Losses

If you make a tax loss, you can generally carry it forward and deduct it from income made in future years.

What is a tax loss?

You make a tax loss when your total deductions exceed your total assessable and net exempt income for the year.

How to claim a tax loss

The method of claiming varies depending on if you are an individual, partnership, trust, company or consolidated group.

Who should lodge a losses schedule?

The are 2 types of schedules – one for consolidated groups and one for non-consolidated companies and other entities.

Keeping records for losses

When you are claiming or carrying forward a tax loss, you may need to keep your tax records for longer than usual.

Non-commercial losses

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What is a tax loss?

You make a tax loss when your total deductions exceed your total assessable and net exempt income for the year.

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Some deductions can't give rise to a loss

Certain deductions that would normally be allowed can't be claimed as deductions if they would result in a tax loss. They are:

- payments of pensions, gratuities or retirement allowances to employees, former employees, or their dependents
- gifts or contributions made to deductible gift recipients
- payments made under conservation covenants
- personal superannuation contributions.

Is it a tax loss or a capital loss?

A tax loss is different from a capital loss. A capital loss occurs when you dispose of a capital asset for less than its tax value.

A capital loss can't be offset against income. It can only be either:

- offset against any **capital gains** in the same income year
- carried forward to offset against future capital gains.

Australian and foreign residents

Australian residents calculate an overall tax loss on the basis of their worldwide income and deductions.

Foreign residents calculate a tax loss on the basis of their Australian income and deductions incurred in earning that income.

You may be able to offset your business loss against other income if you're a sole trader or in a partnership, see **Non-commercial losses**.

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How to claim a tax loss

The method of claiming varies depending on if you are an individual, partnership, trust, company or consolidated group.

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Individuals

Individuals can generally carry forward a tax loss indefinitely, but they must claim a tax loss at the first opportunity. You can't choose to hold onto losses to offset them against future income if they can be offset against the current year's income.

Carried-forward tax losses are first offset first against any **net exempt income**, and then against assessable income. Losses must be claimed in the order in which they were incurred.

To claim prior year tax losses on your tax return, see label **L1** of the **Individual tax return instructions**.

If you're using **myTax**, tick the box 'You had tax losses from earlier income years'.

Non-commercial losses

If you're carrying on a non-commercial business activity as an individual, either alone or in a partnership, and your business makes a loss, you must check the **non-commercial loss** rules. The rules determine if you can offset the loss against your income from other sources, such as wages.

Partnerships

If a partnership makes a tax loss, each partner takes the proportionate share of the loss and treats it like a loss from any business activity (including applying the **non-commercial loss** rules).

Trusts

If you operate your business as a trust and you incur a tax loss, you can't distribute the loss to the trust's beneficiaries.

Losses must be quarantined in a trust to be carried forward by the trust indefinitely until they can be offset against future net income. It is possible to use those losses as deductions against income in the trust in future income years if the trust satisfies certain tests relating to ownership or control of the trust. If the trust terminates before the losses can be offset against income, they are lost.

The **trust loss rules** apply in different ways to:

- fixed trusts
- non-fixed trusts
- excepted trusts.

The trust loss legislation is contained in **Schedule 2F to the Income Tax Assessment Act 1936**.

How to claim a tax loss on your trust tax return is explained in Question **27** of the Trust tax return instructions.

Companies

Companies can carry forward a tax loss indefinitely, and use it when they choose, provided they have maintained the same majority ownership and control. If there is a change of at least 50% in the ownership or control of a company, the company needs to satisfy **either** the:

- same business test
- similar business test (this applies to losses incurred in an income year beginning on or after 1 July 2015).

For guidance on the same business test and similar business test, see Taxation Ruling TR 1999/9 and Law Companion Ruling LCR 2019/1.

A company that has **not** maintained the same majority ownership will not be able to use its carried-forward tax losses if it has closed its business completely (for example, discontinued the business previously carried on and has no intention to resume). This is because it will fail the same business test and similar business test.

If a company is still carrying on its business, it will not fail the same business test or similar business test merely because it has:

- reduced the scale of its business, including if its activities have reduced to a minimum or are almost entirely suspended
- suspended or temporarily closed its business only because of temporary adversity or due to reasons beyond its control which it intends to overcome.

In determining whether a company's business is still being carried on, both the following must be considered:

- The reasons for the inactivity, for example, whether the company is actively holding itself out for business though obtaining none.
- Is there an expectation that the business will resume active operations within a reasonable time?

These principles should be taken into account if a company's business has been affected by circumstances relating to COVID-19 after its majority ownership has changed. For instance, if a gym closed temporarily for 3 months because of restrictions on its operations, this will not cause it to fail the same business test or similar business test.

A company will not fail the same business test or similar business test merely because it has received JobKeeper payments.

The normal loss deduction rules are modified for widely held or eligible **Division 166** companies so the rules are easier to apply.

How to claim a tax loss on your company tax return is explained in Question **13** of the **Company tax return instructions**.

For more information, see:

- the general company loss recoupment rules in **Division 165**
- the modified loss recoupment rules for widely held and eligible **Division 166** companies
- the modified rules in **Division 167** for companies whose shares carry unequal rights to dividends, capital distributions or voting power
- **Taxation Ruling TR 1999/9**, concerning the application of the same business test.
- **Law Companion Ruling LCR 2019/1** *The business continuity test – carrying on a similar business*
- **Loss carry back tax offset**

Current year losses

If there is a change of ownership or control of a company during an income year and the company does not maintain the same business or similar business, it must work out its taxable income and tax loss under subdivision 165-B of the ITAA 1997.

In broad terms, a company in this situation has both a taxable income and a tax loss for the same year. In some circumstances, the loss may be carried forward and used in later years, subject to the usual restrictions.

Consolidated groups

Consolidation allows a wholly owned group of entities to be treated as a single entity for income tax purposes, with the head company of the consolidated group the only entity recognised for determining the income tax liability of the group.

A consolidated group generally has two types of losses:

- losses generated by the consolidated group (group losses)
- transferred losses that were generated by an entity before it became a member of the group.

Transferring losses to the consolidated group

When an entity becomes a member of a consolidated group (whether as head company or as a subsidiary) its unused carry-forward losses are transferred to the head company if the losses satisfy modified versions of the general company loss recoupment tests.

Broadly, the tests are applied as though the 12 months prior to the joining time were the loss claim year (known as the trial year). The loss is transferred to the head company of the group if the joining entity could have claimed the loss in the trial year assuming it had sufficient income or gains of the relevant type. The rules are outlined in Subdivision 707-A of the ITAA 1997.

Available fraction

The amount of a transferred loss that can be claimed by the head company from a particular joining entity is calculated by reference to an available fraction. The available fraction limits the annual rate at which transferred losses may be claimed by the head company. For more information, see Subdivision 707-C of the ITAA 1997.

Using losses in the consolidated group

Before claiming a group loss or a transferred loss, the head company is required to apply the general loss recoupment provisions. This necessitates the head company passing the continuity of ownership and control tests or the business continuity test. For transferred losses, these recoupment tests are modified for the purposes of determining whether the company has maintained the same ownership. The modifications are outlined in Subdivision 707-B of the ITAA 1997.

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Who should lodge a losses schedule?

The are 2 types of schedules – one for consolidated groups and one for non-consolidated companies and other entities.

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Losses schedule

Companies (not consolidated groups), trusts and superannuation funds may be required to lodge a *Losses schedule* with their tax return if any of the following apply. The entity:

- has total of tax losses and net capital losses greater than $100,000 carried forward to later income years
- is required to satisfy the business continuity test to deduct or apply a loss either in the current income year or in a later income year or, having passed the continuity of ownership test, has claimed a deduction for tax losses and/or applied net capital losses greater than $100,000
- is a listed widely-held trust that is required to satisfy the business continuity test to deduct a tax loss in the current or later income years or, having passed the 50% stake test, has claimed a deduction for tax losses greater than $100,000
- has determined that it has an unrealised net loss as defined in the provisions of Subdivision 165-CC of the ITAA 1997

- is a life insurance company and has a total of complying superannuation class tax losses and net capital losses carried forward to later income years greater than $100,000
- has an interest in a controlled foreign company (CFC) that has current year losses greater than $100,000
- has an interest in a CFC that has deducted or carried forward a loss greater than $100,000 to later income years.

Consolidated groups losses schedule

The head company of a consolidated group or multiple entry consolidated (MEC) group must complete the *Consolidated groups losses schedule* and lodge it with the *Company tax return*, if any of the following apply:

- The total of the group's tax losses and net capital losses carried forward to later income years is greater than $100,000.
- The total of its tax losses and net capital losses transferred from joining entities is greater than $100,000.
- The total of its tax losses deducted and net capital losses applied is greater than $100,000.
- It has an interest in a CFC that has current year losses greater than $100,000.
- It has an interest in a CFC that has deducted or carried forward a loss to later income years greater than $100,000.
- It is a life insurance company, or is treated as a life insurance company under Subdivision 713-L of the ITAA 1997, and has a total of complying superannuation class tax losses and net capital losses carried forward to later income years greater than $100,000.

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Keeping records for losses

When you are claiming or carrying forward a tax loss, you may need to keep your tax records for longer than usual.

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If you use information about tax losses in a later tax return – for example, you carry forward a tax loss – you must keep the records until the end of any period of review for the income tax return in which the loss is fully deducted.

For more information, see Taxation Determination TD 2007/2 *Income tax: should a taxpayer who has incurred a tax loss or made a net capital loss for an income year retain records relevant to the ascertainment of that loss only for the record retention period prescribed under income tax law?*

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