


TD 2004/49 - Income tax: consolidation: capital gains: does the single entity rule in section 701-1 of the Income Tax Assessment Act 1997 apply in determining whether the consequences in Subdivision 125-C of the Income Tax Assessment Act 1997 apply to the head company of a consolidated group where one or more subsidiary members hold ownership interests in an entity outside the group that is being demerged?

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Taxation Determination

Income tax: consolidation: capital gains: does the single entity rule in section 701-1 of the *Income Tax Assessment Act 1997* apply in determining whether the consequences in Subdivision 125-C of the *Income Tax Assessment Act 1997* apply to the head company of a consolidated group where one or more subsidiary members hold ownership interests in an entity outside the group that is being demerged?

Preamble

*The number, subject heading, date of effect and paragraphs 1 to 6 of this document are a 'public ruling' for the purposes of Part IVA of the **Taxation Administration Act 1953** and are legally binding on the Commissioner.*

1. Yes. The single entity rule in section 701-1 of the *Income Tax Assessment Act 1997* (ITAA 1997) has effect in determining whether Subdivision 125-C of the ITAA 1997 applies to a capital gain or capital loss made by the head company of the consolidated group from a CGT event happening to the subsidiary members' ownership interests in the entity being demerged (the 'demerged entity').
2. Division 125 of the ITAA 1997 provides CGT relief to entities involved in a demerger. Subdivision 125-C of the ITAA 1997 deals with the CGT consequences for entities that are members of the demerger group, including the disregarding of capital gains or capital losses made by demerging entities when certain CGT events happen to their ownership interests in the demerged entity. Subdivision 125-C relies on a number of concepts – *demerger*, *demerger group* and *demerging entity* – the meanings of which are established in Subdivision 125-B of the ITAA 1997.
3. In cases where the subsidiary members of a consolidated group hold ownership interests in a demerged entity outside of the group, the application of the demerger relief provisions in Division 125 of the ITAA 1997 will be affected by the single entity rule.
4. The single entity rule in section 701-1 of the ITAA 1997 treats subsidiary members of a consolidated group as parts of the head company, rather than separate entities, for the group's income tax purposes. A consequence of the single entity rule is that the assets and liabilities of the subsidiary members are treated as if they were assets and liabilities of the head company.

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5. In applying Subdivision 125-C of the ITAA 1997, the head company of the consolidated group will be taken to hold the subsidiary members' ownership interests in the demerged entity.

6. The operation of the single entity rule would extend to the definitions of *demerger group*, *demerger* and *demerging entity* in Subdivision 125-B of the ITAA 1997, but only for the purposes of establishing the head company's compliance with the demerger relief provisions in Subdivision 125-C of the ITAA 1997.

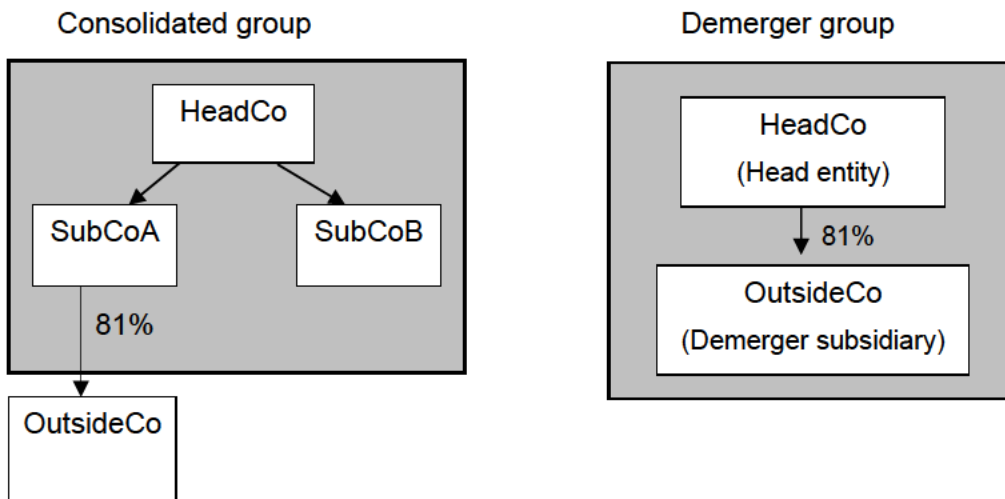
Note: The single entity rule has no application in determining the eligibility of non-members of the consolidated group (for example, shareholders of the head company) for demerger relief.

Example

7. *HeadCo is the head company of a consolidated group. The subsidiary members of the consolidated group include two Australian resident companies, SubCoA and SubCoB each of which is wholly owned by HeadCo.*

8. *SubCoA owns 81% of the ownership interests in OutsideCo. The remaining shares are held by various entities outside the consolidated group.*

9. *In December 2003, SubCoA demerges all of its interests in OutsideCo. Under the restructure, SubCoA's ownership interests in OutsideCo are transferred to HeadCo's shareholders, in proportion to their existing shareholding in the head company.*



10. *Under the single entity rule, HeadCo is taken to be the owner of SubCoA's shares in OutsideCo. In this case it is considered that HeadCo and OutsideCo have formed a **demerger group** within the meaning of the term in subsection 125-65(1) of the ITAA 1997. HeadCo is the head entity as no other member of the group owns ownership interests in it: subsection 125-65(3) of the ITAA 1997. OutsideCo is a demerger subsidiary of HeadCo which, by virtue of the single entity rule, has the right to receive more than 20% of any distribution of income or capital by the company: subsection 125-65(6) of the ITAA 1997.*

11. *HeadCo would also meet the requirements of a **demerging entity** under subsection 125-70(7) of the ITAA 1997 as:*

- *it is a member of a demerger group just before the relevant CGT event happens to the ownership interest in OutsideCo, and*
- *by virtue of the single entity rule, HeadCo is taken to have disposed of at least 80% of its ownership interests in OutsideCo to its own shareholders under the demerger.*

12. *As HeadCo is a demerging entity and the restructure of OutsideCo satisfies the requirements of a demerger, a capital gain or capital loss made by HeadCo from CGT event A1 happening to the transfer of interests in OutsideCo will be disregarded under section 125-155 of the ITAA 1997.*

Date of effect

13. This Determination applies to years commencing both before and after its date of issue. However, it does not apply to taxpayers to the extent that it conflicts with the terms of settlement of a dispute agreed to before the date of the Determination (see paragraphs 21 and 22 of Taxation Ruling TR 92/20).

Commissioner of Taxation

6 October 2004

Previous draft:

TD 2004/D19

- single entity rule

Related Rulings/Determinations:

TR 92/20

Legislative references:

- TAA 1953 Pt IVAAA
 - ITAA 1997 Div 125
 - ITAA 1997 Subdiv 125-B
 - ITAA 1997 125-65(1)
 - ITAA 1997 125-65(3)
 - ITAA 1997 125-65(6)
 - ITAA 1997 125-70(7)
 - ITAA 1997 Subdiv 125-C
 - ITAA 1997 125-155
 - ITAA 1997 701-1

Subject references:

- capital gains tax
 - CGT exemptions
 - consolidation
 - consolidation – capital gains tax
 - demerger
 - demerger group
 - demerger subsidiary
 - head entity

ATO references

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