TD 2006/D25 - 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 document has been finalised by TD 2006/65.

Draft 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'?

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Ruling

1. Yes. A share in a company or an interest in a trust can qualify as an active asset under subsection 152-40(3) of the *Income Tax Assessment Act 1997* (ITAA 1997) if the company or trust owns interests in another entity that satisfies the '80% test' in paragraph 152-40(3)(b) of the ITAA 1997. The '80% test' operates successively at each level in a chain of entities to determine the active asset status of the underlying interests.

Example 1

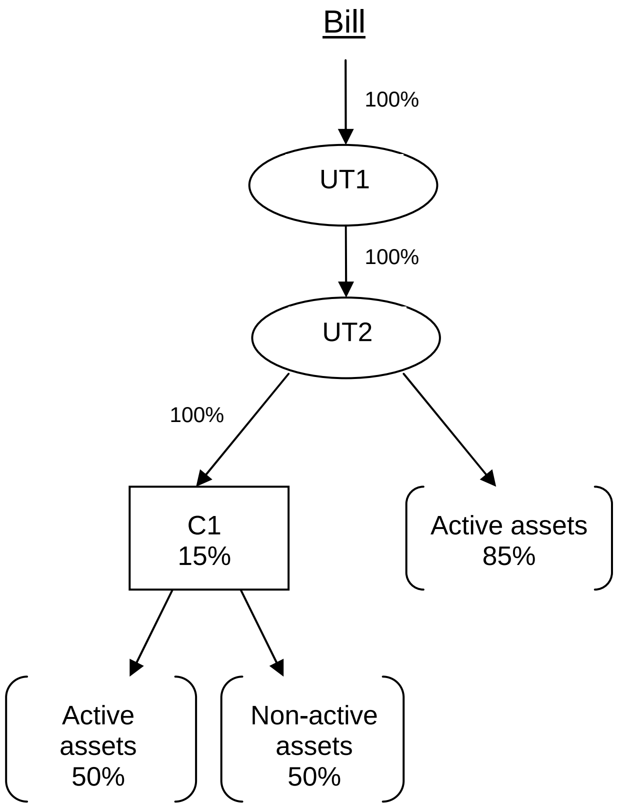
2. *Ben owns all the shares in Holding Co which, in turn, owns all the shares in Operating Co (both are resident companies). The only assets of Holding Co are the shares in Operating Co and all of Operating Co's assets are active assets.*

3. *As Operating Co satisfies the 80% test, the shares owned by Holding Co in Operating Co are active assets. As those shares are the only assets owned by Holding Co, Holding Co also satisfies the 80% test and therefore the shares owned by Ben in Holding Co are also active assets.*

Example 2

4. *Bill owns all the units in a unit trust (UT1). UT1 owns all the units in another unit trust (UT2). UT2 owns all the shares in a private company (C1). All of UT2's other assets are active assets. The market value of the C1 shares is 15% of the market value of all the assets owned by UT2.*

5. *C1 owns an active asset, the market value of which is 50% of the market value of all C1's assets. All entities are Australian residents.*



6. *The operation of the '80% test' is set out in the following table:*

Asset	***Analysis***	***80% test***	***Active asset***
Shares in C1	*The market value of C1's active assets is only 50% of the market value of all its assets.*	*Not satisfied (50%)*	*No*
Units in UT2	*The market value of UT2's active assets is 85% of the market value of all its assets.*	*Satisfied (85%)*	*Yes*
Units in UT1	*All of UT1's assets, being the units in UT2, are active assets.*	*Satisfied (100%)*	*Yes*

7. *The shares in C1 are not active assets of UT2 because C1 does not satisfy the ‘80% test’. The market value of C1’s active assets is only 50% of the market value of all its assets.*

8. *The units in UT2 are active assets of UT1 because UT2 satisfies the ‘80% test’. Although UT2’s shares in C1 are not active assets, the market value of UT2’s active assets is 85% of the market value of all its assets.*

9. *The units in UT1 are active assets of Bill because UT1 satisfies the ‘80% test’. All of UT1’s assets, being the units in UT2, are active assets.*

Date of effect

10. 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.

Commissioner of Taxation
14 June 2006

Appendix 1 – Explanation

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

Explanation

11. The '80% test' is a numerical calculation that determines whether a company or trust owns sufficient active assets to allow active asset status to effectively flow through to the underlying interests.

12. Under the '80% test' a share in a company or an interest in a trust is an active asset at a given time if:

- the company is an Australian resident at that time or the trust is a resident trust for capital gains tax (CGT) purposes for the income year in which that time occurs; and
- the total of:
  - the market values of the active assets of the company or trust; and
  - any capital proceeds the company or trust received, during the two years before that time, from CGT events happening to active assets the company or trust holds in the form of cash or debt pending the acquisition of new active assets;

  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).

13. If an entity owns a share in a company or interest in a trust that is an active asset because the company or trust satisfies the '80% test', the share or interest is included in that entity's '80% test' calculation to determine if the underlying interests in the entity are themselves active assets.

14. As the active asset test requires a CGT asset to be an active asset for at least half a particular period (generally the ownership period), the '80% test' must also be satisfied for that same period for a share in a company or interest in a trust to satisfy the active asset test.

Note

15. 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 Draft Taxation Determination is part of the Commissioner's response to Recommendation 7.3 of the Board's report.

Appendix 2 – Your comments

16. We invite you to comment on this draft Taxation Determination. Please forward your comments to the contact officer by the due date. (Note: The Tax Office prepares a compendium of comments for the consideration of the relevant Rulings Panel. The Tax Office may use a sanitised version (names and identifying information removed) of the compendium in providing its responses to persons providing comments. Please advise if you do not want your comments included in a sanitised compendium.)

Due date: **11 August 2006**

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References

Previous draft:

Not previously issued as a draft

Subject references:

- active asset
- active asset test
- basic condition for relief
- capital gains tax
- CGT events
- CGT small business relief

Legislative references:

- ITAA 1997 152-40(3)
- ITAA 1997 152-40(3)(b)

Other references

- Treasurer's Press Release No. 38 of 2006

ATO references

NO:	2006/8977
ISSN:	1038-8982
ATOlaw topic:	Income Tax ~~ Capital Gains Tax ~~ small business relief - basic conditions for relief Income Tax ~~ Capital Gains Tax ~~ small business relief - 'active asset test'