


***TD 2004/D19 - 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 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?***

 This cover sheet is provided for information only. It does not form part of *TD 2004/D19 - 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 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?*

This document has been finalised by TD 2004/49.



---

## Draft 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 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**

*This document is a draft for industry and professional comment. As such, it represents the preliminary, though considered views of the Australian Taxation Office. This draft may not be relied on by taxpayers and practitioners as it is not a ruling for the purposes of Part IVA of the **Taxation Administration Act 1953**. It is only final Taxation Determinations that represent authoritative statements by the Australian Taxation Office.*

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 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 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* – whose meaning is established earlier in Division 125.
3. In cases where the members of a consolidated group hold ownership interests in the demerged entity, the application of the demerger relief provisions in Division 125 of the ITAA 1997 may 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 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.

**TD 2004/D19**

5. The single entity rule would therefore apply in working out whether the CGT relief provided by Subdivision 125-C of the ITAA 1997 affects the head company's income tax liability. For these purposes, the head company of the consolidated group will therefore be taken to hold the subsidiary members' ownership interests in the demerged entity.

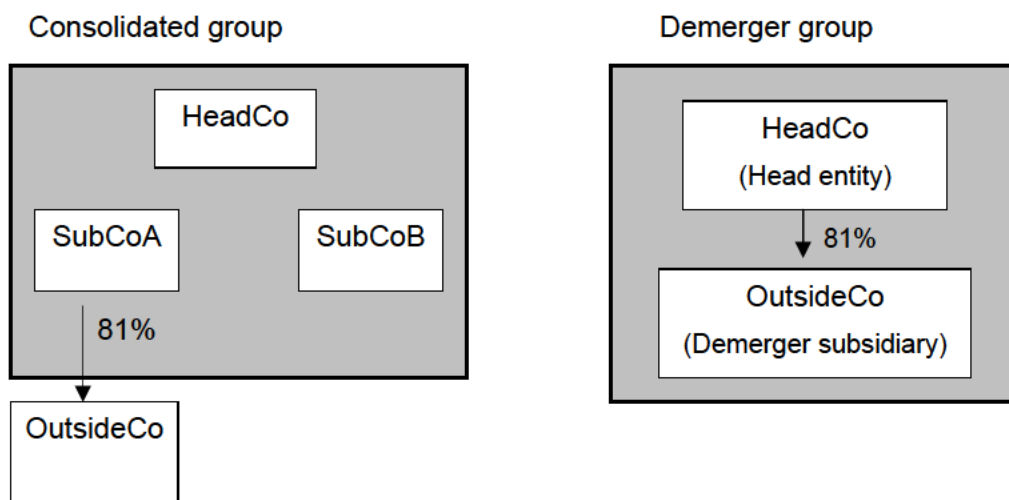
6. The operation of the single entity rule would naturally extend to the definitions of demerger group, demerger and demerging entity in Subdivision 125-B of the ITAA 1997, but only for the purposes of establishing the head company's compliance with the demerger relief provisions in Subdivision 125-C. The single entity rule would not apply to taxpayers seeking to obtain rollover relief under Subdivision 125-B.

**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 SubCo A'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). 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).*

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. When the final Determination is issued, it is proposed to apply both before and after its date of issue. However, the Determination will 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 21 and 22 of Taxation Ruling TR 92/20).

### **Your comments**

14. We invite you to comment on this draft Taxation Determination. Please forward your comments to the contact officer by the due date.

**Due date:** 30 July 2004  
**Contact officer:** Angela Jankovic  
**E-mail address:** angela.jankovic@ato.gov.au  
**Telephone:** (07) 3213 5822  
**Facsimile:** (07) 3213 5971  
**Address:** GPO Box 9990  
Brisbane Qld 4000

---

### **Commissioner of Taxation**

30 June 2004

---

#### *Previous draft:*

Not previously issued in draft form

#### *Related Rulings/Determinations:*

TR 92/20

#### *Subject references:*

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

- head entity
- single entity rule

#### *Legislative references:*

- TAA 1953 Pt IVA
- 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

---

#### **ATO references**

NO: 2004/7318  
ISSN: 1038-8982