ITAA 1997 711-30(2)

ATO references

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