

# **SUBMISSION – The Board of Taxation**

## **Post-implementation Review of the Small Business Capital Gains Tax (CGT) Concessions**

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**SUBMISSION – The Board of Taxation**

# LOWENSTEIN SHARP PTY LTD

## Post-implementation Review of the Small Business Capital Gains Tax (CGT) Concessions

### 1.0 Introduction

The purpose of this brief submission is to provide comments to the Board of Taxation “the Board” in its post-implementation review of Division 152 of the Income Tax Assessment Act 1997 (“ITAA 1997”).

### 1.1 Aim

The aim of this submission is to provide the Board opinions on the quality and effectiveness of the Small Business CGT Concessions in Division 152 of the Income Tax Assessment Act 1997.

### 2.0 Specific Comments

The writer has identified the following concerns, which he believes the Board should be addressing in its post-implementation review. It must be noted this submission reflects the views of the writer only and may not correspond to the views held by Lowenstein Sharp on the subject matter.

#### 2.1 Personal Dwellings and the Net Asset Value Test

It is understood that a taxpayer’s home (where part of it is used for business purposes), then the dwelling will be counted as an active asset. Specifically, if the individual had incurred interest on a loan taken out to purchase the home and would have been able to deduct at least some of that interest from their assessable income, the total market value of their home is included in the maximum net asset value test under s.152-15. This is even if the home is predominantly used for private purposes.

The above is a hypothetical interest deductibility test, ie if the individual did not actually incur any interest, the test looks at whether they would have been entitled to a deduction if they had taken out a loan to purchase their home.

It is submitted this harsh outcome is extremely unfair and it is recommended that the test is more fairly employed if it is based on the following:

- Where no interest had previously been claimed, it is not included in the maximum net asset value test.
- Where part of the interest had been previously claimed, then the market value of the home included in the net asset value test should be relative to the proportion of the interest claimed and not the total market value of the home.

#### 2.2 Small Business 15-Year Exemption

Subdivision 152-B ITAA 1997 provides where certain conditions are satisfied, a taxpayer can disregard a capital gain from a CGT event happening to a CGT asset that one have continuously owned for at least 15 years.

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However, it is understood that if an asset was the result of either a business or replacement asset rollover (and not from an involuntary disposal), then the period of ownership will recommence for the purposes of the 15 year period, ie the “clock resets”. In this case, the period of ownership of the original asset and the replacement asset cannot be aggregated for the purposes of determining whether the replacement asset has been held continuously for 15 years.

It is submitted this provision is extremely harsh and prevents small business taxpayers being able to freely alter or restructure their business entities or business assets without the punitive aspects of “having to re-set the 15 year clock”. This is a very serious impediment which distorts small business reorganisation and capital investment decisions.

It is recommended that the 15-year qualifying period should not recommence due to a business or replacement asset rollover.

## **2.3 Section 152-30(2) - Connected Entity**

This section covers which entities are connected with a taxpayer. Specifically, the issue relates to the application of the control tests in para (a) and (b) of s.152-30(2) where the shares or units are held by the trustee of a discretionary trust.

For example, for a discretionary trust to control a company, in order to met the above provisions, it is necessary for the trustee of the discretionary trust to “beneficially owns” the shares held by the trustee in the company.

It is submitted that, based on the experience of the carry forward of company loss provisions (both statutory and judicially), and as stated in TD 2000/27, shares held by the trustee of a discretionary trust cannot be beneficially owned in the context of s.152-30. This is also further illustrated with s.165-207 ITAA 1997, which states beneficial ownership is established where the discretionary trust has elected to be “family trust”. Therefore, unless the ATO extends the meaning beyond what is stipulated above, then it is doubtful that a discretionary trust could control a company within the meaning of s.152-30(2) (a) or (b).

It is recommended that the Board reviews and clarifies the ATO’s position in relation to the control tests under 152-30(2) where shares or units are held by the trustee of a discretionary trust.

## **3.0 CONTACT DETAILS**

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