Worked example

Pre-CGT factor for assets of a joining entity

Note:

These pre-CGT factor rules apply to an entity that joined a consolidated group before 10 February 2010 unless the head company makes a choice for the new pre-CGT proportion rules to apply. For details of the new pre-CGT proportion rules that apply from 10 February 2010 see → 'Pre-CGT status of membership interests in a joining entity – pre-CGT proportion rules', C2-4-813.

Description

This example shows how the pre-CGT status of the membership interests acquired by the group before 20 September 1985 is preserved by attaching a pre-CGT factor to each asset (other than current assets) of the joining entity. This only applies where an entity joins a consolidated group before 10 February 2010.

Commentary

The pre-CGT status of membership interests in a joining entity is an attribute of the assets of the group being joined (as opposed to being an attribute of the assets of the joining entity).

To preserve that status a pre-CGT factor is attached at the joining time to each of the joining entity's assets (other than current assets). This allows a proportion of the membership interests in a leaving entity to be treated as pre-CGT assets by reference to the pre-CGT factors attached to the assets that leave with it. (Note that the asset with the pre-CGT factor attached does not need to have belonged to the leaving entity when it joined, nor do any of the leaving entity's membership interests need to have been pre-CGT interests at that time.) → 'Pre-CGT membership interests in a leaving entity (with pre-CGT factor attached to assets)', C2-5-710

The pre-CGT factor that applies to each asset (other than current assets) is calculated as follows:

$$\frac{\sum \text{Market value of each pre-CGT membership interests held by head company} + \sum \text{Market value of each membership interest held by a subsidiary member multiplied by its pre-CGT factor}}{\sum \text{Market value of joining entity's assets other than current assets}}$$

Note: If the amount calculated in this way is more than 1, the pre-CGT factor will be 1.

In terms of membership interests in the joining entity, the pre-CGT assets of the members are the interests (such as shares) or rights those members have held continuously since 19 September 1985.

Note: Division 149 of the *Income Tax Assessment Act 1997* (previously Division 20, section 160ZZS of the *Income Tax Assessment Act 1936*) will apply under consolidation in that a greater than 50% continuity of underlying ownership must be maintained since 19 September 1985 to maintain the pre-CGT status of assets. The pre-CGT status is removed from the assets under existing law if this continuity of majority underlying ownership is not maintained.

→ Explanatory Memorandum to the New Business Tax System (Consolidation) Bill (No. 1) 2002, paragraph 2.47

Where pre-CGT status is removed from assets under existing law, the cost bases of the affected assets are reset at their market values as at the time of the trigger event.

Further, a pre-CGT factor only attaches to assets that existed at the joining time, and if an asset is disposed of after the joining time (other than by the sale of an entity), its pre-CGT factor is lost to the group and the factor does not attach to any replacement asset.

Example 1

Facts

ACo acquired 60% of the shares in BCo before 20 September 1985. On consolidation the financial positions are as shown in tables 1 and 2.

Table 1: ACo – financial position at 1 July 2003

Shares (100 in BCo)	$100	Equity	$100

Table 2: BCo – financial position at 1 July 2003

Land (MV $500)	$50	Equity	$100
Asset 2 (MV $100)	$50		
	$100		$100

Notes: MV: = market value
Asset 2 is not a current asset.

Calculation

Pre-CGT factor for all assets (other than current assets)

Step 1

Work out the market value of the pre-CGT membership interests in the joining entity:

(Land, $500 + Asset 2, $100) x 60% = $360

Step 2

Work out the market value of all the joining entity's assets (other than current assets) at the joining time:

Land ($500) + Asset 2 ($100) = $600

Step 3

Work out the pre-CGT factor:

$360 (step 1) / $600 (step 2) = 0.6

Therefore, the pre-CGT factor to be attached to all of the joining entity's (BCo) assets other than current assets (Land and Asset 2 in this example) is 0.6.

Example 2

Facts

HCo acquired 60% of ACo in July 1985 for a consideration of $600. ACo's financial position at this time was as shown in table 3.

Table 3: ACo – financial position at 1 July 1985

Cash	$1,000	Equity	$1,000

On 30 June 2003 the remaining equity of ACo is acquired by HCo for $680 (40% of $1,700 – see step 1 below) with the financial position as shown in table 4.

Table 4: ACo – financial position at 30 June 2003

Cash	$200	Equity	$1,000
Land (MV $2,000)	$1,300	Liabilities	$500
	$1,500		$1,500

Note: MV = market value

Calculation

Pre-CGT factor for all assets (other than current assets)

Step 1

Work out the market value of the pre-CGT membership interests in ACo:

The market value of all the membership interests in ACo at the joining time is $1,700 (Cash of $200 plus market value of Land, $2,000, less Liabilities of $500). Therefore, the market value of the pre-CGT membership interests is $1,020 (60% of $1,700).

($200 + $2,000 – $500) x 60% = $1,020

Step 2

Work out the market value of all the joining entity's assets (other than current assets) at the joining time:

The market value of all the assets (for which a pre-CGT factor is to be worked out) that ACo holds at the joining time (Land) is $2,000.

Note: Cash is excluded by virtue of subsection 705-125(2) of the ITAA 1997.

Step 3

Work out the pre-CGT factor:

$1,020 (step 1) / $2,000 (step 2) = 0.51

Therefore, the pre-CGT factor to be attached to all of the joining entity's (ACo) assets other than current assets (Land in this example) is 0.51.

References

Income Tax Assessment Act 1997, section 705-125; as inserted by *New Business Tax System (Consolidation) Act (No. 1) 2002* (No. 68 of 2002), Schedule 1, and amended by *Tax Laws Amendment (2010 Measures No. 1) Act 2010* (No. 56 of 2010), Schedule 5, Part 3

Explanatory Memorandum to New Business Tax System (Consolidation) Bill (No. 1) 2002, paragraphs 5.108–113

Explanatory Memorandum to Tax Laws Amendment (2010 Measures No. 1) Bill 2010, paragraphs 5.111 to 5.142

Revision history

Section C2-4-810 first published (excluding drafts) 2 December 2002.

Further revisions are described below.

Date	Amendment	Reason
6.5.11	Changes to Commentary to reflect changes to the method of working out the proportion of the pre-CGT membership interests in a joining entity.	Legislative amendments.
15.7.11	Additional information added to Note on p. 1.	Clarification