TD 2004/45 - Income tax: consolidation: capital gains: how does the significant individual condition in paragraph 152-110(1)(c) of the Income Tax Assessment Act 1997 (one of the conditions for the small business 15 year exemption in Subdivision 152-B) apply to the head company of a consolidated group in respect of the sale of an asset brought into the group by a subsidiary member?

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This document has changed over time. This is a consolidated version of the ruling which was published on *19 December 2012*

Taxation Determination

Income tax: consolidation - capital gains - how does the significant individual condition in paragraph 152-110(1)(c) of the *Income Tax Assessment Act 1997* (one of the conditions for the small business 15 year exemption in Subdivision 152-B) apply to the head company of a consolidated group in respect of the sale of an asset brought into the group by a subsidiary member?

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[**Note:** This is a consolidated version of this document. Refer to the Legal Database (http://law.ato.gov.au) to check its currency and to view the details of all changes.]

1. Under the single entity rule in section 701-1 of the *Income Tax Assessment Act 1997* (ITAA 1997) the significant individual condition in paragraph 152-110(1)(c) of the ITAA 1997 is applied to the head company of the consolidated group.

2. However, the condition must be met for a total of at least 15 years during the period which the asset was owned by the subsidiary before it became a subsidiary member of the group, and it was owned by the subsidiary or other group members after the subsidiary became a member.

3. Under the entry history rule in section 701-5 of the ITAA 1997, the head company inherits the subsidiary's history in respect of the significant individual condition for the period before the subsidiary became a member of the group. Therefore, the head company will be taken to meet the condition for the subsidiary's pre-consolidation

ownership period if the subsidiary met it for that period. The head company will not meet the condition for that period if the subsidiary did not meet it.

4. For the period after the subsidiary became a group member, the condition is applied directly to the head company.

Note: This Determination does not apply to intra-group assets including membership interests.

Explanation

5. Under the single entity rule, a CGT event from the sale of an asset by a subsidiary member is taken to happen to the head company of the consolidated group. Any resulting capital gain or loss is therefore made by the head company.

6. Accordingly, it is the head company that must satisfy the significant individual condition in paragraph 152-110(1)(c) of the ITAA 1997 if it wishes to use the small business 15 year exemption to reduce a capital gain from the sale of an active asset.

7. That condition requires that the entity have a significant individual for a total of at least 15 years (even if the 15 years was not continuous and it was not always the same significant individual) during which the entity owned the CGT asset.

Note

7A. The effect of the application provision for *Tax Laws Amendment (2006 Measures No. 7) Act 2007* is that for CGT events happening in the 2006-07 income year and later income years a company or trust will need to have had a significant individual in earlier years to access the 15 year exemption, not a controlling individual (refer to Schedule 1, item 68 of *Tax Laws Amendment (2006 Measures No. 7) Act 2007* and paragraphs 1.54, 1.55 and 1.104 of the accompanying Explanatory Memorandum).

8. An individual is a significant individual in a company at a time, if at that time, the individual has a small business participation percentage in the company of at least 20% (section 152-55 of the ITAA 1997). An entity's small business participation percentage in another entity at a time is the percentage that is the sum of the entity's direct small business participation percentage and indirect small business participation percentage in the other entity at that time (section 152-65 of the ITAA 1997).

9. While under the entry history rule the head company inherits the subsidiary's ownership period for the asset, it also inherits the subsidiary's history in respect of the significant individual condition. Therefore, whether or not the subsidiary has met the condition pre-consolidation is relevant to determining whether the head company has met the condition.

10. For the period after becoming a group member, the subsidiary's circumstances are irrelevant and the condition is applied directly to the head company.

Example 1

11. *X Co acquired an active asset in January 1989. X Co had a significant individual from January 1989 until January 2003.*

12. *In January 2003, X Co became a member of a consolidated group when the head company of the group (H Co) acquired all of the shares in it.*

13. *H Co had a significant individual from January 2000 until June 2011.*

14. *The active asset was sold in January 2011 which resulted in a capital gain. H Co sought to disregard it under the small business 15 year exemption.*

15. *The significant individual condition is effectively applied to X Co for the period before it joined the consolidated group and to H Co after that time. As X Co had a significant individual from 1989 until it joined the group and H Co had a significant individual from that time until the asset was sold, H Co may claim the 15 year exemption if all of the other conditions for the exemption are satisfied.*

Example 2

16. *X Co was incorporated in 1985 and its shares have been owned since that time by a significant individual.*

17. *In 1986, X Co incorporated Y Co and since that time X Co has been its sole shareholder.*

18. *In 1987, Y Co purchased an active asset.*

19. *In June 2003, X Co elected to form a consolidated group with Y Co.*

20. *In June 2011, the active asset was sold by Y Co and a capital gain resulted.*

21. *The effect of the single entity rule is that the sale is taken to happen to X Co and the capital gain is made by X Co.*

22. X Co has had a significant individual for its entire existence and it is now, because of the single entity rule and the entry history rule, taken to have owned the active asset for the 15 year period. It is entitled to apply the 15 year exemption in section 152-110 of the ITAA 1997. This is because although the significant individual condition in paragraph 152-110(1)(c) of the ITAA 1997 is effectively applied to Y Co before the formation of the consolidated group, Y Co has had a significant individual (traced indirectly through X Co) for its entire existence.

Date of effect

23. This Determination applies to years commencing both before and after its date of issue. However, it does not apply to taxpayers to the extent that it conflicts with the terms of settlement of a dispute agreed to before the date of the Determination (see paragraphs 75 and 76 of Taxation Ruling TR 2006/10)

Note

23A. The amendments applied to this consolidated Determination apply to CGT events happening in the 2006-07 income year or later income years..

Commissioner of Taxation
6 October 2004

Previous draft:
TD 2004/D16

Related Rulings/Determinations:
TR 2006/10

Subject references:
- capital gains tax
- CGT event
- consolidated group

- entry history rule
- head company
- single entity rule
- significant individual
- small business relief
- small business 15 year exemption
- subsidiary member

Legislative references:

- TAA 1953 Pt IVAAA
- ITAA 1997 152-55
- ITAA 1997 152-110
- ITAA 1997 152-110(1)(c)
- ITAA 1997 Subdiv 152-B
- ITAA 1997 152-65
- ITAA 1997 701-1
- ITAA 1997 701-5

ATO references
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