TD 2006/69 - Income tax: capital gains: small business concessions: must a taxpayer receive actual capital proceeds from a CGT event to qualify for the small business retirement exemption under Subdivision 152-D of the Income Tax Assessment Act 1997?

Taxation Determination

Income tax: capital gains: small business concessions: must a taxpayer receive actual capital proceeds from a CGT event to qualify for the small business retirement exemption under Subdivision 152-D of the *Income Tax Assessment Act 1997*?

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This publication (excluding appendixes) is a public ruling for the purposes of the *Taxation Administration Act 1953*. A public ruling is an expression of the Commissioner's opinion about the way in which a relevant provision applies, or would apply, to entities generally or to a class of entities in relation to a particular scheme or a class of schemes. If you rely on this ruling, we must apply the law to you in the way set out in the ruling (unless we are satisfied that the ruling is incorrect and disadvantages you, in which case we may apply the law in a way that is more favourable for you – provided we are not prevented from doing so by a time limit imposed by the law). You will be protected from having to pay any underpaid tax, penalty or interest in respect of the matters covered by this ruling if it turns out that it does not correctly state how the relevant provision applies to you.

Ruling

1. Yes. A taxpayer must receive actual capital proceeds from a CGT event to qualify for the retirement exemption under Subdivision 152-D of the *Income Tax Assessment Act 1997* (ITAA 1997). If the market value substitution rule in section 116-30 of the ITAA 1997 has applied to increase the capital proceeds taken to be received, the retirement exemption is available only to the extent of the actual capital proceeds received by the taxpayer.

2. A taxpayer who makes a capital gain from CGT event J2 or J3, in section 104-185 or 104-190 of the ITAA 1997, respectively, following an earlier small business rollover, can disregard the capital gain under the small business retirement exemption if they qualify for the retirement exemption.

3. If the original CGT event did not involve actual capital proceeds such that the retirement exemption was not available, the capital gain under CGT event J2 or J3 remains ineligible for the exemption.

Example 1

4. *Charlie transfers his farm to his son for no consideration. The market value of the farm is more than the cost base of the farm.*

5. *CGT event A1 happens. As Charlie did not receive any capital proceeds for the farm, the market value substitution rule applies to treat the capital proceeds to be an amount equal to the market value of the farm. Charlie makes a capital gain from the CGT event but no part of the gain is eligible for the small business retirement exemption because Charlie did not receive any actual capital proceeds.*

6. *The capital gain may be eligible for the CGT discount, the 50% active asset reduction or the small business rollover.*

Example 2

7. *Following on from the facts in Example 1, six months later, Charlie buys a replacement farm closer to the town and chooses the small business roll-over to defer the capital gain from the transfer of his original farm. Two years later he decides to retire and sells the replacement farm to a third party for an amount equal to the cost base of the farm. Charlie now wants to choose the small business retirement exemption.*

8. *CGT event J2 happens when Charlie sells the replacement farm and realises the deferred capital gain from the original farm. This capital gain remains ineligible for the small business retirement exemption because the original CGT event, that is the sale of the original farm, did not involve actual capital proceeds.*

Date of effect

9. This Determination applies to years commencing both before and after its date of issue. However, the Determination 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 issue of the Determination (see paragraphs 75 and 76 of Taxation Ruling TR 2006/10).

Commissioner of Taxation
15 November 2006

Appendix 1 – Explanation

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

Explanation

10. A taxpayer can choose to disregard an amount of a capital gain if the taxpayer satisfies the conditions for the small business retirement exemption in sections 152-305 and 152-315 of the ITAA 1997. Additional conditions in section 152-325 of the ITAA 1997 apply to a company or a trust.

11. The amount of the capital gain that can be disregarded is limited to the actual capital proceeds received from the CGT event. In working out the capital proceeds received for the purposes of the small business retirement exemption, the market value substitution rule in section 116-30 of the ITAA 1997 is not taken into account (subsections 152-310(3) and 152-325(4) of the ITAA 1997).The exempt amount is limited to the actual capital proceeds received and the life time CGT retirement exemption limit of $500,000 (subsection 152-315(2) and section 152-320 of the ITAA 1997).

Capital gains from CGT event J2 and J3

12. A taxpayer who has chosen a small business rollover and realises the previously rolled over capital gain under CGT event J2 or J3 can disregard the capital gain under the small business retirement exemption if they qualify for the exemption.

13. CGT event J2 happens when a replacement CGT asset changes status (section 104-185 of the ITAA 1997). For example, CGT event J2 happens if the replacement asset is sold, stops being used or held ready for use in the business, starts being trading stock or starts being used to produce exempt income.

14. CGT event J3 happens, in relation to a replacement CGT asset that is a share in a company or an interest in a trust, when there is a change in circumstances (section 104-190 of the ITAA 1997). For example, CGT event J3 happens if the share or interest ceases to be an active asset or the taxpayer stops being a controlling individual of the company or trust.

15. There are no capital proceeds from CGT event J2 or J3. In determining whether the small business retirement exemption can apply, the taxpayer should take into account the capital proceeds received for the original CGT event.

16. If the original CGT event did not involve actual capital proceeds such that the retirement exemption was not available, the capital gain under CGT event J2 or J3 remains ineligible for the exemption.

Note

17. 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 Taxation Determination is part of the Commissioner's response to Recommendation 12.4 of the Board's report. The Board's report also contains a number of legislative recommendations. This Taxation Determination may be affected by the legislative change relating to Recommendation 12.5 of the Board's report.

References

Previous draft:

TD 2006/D30

Related Rulings/Determinations:

TR 2006/10

Subject references:

- basic condition for relief
- capital gains
- capital gains tax
- CGT capital proceeds
- CGT capital proceeds modification market substitution rule
- CGT capital proceeds modification rule
- CGT event A1 - disposal of CGT asset
- CGT event J1-J2 - rollovers
- CGT exemption
- CGT replacement assets
- CGT retirement exemption
- CGT roll-over relief
- CGT small business relief
- small business retirement exemption
- small business roll-over

Legislative references:

- ITAA 1997 104-185
- ITAA 1997 104-190
- ITAA 1997 116-30
- ITAA 1997 Subdiv 152-D
- ITAA 1997 152-305
- ITAA 1997 152-310(3)
- ITAA 1997 152-315
- ITAA 1997 152-315(2)
- ITAA 1997 152-320
- ITAA 1997 152-325
- ITAA 1997 152-325(4)
- TAA 1953

Other references

- Treasurer's Press Release No. 38 of 2006 (9 May 2006)

ATO references

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