

## Worked example

## Pre-CGT factor for assets where subsidiary has membership interests in another member – formation before 10 February 2010

### Note:

These pre-CGT factor rules do not apply to an entity that joins a consolidated group on or after 10 February 2010. 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, on formation of a consolidated group before 10 February 2010, the pre-CGT status of membership interests held directly and indirectly by the head company is preserved by attaching a pre-CGT factor to assets (other than current assets) held by subsidiary members of the group.

### Commentary

The pre-CGT status of membership interests held directly by the head company (that is, in the first subsidiary) is preserved by attaching a pre-CGT factor to the assets (other than current assets) of the first subsidiary at the formation time.

If, on formation, the first subsidiary holds membership interests in another subsidiary member (the second subsidiary), the pre-CGT factor must first be worked out for the first subsidiary's assets before any pre-CGT factor can be worked out for the second subsidiary's assets. The market value of each membership interest owned by the first subsidiary in the second subsidiary is multiplied by the pre-CGT factor that was worked out and attached to the first subsidiary's assets. → section 705-165, *Income Tax Assessment Act 1997* (ITAA 1997)

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 factor of assets in the leaving entity. → 'Pre-CGT membership interests in a leaving entity (with pre-CGT factor attached to assets)', C2-5-710

Note: section 705-165 of the ITAA 1997 was repealed on 10 February 2010, which means that this process does not apply to groups forming on or after this date. → *Tax Laws Amendment (2010 Measures No. 1) Act 2010* (No. 56 of 2010), Schedule 5, Part 3

### Example

#### Facts

ACo, the future head company, was incorporated in 1983 with its sole asset being \$300 in cash. On 1 July 1985, ACo paid \$60 for 60% of BCo (which had been incorporated 1 July 1984 with a cash asset of \$200).

Previously, on 30 January 1985, BCo had paid \$160 for an 80% interest in CCo, with the other 20% being owned by a third party. (CCo had assets of Cash \$100 and Land \$100.) In 1999 CCo bought Asset 1 at a cost of \$10.

The financial positions of ACo, BCo and CCo are shown in tables 1, 2 and 3.

Table 1: ACo – financial position at 1 July 1985

Cash	\$240	Contributed capital	\$300
Shares BCo	\$60		
Total	\$300	Total	\$300

Table 2: BCo – financial position at 1 July 1985

Cash	\$40	Contributed capital	\$200
Shares CCo	\$160		
Total	\$200	Total	\$200

Table 3: CCo – financial position at 1 July 1985

Cash	\$100	Contributed capital	\$200
Land (MV \$100)	\$100		
Total	\$200	Total	\$200

Note: MV = market value

On 1 July 2002, ACo acquires the 40% balance of BCo for \$99.20. BCo acquires the 20% balance of the shares in CCo for \$52 after borrowing \$12 from an external source.

On 1 July 2002, ACo forms a consolidated group with the other companies. The group structure is shown in Figure 1, and their financial positions are shown in tables 4, 5 and 6.

Figure 1: Group structure at formation time

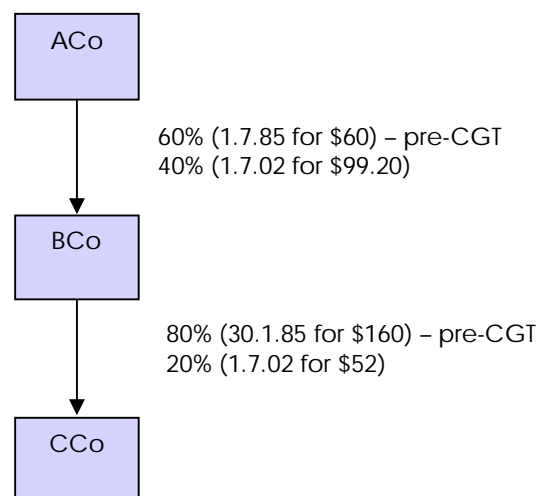


Table 4: ACo – financial position at 1 July 2002

Cash	\$140.80	Contributed capital	\$300
Shares BCo (MV \$248)	\$159.20		
Total	\$300	Total	\$300

Table 5: BCo – financial position at 1 July 2002

Shares CCo (MV \$260)	\$212	Contributed capital	\$200
		Liability - bank loan	\$12
Total	\$212	Total	\$212

Table 6: CCo – financial position at 1 July 2002

Cash	\$90	Contributed capital	\$200
Land (MV \$150)	\$100		
Asset 1 (MV \$20)	\$10		
Total	\$200	Total	\$200

## Calculation Pre-CGT factor For BCo's assets (other than current assets)

### Step 1

Work out the market value of the pre-CGT membership interests (which are pre-CGT assets) that the head company ACo holds in BCo at formation time.

Market value of shares in BCo is \$248 (MV of Shares in CCo, \$260, less Liability of \$12).

$$\$248 \times 60\% = \$148.80$$

### Step 2

Work out the market value of all of BCo's assets (other than current assets), at the formation time:

MV of Shares in CCo is \$260.

### Step 3

Work out the pre-CGT factor:

$$\$148.80 \text{ (step 1)} / \$260 \text{ (step 2)} = 0.5723076$$

Therefore, the pre-CGT factor to be attached to all assets, other than current assets, (shares held by BCo in CCo) is 0.5723076.

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Pre-CGT factor for CCo's assets (other than current assets)

*Step 1*

Multiply the market values of the membership interests held by BCo in CCo by their pre-CGT factors (worked out above):

$$\text{Market value of Shares in CCo } (\$260) \times 0.5723076 = \$148.80$$

*Step 2*

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

$$\text{Land } (\$150) + \text{Asset 1 } (\$20) = \$170$$

*Step 3*

Work out the pre-CGT factor:

$$\$148.80 \text{ (step 1)} / \$170 \text{ (step 2)} = 0.8752941$$

Therefore, the pre-CGT factor to be attached to CCo's assets, other than current assets, (Land and Asset 1) is 0.8752941.

## References

*Income Tax Assessment Act 1997*, section 705-165; as inserted by *New Business Tax System (Consolidation, Value Shifting Demergers and Other Measures) Act 2002* (No. 90 of 2002), Schedule 3, and repealed 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, Value Shifting, Demergers and Other Measures) Bill 2002, paragraphs 1.72-1.73

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

### Revision history

Section C2-4-820 first published (excluding drafts) 2 December 2002.

Further revisions are described below.

Date	Amendment	Reason
6.5.11	Revisions to reflect changes to the method of working out the proportion of the pre-CGT membership interests in a joining entity.	Legislative amendments.