TD 2006/D33 - Income tax: capital gains: small business concessions: is the part of a payment which is a small business 50% reduction amount a non-assessable part under CGT event E4 in section 104-70 of the Income Tax Assessment Act 1997 ?

Draft Taxation Determination

Income tax: capital gains: small business concessions: is the part of a payment which is a small business 50% reduction amount a non-assessable part under CGT event E4 in section 104-70 of the *Income Tax Assessment Act 1997*?

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Ruling

1. Yes. The part of a payment which is a small business 50% reduction amount is a non-assessable part under CGT event E4 in section 104-70 of the *Income Tax Assessment Act 1997* (ITAA 1997).

Example 1

2. *The Trustee of the Gillies Family Unit Trust carries on a business. Gilbert and another beneficiary have each owned one unit in the trust for ten years. The trustee makes a capital gain of $4,000 (capital proceeds $9,000 less cost base $5,000) from the disposal of an active asset owned for eight months. The trust satisfies the conditions for the small business 50% active asset reduction and the gain is reduced to $2,000. The net income of the trust is $2,000. The trustee distributes the capital proceeds of $9,000 equally to Gilbert and the other beneficiary in the income year in which the capital gain is made. The tax consequences for Gilbert are:*

Gilbert's trust net income under section 97 of the Income Tax Assessment Act 1936 (ITAA 1936)	*$1,000*

Gilbert calculates his capital gain under Subdivision 115-C:

Gross-up trust gain under paragraph 115-215(3)(b) ($1,000 × 2)	*$2,000*
less: SB 50% reduction under paragraph 115-215(4)(b)	*$1,000*
Capital gain	*$1,000*
Gilbert's deduction under subsection 115-215(6)	*$1,000*

Gilbert calculates his non-assessable part under CGT event E4:

Payment of capital proceeds made by trustee	*$4,500*
less: trust net capital gain assessed under section 97 of the ITAA 1936	*$1,000*
Non-assessable part of payment	*$3,500*

The cost base of Gilbert's unit in the trust is $500. Since the non-assessable part of the payment is more than the cost base, Gilbert reduces the cost base of his unit to nil and makes a capital gain under CGT event E4:

Non-assessable part of payment	*$3,500*
less: cost base	*$500*
Capital gain under CGT event E4	*$3,000*

As Gilbert has owned his unit for more that 12 months he satisfies the conditions for the CGT discount and is also eligible for the small business 50% reduction. His CGT event E4 capital gain can be reduced to:

Capital gain under CGT event E4	*$3,000*
less: 50% CGT discount	*$1,500*
	$1,500
less: small business 50% reduction	*$750*
Reduced capital gain	*$750*

The net tax result for Gilbert is that he is taxed on a net capital gain of $1,750 ($1,000 capital gain under Subdivision 115-C plus $750 CGT event E4 capital gain).

Example 2

3. *Assume the same facts in Example 1, except that the active asset has been owned by the trust for more than 12 months and the capital gain can be reduced by the 50% CGT discount and the 50% small business reduction. The tax consequences for Gilbert are:*

Gilbert's trust net income under section 97 of the ITAA 1936	*$500*

Gilbert calculates his capital gain under Subdivision 115-C:

Gross-up trust gain under paragraph 115-215(3)(c) ($500 × 4)	*$2,000*
less: CGT discount reduction under paragraph 115-215(4)(a)	*$1,000*
	$1,000
less: SB 50% reduction under paragraph 115-215(4)(b)	*$500*
Capital gain	*$500*
Gilbert's deduction under subsection 115-215(6)	*$500*

Gilbert calculates his non-assessable part under CGT event E4:

Payment of capital proceeds made by trustee	*$4,500*
less: trust net capital gain assessed under section 97 of the ITAA 1936	*$500*
	$4,000
less: CGT discount adjustment (subsection 104-71(4) table item 1)	*$1,000*
Non-assessable part	*$3,000*

The cost base of Gilbert's unit in the trust is $500. Since the non-assessable part of the payment is more than the cost base, Gilbert reduces the cost base of his unit to nil and makes a capital gain under CGT event E4:

Non-assessable part of payment	*$3,000*
less: cost base	*$500*
Capital gain under CGT event E4	*$2,500*

Gilbert satisfies the conditions for the CGT discount and the small business 50% reduction. His CGT event E4 capital gain can be reduced to:

Capital gain under CGT event E4	*$2,500*
less: 50% CGT discount	*$1,250*
	$1,250
less: SB 50% reduction	*$625*
Reduced capital gain	*$625*

The net tax result for Gilbert is that he is taxed on a net capital gain of $1,125 ($500 capital gain under Subdivision 115-C plus $625 CGT event E4 capital gain).

Date of effect

4. 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

5. CGT event E4 in section 104-70 of the ITAA 1997 happens when the trustee of a trust makes a non-assessable payment to a beneficiary in respect of the beneficiary's unit or interest in the trust (except for CGT event A1, C2, E1, E2, E6 and E7 happening in relation to it), and some or all of the payment (the non-assessable part) is not included in the beneficiary's assessable income.

6. A non-assessable part under CGT event E4 may include amounts associated with the small business 50% reduction, frozen indexation, building allowance and accounting differences in income. Subsection 104-70(1) of the ITAA 1997 indicates that, in working out what part of the payment is included in your assessable income, you disregard your share of the trust's net income that is subject to the rules in 115-215(3) of the ITAA 1997. This means you disregard the amount by which the capital gain was increased under those rules.

7. A non-assessable part excludes payments listed under section 104-71 of the ITAA 1997 such as the payment of a CGT discount amount (item 1 subsection 104-71(4) of the ITAA 1997) and a small business 15-year exemption amount (paragraph 104-71(1)(g) and section 152-125 of the ITAA 1997).

8. CGT event E4 applies to reduce the cost base and reduced cost base of the beneficiary's unit or interest in the trust, but it cannot give rise to a capital loss. If the cost base is reduced to nil, a capital gain may arise (subsections 104-70(4), 104-70(5) and 104-70(6) of the ITAA 1997). This gain may be reduced by applying the CGT discount and the small business 50% reduction if the relevant conditions are satisfied.

Note: CGT event E4 does not happen to payments made to certain beneficiaries: see Taxation Determination TD 2003/28.

Note

9. 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 11.1 of the Board's report.

Appendix 2 – Your comments

10. 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.)

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References

Previous draft:

Not previously issued as a draft

Related Rulings/Determinations:

TD 2003/28

Subject references:

- CGT 50% individual discount
- CGT event E1-E9 – trusts
- small business 50% reduction

Legislative references:

- ITAA 1936 97
- ITAA 1997 104-70
- ITAA 1997 104-70(1)
- ITAA 1997 104-70(4)
- ITAA 1997 104-70(5)
- ITAA 1997 104-70(6)
- ITAA 1997 104-71
- ITAA 1997 104-71(1)(g)
- ITAA 1997 104-71(4)
- ITAA 1997 Subdiv 115-C
- ITAA 1997 115-215(3)
- ITAA 1997 115-215(3)(b)
- ITAA 1997 115-215(3)(c)
- ITAA 1997 115-215(4)(a)
- ITAA 1997 115-215(4)(b)
- ITAA 1997 115-215(6)
- ITAA 1997 152-125

Other references:

- Treasurer's Press Release No. 38 of 2006

ATO references

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