


TD 2006/65A Addendum - Income tax: capital gains: small business concessions: can a share in a company or an interest in a trust qualify as an active asset under subsection 152-40(3) of the Income Tax Assessment Act 1997 if the company or trust owns interests in another entity that satisfies the '80% test'?

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Addendum

Taxation Determination

Income tax: capital gains: small business concessions: can a share in a company or an interest in a trust qualify as an active asset under subsection 152-40(3) of the *Income Tax Assessment Act 1997* if the company or trust owns interests in another entity that satisfies the '80% test'?

This Addendum was foreshadowed in Note 3 of Taxation Determination 2006/65 and amends TD 2006/65 to reflect changes in the law made by *Tax Laws Amendment (2006 Measures No. 7) Act 2007* that apply to CGT events happening in the 2006-07 income year or later income years.

Significant individual

- The 50% controlling individual test (which only had regard to direct interests) has been repealed and a 20% significant individual test (which allows tracing of indirect interests) introduced.
- Subsection 152-10(2) of the *Income Tax Assessment Act 1997* (ITAA 1997), which sets out additional basic conditions if the CGT asset is a share in a company or an interest in a trust, has been amended to allow interposed entities to qualify for the small business concessions if a new '90% test' is satisfied (paragraph 152-10(2)(b) of the ITAA 1997). Accordingly, the notes in both Example 1 (paragraph 4) and Example 2 (paragraph 11) of TD 2006/65 are no longer correct.
- In Example 1 of TD 2006/65, as a result of the changes to the law mentioned above, Operating Co has a significant individual (Ben). As well, the amended additional basic condition in paragraph 152-10(2)(b) of the ITAA 1997 is satisfied. Therefore, if Holding Co sold its shares in Operating Co and made a capital gain the concessions may apply if other conditions are satisfied.

TD 2006/65

- Similarly in Example 2 of TD 2006/65, UT2 has a significant individual (Bill). As well, the amended additional basic condition in paragraph 152-10(2)(b) of the ITAA 1997 is satisfied. Therefore, if UT1 sold its units in UT2 and made a capital gain the concessions may apply if other conditions are satisfied.

'80% test'

- Subparagraph 152-40(3)(b)(ii) of the ITAA 1997 has been repealed and new subparagraphs 152-40(3)(b)(ii) and (iii) of the ITAA 1997 inserted. As a result, the market value of any financial instruments of the company or trust that are inherently connected with a business that the company or trust carries on and any cash of the company or trust that is inherently connected with such a business are taken into account in determining if the company or trust satisfies the '80% test'. The repealed subparagraph 152-40(3)(b)(ii) of the ITAA 1997, which included certain capital proceeds in the '80% test', is no longer necessary because the new inclusions for cash and financial instruments covers such capital proceeds.

TD 2006/65 is amended as follows:

1. Paragraph 4

Omit the paragraph; substitute:

4. *The small business concessions may apply if Ben sold his shares in Holding Co. Further, Operating Co has a significant individual (Ben) and the additional basic condition in paragraph 152-10(2)(b) of the ITAA 1997 is satisfied. Therefore, if Holding Co sold its shares in Operating Co and made a capital gain, the concessions may apply if other conditions are satisfied.*

2. Paragraph 11

Omit the paragraph; substitute:

11. *The small business concessions may apply if Bill sold his units in UT1. Further, UT2 has a significant individual (Bill) and the additional basic condition in paragraph 152-10(2)(b) of the ITAA 1997 is satisfied. Therefore, if UT1 sold its units in UT2 and made a capital gain, the concessions may apply if other conditions are satisfied.*

3. Paragraph 14

Omit the second dot point; substitute

- the total of:
 - the market values of the active assets of the company or trust;
 - the market value of any financial instruments of the company or trust that are inherently connected with a business that the company or trust carries on; and
 - any cash of the company or trust that is inherently connected with such a business.

is 80% or more of the market value of all the assets of the company or trust (subsection 152-40(3) of the ITAA 1997).

4. Paragraph 17

Omit the third and fourth sentences.

5. Legislative references

Insert:

- ITAA 1997 152-10(2)(b)

Commissioner of Taxation

29 October 2008

ATO references

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Income Tax ~~ Capital Gains Tax ~~ small business relief - 'active asset test'