

SBCGTintegrity

From: Richard Bowden <rbowden@accruadel.com.au>
Sent: Tuesday, 20 February 2018 11:21 PM
To: SBCGTintegrity
Cc: James Orchard; Chris Marshall; Sam Facy; Ainsley Coggins; Sarah Stribley
Subject: Enquiry about: Improving the integrity of the small business CGT concessions

Categories: Saved

Attention Gregory Derlacz

Hello Gregory

We wish to express our concern in respect of the exposure draft legislation and accompanying explanatory materials implementing these changes.

By way of background, we are a medium sized firm of Chartered Accountants located in Adelaide. Our client base consists predominantly of SMEs. For these clients the Small Business CGT Concessions provides the means by which they can extract a meaningful return on their labour, capital and risk borne over a long period of time in operating their businesses. SME owners typically draw minimal salaries and make minimal contributions to superannuation as their primary focus tends to be on preserving cashflow during the life of their business as a means of funding business expansion. Being able to access the small business CGT concessions on disposal of their business goes a long way compensating SME owners for the often minimal returns they received whilst they operated their business.

Budget Paper Number 2 contained the following explanatory text around the budget announcement in respect of the proposed integrity measures:

“However, some taxpayers are able to access these concessions for assets which are unrelated to their small business, for instance through arranging their affairs so that their ownership interests in larger businesses do not count towards the tests for determining eligibility for the concessions.” (emphasis added).

It was commonly understood within the tax advisory profession that the mischief being targeted here was scenarios where a taxpayer would hold a valuable asset unrelated to their business activity and be able to claim the small business concessions in respect of the non-business asset due to their being no requirement that the asset being disposed of actually be used in the course of the business carried on by that entity. This was accepted by the profession as a fair and reasonable solution to address scenarios that were outside the intended scope of the concessions

It is therefore quite alarming to note that the Exposure Draft released on 8 February would seem to go well beyond addressing the mischief at which the May 2017 budget announcement was aimed and would seem to significantly restrict access to the small Business CGT concessions for SMEs that have legitimately structured their affairs without seeking to rely on any “loopholes”. Whilst clause 1.1 of the EM accompanying the ED is seemingly consistent with the Budget announcement in noting that *“The new conditions ensure that the small business CGT concessions in Division 152 of the ITAA 1997 are only available for assets that are either used or held ready for use in the course of a small business or are an interest in a small business* (emphasis added), this would seem at odds with what the legislation actually achieves however.

The main offending provision in this regard is proposed s152-10(2)(c) which requires an entity to carry on business on order that a taxpayer disposing of an interest in the entity be able to access the concessions. The effect of this provision will be to deny access to the concessions where a taxpayer holds certain business assets through a separate entity to that carrying on the underlying business which is a common structuring approach for SME taxpayers, predominantly for asset protection purpose. In this scenario a taxpayer disposing of interests in the passive asset owning entity will not be entitled to the concessions due to proposed s152-10(2)(c). This is a scenario which often occurs in a succession planning scenario and is likely to have a significant adverse impact on succession arrangements.

Further, where a taxpayer has a holding company interposed between himself and the operating company (again a common structure that is used to protect retained trading profits from risks of trading), the taxpayer would presumably be denied access to the concessions on disposing of interests in the holding company due to s152-

10(c). We have a number of clients that have implemented structuring initiatives along these lines during the period 1 July 2017 to 8 Feb 2017 that are directly affected by this change. Whilst the retrospective aspect of this change is difficult to comprehend, the effect of the change would seem to be at odds that the general scheme of the concessions that the concessions should apply equally to a taxpayer that disposes of a physical asset directly or an indirect (significant) interest in an asset, where either the SBE or MNAV tests are met. Accordingly this provision should simply be scrapped.

Further s 152(10)(2)(d) requires the object entity satisfy the MNAV test – this in effect precludes taxpayers that are significant individuals in respect of an object company from accessing the concessions unless the object company satisfies the MNAV test. Again this is a significant change from the current regime and is a significant extension of the budget announcement that wasn't reasonably foreseeable from the text of the budget announcement. Accordingly to make this provision retrospective to 1 July 2017 is grossly unfair as it is not a change that could be reasonably anticipated from a reading of the budget text.

In summary, we would request the following changes be made to the ED:

- Abolish s152-10(2)(c) or otherwise amend to remove require requirement that an object company carry on a business if it holds assets that are used in a business carried on by an affiliate or connected entity and the object entity satisfies the 80% test.
- Remove retrospectivity of proposed s152-10(2)(d) given that the effect of this change couldn't be reasonably foreseen on the basis of the budget announcement.
- Introduce grandfathering for structures that were in place prior to the introduction of the ED

I will be happy to discuss the above with you as part of the consultation process.


Kind regards


Richard Bowden
Director - Tax & Business Services




We're here to build great businesses.

172 Fullarton Road Dulwich, SA 5065 Australia
Email rbowden@accruadel.com.au
Telephone +61 8 8431 1488
Facsimile +61 8 8431 1441
www.accruharrisorchard.com.au

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