



20 April 2011

Via email: taxboard@treasury.gov.au

Review of Rights to Future Income and
Residual Tax Cost Setting Rules
The Board of Taxation
c/- The Treasury
Langton Crescent
Canberra ACT 2600

Attention: Mr Chris Jordan AO, Acting Chairman, Board of Taxation

Dear Mr Jordan,

Review of Rights to Future Income and Residual Tax Cost Setting Rules (*Review*)

1. The Business Law section of the Law Council of Australia is pleased to provide to the Board the comments below, from members of its Taxation Committee, in response to the Board's invitation to make submissions in relation to the Review.
2. The Assistant Treasurer's Media Release No. 045, which announced the Review, noted uncertainty in the scope of application of the rights to future income rules. We acknowledge that uncertainty.
3. The then Minister for Revenue and Assistant Treasurer announced in his Media Release No. 098 on 1 December 2005 that the consolidation tax cost setting rules would be clarified. In that Media Release it was announced that amendments would be made, among other things, to treat "rights to future income (such as work-in-progress amounts and unbilled revenue)" as retained cost base assets and the head company would be taken to have incurred expenditure to acquire those rights.
4. The scope of section 701-90 of the *Income Tax Assessment Act 1997* goes further than was indicated in that Media Release. Section 701-90 applies to "a valuable right (including a contingent right) to receive an amount for the performance of work or services or the provision of goods" if certain other requirements are met.
5. It is clear from examples 2.1, 2.2 and 2.3 in the Supplementary Explanatory Memorandum to *Tax Laws Amendment (2010 Measures No. 1) Bill 2010*, which inserted section 701-90, that it covers not only work-in-progress and unbilled revenue as at the joining time, but also rights to receive income

from the performance of work or services or the provision of goods after the joining time (hence the description "rights to future income rules").

6. It is clear that there is uncertainty regarding the scope of this provision because it is not clear how proximate to the joining time those rights must be to be within the scope of section 701-90, nor is it clear how contingent those rights may be without falling outside the scope of section 701-90. It is not clear whether the provision is limited to present rights, or whether it includes present contractual rights which are terminable at the election of the other party to the contract.
7. Rights which are sufficiently proximate to the joining time and subject to an appropriate degree of customer commitment at the joining time appear clearly to have been intended to be within the scope of this measure. It may be thought that rights which are not the subject of a sufficient degree of customer commitment at the joining time could be regarded as part of goodwill and therefore not appropriately within the scope of these measures. The challenge is to identify an appropriate basis on which to distinguish between the two categories.
8. That is a policy question upon which there is a divergence of views among members of the Taxation Committee and we are therefore not able to advocate any particular position.
9. Despite this, we would like to express a very strong view about the commencement and application dates of any changes to these rules which the Government may ultimately decide to make.
10. First, the rights to future income and residual tax cost setting rules as presently reflected in sections 701-90, 716-405, 716-410, 701-55 and 701-56 have been in effect since the enactment of *Tax Laws Amendment (2010 Measures No. 1) Act 2010* on 3 June 2010. It would therefore unfairly prejudice taxpayers if any amendments to those rules were made to apply to relevant events which occurred from the time of that enactment at least until the Media Release indicated on 30 March 2011 that some change might occur. By the same token, no such changes should be made applicable in relation to consolidation joining events which occur after that period pursuant to binding contractual commitments entered into during that period or pursuant to transactions undertaken in accordance with public announcements to a relevant stock exchange during that period.
11. Second, no amendments which treat taxpayers less favourably than was indicated in the 1 December 2005 Media Release should be made applicable to relevant events occurring prior to the issue of the Media Release on 30 March 2011, or pursuant to binding contractual commitments or relevant stock exchange announcements prior to that date. In view of the enactment of provisions at least as favourable to taxpayers as were foreshadowed in the 1 December 2005 Media Release, it would be unfair to taxpayers who would have conducted their affairs on the basis that those amendments would be, and in fact were, made, to change them with effect prior to the public announcement that changes would be considered. To do so would clearly be unfairly prejudicial and inconsistent with sound prior practice.
12. Third, it would be at best highly contentious if any amendments to narrow the present scope of the rights to future income rules were made applicable to relevant

events occurring prior to 30 March 2011, even if those changes were no less favourable to taxpayers than was indicated in the 1 December 2005 Media Release. It is acknowledged that the provisions as enacted are more favourable to taxpayers than was indicated in that Media Release. However, once those more favourable amendments were in fact made, many, if not most, taxpayers would consider that it would be unfair to change them with effect prior to a public announcement that such a change would be considered.

13. We trust these comments, although brief, will be of some assistance to the Review. The Business Law Section would be happy to arrange for members of its Taxation Committee to discuss these matters further with members of the Review, if that would be helpful. Thank you for your consideration.

Yours sincerely

A handwritten signature in black ink, appearing to read "W Grant". The signature is fluid and cursive, with a large initial "W" and a long, sweeping tail.

Bill Grant
Secretary-General