TD 2006/71 - Income tax: capital gains: small business concessions: is the part of a payment which is a small business 50% reduction amount a non-assessable part under CGT event E4 in section 104-70 of the Income Tax Assessment Act 1997?

Taxation Determination

Income tax: capital gains: small business concessions: is the part of a payment which is a small business 50% reduction amount a non-assessable part under CGT event E4 in section 104-70 of the *Income Tax Assessment Act 1997*?

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This publication (excluding appendixes) is a public ruling for the purposes of the *Taxation Administration Act 1953*. A public ruling is an expression of the Commissioner's opinion about the way in which a relevant provision applies, or would apply, to entities generally or to a class of entities in relation to a particular scheme or a class of schemes. If you rely on this ruling, we must apply the law to you in the way set out in the ruling (unless we are satisfied that the ruling is incorrect and disadvantages you, in which case we may apply the law in a way that is more favourable for you – provided we are not prevented from doing so by a time limit imposed by the law). You will be protected from having to pay any underpaid tax, penalty or interest in respect of the matters covered by this ruling if it turns out that it does not correctly state how the relevant provision applies to you.

Ruling

1. Yes. The part of a payment which is a small business 50% reduction amount is a non-assessable part under CGT event E4 in section 104-70 of the *Income Tax Assessment Act 1997* (ITAA 1997).[1]

Example 1

2. *The Trustee of the Gillies Family Unit Trust carries on a business. All of the trust's assets have always been active assets. Gilbert and the only other beneficiary have each owned one unit in the trust for ten years (so they are both controlling individuals). The sum of net assets of Gilbert, the trust and any other relevant entities does not exceed $5 million. The trustee makes a capital gain of $4,000 (capital proceeds $9,000 less cost base $5,000) from the disposal of an active asset owned for eight months. The trust satisfies the conditions for the small business 50% active asset reduction and the gain is reduced to $2,000. The net income of the trust is $2,000. The trustee distributes the capital proceeds of $9,000 equally to Gilbert and the other beneficiary in the income year in which the capital gain is made. The tax consequences for Gilbert are:*

[1] All references are to the ITAA 1997 unless otherwise stated.

Gilbert's trust net income under section 97 of the Income Tax Assessment Act 1936 (ITAA 1936)	*$1,000*

Gilbert calculates his capital gain under Subdivision 115-C:

Gross-up trust gain under paragraph 115-215(3)(b) ($1,000 × 2)	*$2,000*
less: SB 50% reduction under paragraph 115-215(4)(b)	*$1,000*
Capital gain	*$1,000*
Gilbert's deduction under subsection 115-215(6)	*$1,000*

Gilbert calculates his non-assessable part under CGT event E4:

Payment of capital proceeds made by trustee	*$4,500*
less: trust net capital gain assessed under section 97 of the ITAA 1936	*$1,000*
Non-assessable part of payment	*$3,500*

The cost base of Gilbert's unit in the trust is $500. Since the non-assessable part of the payment is more than the cost base, Gilbert reduces the cost base of his unit to nil and makes a capital gain under CGT event E4:

Non-assessable part of payment	*$3,500*
less: cost base	*$500*
Capital gain under CGT event E4	*$3,000*

As Gilbert has owned his unit for more that 12 months he satisfies the conditions for the CGT discount. Gilbert is also eligible for the small business 50% reduction because he satisfies all the basic conditions in Subdivision 152-A (see paragraph 9 of this Determination). His CGT event E4 capital gain can be reduced to:

Capital gain under CGT event E4	*$3,000*
less: 50% CGT discount	*$1,500*
	$1,500
less: small business 50% reduction	*$750*
Reduced capital gain	*$750*

The net tax result for Gilbert is that he is taxed on a net capital gain of $1,750 ($1,000 capital gain under Subdivision 115-C plus $750 CGT event E4 capital gain).

Example 2

3. *Assume the same facts in Example 1, except that the active asset has been owned by the trust for more than 12 months and the capital gain can be reduced by the 50% CGT discount and the 50% small business reduction. The tax consequences for Gilbert are:*

Gilbert's trust net income under section 97 of the ITAA 1936	*$500*

Gilbert calculates his capital gain under Subdivision 115-C:

Gross-up trust gain under paragraph 115-215(3)(c) ($500 × 4)	*$2,000*
less: CGT discount reduction under paragraph 115-215(4)(a)	*$1,000*
	$1,000
less: SB 50% reduction under paragraph 115-215(4)(b)	*$500*
Capital gain	*$500*
Gilbert's deduction under subsection 115-215(6)	*$500*

Gilbert calculates his non-assessable part under CGT event E4:

Payment of capital proceeds made by trustee	*$4,500*
less: trust net capital gain assessed under section 97 of the ITAA 1936	*$500*
	$4,000
less: CGT discount adjustment (subsection 104-71(4) table item 1)	*$1,000*
Non-assessable part	*$3,000*

The cost base of Gilbert's unit in the trust is $500. Since the non-assessable part of the payment is more than the cost base, Gilbert reduces the cost base of his unit to nil and makes a capital gain under CGT event E4:

Non-assessable part of payment	*$3,000*
less: cost base	*$500*
Capital gain under CGT event E4	*$2,500*

Gilbert satisfies the conditions for the CGT discount. He is also eligible for the small business 50% reduction because he satisfies all the basic conditions in Subdivision 152-A (see paragraph 9 of this Determination). His CGT event E4 capital gain can be reduced to:

Capital gain under CGT event E4	*$2,500*
less: 50% CGT discount	*$1,250*
	$1,250
less: SB 50% reduction	*$625*
Reduced capital gain	*$625*

The net tax result for Gilbert is that he is taxed on a net capital gain of $1,125 ($500 capital gain under Subdivision 115-C plus $625 CGT event E4 capital gain).

Date of effect

4. This Determination applies to years commencing both before and after its date of issue. However, the Determination 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 issue of the Determination (see paragraphs 75 and 76 of Taxation Ruling TR 2006/10).

Commissioner of Taxation
15 November 2006

Appendix 1 – Explanation

This Appendix is provided as information to help you understand how the Commissioner's view has been reached. It does not form part of the binding public ruling.

Explanation

5. CGT event E4 in section 104-70 happens when the trustee of a trust makes a non-assessable payment to a beneficiary in respect of the beneficiary's unit or interest in the trust (except for CGT event A1, C2, E1, E2, E6 or E7 happening in relation to it), and some or all of the payment (the non-assessable part) is not included in the beneficiary's assessable income.

6. A non-assessable part under CGT event E4 may include amounts associated with the small business 50% reduction, frozen indexation, building allowance and accounting differences in income. Subsection 104-70(1) indicates that, in working out what part of the payment is included in your assessable income, you disregard your share of the trust's net income that is subject to the rules in subsection 115-215(3). This means you disregard the amount by which the capital gain was increased under those rules.

7. A non-assessable part excludes payments listed under section 104-71 such as the payment of a CGT discount amount (item 1 subsection 104-71(4)) and a small business 15-year exemption amount (paragraph 104-71(1)(g) and section 152-125).

8. CGT event E4 applies to reduce the cost base and reduced cost base of the beneficiary's unit or interest in the trust, but it cannot give rise to a capital loss. If the cost base is reduced to nil, a capital gain may arise (subsections 104-70(4), 104-70(5) and 104-70(6)). This gain may be reduced by applying the CGT discount and the small business 50% reduction if the relevant conditions are satisfied.

9. The small business 50% reduction may apply to the CGT event E4 capital gain if the basic conditions in Subdivision 152-A are satisfied. In particular, paragraph 152-10(1)(a) is satisfied as CGT event E4 happens in relation to the unit in the trust. The maximum net asset value test, the active asset test (incorporating the 80% test) and the additional basic conditions (controlling individual/concession stakeholder tests) in subsection 152-10(2) must also be satisfied.

Note: CGT event E4 does not happen to payments made to certain beneficiaries: see Taxation Determination TD 2003/28.

Note

10. As noted in the Treasurer's Press Release No. 38 of 2006 (9 May 2006), the Board of Taxation's report on its Post-Implementation Review of the small business CGT concessions contains a number of administrative recommendations. This Taxation Determination is part of the Commissioner's response to Recommendation 11.1 of the Board's report.

References

Previous draft:

TD 2006/D33

Related Rulings/Determinations:

TR 2006/10; TD 2003/28

Subject references:

- CGT 50% individual discount
- CGT event E1-E9 - trusts
- small business 50% reduction

Legislative references:

- ITAA 1936 97
- ITAA 1997 104-70
- ITAA 1997 104-70(1)
- ITAA 1997 104-70(4)
- ITAA 1997 104-70(5)
- ITAA 1997 104-70(6)
- ITAA 1997 104-71
- ITAA 1997 104-71(1)(g)
- ITAA 1997 104-71(4)
- ITAA 1997 Subdiv 115-C
- ITAA 1997 115-215(3)
- ITAA 1997 115-215(3)(b)
- ITAA 1997 115-215(3)(c)
- ITAA 1997 115-215(4)(a)
- ITAA 1997 115-215(4)(b)
- ITAA 1997 115-215(6)
- ITAA 1997 Subdiv 152-A
- ITAA 1997 152-10(1)(a)
- ITAA 1997 152-10(2)
- ITAA 1997 152-125
- TAA 1953

Other references:

- Treasurer's Press Release No. 38 of 2006 (9 May 2006)

ATO references

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