FSC Guidance Note No. 31

Provisioning for Deferred Tax Assets

19 December 2012

Purpose of this Guidance Note:	To provide industry participants with guidance in the provisioning for deferred tax assets within the valuation of scheme assets supporting the calculation of unit prices.
Date of this version:	19 December 2012
History (prior versions) of this Guidance Note:	No prior versions.

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1 Title

1.1 This Guidance Note may be cited as FSC Guidance Note No. 31 *Provisioning for Deferred Tax Assets*.

2 Date of Issue

2.1 This Guidance Note was issued on 19 December 2012.

3 Application

3.1 This Guidance Note was prepared by the FSC Unit Pricing Working Group. This Guidance Note is to be used by Scheme Operators when formulating and applying a policy for the treatment of Deferred Tax Assets (**DTA**). This Guidance Note will have specific application when calculating the DTA for unit pricing purposes.

3.2 This Guidance Note applies to:

- Open ended Schemes that allow investors to transact on a regular basis.
- Closed ended Schemes (where investors cannot transact at regular intervals). However, for these Schemes the principles only apply at points when investors can enter or exit the scheme.

This Guidance Note does not apply to listed Schemes.

3.3 When formulating a policy, the Scheme Operator should also refer to FSC Standard No. 8 *Scheme Pricing* and FSC Standard No. 9 *Valuation of Scheme Assets and Liabilities*. Scheme Operators should also have regard to any applicable regulatory guidance such as the ASIC/APRA *Unit pricing: Guide to good practice* (being ASIC Regulatory Guide 94).

3.4 The interpretation contained within this Guidance Note does not take into account every specific unit pricing circumstance, and hence consideration should be given to each specific situation. In particular, consideration should be given to the Scheme's constituent documents (*including* the constitution, trust deed and governing rules of the Scheme), and any legislative, regulatory and other applicable obligations or guidelines applicable to the Scheme Operator.

3.5 Users must take their own advice and consider their own circumstances. Users of this Guidance Note (including Scheme Operators) should not rely solely on this Guidance Note without also assessing the particular factual circumstances applicable to their situation, and also obtaining appropriate advice specific to their circumstances. This document does not constitute any form of advice (including taxation, legal, actuarial, accounting or other advice) and should not be relied upon as such. Users of this document (including Scheme Operators) should take their own advice on legal, taxation, accounting, actuarial, regulatory, and any other relevant matters as appropriate in relation to unit pricing and other matters.

4 Statement of Purpose

4.1 The main features and purpose of this Guidance Note are to:

- specify the principles to be applied by Scheme Operators when formulating a policy relating to the calculation of DTAs;
- provide indicative examples to assist the interpretation and application of these principles; and
- assist in the standardisation of the practices and procedures in respect of the principles to be applied in the calculation of DTAs for unit pricing purposes.

5 Definitions

5.1 **Capital assets** – assets, the gains and losses from which, are determined and assessable under the capital gains provisions of the *Income Tax Assessment Act 1936* (Cth) or the *Income Tax Assessment Act 1997* (Cth). The gain may be subject to discounting depending on the type of entity receiving the gain. For example a Superannuation Fund, Pooled Superannuation Trust (**PST**) or Virtual PST (**VPST**) of a Life Company, receive a one-third discount on the net capital gain amount for assets held for more than 12 months. Where there is a net capital loss amount this cannot be claimed as a deduction in the current year and must be carried forward to offset against future capital gains.

5.2 **Carried forward realised capital losses** – the sum of realised capital losses from prior tax periods which may be utilised to offset current and future year realised capital gains.

5.3 **Carried forward revenue losses** – the sum of revenue losses from prior tax periods which may be utilised to offset current and future year income and revenue gains.

5.4 **Deferred Tax Asset (DTA)** - represents the present value of future tax benefits arising from the carrying of revenue losses and/or capital losses within a Scheme which pays tax on behalf of Investors.

5.5 **Deferred Tax Liabilities (DTL)** – the value assigned to tax liabilities expected to arise in future tax years associated with unrealised revenue and capital gains.

5.6 **DTA Provision** - the value of DTA included within Scheme pricing after the allowance for any impairment e.g. after application of a DTA cap.

5.7 **DTA Provisioning rate** – the rate applied to revenue/capital losses when calculating DTA. This rate may include a discount to reflect the time value of money associated with the benefit arising in the future.

5.8 **Effective tax cost** – the cost of assets determined in accordance with Australian Tax legislation.

5.9 **Growth Assets** – assets which have the capacity to generate future capital and revenue gains which may be utilised to offset losses underpinning a DTA provision.

5.10 **Investment Pool** – a portfolio of investment assets representing the interests of a distinct group of investors held within a common taxpaying entity.

5.11 **Loss Trading** – the transfer of net revenue/capital losses between constituent investment pools within a common tax-paying entity in exchange for assets.

5.12 **Net capital losses** – the sum of:
- Realised capital losses;
- Unrealised es; and
- Carried forward realised capital losses.

5.13 **Net revenue losses** – the sum of:
- Realised revenue losses;
- Unrealised revenue losses; and
- Carried forward revenue losses.

5.14 **Realised capital losses (gains)** – the difference between the effective tax cost of capital assets sold in the current tax year less the proceeds received.

5.15 **Realised revenue losses (gains)** – the difference between the effective tax cost and proceeds for revenue assets which have been disposed of in the current tax year.

5.16 **Revenue account** – assets that are assessed for tax purposes as being on revenue account for Australian tax purposes and accordingly derived as ordinary income by the legal entity. A realised revenue gain is fully assessable within the year the gain is incurred; similarly a realised revenue loss is able to be claimed as a full deduction (against revenue income) within the year it is incurred or rolled forward in the case of net revenue losses.

5.17 **Unrealised capital losses (gains)** – difference between the effective tax cost of capital assets less their current redeemable value.

5.18 **Unrealised revenue losses (gains)** – the difference between the effective tax cost and the current redeemable value of revenue assets.

5.19 Unless the context requires otherwise, other terms defined in **FSC Guidance Note 5** *Industry Definitions* have the same meaning in this Guidance Note.

6 Background

6.1 Section 5.2 of the ASIC/APRA *Unit Pricing: Guide to Good Practice*[1] (the "**APRA/ASIC Unit Pricing Guide**") states (at page 64):

> ***"Treatment of deferred tax assets (future income tax benefits – FITBs)***
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> *Funds may have actual or net unrealised tax losses that can be carried forward as deferred tax assets or future income tax benefits (FITBs). These FITBs are available to offset future capital gains tax liabilities or future unrealised gains. FITBs may also be written off – for example, if market movements mean they are unlikely to be realised. Issues arise relating to the amount of FITBs that can be recognised, and the circumstances in which FITBs can be recognised.*

[1] The ASIC/APRA *Unit pricing: Guide to good practice* is ASIC Regulatory Guide 94.

Our unit pricing survey showed a range of practice in recognising FITBs. Our review also found that where a view has been formed that the deferred tax benefits have been overstated, FITBs may not have been reduced to an appropriate level."

At page 68, the APRA/ASIC Unit Pricing Guide states:

"FITBs should be included in unit prices to the extent that they have value for present or future unit holders, taking into account the circumstances of the fund, the governing documentation, possible events, the likelihood and timing of those events, and your approach to discounting to allow for the time value of money. The value of FITBs included in unit prices should be systematically reviewed to help achieve equity between investors and to minimise price discontinuities in unit prices.

We would not expect to see a tax policy that always, or never, recognises FITBs. It is reasonable to consider capping the amount of FITBs included in unit prices.

For these and other reasons, the amount of FITBs included in unit prices may not match the amount of FITBs reported in financial statements. Depending on the size or the reasons for the difference, differences may need to be explained in the financial statements.

When determining the amount of FITBs in unit prices and any cap on FITBs, factors you should consider may include, but are not limited to:

- *the level of unrealised gains/losses*
- *expectations of market movements and their likely volatility*
- *the investment timeframe*
- *likely investment inflows and outflows for the fund*
- *the extent to which FITBs in one pool can be applied against gains elsewhere in the same entity or consolidated entity*
- *the applicable tax rate*
- *exposure of the fund to possible significant redemptions, and*
- *marked change in the circumstances of your product."*

6.2 Section 9.2 of FSC Standard 8 – *Scheme Pricing* dated October 2006 states as one of the principles of unit pricing:

"An equitable unit pricing process that treats all types of investor including different classes of investors fairly, and does not favour:

- *transacting or non-transacting investors;*
- *current or future generations of investors; and*
- *different classes of investor (where applicable)."*

7 Guidance

7.1 Scheme Operators should set in place policies to ensure that investor interests are equitably managed where a Scheme is carrying net revenue losses and/or capital losses which may be utilised in future periods to offset tax liabilities from future earnings of the Scheme.

7.2 Each time unit prices are calculated (for the purposes of processing unitholder transactions) the DTA Provision should be consistent with these policies and the calculation should provide for equitable treatment of investors.

The policies should recognise the respective interests of current and future Investors within the Scheme by taking into account the:

- respective interests of investors in constituent investment pools within a common tax-paying entity;
- likelihood of the Scheme generating future tax savings for losses held; and
- expected timeframe in securing these benefits.

7.3 Satisfying the above requirements does not necessarily always require, for each unit pricing cycle, a highly detailed analysis to determine the DTA Provision (for example approaches which incorporate detailed information in relation to each asset's market value and effective tax cost). Nonetheless, the Scheme Operator must be satisfied that where approximate approaches are adopted to derive the DTA Provision, that they produce reasonable estimates. Any approximate approaches, for example which may be applied on a daily basis, should be supported by adequate monitoring and reporting processes, including more detailed analysis performed periodically.

7.4 The policies, processes and procedures should be tailored to the specific circumstances of each Scheme Operator. Nonetheless, monthly is the minimum acceptable frequency for undertaking a reasonable analysis which considers revenue and capital gains/losses, potential DTA calculations and adjustments for the DTA Provision.

7.5 However, where DTA values and assessments of recoverability are subject to sudden change, for example in the case of large market movements and/or cashflows, immediate changes/action may be required, rather than waiting until the next scheduled periodic analysis.

7.6 The DTA policies and supporting procedures should be reviewed regularly to ensure that all assumptions underpinning the calculation remain valid.

7.7 The Scheme Operator must recognise that judgement needs to be exercised when determining DTA Provisions.

As such, models and processes (and assumptions underlying them) used to determine the DTA Provision should be reviewed and monitored regularly. By way of example, where market conditions improve, the Scheme Operator will need to consider whether or not any DTA Provision ought to be increased or otherwise amended in light of the change in market

conditions, and also having regard to all other relevant factors in determining the DTA Provision (including, without limitation, the factors set out in paragraph 6.1 of this Guidance Note, which refers to non-exhaustive factors set out in the ASIC/APRA Unit Pricing Guide).

7.8 The Scheme Operator should ensure that where a material application or redemption is received, that processes are in place to ensure the interests of non-transacting investors are not materially impacted as a result of the use of a DTA Provision within the calculation of the entry or exit value.

7.9 The Scheme Operator should ensure that Loss Trading occurs on a basis that treats investors equitably. This principle is also to be applied when establishing DTA Provisions and impairment amounts at the time of a successor fund transfer where roll over relief is available.[2]

8 Examples of Current Practice

8.1 *Calculation of DTAs*

8.1.1 The level of detail at which the DTA Provision is calculated varies between Scheme Operators reflecting differing operational capability in the systems and processes supporting the calculation of tax provisions utilised within unit prices. An increasing proportion of operators are calculating and making adjustments to DTA Provisions on a daily basis to mitigate the risks associated with the coincidence of volatile markets and the growing propensity of investors to switch between constituent pools within Schemes.

8.1.2 Many Scheme Operators conduct reasonably detailed calculations and adjustments to set the DTA Provision on a weekly or monthly basis with a small number reviewing positions less frequently. In these cases, estimates are often utilised to allow for changes in assets values between these dates. These estimates typically adjust the last available DTA calculation by a fixed proportion of an observable proxy such as accounting income.

8.1.3 DTAs are usually calculated for investment pools supporting superannuation products held within superannuation funds, PSTs and after tax investment products issued by Life Companies. These investment pools may be either unitised or have a crediting rate applied.

8.1.4 Superannuation products are currently subject to a 15% tax rate applied on both capital and revenue gains whilst a tax rate of 30% is applied to ordinary class life insurance policies. Superannuation products may also obtain the benefit of a one-third discount on capital gains if the assets are held for more than 12 months, and other legislative requirements are met.

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[2] For example, where Life Companies merge in accordance with Part IX of the *Life Insurance Act 1995* (Cth).

8.1.5 Therefore Scheme Operators normally calculate DTA and DTL utilising a DTA Provisioning Rate of between 10% and 15% for superannuation products and 30% for ordinary class life insurance policies.

8.1.6 The DTA Provisioning Rate may include (either implicitly or explicitly in its derivation) an allowance for the impact of the time value of money between the point of calculation and the expected future date when tax payments are made (or in the case of DTAs when losses are offset against future gains). Discounting has become less common as it increases the complexity of reconciling DTAs and DTLs used in unit pricing to those used in the preparation of financial accounts where discounting of DTLs or DTAs is not permissible under current Accounting Standards[3]. Nonetheless, if Scheme Operators do not include an allowance for time value of money discounting, they should be satisfied that this does not materially impact unitholder equity and that such an approach is permitted (e.g. that there are no requirements in constituent documents to adopt time value of money discounting).

8.1.7 One example of how DTA Provisions are calculated is to apply the DTA Provisioning Rate to the net capital/revenue losses, and then incorporate adjustments for risks of recoverability (i.e. the risk that insufficient capital gains/income will be made to realise the value of the net capital/revenue losses).

8.2 *Policy Setting*

8.2.1 Scheme Operators normally utilise a unit pricing and tax provisioning policy. These policies would include guidance as to the calculation of DTAs and management of risks associated with them.

8.2.2 Such policies would normally include reference to the:

- Allocation of responsibility for the calculation of tax provisions, including DTAs.
- Frequency of calculations.
- Calculation basis for DTAs.
- Process for assessing risks associated with DTAs, including monitoring changes which may require a revision to any impairment of DTA Provision values.
- Processing of material applications and redemptions, and the impact on DTAs, DTLs and the equitable allocation of DTAs and DTLs between transacting and non-transacting investors.

8.3 *Management of Risks*

[3] Refer AASB 112.

8.3.1 DTA Provisions represent an assessed current value of a future tax benefit. Therefore there are a number of assumptions underpinning this value including:

- The Scheme is a going concern.
- The Scheme will be able to generate sufficient capital and revenue gains/income to offset carried forward and unrealised losses held.
- There will be no material change to the taxation treatment utilised in determining current positions.
- The timeframe in which net capital/revenue losses held by the tax entity are likely to be offset by future gains/revenue.

8.3.2 Changes to Scheme circumstances and outlook may materially impact the assessed present value of future tax benefits, and the appropriate value for the DTA Provision. As such, Scheme Operators periodically reassess the validity of the assumptions and the analysis for evaluating the likelihood that sufficient capital gains/income will be made to realise the value of the net capital/revenue losses.

8.3.3 This analysis includes assessment of factors such as:

- Projected unit-holder contributions (or withdrawals).
- Expected capital growth rates and volatilities.
- Proportion of growth assets held within the Scheme.
- Proportion of members moving from Accumulation to Pension stages in coming years.
- Concentration of Scheme holdings by single investors and dealer groups.

8.3.4 Utilising this information the Scheme Operator would then determine, if appropriate, an impairment factor e.g. a DTA cap. Impairment factors may be applied at the tax-paying entity level and (or) specific constituent pool level.

8.3.5 Common methods of applying impairment factors are: (1) reductions in the DTA Provisioning Rates and (2) capping DTAs.

8.3.6 A key risk associated with carrying DTAs is failing to apply impairment factors on a timely basis. Therefore, it is not uncommon for Scheme operators to utilise unit pricing systems which automatically update DTA values and apply impairment factors. Nonetheless, as noted in sections 7.3 to 7.5 Scheme operators should be aware of the limitations of any automatically applied impairment calculations which are approximate and the need to undertake further detailed analysis in certain circumstances.

8.3.7 DTA caps are most commonly applied as a percentage of growth assets held by the tax-paying entity and/or constituent pool. This approach has the benefit of the cap resetting in line with changes in the value of Scheme assets held, thereby making it relatively easy to implement.

8.4 *Factors to consider when electing to apply entity or constituent pool DTA caps*

8.4.1 When applying a tax-paying entity level DTA cap, an allocation of the value available under the cap needs to be made to individual constituent investment pools.

8.4.2 However, the tax law does not recognise distinctions between constituent pools within the tax entity and, as such, DTA recoverability depends on the future gains of the tax entity in total. Therefore, an approach too heavily focused on constituent pool analysis may fail to appropriately recognise opportunities to realise the tax value of losses in one constituent pool by setting those losses against gains in others.

8.4.3 (FSC acknowledges that the following section is substantially identical to that contained in an Information Note previously issued by the Institute of Actuaries of Australia (IAA). FSC acknowledges the IAA albeit FSC accepts full responsibility for this Guidance Note[4]). On the other hand, various issues may be involved when setting high DTA levels at the individual constituent pool level, even when the DTA does not seem unreasonable based on high level analysis at the overall tax entity level. These issues include:

a) **discounting for time value of money** – as noted above, the DTA is a non income producing asset. There may be circumstances where an undiscounted DTA provision is considered reasonable at the overall fund level, but where time value of money impacts are significant for constituent pools where the DTA is large;

b) **asset mix** – where holding a DTA results in reduced exposure to investments it can dilute the earnings of a constituent pool. Where such impacts are considered likely to be material, management may consider taking action, for example through the use of other funds available within the complying superannuation/ FHSA asset pool/ superannuation fund/ PST, or by investing in derivatives. However, such actions must take into account the interests of all unitholders and be permitted under law;

c) **other constraints** – some funds may specify in their PDS that the level of cash and other assets will not exceed a certain level. This may represent an additional constraint for the manager to consider when setting the DTA. Managers that do not monitor or automatically cap on a daily basis may decide to cap the DTA at a lower level to avoid temporary increases in the DTA between formal reviews resulting in investment guideline breaches;

d) **exposure to risk** – as the DTA is a contingent asset dependent upon future experience, any point in time assessment of the DTA cap/value used for unit pricing may need updating as future experience emerges;

e) **write down impacts** - Where an individual constituent pool has a large DTA, the unitholders' exposure to significant write downs may represent a risk that they were not expecting and/or were not notified of when they invested in the product. This may be the case even where the assessed value at the time of setting the DTA was reasonable. This may increase

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[4] See Institute of Actuaries of Australia: *Information Note: Deferred Tax Assets – Issues and Considerations for Life Insurance Companies and Superannuation Funds (June 2010)*.

the importance of the DTA capping/valuation analysis, as well as the level and frequency of monitoring; and

f) **fund level versus investment option level materiality** - Related to the above point on exposure to risk of DTA write downs, is the point that small differences in fund level caps can result in more material differences at the investment option level. This may increase the ***importance of regularly reviewing*** the appropriateness of the DTA capping/valuation analysis, as well as the level and frequency of monitoring.

8.5 *Illustrative Example*

8.5.1 Below is provided a fund scenario designed to assist in highlighting some of the issues noted in the above section.

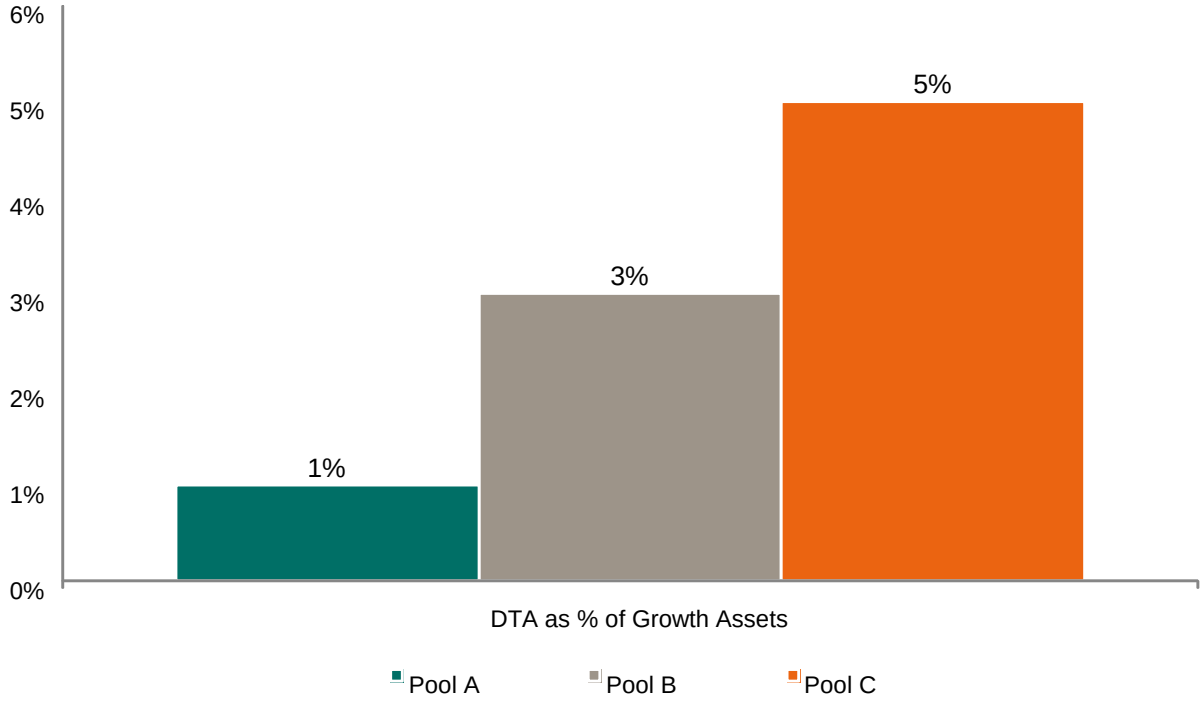
8.5.2 The working calculations for the worked example below in this section 8.5 are set out in **Appendix 1** to this Guidance Note. Each calculation is referenced with a "1", "2" or "3" etc, which refers to the Endnotes in the Appendix to this Guidance Note.

Consider *Superannuation Fund which consists of four investment pools. Each pool has investment assets totalling $500,000 of which three are fully invested in growth assets and the fourth holds a mixture of bonds and cash.*

The three pools which are invested in growth assets are carrying net capital losses totalling $450,000, split as follows: Pool A - $50,000, Pool B - $150,000 and Pool C - $250,000.

The fund utilises a DTA provisioning rate of 10% resulting in a total DTA of $45,000 or 3%[1] of growth assets at the Fund level and 1%[1], 3%[1] and 5%[1] for Pools A, B and C respectively.

The DTA amounts (before impairment) are represented in the graph below.



If the Scheme operator applied an investment option level cap, of say 3%, only Pool C would have an impairment applied to its DTA (of about 2% of its NAV).

Care should be taken that this option level capping is fair to all options, taking into account all relevant factors, including that future capital gains from assets supporting Pool A and Pool B may assist in realising the value of the DTA within Pool C (this may occur after they have generated sufficient gains to realise the value of their own DTA).

This example highlights the issue noted above at 8.4.2 that an approach too heavily focused on constituent pool analysis may fail to appropriately recognise opportunities to realise the tax value of net capital losses in one constituent pool by setting those losses against capital gains in others.

On the other hand if the Scheme operator applied a fund level cap, of say 3%, then no Pool would have an impairment applied to its DTA. Consequently Pool C would have a full DTA of 5%.

This example highlights the issues noted at 8.4.3 that within a fund level cap individual investment options can have significantly higher caps, potentially impacting their asset allocation and potential exposure to risk if DTAs, at some stage in the future, ultimately are impaired.

For both capping approaches it is possible to envisage other examples in which the impacts are much greater than those illustrated (e.g. an individual option having a DTA Provision much larger than 5% where a fund applies an entity level cap without considering the DTA at an option level).

8.6 *Issues to be considered when applying DTA caps*

8.6.1 The issues associated with the use of DTA caps include:

- The performance of an investment option may materially differ depending on whether the cap has been breached.

  Under the investment option capping example in section 8.5.2, if the return on investment assets for Pools A and C equals 5% and the investment pool level DTA cap is set to 3% of growth assets. Whilst the return on underlying assets is equal for each pool the unit price return of Pool A is 4.56%[2] whilst the return of Pool C is 5%[3]. The difference in return is attributable to Pool A having its investment asset return offset by a reduction in the DTA provision of $2,500 whilst the DTA provision in Pool C actually rises by $750 (3% of the change in value of investment assets).

- Once the cap is breached then the performance of the investment pool is also impacted by investors applying and redeeming units as the DTA provision is linked to the value of growth assets held by the investment pool.

  Under the investment option capping example in section 8.5.2, suppose that the investment return is zero for the period but members switch $50,000 from Pools A and C to a fourth Pool which invests in Bonds and Cash. In this case the unit price return of Pool A is zero but the return for Pool C is -0.32%[4] due to the impact of the DTA cap. The impact on Pool C is attributable to switching members withdrawing $50,000 of investment assets which includes a payment of $1,500 for the DTA value which was included within their exit price. The non-transacting members effectively fund an increased proportionate interest in DTA. However, because of the reduction in overall growth assets, this increase in DTA is impaired (its value is not recognised in the unit price immediately) and the unit price falls.

8.7 *Risks associated with material investor applications and redemptions*

8.7.1 Scheme Operators need to also deal with the risks associated with the processing of material redemptions arising from either a single investor or group of investors. Such redemptions result in potential funding and equity issues as the exiting investor receives cash in exchange for their interest in DTAs. Normally the Scheme funds the redemption thereby increasing the proportional value of the DTA provision held by non-transacting investors, if scope remains under the DTA cap, which may dilute future performance (as the DTA provision increases as a portion of Net Asset Value). Where the redemption results in the DTA cap being breached or if the cap has already been breached, then a number of Scheme Operators discount the DTA provision applied when calculating a price to process the material redemption. This discount effectively compensates non-transacting investors and assists in mitigating any last man standing issues.

8.7.2 Conversely, where a material application occurs for an investment option which has previously breached its DTA cap, the cash in-flow (from the application) raises the DTA cap thereby releasing additional value in the form of a larger DTA Provision being applied. The Scheme Operator must consider the allocation of this benefit between existing investors and the new investor. Where the DTA Cap is linked to the value of growth assets and no adjustment is made, then both the new and existing investors will equally share the benefit

through an increase in subsequent unit prices. The Scheme Operator may alter the entry price to reallocate all or a larger portion of this released DTA to existing investors based on their assessment of the position of both parties. This assessment should consider whether the material cashflow decreases the risks borne by existing investors and therefore warrants a portion of the benefit accruing to the new investor.

8.8 *Transferring of losses between constituent pools where permitted*

8.8.1 Revenue and capital losses are generated by the disposal of assets within specific pools. These pools in turn may form part of a common tax-paying entity.

8.8.2 The utilisation of these losses to offset gains for tax purposes may occur at the tax-entity level. Therefore Scheme Operators normally optimise the use of these losses at the tax-payer level.

8.8.3 This optimisation therefore results in the use of Loss Trading (i.e. the transfer of losses where permitted by law) between constituent investment pools where the losses of one pool are used to offset the gains of another. This practice is limited to realised losses and gains (including distributed gains from trust holdings), with the netting off of tax events at the tax-paying entity level. The resulting benefits of such netting are then equitably allocated to the constituent investment pools.

Appendix 1 – Supporting Calculations for examples included in Sections 8.5 and 8.6

[1] DTA equals 10% of losses totalling $450,000 or $45,000. Total growth assets across Pools A, B and C equal $1,500,000 hence a DTA position total of 3% ($45,000/$1,500,000). Pool A has a DTA position of $5,000 with growth assets of $500,000 or 1%. Pool B has a DTA position of $15,000 with growth assets of $500,000 or 3%. Pool C has a DTA position of $25,000 with growth assets of $500,000 or 5%.

[2] The Net Asset Value of Pool A was previously equal to $505,000, consisting of $500,000 investment assets and a DTA provision of $5,000 (10% of losses totalling $50,000). The value of investment assets rise to $525,000 (5% return). This results in total losses falling to $25,000 and the corresponding DTA provision falling to $2,500. Therefore the Net Asset Value in the next period equals $527,500 (assets of $525,000 plus DTA provision of $2,500). The resulting change in NAV prices is 4.56% ($527,500/$505,000 -1) which equates to an effective tax rate of 10% after allowance for the performance dilution resulting from carrying the DTA provision as a non performing asset.

[3] The Net Asset Value of Pool C is previously equal to $515,000, consisting of $500,000 investment assets and an impaired DTA provision of $15,000 (lesser of 3% of growth assets or 10% of losses totalling $250,000). The value of investment assets rise to $525,000 (5% return). This results in total losses falling to $225,000 and the corresponding DTA provision rises to $15,750 (lesser of 3% of growth assets $525,000 or 10% of losses totalling $225,000). Therefore the Net Asset Value in the next period equals $540,750 (assets of $525,000 plus DTA provision of $15,750). The resulting change in NAV price is 5% ($540,750/$515,000 -1).

[4] Members withdraw $50,000 using the unit price for the previous period. As there has been no change in the market value of investment assets then the closing value is $450,000 for both pools A and C. If we assume that the realisation of investment assets merely results in the associated loss moving from unrealised to realised then the DTA position of Pool A remains at $5,000. The Net Asset Value of Pool A therefore remains at $455,000 after processing the redemption. Whereas the situation for Pool C is different due to the operation of the DTA Cap. For Pool C the value of the DTA cap becomes $13,500 (3% of $450,000). Therefore the Net Asset Value becomes $463,500 (investment assets of $450,000 plus impaired DTA provision of $13,500). The price return therefore is -0.32% ($463,500 / $465,000) where the previous net asset value equals investment assets of $450,000 and DTA provision of $15,000.