

**Focus**

Tax

**Business Restructure Rollover Bill Introduced**

9 February 2016

**WHO SHOULD READ THIS**

Accountants and Tax Advisers

**THINGS YOU NEED TO KNOW**

How the proposed rollover will affect your client's planning opportunities

**WHAT YOU NEED TO DO**

Follow the progress of the Bill and seek further guidance where necessary

Last week the *Tax Laws Amendment (Small Business Restructure Roll Over) Bill 2016* (the **Bill**) was introduced to Parliament, confirming the Government's commitment to delivering the "Small Business Restructure Rollover". While it remains clear that the proposed roll-over will provide a useful mechanism for small businesses to restructure their affairs without tax implications, the planning opportunities present in the first exposure draft appear to have been reined in.

Broadly, the proposed roll-over will apply for CGT assets, trading stock, revenue assets and depreciating assets where:

- a small business entity (being an entity that meets the requirements under Subdivision 328-C ITAA 1997);
- transfers an active asset of the business (as defined in section 152-40 ITAA 1997);
- to another small business entity;
- as part of a 'genuine' business restructure (proposed ss328-430(1)(a) and s328-435 in the Bill).

A safe harbour mechanism has been included in the Bill providing that the genuine restructure requirement will be taken to be satisfied where, for three years following the roll-over:

- there is no change in the ultimate economic ownership of any of the significant assets of the business (other than trading stock) that were transferred under the transaction;
- those significant assets continue to be active assets; and
- there is no significant or material use of those significant assets for private purposes.

Importantly, a failure to satisfy the safe harbour provisions does not result in the roll-over being unavailable. It will otherwise be a question of fact whether a genuine restructure of an ongoing business has taken place, in full view of the available evidence.

The Explanatory Memorandum to the Bill provides examples of situations that would indicate a genuine restructure. These include:

- there is a bona fide commercial arrangement undertaken to enhance business efficiency;
- the business continues to operate following the transfer, through a different entity structure but under the same ultimate economic ownership;
- the transfer of assets continue to be used in the business;
- the restructure results in a structure likely to have been adopted had the business owners obtained appropriate professional advice when setting up the business;
- the restructure is not artificial or unduly tax driven; and
- it is not a divestment or preliminary step to facilitate the economic realisation of assets.

Any purported application of the roll-over would of course be subject to Part IVA ITAA 1936.

Another key requirement of the proposed Subdivision 328-G is that there is no change in the 'ultimate economic ownership' of the active asset. Importantly, ultimate economic ownership refers to underlying interests of individuals only. Where there is more than one individual with ultimate economic ownership, there is an additional requirement that each individual's share of ultimate economic ownership be maintained.

At first blush this concept is difficult for discretionary trusts, as discretionary beneficiaries would not be considered to hold any ultimate economic interest. The Bill provides that in the context of a non-fixed (discretionary) trust, every individual who has ultimate economic ownership of the transferred asset before and after the transfer must be a member of the same 'family group'. This would mean that family trust elections would be necessary for a discretionary trust.

The Explanatory Memorandum to the Bill provides a useful example at the end of paragraph 1.36:

*'Chris and Victoria are husband and wife and are the only shareholders in Puppy Co, with each owning one share with a cost base of \$2 per share.*

*Puppy Co has successfully carried on a puppy training school and has acquired significant assets including puppy boarding facilities, a vehicle, and goodwill.*

*Victoria and Chris wish to transfer the puppy boarding premises from Puppy Co to a recently settled discretionary trust, the Fluffy Trust, which will lease the premises to Puppy Co. The family trust election is made nominating Victoria as the primary individual controlling the trust. Victoria and Chris are members of Victoria's family group.*

*For the purpose of the roll-over, there will not be a change in the ultimate economic ownership of the premises as a result of the transfer of the asset from Puppy Co to the Fluffy Trust. Therefore, assuming that the other requirements are also met, the roll-over would be available in respect of the transfer. '*

There are other aspects of Subdivision 328-G worth noting:

- the roll-over will only protect the income tax consequences relating to active assets of a small business. Non-active assets, such as an existing Division 7A loan or assets that have ceased to be active, are not eligible for the roll-over (see Example 1.5 of the Explanatory Memorandum);
- the transferor and transferee of the assets must be residents of Australia and cannot be exempt entities or complying superannuation entities;
- whilst the intended effect of the roll-over is to 'switch off' the application of the existing income tax law - GST and stamp duty implications would need to be addressed depending on the requirements of the relevant jurisdictions.
- the potential impact of Division 7A ITAA 1936 discussed in the author's earlier article has been addressed by the Bill. Subdivision 328-G makes it clear that the income tax law will be 'switched off', meaning that deemed dividends will not arise where they otherwise would.
- unlike the entry points for the concessions under Division 152 ITAA 1997, the maximum net asset value test is irrelevant when considering the application of Subdivision 328G. The proposed roll-over relies only on the \$2 million turnover test;
- it also won't be necessary for an 'active asset' to satisfy the 'active asset test' (section 152-35 ITAA 1997). It simply needs to be active at the time of the transfer for which the rollover is chosen.
- like other roll-overs, pre-CGT assets transferred under the roll-over would retain their pre-CGT status.
- In the context of the general 50% CGT discount, the 12 month period recommences from the time of the transfer. This prevents an entity who is otherwise ineligible for the discount (such as a company) from transferring assets to access the CGT discount and counting the previous ownership period.
- In the context of small business CGT concessions:
  - where the transferor has previously chosen to apply a small business roll-over under Subdivision 152-E ITAA 1997, and a replacement asset is transferred under this roll-over, the transferee is taken to have made the choice under Subdivision 152-E ITAA 1997 for the purposes of CGT events J2, J5 and J6;
  - the transferee will be taken as having acquired the asset when the transferor acquired it for the purposes of the 15 year CGT exemption.

Whilst it is unfortunate that the ambit of Subdivision 328-G has been narrowed, the proposed roll-over will represent a useful 'tool in the kit bag' for practitioners advising private and closely held businesses. It may be especially useful in circumstances where a business owner has established their structure without taking proper advice.

If the Bill is passed, the new Subdivision 328-G will apply from 1 July 2016.

For further information on any of the issues raised in this alert please contact:

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