General value shifting regime

Detailed information about consolidation and the general value shifting regime.

Overview of provisions

An overview document that contains summary information about the 'General value shifting regime'.

Who it affects

Who the general value shifting regime affects.

Guide to the general value shifting regime

Use this guide to understand the regime and the circumstances where it is relevant.

Rulings, law and objections

The primary legislative references and extrinsic material relating to the general value shifting regime.

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General value shifting regime – who it affects

Who the general value shifting regime affects.

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Most value shifts happen when dealings or transactions between two parties are not at market value and result in the value of one asset decreasing and (usually) another asset increasing.

Value shifts distort the relationship between an asset's market value and tax value. This can create artificial losses and deferred gains.

There are exclusions to minimise the impact on small business.

Generally, the GVSR does not apply to:

- small value shifts
- normal commercial dealings conducted at market value
- dealings within consolidated groups.

Where the GVSR applies, you may need to adjust the tax values of interests affected by the value shift, or adjust a realised loss or gain. In some cases there may be an immediate capital gain.

Adjustments are made for revenue assets and trading stock, and for assets held on capital account.

Provisions

Current provisions

The current value shifting provisions in Divisions 723, 725 and 727 of the *Income Tax Assessment Act 1997* are more extensive than the previous rules. They apply to:

- shares or other interests in companies
- units or other interests in trusts

- loan interests in companies and trusts
- interests held as trading stock and on revenue account.

However, the GVSR has a range of exclusions and safe harbours to ensure it applies only to significant value shifts.

Changes to value shifting provisions

Changes to value shifting provisions

Previous provisions

Value shifting rules have been included in tax law since the mid-1990s – most recently in Divisions 138, 139 and 140 of the *Income Tax Assessment Act 1997*. These divisions ceased on 1 July 2002 (but continue to apply to arrangements operating prior to 1 July 2002).

Application and avoidance

There is no need for a finding of a tax avoidance motive for the GVSR provisions to apply. In addition, the 'de minimis' exclusions (such as the minimum value shift amounts required to trigger the provisions) may not apply where it is reasonable to conclude that value shifts happen under more than one scheme for the purpose of accessing those exclusions.

It is also possible for anti-avoidance provisions (such as Part IVA of the *Income Tax Assessment Act 1936*) to apply to a value shift where the GVSR is not applicable.

Examples

- Indirect value shifting
- Direct value shifts on interests
- Direct value shifts by creating rights

Work through the following three scenarios to determine if you are affected by the general value shifting regime (GVSR) rules.

Example 1

Do you have interests in an entity whose dealings (such as providing loans or other services, or transferring assets) with another entity are *neither at market value* nor arm's length?

and

Is the difference in value of what is given and received more than $50,000?

If you answered **yes** to both questions the rules for **indirect value shifting** may affect you.

Example 2

Do you have interests in a company or trust in which equity or loan interests have been issued or bought back at *other than market value*, or varied such that the values of some interests have increased while others have decreased?

and

Did the interests that decreased in value do so by a total of at least $150,000?

If you answered **yes** to both questions the rules for **direct value shifts on interests** may affect you.

Example 3

Have you made a loss on:

- a non-depreciable asset over which a right (such as a lease) was granted to an associate of yours for *less than market value*, or
- an asset (including a share or trust interest) that was acquired under a capital gains tax (CGT) rollover as a replacement for such an asset?

and

Did the right decrease the value of the asset by more than $50,000?

If you answered **yes** to both questions the rules for **direct value shifts by creating rights** may affect you.

Note: if you answered **no** to at least one of the questions from each of the three scenarios the rules don't affect you now.

Indirect value shifting

The 'indirect value shifting' provisions are located on the ATO Legal Database in Division 727 of the Income Tax Assessment Act 1997.

Occurs where:

Two entities under the same control or ownership conduct dealings or transactions that are neither at market value nor otherwise at arm's length. This might occur where, for example, services or assets are transferred between two companies under your control and no payment is made (or the payment is less than market value).

Does not apply if:

- the value shift is $50,000 or less
- the value shift is from a superannuation entity or an entity that is neither a company nor a trust
- the value is shifted down a wholly-owned chain of entities (except if the value of a loan is affected)
- the shift relates almost entirely to loans or other services that are provided for at least their direct cost, or not more than a commercially realistic price, or
- the shift relates to an asset and the transfer is for at least the asset's cost base or cost, whichever is greater, and not for more than the asset's market value (in most cases).

Also, holders of interests in the two entities are excepted from the general value shifting regime impacts if either:

- they are a small business entity
- they, together with related entities, have net assets of $6 million or less (the capital gains tax maximum net asset threshold test).

Note:

- for the 2007-8 and later income years the simplified tax system no longer operates and has been replaced by the small business entity provisions.

- a limit of $5 million or less applies to 2006-7 and earlier income years.

Effects

This provision may affect equity or loan interests held by the controller of the company or trust, the controller's associates and (if the company or trust is closely held) common owners, the common owners' associates and active participants in the arrangement.

Adjustments are made to prevent artificial losses (for interests in the losing entity) and gains (for interests in the gaining entity).

For value shifts of less than $500,000, adjustments may not be required for losses made more than four years after the value shift happened.

Example: indirect value shifting

Example: indirect value shifting

- Mr and Mrs Smith each own one ordinary share in AssetCo (50% of the issued share capital) with a cost base of $250,000. They also each own 50% of NewCo.
- AssetCo transfers an asset worth $5 million to NewCo for $2 million in a non-arm's length dealing. The effect of the transaction is to reduce the market value of each share in AssetCo to $1 million. The market value of each share in NewCo increases by $1.5 million.
- The adjustable values of Mr and Mrs Smith's shares in these entities are adjusted to prevent inappropriate losses and gains arising. Alternatively, the provisions reduce or extinguish any loss or gain made when the shares are realised.

Direct value shifts on interests

The 'direct value shifts on interests' provisions are located on the ATO Legal Database in Division 725 of the Income Tax Assessment Act 1997.

Occurs where:

A company or trust is controlled by an entity (or an entity and its associates). For example, the entity and its associates control at least 40% of the voting power or have beneficial rights to 40% of the dividends or distributions the company or trust makes.

Something is done that causes the value of some of the interests in the company or trust to decrease, and some other interests in the company or trust to increase in value or be issued at a discount.

This might occur if:

- shares, units (or similar interests) or loan interests in a company or trust are issued or bought back at other than market value, or
- existing rights attached to such shares, units or loan interests are varied.

Does not apply if:

- the total reduction in market value of the interests that decrease in value is less than $150,000
- under the terms of the arrangement that causes the value shift, the arrangement reverses within four years, or
- the company or trust concerned and all entities with interests affected by the value shift are members of the same consolidated group.

Effects

This provision may affect equity or loan interests held by the controller of the company or trust, the controller's associates and (if the company or trust is closely held) any active participants in the arrangement. It does not affect equity or loan interests held indirectly (through another entity).

There may be a deemed gain for the holders of interests that lose value but not a loss.

The adjustable value (for example, the cost base) of the interests that decrease in value is decreased, and the adjustable value of the new interests or the interests that increase in value is increased.

Example: direct value shifts on interests

Example: direct value shifts on interests

- OpCo originally had 400 shares, 200 each owned by Mr and Mrs Smith. These shares were issued for $10 each and now have a market value of $1,000 each.
- OpCo issues 400 new shares to Sonny Smith for $200 per share. Forty per cent of the market value of OpCo's shares before the new issue has been shifted from Mr and Mrs Smith to Sonny Smith (who now has a 50% interest in the company).
- Mr and Mrs Smith are taken to have made a capital gain of $79,200 each, calculated as if they had disposed of 40% of their interests to Sonny Smith.
- The cost bases of Sonny's shares are equal to their market value ($600 each) and the cost bases of Mr and Mrs Smith's shares are reduced (to $6 each) on the basis that, effectively, 40% of each of their interests is disposed of.

Direct value shifts by creating rights

The 'direct value shifts by creating rights over non-depreciable assets' provisions are located on the ATO Legal Database in Division 723 of the Income Tax Assessment Act 1997.

Occurs where:

A non-depreciable asset is disposed of at a loss because the owner granted an associate a right (for example, a lease or other right of use) over the asset for less than market value. The rules can also apply where a non-depreciable asset over which a right was granted is replaced by an asset (including a share or trust interest) acquired under a capital gains tax rollover.

Does not apply if:

- the shortfall on granting the right is $50,000 or less
- the right is created when the owner of the asset dies or is a conservation covenant over land, or
- the asset and right remain within the same consolidated group.

Effects:

This provision may affect the entity that creates the right and realises the non-depreciable asset, and an entity that acquires the underlying asset under a rollover.

In general, the loss made on the underlying asset is reduced by the lesser of:

- the difference between the market value of the right at the time it was created and the consideration received for it, and
- the amount by which the right affects the market value of the underlying asset when it is realised.

Example: direct value shifts by creating rights

Example: direct value shifts by creating rights

- Mr and Mrs Smith each own 50% of OpCo. Their son Sonny Smith owns a non-depreciating asset (some land).
- Sonny Smith grants OpCo a 25-year lease to use his land, at no cost.

- Sonny sells the land, with the lease intact, at a substantial loss – of which $80,000 is attributable to the continuing existence of the lease.

Sonny cannot claim the loss attributable to the continuing existence of the lease

Next steps:

- General value shifting regime
  - overview of provisions
  - comprehensive guide

- Go to the 'General value shifting regime' homepage

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Guide to the general value shifting regime

Use this guide to understand the regime and the circumstances where it is relevant.

20 July 2017

The *Guide to the general value shifting regime* comprehensively explains:

- the key features of the regime (including the exclusions and safe harbours)
- the circumstances where it is relevant.

Worked examples are provided to illustrate the rules of the regime in operation.

Before deciding to download the *Guide to the general value shifting regime*

- **determine whether the regime may apply to your situation** or
- **read an overview of the regime** which contains introductory information about the key features of the regime and a summary of its components.

Next steps

- Download the Guide to the general value shifting regime (PDF, 1.13MB)
- **Browse ATO Legal Database information relevant to the regime**
- Go to the **General value shifting regime** homepage

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General value shifting regime – rulings, law and objections

The primary legislative references and extrinsic material relating to the general value shifting regime.

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The ATO Legal Database provides access to legal and policy information used by the ATO to make decisions.

The information below contains links to relevant general value shifting regime (GVSR) information located on the ATO Legal Database.

Legislation and supporting material

Primary legislative references

- Division 723 of the Income Tax Assessment Act 1997
- Division 725 of the Income Tax Assessment Act 1997
- Division 727 of the Income Tax Assessment Act 1997
- Schedule 15 of the New Business Tax System (Consolidation, Value Shifting, Demergers and Other Measures) Act 2002)
  - introduce a GVSR that replaces former value shifting provisions.

The GVSR covers three categories of value shifting:

1. Direct value shifts through creation of rights over non-depreciating assets.
2. Direct value shifts of equity or loan interests in a single company or trust.
3. Indirect value shifts of equity or loan interests in companies and trusts not dealing with each other at arm's length.

See also:

- Chapters 7 to 12 and chapter 14 of the revised explanatory memorandum that accompanied the legislation.

Consolidation interactions

- Subdivision 715-G of the Income Tax Assessment Act 1997
- Subdivision 715-H of the Income Tax Assessment Act 1997
- 719-T of the Income Tax Assessment Act 1997
- Schedule 7 of the New Business Tax System (Consolidation and Other Measures) Act 2003
  - ensure that the GVSR applies in an appropriate way for consolidated groups and multiple entry consolidated (MEC) groups, and
  - provide rules to preserve the integrity of the indirect value shifting rules (and the loss integrity rules) where it is unrealistic for those provisions to apply in the consolidation environment (loss reduction method).

See also:

- Chapter 11 of the explanatory memorandum that accompanied the legislation.

Transitional relief

Schedule 2 of the Taxation Laws Amendment Act (No. 2) 2004 modifies the application of the indirect value shifting rules to exclude most services related value shifts during the consolidation transitional period.

See also:

- Chapter 2 of the explanatory memorandum accompanying the legislation.

ATO interpretative decisions

An ATO interpretative decision (ATO ID) is a summary of a decision on an interpretative issue and is indicative of our view on the interpretation of the law on that particular issue.

ATO IDs are produced to help ATO officers apply the law consistently and accurately to particular situations.

Next steps:

- Read a comprehensive Guide to the general value shifting regime
- Learn more about the ATO Legal Database
- Visit the 'General value shifting regime' homepage

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