

Tax Brief

2 December 2011

Tax consolidation – fundamental retrospective and prospective changes announced

On 25 November 2011 the Assistant Treasurer issued a press release announcing a range of critically important changes to the tax consolidation regime, some with retrospective application. An associated Board of Taxation (**BoT**) report was simultaneously released.

The significance of this announcement from revenue, policy and technical perspectives cannot be understated.

1 Outline

As foreshadowed in the Assistant Treasurer's initial 30 March 2011 press release, consolidation legislative amendments enacted in June 2010 have subsequently been determined to have a revenue cost far in excess of expectations. Therefore, the amendments announced in this most recent press release primarily seek to significantly reduce the immediate cost of the June 2010 measures, although revenue impact projections are not contained in this release. However, from a go-forward perspective it is also proposed to re-calibrate tax consolidation outcomes – particularly in relation to corporate groups in the service sector.

Importantly, the package also includes proposed retrospective and prospective amendments dealing with interactions between the taxation of financial arrangements (TOFA) provisions and tax consolidations. These TOFA related proposals are also fundamental and may have significant consequences in relation to both (i) corporate acquisitions from the commencement of the TOFA regime and (ii) the calculation of a taxpayer's TOFA transitional balancing adjustment amount.

The 'big picture'

While further details in relation to this package are noted at 3 and 4 below and in the attached tables, the 'big picture' position is broadly as follows.

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- (a) Subject to the normal four-year amended assessment period proposed, clarificatory retrospective changes are to apply to preclude consolidation related deductions that may have been claimed in relation to:
 - customer relationships, know-how and certain accounting intangibles;
 - renewal rights under service type contracts;
 - certain mine improvements that are not depreciating assets.
- (b) Where rulings have been obtained, these retrospective adjustments will not apply.
- (c) Where an entity joined a consolidated group before the initial legislative provisions were passed by Parliament (12 May 2010) and associated deductions were not claimed in assessments issued before 30 March 2011, unfortunately harsher treatment will apply to certain deductions that are now sought to be claimed. In particular, deduction claims relating to rights to future income in respect of services to be performed after the joining time will not be allowed, even though they may have been allowed if deductions had been claimed and assessments had been issued before 30 March 2011.
- (d) For joining times after 30 March 2011 (unless committed before that date), deductions for rights to future income in respect of services to be performed after the joining time will similarly be precluded. Further, in determining various other associated tax impacts it will be necessary to determine what the outcomes would have been if the transaction had instead been undertaken as a business acquisition (rather than an entity acquisition).
- (e) The TOFA related changes will primarily apply (with retrospective application) in relation to TOFA liabilities which are prima facie deductible.

Retrospectivity

The fact that this package contains some proposed retrospective amendments raises equity concerns (with the alternative no doubt being a substantial and unbudgeted revenue cost). These retrospectivity equity concerns follow other announcements in recent months where the Government has foreshadowed that it intends to also use a retrospective legislative approach in relation to aspects of the Petroleum Resources Rent Tax regime and in relation to possible transfer pricing measures.

Key implications

From a very high level perspective, the key implications of the Assistant Treasurer's press release are as follows.

- (a) Revenue: the revenue involved in relation to these proposed legislative adjustments is not stated. However, the BoT report flags that in excess of \$30 billion of deduction claims relate to these issues.

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- (b) Selective retrospectivity: as noted above, for entities that joined consolidated groups before 12 May 2010, these measures will have retrospective application in a manner that primarily focuses on corporate groups that have yet to self-assess the specific benefits of the provisions that are now to be amended. Therefore, in many cases taxpayers who have been more prudent (in that they had sought and were awaiting ATO approval for refund claims by way of objections or private binding ruling requests) will be most directly impacted. Conversely, in respect of the pre-12 May 2010 period the likelihood of taxpayers who have been assessed now having to make further tax payments will be reduced.
- (c) Policy outcomes: the policy thrust of the proposed measures is to significantly limit deductions that can be claimed on the acquisition of a target entity in respect of its valuable assets which represent:
 - expected future services-related income where the relevant services have yet to be provided; or
 - various intangible assets including customer relationships and know-how.
- (d) Technical: albeit in a limited and ad hoc manner, the tax consolidation regime will commence to apply a 'business acquisition' approach, such that certain tax outcomes will now implicitly only be obtained via an entity acquisition if they would have been obtained had the transaction been structured as a direct asset acquisition. However, in some circumstances more restrictive outcomes will now apply on an entity acquisition as compared to a business acquisition.
- (e) Uncertainty: this area has been plagued with uncertainty, firstly in regard to the extremely long gestation period relating to the initial measures enacted in 2010, and then from the Assistant Treasurer's press release on 30 March 2011. It is encouraging to note that it has been stated that the drafting of these measures will be given 'priority' status, because it is only when these amendments are enacted that taxpayers will be able to ascertain their full implications.

2 Background

The following key points summarise the background to this amendment.

- (a) 1 July 2002 commencement: When the consolidation regime commenced on 1 July 2002, the provisions dealing with impacts on underlying assets of an acquired subsidiary focused primarily on 'hard' assets such as trading stock and plant etc, while the policy framework in regard to general 'revenue' type assets (and in particular rights to future income under service type arrangements) was absent.
- (b) December 2005 press release: This technical and policy void regarding more general 'revenue' type assets were considered by the Government

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and addressed in a high level press release issued in December 2005, which stated that the relevant legislative amendments to correct these deficiencies when drafted and enacted would have retrospective application back to 1 July 2002.

- (c) Formulation period: Governments (of both parties) and Treasury did not prioritise these measures, and ultimately it took over four and a half years for the associated legislative amendments to be introduced and passed by the Parliament. In this context, over this period various Exposure Drafts and other materials were released (some only on a limited basis), with the first of such Exposure Drafts being issued in April 2009.
- (d) Enactment: Ultimately the provisions were enacted on 3 June 2010, after being first introduced into Parliament on 10 February 2010 and then subject to some revision while in the Senate. This package of measures included another 21 major consolidation related corrections, a number of which also had retrospective application back to 1 July 2002. In the final Explanatory Memorandum that accompanied the legislation, it was stated that these measures would have a 'substantial but unquantifiable' revenue cost.
- (e) 30 March 2011 press release: As noted above, the Assistant Treasurer ultimately issued a press release on 30 March 2011, stating that these provisions had been determined to have a substantially greater revenue impact than previously anticipated, and requested that the BoT review the position and prepare a report within two months. This BoT report was released simultaneously with the Assistant Treasurer's 25 November 2011 press release.
- (f) Concurrent BoT review: Since June 2009 the BoT has been undertaking a more general post-implementation review of the consolidation regime, with a position paper outlining its preliminary views on a wide range of consolidation issues being released back in October 2010. It is anticipated that the BoT will conclude its work and lodge its report with the Government in the first half of 2012, which may initiative a raft of other consolidation amendments. The Assistant Treasurer's press release foreshadows that the BoT will now review some additional specific consolidation matters (refer 5 below).

3 Proposed general changes

Unfortunately, the attachment to the Assistant Treasurer's press release is complex in its description of the proposed changes and the relevant periods to which they are to apply.

The tables attached to this Tax Brief summarise what is proposed, with the following being only a very high level outline. The TOFA related proposed changes are separately discussed at 4 below.

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As will be apparent, a critical aspect is when the relevant entity joined the consolidated group (or when the arrangement that ultimately led to that event was initially entered into).

Joining time period	Key points
Pre-12 May 2010	<ul style="list-style-type: none"> • Outcomes can vary significantly, depending on when the assessment/amended assessment issued claiming relevant deductions. Where a private ruling has been obtained, tax outcomes will remain unchanged. • Generally, non-deductible goodwill status will be confirmed to apply to customer relationships, know-how and other accounting intangibles. • Outcomes in respect of rights to future income, life and general insurance in-force value, and mine improvements that are not depreciating assets will vary, depending on the date of issue of relevant notices of assessments (including the assessment for the year that includes the joining time, but also the date of assessments for subsequent tax years that may be impacted by the 'tail' of associated deductions or tax losses).
12 May 2010 to 30 March 2011	<ul style="list-style-type: none"> • Where a private ruling from the ATO has been obtained, it will continue to apply without modification. • Generally, the provisions enacted on 3 June 2010 will continue to apply, with the only restrictions being in respect of: <ul style="list-style-type: none"> – customer relationship, know-how and other accounting intangible assets; – right to future income deductions relating to contracts that are required to be renewed, or that can be unilaterally cancelled by the customer; and – mine site improvements that are not depreciating assets. <p>Market valuation clarifications will also apply.</p>
Post-30 March 2011	<ul style="list-style-type: none"> • Deductions in respect of rights to future income will be limited in the scope of the current WIP provisions of s.25-95, being 'work (but not goods) that has been partially performed ... but not yet to a stage where a recoverable debt has arisen'. • In the application of the residual tax outcome provisions of s.701-55(6), impacts will be determined by applying a 'business acquisition' approach.

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Joining time period	Key points
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- Assets that cannot be sold separately by the joining entity (stated to be non-contractual customer relationships, know-how and other accounting intangibles) will be specifically deemed to be goodwill.
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Given the complexity of the announcement, the above is very much a high level summary, with a more detailed outline included in the attachment to this Tax Brief.

Amended assessments and interest/penalties

These retrospective period amendments will only be restricted from applying where the taxpayer has obtained a binding private ruling or written advice under an advance compliance agreement from the ATO, and the taxpayer continues to act in accordance with that ruling/advice. Otherwise, generally the ATO will be able to seek to issue amended assessments within the normal four-year amendment period to disallow deductions claimed that now fall outside the re-defined deductible categories.

Taxpayers still seeking to claim refunds in the light of these proposed amendments will be able to do so within the normal four-year amended assessment period or in an additional two year period from the date of enactment of the proposed provisions. However, in respect of the pre-12 May 2010 period, taxpayers can only seek amendments through the application of these proposed pre-12 May 2010 provisions.

For any resulting amended assessments that increase tax payable in respect of both the pre-12 May 2010 and transitional periods, interest and penalties will not be able to be imposed by the ATO (no such statement is made in relation to amended assessments that relate to the post-30 March 2011 period). For an amended assessment requests by taxpayers that will result in refunds, interest will not be payable relating to the pre-12 May 2010 period changes.

4 Proposed TOFA / Consolidation changes

Even the most enthusiastic tax practitioner may develop a slightly glazed look when the words “TOFA” and “Consolidation” interactions are mentioned. Frequently, the hope is that any such changes are mere “mechanical” or “technical” changes and do not have significant consequences.

Unfortunately, the changes proposed in the press release do not fall into this category. Indeed, although there will be some minor changes, two fundamental changes have been proposed – these relate to:

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- (a) the treatment of certain liabilities (that are TOFA “financial arrangements”) held by an entity that joins a consolidated group – although not clear from the press release, the effect of the proposed change is likely to lead to the acquiring group not obtaining future deductions in relation to these liabilities. The liabilities affected appear to be all TOFA financial arrangements other than liabilities relating to repayments of principal – as such, although the face value of a loan should not be treated as a liability for these purposes, any further “loss” reflecting movements in the fair value of the loan will be caught. The provisions will also cover other financial arrangements with “out-of-the-money” derivatives being the main example. This is a fundamental change from current law and may have significant implications in relation to the pricing of corporate acquisitions; and
- (b) for taxpayers that have elected to “un-grandfather” their existing TOFA financial arrangements to change the manner in which they are required to calculate their transitional balancing adjustment amount in relation to financial arrangements that they have previously acquired as part of a corporate acquisition.

Each of these proposed changes is considered in further detail below.

Liabilities

Under current law, if an entity that joins a consolidated group (a joining entity) has liabilities then, in broad terms, there will be an increase in the ACA (Step 2) to reflect the liability and assuming that the liability is discharged at a later point in time, the head company should get a deduction when the liability is discharged (assuming the amount is otherwise deductible). This has been the position since the consolidation regime was introduced.

As a result of recent acquisitions (and the size of the liabilities in a GFC environment), the ATO formed the view that this result is inconsistent with principles of “economic taxation”. This is essentially on the basis that it provides the taxpayer with a double benefit being the increased ACA (albeit reduced by 30%) and the future deduction. Although this issue has existed since the consolidation provisions were introduced it has suddenly become “news” as a result of the size of the numbers involved in a GFC environment. Further, although the issue applies to all liabilities, the focus has been on liabilities that are “financial arrangements”. Again, this distinction appears to be driven by the fact that this is where the big numbers exist.

This fundamental issue is not once referred to in the Assistant Treasurer’s press release (it is alluded to very briefly in the BoT report). The press release simply states that for financial arrangements that are liabilities, the head company will be deemed to have assumed the liability for its accounting value at the joining time. Although not discussed in the press release, the purpose of the amendment is almost certainly to deny the head company the future deductions (it is difficult to be absolutely certain about this without seeing the further changes that will also be required).

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There are a myriad of further issues and questions that arise in relation to the proposed change (which are beyond the scope of this tax brief). However, a few initial comments:

- (a) the changes may lead to the loss of significant deductions in relation to liabilities acquired as part of a corporate acquisition. The loss of these deductions may affect the pricing of corporate acquisitions;
- (b) if the current position is regarded as uneconomical, why not deny the Step 2 ACA uplift rather than the future deduction? Presumably, the answer to this is simply dollars as the future deduction is potentially of much greater significance than the increased ACA (which may be pushed into a variety of assets);
- (c) whether “economic taxation” is truly achieved may depend on the tax position of the joining entity prior to it being acquired (for instance, was it subject to TOFA, what methods was it applying, etc).
- (d) these changes will apply to all taxpayers that are subject to TOFA and not just taxpayers that have made elections to apply any of the TOFA elective methods. As such, do not assume that these changes do not apply to you simply because you are only applying the default TOFA accruals/realisation methods; and
- (e) the changes will apply from the time that TOFA started to apply to a taxpayer (generally 1 July 2010). As such, the changes will apply to a number of recent acquisitions. It is hard to see how this can be regarded as equitable when such acquisitions will have been modelled on a completely different basis.

In short, these changes will be of great significance to many corporate acquisitions.

Transitional balancing adjustments

When a taxpayer became subject to the TOFA regime (generally from 1 July 2010) a taxpayer could elect to “un-grandfather” its existing financial arrangements. If a taxpayer made such an un-grandfathering election then it was required to calculate a transitional balancing adjustment amount (a **TBA amount**) in relation to all its financial arrangements; the TBA amount reflecting the difference between the historic tax treatment of its financial arrangements and the gains/losses it would have recognised in relation to those financial arrangements if TOFA had applied to those financial arrangements. This calculation is generally undertaken under what is referred to as the “long-form” method. However, taxpayers that have elected to apply the financial reports method to their financial arrangements can apply a “short-form” method to calculate their TBA amount. The short-form method essentially reflects the grossed-up DTAs and DTLs in a taxpayer’s financial reports (with certain items excluded). Once calculated (under either the long-form or short-form method), the total gain/loss from the TBA amount is spread over a four year period as an assessable or deductible amount.

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The proposed changes to the calculation of the TBA amount are complicated. However, in essence what is proposed is that for taxpayers that have made historic corporate acquisitions (i.e. generally corporate acquisitions prior to 1 July 2010):

- (a) in relation to the financial arrangements acquired as a result of those corporate acquisitions, the short-form method cannot be applied (i.e. the taxpayer will have to apply the long-form method to those financial arrangements); and
- (b) in calculating the TBA amount under the long-form method the taxpayer will have to take into account the various TOFA/consolidation interaction provisions.

These issues are most easily shown by reference to a simple example.

Example

- A Co (the head company of a consolidated group) acquired B Co in 2006. In 2006, B Co had a number of financial arrangements which A Co (as head company) still holds at 30 June 2010.
 - The TOFA provisions apply to A Co from 1 July 2010 and A Co elects to un-grandfather its existing financial arrangements. A Co is required to calculate its TBA amount. As A Co has made the financial reports election, A Co can, prima facie, apply the short-form method.
 - As a result of the proposed changes, A Co will have to apply the long-form method to calculate its TBA amount in relation to the financial arrangements that it acquired on acquisition of B Co (even though it can still apply the short-form method to its other financial arrangements).
 - Furthermore, in calculating its TBA in relation to these financial arrangements, A Co will have to apply a number of detailed TOFA/tax consolidation interaction provisions which can apply to set the tax cost of certain assets and liabilities at their accounting value (rather than the actual tax cost that has previously been pushed into them).
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The implications of these changes for taxpayers that have un-grandfathered their existing financial arrangements is potentially very significant as:

- (a) they will almost certainly have to re-calculate their TBA amounts (potentially applying the long-form method to things that they had previously applied the short-form method to);
- (b) in doing so, they may have to recalculate ACA calculations that were undertaken in relation to historic corporate acquisitions (and reset the tax cost of assets/liabilities at their accounting value at this time); and
- (c) although the scope of the “TOFA/consolidation interaction” provisions that they will have to apply in doing this is unclear, this could potentially lead to

the loss of deductions in relation to liabilities assumed on historic acquisitions.

These amendments are fundamental changes which go significantly beyond ensuring that the TOFA transitional balancing adjustment provisions operate as “intended” (as stated in the press release).

Furthermore, the announcement of such changes (with no real details) a few weeks prior to most taxpayers lodging tax returns which include their TBA amounts is extremely disappointing. Again, the dollars at stake from these changes may be significant.

5 Further consolidation issues under review

The BoT report released simultaneously with the Assistant Treasurer’s press release recommends that further consideration be given to other aspects, and the Assistant Treasurer has confirmed that the BoT will now undertake that more detailed review. These two areas are as follows.

- (a) Consolidation outcomes in respect of ‘majority-owned’ assets – ie outcomes where the acquiring group own more than 50% interest in the joining entity before the joining time. This review will apparently consider whether, in such circumstances, the deductible status in respect of asset step-ups should be limited.
- (b) Issues in relation to the consolidation treatment of liabilities are to be considered, particularly in relation to derivatives and insurance contract related liabilities. Approaches flagged by the BoT are that:
 - there may be some circumstances in which it would be appropriate for future income tax deductions to be denied for the amount of such a liability; or
 - for such liabilities to be wholly excluded from the consolidation asset tax value resetting calculation.

As outlined at 4 above, to some extent the TOFA changes that have already been announced deal with liabilities in this context, but obviously only financial arrangement related liabilities rather than liabilities more broadly.

In addition, the BoT is in the course of finalising their more wide-ranging post-implementation consolidation review, with a Position Paper outlining their preliminary thoughts being released back in October 2010.

6 What to do now

Obviously, as a matter of urgency impacted companies will be assessing the potential implications of these changes. Although final implications will not be able to be determined until the relevant legislation is introduced into Parliament and ultimately enacted, additional details will no doubt emerge via the further

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consultation that is proposed. However, it is likely that this consultation will be limited as the Assistant Treasurer has indicated that these amendments are to be fast tracked.

Difficult financial accounting issues will also have to be faced in relation to what, if any, impact this announcement should have on 31 December 2011 financial reports.

Since March 2011, the Australian Taxation Office (**ATO**) have been deferring decisions on a large number of rulings, objections and various amended assessment requests pending clarification as to likely legislative action following the Assistant Treasurer's initial 30 March 2011 press release. As a matter of urgency, it will be essential for the ATO to now provide some guidance as to how it intends to proceed, given the fact that the relevant amendments may not be enacted for at least four months.

Notwithstanding issues of detail that may evolve during the formulation of the amending legislation, two broader high level technical issues emerge which now justify detailed review and consideration, being:

- (a) the precise scope and application of the pre-June 2010 version of the residual cost setting provisions of subsection 701-55(6), because it is intended that this provision will again be returned to 'active service' in relation to the pre-12 May 2010 period; and
- (b) in respect of the prospective period, a range of broader technical issues demand consideration as to the application of a 'business acquisition' approach/overlay that is to apply to subsection 701-55(6).

Both of these aspects will create considerable interpretational challenges for both taxpayers and the ATO, and no doubt ultimately at the margin judicial direction will be required.

Finally, as noted at 5 above, a range of other significant consolidation related amendments are likely to flow from the BoT's post-implementation consolidation report when it finally issues, in the first half of 2012. The wide range of issues under consideration by the BoT was flagged in their Position Paper released in October 2010. Therefore, potentially impacted groups should familiarise themselves with the implications that might ultimately flow from this further work by the BoT.

In short, 2012 will be another very active and important year for tax consolidated groups.

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Summary tables – Assistant Treasurer’s 25 November 2011 announcement

Consolidation changes to the residual tax cost setting and right to future income rules

A Introduction

These summary tables are only intended as a general overview of the proposals outlined in the Assistant Treasurer’s press release of 25 November 2011 and the associated material released on that day. Therefore, it is important to note that:

- (a) significant changes may be made by the Government or the Parliament prior to the enactment of these proposals;
- (b) the material released contains some ambiguities which may be reflected in this material;
- (c) the following information should only be seen as a general summary, and therefore before any actions or decisions are taken it is essential that the actual material released by the Assistant Treasurer be considered in detail and specific advice be obtained.

B Outline

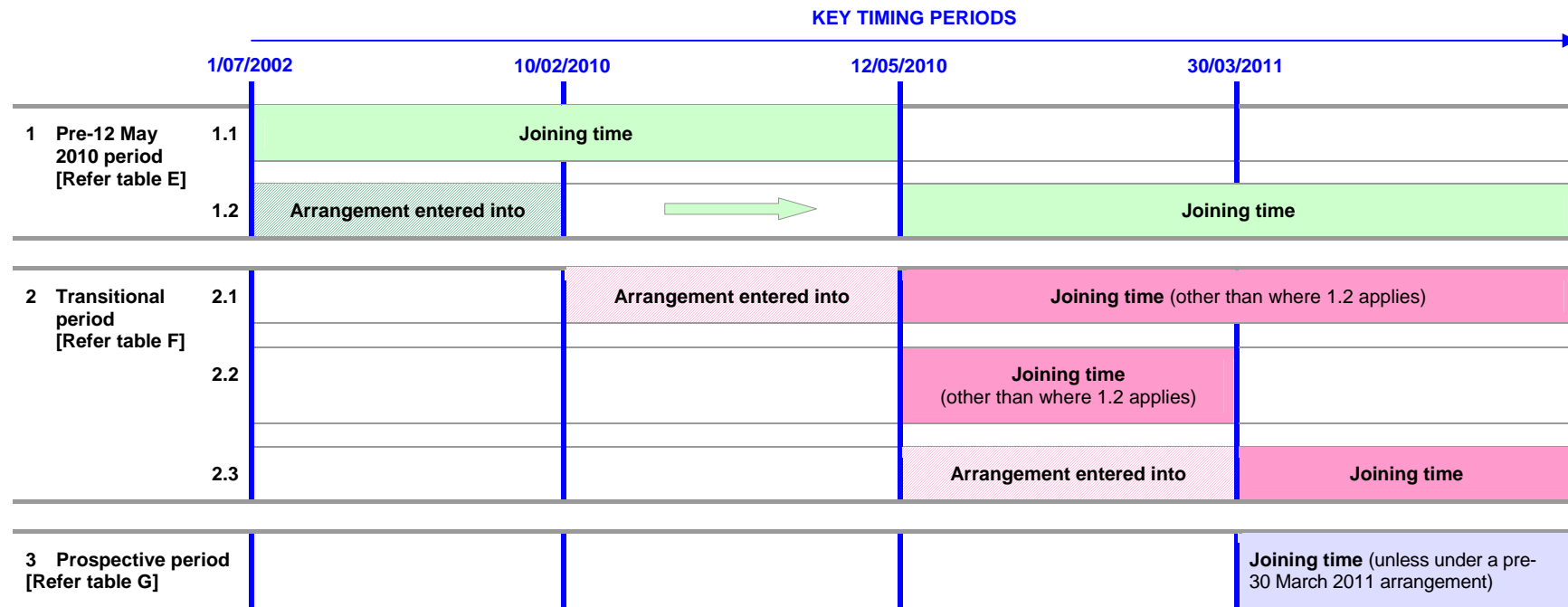
The following table provides a very high level outline of the proposed changes, with more detailed summaries contained in tables E, F and G. As is apparent from the following table, outcomes can vary significantly depending on the period to which the joining time relates, with C below covering this aspect in more detail.

Joining time	Key points
Pre-12 May 2010	<ul style="list-style-type: none"> • Outcomes can vary significantly, depending on when the relevant assessment/amended assessment issued claiming relevant deductions. Where a private ruling has been obtained, tax outcomes will remain unchanged. • Generally, non-deductible goodwill status will be confirmed to apply to customer relationships, know-how and other accounting intangibles. • Outcomes in respect of rights to future income, life and general insurance in-force value, and mine improvements that are not depreciating assets will vary, depending on the date of issue of relevant notices of assessments (including the assessment for the year that includes the joining time, but also the date of assessments for subsequent tax years that may be impacted by the ‘tail’ of associated deductions or tax losses).
12 May 2010 to 30 March 2011	<ul style="list-style-type: none"> • Where a private ruling from the ATO has been obtained, it will continue to apply without modification. • Generally, the provisions enacted on 3 June 2010 will continue to apply, with the only restrictions being in respect of: <ul style="list-style-type: none"> – customer relationship, know-how and other accounting intangible assets; – right to future income deductions relating to contracts that are required to be renewed, or that can be unilaterally cancelled by the customer; and – mine site improvements that are not depreciating assets. Market valuation clarifications will also apply.
Post-30 March 2011	<ul style="list-style-type: none"> • Deductions in respect of rights to future income will be limited in the scope of the current WIP provisions of s.25-95, being ‘work (but not goods) that has been partially performed ... but not yet to a stage where a recoverable debt has arisen’. • In the application of the residual tax outcome provisions of s.701-55(6), impacts will be determined by applying a ‘business acquisition’ approach. • Assets that cannot be sold separately by the joining entity (stated to be non-contractual customer relationships, know-how and other accounting intangibles) will be specifically deemed to be goodwill.

A number of refinements to the interaction between the consolidations and taxation of financial arrangements (TOFA) regimes are also announced, which will have both retrospective and prospective application (refer table H).

C Key timing periods

As noted above and outlined in the following tables E, F and G, outcomes vary significantly depending on what ‘period’ classification (as outlined below) will apply. Therefore, it is essential to establish what period classification is likely to be relevant to any particular joining entity. In respect of the pre-12 May 2010 period classification, outcomes can also vary significantly depending on the date on which relevant assessments and amended assessments that include associated deduction claims have issued. Importantly, more restrictive deduction criteria will apply in the context of pre-12 May 2010 joining entities where assessments/amended assessments claiming relevant deductions have yet to issue.



D Categories of rights to future income

The material released breaks rights to future income into three broad categories, with different tax outcomes potentially applicable to each of them. The categories as described in the material are as follows.

Rights to future income categories

Category 1	Rights to receive income where the work has been done, or the goods or services have been provided, by the joining entity before the joining time.
Category 2	Rights to receive income where the work will be done, or the goods or services will be provided, after the joining time under a contract that was entered into before the joining time, excluding any rights to income that are contingent on the renewal of the contract (such as rights under a renewal clause which may give rise to the extension of an existing contract, or to a future contract, under which income would be receivable).
Category 3	Right to receive income arising from an expectation of future work or future provision of goods or services (due to, for example, existing customer relationships), including any rights to income that are contingent on the renewal of the contract.

It is important to note that there is some ambiguity as to whether Category 2 or Category 3 is intended to apply in the case of an existing non-cancellable contract where the level of expected work to be done under that contract is known and anticipated but not contractually determined. This aspect is under consideration by Treasury.

E Pre-12 May 2010 joining times (plus post-12 May 2010 joining times where the relevant arrangement commenced before 10 February 2010)

DATE OF ASSESSMENT/AMENDED ASSESSMENT THAT CLAIMED/CLAIMS RELEVANT DEDUCTIONS ¹				
	1/07/2002	12/05/2010	31/03/2011	ongoing
APPLICATION OF AMENDMENTS				
Private Ruling or Advanced Compliance Agreement obtained	Ruling or Advanced Compliance Agreement continues to apply.			
Ability of ATO to amend to increase tax payable	Within the normal amendment periods, the ATO can issue amended assessments adopting the revised provisions. As outlined below, outcomes will vary depending on the date at which the assessment/amended assessment issued in which relevant deductions were claimed. No interest or penalties will be payable on related amended assessments increasing tax payable.			
Ability for taxpayers to seek an amendment to now reduce tax payable	Taxpayers can request an amendment within the normal four-year period, plus two years from the date of enactment, but only to apply the pre-12 May 2010 period changes as summarised in the right-hand column under 'Scope/nature of amendments'. No interest will be payable on associated refunds issued. (Any interest already paid will not be clawed back.)		Normal four-year amended assessment request period applies. No interest will be payable on associated refunds issued.	
SCOPE/NATURE OF AMENDMENTS				
Consumables	Deductions confirmed/allowed.			
Right to future income categories	Deductions confirmed for Category 1 WIP (ie work/services/goods provided before the joining time). Category 2 and Category 3 deductions not confirmed, but also not specifically precluded from potential deductibility under old s.701-55(6).	Transitional Period rules apply (refer table F).		Deductions restricted to Category 1 (work/services/goods provided before the joining time) – deemed goodwill treatment will apply to Category 2 and Category 3 amounts.
Subsection 701-55(6)	Old s.701-55(6) (narrowly interpreted by the ATO) applies other than to legislatively confirm deductions not available for customer relationships/know-how/accounting intangibles.			Old s.701-55(6) applies other than to confirm deductions not available under this section for: (i) customer relationships/know-how/accounting intangibles; (ii) mine site improvements; (iii) value of life and general insurance in-force business.
Market valuation clarification	In relation to s.701-55(6) and RTFI deductions, a market value clarification will be introduced prescribing that deductions cannot be claimed under a calculation where the relevant value can be regarded as forming part of the value of the underlying asset from which these income rights are derived.			

¹ Where relevant deductions have resulted in a tax loss, it appears that the date of the assessment for the tax year in which the loss is recouped will be the relevant date in this regard.

- F Transitional period: 12 May 2010 to 30 March 2011 joining times** (also includes post-30 March 2011 joining times where the relevant arrangement commenced between 12 May 2010 and 30 March 2011, but excludes joining times where the relevant arrangement commenced before 10 February 2010)

APPLICATION OF AMENDMENTS	
Private Ruling or Advanced Compliance Agreement obtained	Ruling or Advanced Compliance Agreement continues to apply.
Ability to amend assessments by either the ATO or taxpayers	Normal four-year amended assessment period applies (ie no special protection from the amendments where an assessment has already issued). No interest or penalties will be payable on amended assessments resulting from these changes. Interest will, however, be payable to taxpayers on any associated refunds issued.
SCOPE/NATURE OF AMENDMENTS	
General position	The provisions enacted on 3 June 2010 will continue to apply, subject to the following restrictions. (Note: it is confirmed that deductions in respect of consumable stores will continue to apply.)
Non-contractual assets akin to goodwill	Deductions under s.701-55(6) will be precluded in respect of customer relationship assets, know-how, and other accounting intangible assets that are not regarded as separate CGT assets but are akin to or form part of goodwill. Deemed 'goodwill' treatment will apply.
Right to future income categories	Deductions will be disallowed, and deemed goodwill treatment will apply to rights to future income where the value is contingent on the renewal or extension of the contract or the contract can be unilaterally cancelled without penalty by the customer. However, deductions will be confirmed in respect of Category 1 and Category 2 rights to future income.
Market valuation clarification	In relation to s.701-55(6) and RTFI deductions, a market value clarification will be introduced prescribing that deductions cannot be claimed under a calculation where the relevant value can be regarded as forming part of the value of the underlying asset from which these income rights are derived.
Mine improvements	To be excluded from deductions under s.701-55(6) (but it is noted that the ATO is currently determining whether a number of such mine improvements might more correctly be regarded as depreciating assets, and hence deductible under other provisions).

G **Prospective period: post-30 March 2011 joining times** (unless relating to an arrangement that commenced between 10 February 2010 and 30 March 2011)

APPLICATION OF AMENDMENTS	
Ability to amend assessments by either the ATO or taxpayers	Normal four-year amended assessment period applies (ie no special protection from the proposed provisions where an assessment has already issued). As there is currently no statement regarding interest and penalties, presumably it is intended that they could apply to amended assessments increasing tax payable.
SCOPE/NATURE OF AMENDMENTS	
Limiting application of tax cost setting rules	The tax cost setting rules will be limited to apply only to assets otherwise recognised for tax purposes (ie excludes s.40-880 deduction outcomes).
Consumables	Deductions allowed (on an acquisition or usage basis, depending on taxpayers' circumstances).
Right to future income	Deductions only to be obtained through a modified application of s.25-95, being 'work (but not goods) that has been partially performed ... but not yet to a stage where a recoverable debt has arisen'. In other circumstances, the right to future income asset will be taken to be a retained cost base asset – ie it will normally only have a low tax value.
Subsection 701-55(6): other applications	In otherwise applying s.701-55(6), outcomes will be determined as if the relevant asset was being acquired directly as part of a business acquisition in determining whether such amounts are deductible, and if so over what period. Assets that cannot be separately sold by the joining entity (such as non-contractual customer relationships, know-how and other accounting intangibles) will be specifically deemed to be goodwill.

H Consolidation/TOFA interactions (with retrospective application)

Clarifying that the head company is deemed to have acquired financial arrangements that are assets or liabilities from the joining entity at the joining time.

For TOFA liabilities of the joining entity the liabilities will be deemed to have been assumed for their accounting values (rather than original value). This will be the case irrespective of what TOFA methods the head company is subject to (i.e. accruals/realisation, financial reports, fair value, FX retranslation and hedging methods). The fundamental consequence of this change is to potentially deny the acquiring group deductions in relation to the TOFA liability assumed (i.e. up to the amount of the accounting value of the TOFA liability at the joining time). The consequences of this change are significant in relation to any corporate acquisitions from the commencement of the TOFA regime.

In calculating TOFA transitional balancing adjustment amounts (i.e. when a taxpayer enters TOFA) in relation to financial arrangements previously acquired as a result of a corporate acquisition only the “long-form” method will be able to be utilised (i.e. the “short-form” DTA/DTL method that is generally available to taxpayers that have elected to apply the financial reports method will not be available in relation to these financial arrangements). Furthermore, it is proposed that the various TOFA/consolidation interaction provisions will apply as part of calculating the transitional balancing adjustment amount under the “long-form” method. These changes have potentially significant implications in relation to pre-TOFA acquisitions for taxpayers that have elected to un-grandfather their existing financial arrangements.

These notes are in summary form and are designed to alert readers to tax developments of general interest. They are not comprehensive, they are not offered as advice and should not be used to formulate business or other fiscal decisions.

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