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Small Business Entities and Industry Concessions Unit  
The Treasury  
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PARKES ACT 2600

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Dear Mr Derlacz

## PROPOSED AMENDMENTS TO CGT SMALL BUSINESS CONCESSIONS

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Cleary Hoare Solicitors welcomes the invitation to provide comment in relation to the Exposure Draft in relation to the Small Business CGT concessions. The Exposure Draft was released for public comment on 8 February 2018 and seeks to amend Division 152 of the *Income Tax Assessment Act 1997* (Cth).

Cleary Hoare Solicitors are uniquely positioned to comment on these proposals as an advisor to private business clients throughout Australia and as a firm would give advice on the application of the Small Business CGT Concessions to clients on a daily basis.

The proposed amendments (additional basic conditions) only apply to capital gains relating to CGT assets that are a share in a company or interest in a trust (referred to as "the Object Entity"). Broadly, the proposed amendments relate to the asset, the taxpayer and the Object Entity.

It is our view that the proposed amendments are significantly more wide-reaching than the original intentions of the budget announcement and lead to inequity in certain circumstances.

We submit that the proposed amendments should not be implemented in its current form in relation to the below aspects.

In making that submission, the following comments are relevant:

1. Based on the language of the Explanatory Memorandum ("EM"), it is evident that the new conditions are intended to prevent the small business CGT concessions from being inappropriately applied to interests in large businesses. However, this is not reflected in the Exposure Draft, and the amendments should not be enacted in their current form as to avoid unintended consequences
2. We submit that the two of the amendments will lead to unintended consequences and should not be enacted in their current form. They are:
  - 2.1 Proposed Section 152(2)(c); and

2.2 Proposed Section 152(2)(d).

**Proposed Section 152(2)(c)**

3. We submit that the proposed amendments will have unintentional consequences in the event that the Object Entity is liquidated after the sale of a small business. The proposed subsection 152(2)(c) of the Exposure Draft states that one of the additional criteria in order to qualify for the Small Business Concessions:

*"the object entity is carrying on a business just before the CGT event" (underlining added)*

4. It is evident based on the language of the Exposure Draft and EM, that the Object Entity must have carried on a business *immediately* prior to the CGT event.
5. In the scenario where a company goes into liquidation, it stops operation. However, the CGT event (cancellation of the shares on liquidation) will not occur simultaneously with the cessation of operation as the liquidation process obviously means that the business must stop before liquidation.
6. Therefore, the language contained in the Exposure Draft will have unintentional consequences for liquidated Object Entities, which were carrying on a business prior to liquidation, as the shareholders will be unable to satisfy this new condition as it applies to small business concessions.
7. This will result in amounts previously not subject to taxation due to the initial application of the Small Business CGT concessions at the taxpayer level being subject to taxation at a later time.
8. This unintended consequence is not consistent with the overarching aim to "prevent concessions from being inappropriately applied to interests in large business."
9. This will lead to inequity for some taxpayers in that some structures will be able to access the concessions however clients operating in companies will not be able to on liquidation.

**Proposed Section 152(2)(d)**

10. We submit that proposed Section 152(2)(d) will also lead to inequity for taxpayers. The proposed section states that:

*"(d) either:*

- (i) the object entity would be a \*CGT small business entity for the income year; or  
(ii) the object entity would satisfy the maximum net asset value test (see section 152-15);*

*if the following assumptions were made:*

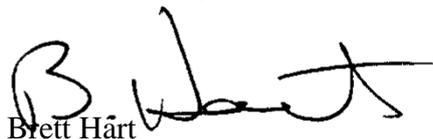
- (iii) the only CGT assets or \*annual turnovers considered were those of the object entity, each affiliate of the object entity, and each entity controlled by the object entity in a way described in section 328-125;  
(iv) each reference in section 328-125 to 40% were a reference to 20%;"*

11. No doubt the intention is to limit access to the concessions where the business operated is large, however the operation of this provision as it applies to normal private business clients is wider than proposed and will lead to inequity and an inability to access to the concessions.

12. In essence, a taxpayer will now be assessed on the turnover and maximum net asset value test twice under these provisions, once at the taxpayer level and once at the Object Entity level.
13. However the inclusion of affiliates and the lowering of the threshold for connected entities in the draft legislation from 40% to 20% for the tests at the Object Entity level will lead to the inclusion of assets or turnover that will not normally have been considered when evaluating the taxpayers position, which will lead to an unfair result on some taxpayers.
14. There will be situations under the new condition due to the reduced tests for a "connected entity" where clients who would normally have access to the concessions (and for whom they are meant to operate) will be excluded from accessing them due to this second test on the object entity.
15. There will also be situations where taxpayers in some structures will be advantaged over taxpayers to which these provisions apply as they will not have to apply the tests twice in order to obtain the concessions.
16. We urge Treasury to reconsider the language used, as these amendments will have negative and unintentional consequences for bona fide taxpayers who would otherwise be able to access the CGT Concessions under Division 152.

Thank you for the opportunity to provide these comments and we are happy to be involved in any further consultation or suggested drafts of the amending legislation. If you require any further clarification on the issues raised and our views on them, please do not hesitate to contact the writer.

Yours faithfully



Brett Hârt

**Cleary Hoare Solicitors**