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Ref: MH:grh

19 September 2012

Manager - Corporate Tax Unit
Business Tax Division
The Treasury
Langton Crescent
PARKES ACT 2600

Email: LossCarryBack@treasury.gov.au

Dear Sir/Ms

IMPROVING ACCESS TO COMPANY LOSSES - INTRODUCING LOSS CARRY-BACK

We welcome the opportunity to provide a submission to the Treasury in relation to the Exposure Draft and the accompanying Explanatory Material that was released for consultation on 23 August 2012.

Pitcher Partners comprises five independent firms operating in Adelaide, Brisbane, Melbourne, Perth and Sydney. Collectively we would be regarded as one of the largest accounting associations outside the Big Four. Our specialisation is servicing and advising smaller public companies, large family businesses and small to medium enterprises (which we refer to as the "middle market"). In making this submission therefore, our focus is on the implications of the Exposure Draft for the middle market.

General comments

Whilst recognising that a reduced consultation period is a strong indicator of the importance placed by the Federal Government on the successful implementation of this reform, it does present a major difficulty in our ability to contribute to the design of that reform in a meaningful way. This submission therefore, only sets out our initial thinking and does not represent our fully considered views on the Exposure Draft.

I.228034.1



Our main concern with the Exposure Draft is the proposed integrity rules - which are too unwieldy for the middle market. We believe that a specific integrity rule is required that is simple for taxpayers in the middle market to understand and implement.

We also believe that the current wording of the provisions (and, in particular, the proposed method statement) is overly complicated for middle market taxpayers and their advisers to implement - making it crucial that clearly worded and easy to follow examples are included in the explanatory memorandum to show how the provisions are intended to work in practice.

Specific comments

Our specific comments on the Exposure Draft are set out in the attached Appendix.

Contacts for further information

If you would like to discuss any aspect of this submission or require any further information, please do not hesitate to contact either Greg Howes (on 03 8610 5564) or me (on 8610 5138).

Yours faithfully

PITCHER PARTNERS ADVISORS PROPRIETARY LIMITED



MICHAEL HAY
Executive Director

Appendix - Specific comments

Integrity rule(s)

We note that in the 6 August 2012 submission made by the Institute of Chartered Accountants Australia (“the ICAA Submission”) in respect of the Discussion Paper they identified that the area of greatest conceptual difficulty is the extent, if any, of the design relationship between the existing loss carry-forward rules and the proposed loss carry-back rules.

Whilst it was natural to look towards the existing, familiar loss carry forward rules for such a specific integrity rule we note that the current loss carry-forward rules are:

1. the subject of further review to clarify the operation of the law; and
2. overly complex.

We do not therefore, believe that simplification for businesses to access the tax benefit under the loss carry-back regime can be achieved by referencing an integrity rule for loss carry-back to the existing carry-forward rules.

Further, we note that even though the Exposure Draft and Explanatory Material contain references to the continuity of ownership and same business test¹, we understand that a parallel review has been undertaken by the Assistant Treasurer to consider a specific integrity rule appropriate to this measure.

We believe that a specific integrity rule is required that is simple for taxpayers in the middle market to understand and implement. As such we submit that the current references to the carry-forward rules be removed and replaced with this specific integrity rule. We will provide comment thereon if such a rule is released for further consultation.

Both the Exposure Draft and the Explanatory Material refer to amendments to the general anti-avoidance rule² as a further means of restricting abuse of the loss carry-back regime. Given that the parallel review referred to above may result in a specific integrity rule, we will defer comment until any such rule is released for public consultation.

Examples

The current wording of the provisions (and, in particular, the proposed method statement) is overly complicated for middle market taxpayers and their advisers to implement - making it crucial that clearly worded and easy to follow examples are included in the explanatory memorandum to show how the provisions are intended to work in practice.

¹ See Schedule 1, item 1, section 160-100 and paragraphs 2.64 to 2.70 respectively.

² See Schedule 2 and paragraphs 3.8 to 3.13 respectively.

We note that example 2.1 essentially covers the on-going (two year) rule. Given that there is a transitional one year carry-back rule, we believe that it is important to show an example using the transitional rule first and to then build on that concept for the on-going two year rule.

From a user's perspective such an example will be more relevant and it allows the reader to conceptualise the proposal on a limited scale first before embarking on the application of the two year rule.

In this regard, we note that example 2.4 actually shows the first year approach so perhaps repositioning this to be example 2.1 may add clarity.

We also consider that it may be beneficial to add a further column to the table that actually shows the loss carry-back amount for each of the years. It would assist in demonstrating that the total amount carried back over the current and middle years is limited to the earliest year taxable income amount.

Example 2.5 would appear to have the second and third paragraphs in the wrong order. The bracketed reference shows a second year claim of \$1m but this is not discussed until the third paragraph so it may confuse the reader initially. Repositioning the third paragraph to be the second would assist in understanding the example.

Limit on Loss Carry-Back Amount

In paragraph 2.5 of the Explanatory Material one of the caps that the loss carry-back amount is limited to is stated as:

“the tax liabilities in either or both of the income year immediately before the current year (the middle year) and the income year before the middle year (the earliest year).”

Further, paragraph (d) in Step 3 of the method statement in proposed subsection 160-15(1) refers to “unutilised income tax liability for the middle year”.

In paragraph 2.8 the opening sentence states that a corporate tax entity is able “to carry back a tax loss **against tax payable for the two preceding income years**”.
[Emphasis added]

Whilst the object of the cap is to limit the tax offset by reference to the income tax liability worked out (under section 4-10) in respect of the earliest year (the ‘target year’ in the Discussion Paper) these references to tax liabilities in both the earliest and middle years may lead to confusion that the tax offset can be claimed in respect of two preceding taxable years - i.e. rather than just the earliest year.

We also believe that the method statement and the definition in proposed section 960-30 may be overly complicated for the targeted beneficiaries of the measure. For example, the use of the word ‘owes’ in proposed subsection 960-30(1) may lead a

person to conclude that the cap is based on what is 'owed' by the entity as opposed to what is paid/payable by the entity in respect of that income year.

We recommend that the language be clarified or simplified so that it is clear that the tax liability worked out in respect of the earliest year is one of the actual caps for the purpose of limiting the loss carry-back amount.

Corporate tax rate

We agree that the use of the prevailing corporate tax rate in the current year in respect of a loss carry-back tax offset would be a more efficient process and conforms to the Federal Government's policy for simplification.

Cap reviews

Whilst the loss carry-back regime will commence with the stated caps in place to limit the tax benefit claimed in a middle or current year, we recommend that there be a process whereby the caps are reviewed to ascertain their effectiveness and to ensure that they keep pace with a changing economy so as to maintain their 'value'.

Five year lodgement requirement

It is not clear from the Explanatory Material in paragraphs 2.71 to 2.73 why a five year lodgement history is required when the rolling two year rule covers a three year period. As long as the earliest income year (the taxable year) is lodged followed by the subsequent middle and current (loss) years then it is difficult to understand what relevance income years preceding the earliest year have on the loss carry-back amount. Either further explanation is required or the lodgement requirement should be limited to the relevant rolling income years under the claim.