



## PAY NO CAPITAL GAINS TAX ON THE SALE OF YOUR BUSINESS

You and your partner have worked hard and are considering selling your business in Australia. You are likely to make a capital gain on the sale and are concerned about the tax implications.

With the application of the Capital Gains Tax (“CGT”) Concessions, containing the 50% CGT Discount and the Small Business CGT Concessions, and the recent CGT law and superannuation changes applicable to sales post 1 July 2009, capital gains tax can be reduced and/or eliminated on the sale of assets where a capital gain is derived. Care must be taken in the structuring of the transaction from initial purchase to just before the sale to ensure that the most tax efficient result is achieved.

### THE CGT CONCESSIONS

#### **50% DISCOUNT CONCESSION**

The major CGT concession is the 50% general discount for capital gains made on the sale of most CGT assets, which includes commercial property, residential property and shares.

The key features of this 50% Discount are as follows :

- the relevant asset must have been owned for at least twelve months;
- it applies to individuals, partnerships, trusts (subject to conditions) and complying superannuation funds;
- the discount is 50% for individuals and where applicable, trusts and partnerships and 33<sup>and</sup>1/3% for complying superannuation funds; and
- the discount is applied to non-indexed capital gains.

For example, Patrick purchases an investment property at Burleigh Heads on the Gold Coast on 1 June 2004 for \$280,000, including stamp duty. He rents it out for 6 years and 3 months and sells it on 1 September 2010 for net capital proceeds of \$380,000. He has derived a \$100,000 capital gain in the 2011 financial year. Nathan is able to apply the 50% Discount Concession on this capital gain as follows :

Capital Gain derived	\$100,000
(Less) 50% General Discount	<u>(\$50,000)</u>
Net Assessable Capital Gain	<u>\$50,000</u>
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Assuming that Nathan was on the top marginal tax rate of 46.5%, the **taxation saving** available to him would be **\$23,250**.



The sale of a business can, however, attract a '0%' tax rate under the small business CGT concessions, which we outline as follows :

### **SMALL BUSINESS CGT CONCESSIONS**

There are four small business CGT concessions that apply to the sale of a business. These are :

- the small business 15-year exemption;
- the small business 50% active asset reduction;
- the small business retirement exemption; and
- the small business roll-over relief.

#### **Basic Conditions – Eligibility Tests**

In order to access the small business CGT concessions, the business owner must firstly satisfy the maximum Net Asset Value test or Turnover Test and the “active asset” test.

#### **15-year Exemption**

A capital gain made by a small business entity from a CGT asset it has owned for at least 15 years will be disregarded if the entity satisfies the above basic conditions.

#### **50% Active Asset Reduction**

For a capital gain derived on the sale of a business or property, which is an “active asset”, a 50% reduction is available, subject to the basic condition tests being satisfied. This concession is available to a business that has not been operating for 15 years, which is the more common case.

#### **Small Business Retirement Exemption**

A business owner can choose that a Capital Gain from a CGT event happening to an asset of a small business be exempt if the capital proceeds from the event are used in connection with retirement at the time of the sale. The mechanics of this exemption will depend if the individuals are under age 55 or over 55 at date of sale. For example :

Paul and Adam (in their early 60's) are partners in a partnership that operates a management rights business in Byron Bay, which was purchased in July 2006. They are considering selling the business and retiring. They will derive a \$400,000 capital gain on the sale of the business. Both partners pass the Eligibility Tests and conditions.

Capital Gain derived	\$400,000
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*The partners can elect the following concessions :*

(Less) 50% General Discount	(\$200,000)
(Less) 50% Active Asset Exemption	(\$100,000)
(Less) Retirement Exemption	(\$100,000)

Net Assessable Capital Gain	<hr style="width: 50px; margin-left: auto; margin-right: 0;"/> \$nil =====
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The partners have been able to access three successive concessions, thereby reducing their capital gain down by 100%. Assuming that Paul and Adam are on the top marginal tax rate of 46.5%, the total **taxation saving** available in this case would be **\$186,000** or \$93,000 each.

**Small Business Roll-over Relief**

The small business roll-over relief concession allows a business owner to “roll” the capital gain derived from the sale of their business to one or more new businesses or business assets. It is generally applicable to business owners under the age of 55 or that are not looking at retiring in the immediate term. The “replacement” asset must be acquired one year before or two years after the CGT event. For example :

Richard and Sue (in their early 50’s) are beneficiaries and controllers of a family discretionary trust that operates a management rights business in New Farm, Brisbane, which was established in July 2002. They are considering selling the business and relocating to Northern New South Wales, where they will purchase a management rights business for \$1,250,000 within 2 years in the same family trust entity.

They will derive a \$800,000 capital gain on the sale of the business. Both partners satisfy the Eligibility Tests and Conditions.

Capital Gain derived – Gold Coast Business	\$800,000
<i>The partners can elect the following concessions :</i>	
(Less) 50% General Discount	(\$400,000)
(Less) 50% Active Asset Exemption	(\$200,000)
(Less) Small Business Roll-over Exemption	(\$200,000)
Net Assessable Capital Gain	<hr/> \$nil =====

In a few years time, Richard and Sue may also take the net \$200,000 Small Business Roll-over amount tax-free from the Brisbane Management Rights business sale together with any capital gain from the Northern NSW business on sale, if they both retire at say age 59, up to a threshold limit of \$500,000 each or \$1 Million combined on a cumulative basis.

**CONCLUSIONS AND RECOMMENDATIONS**

Moving forward, it is imperative that your business is correctly structured to take advantage of the abovementioned CGT concessions which may in certain circumstances allow you to take 100% of the capital gain on the sale of your business tax-free. A review of ownership structure should also extend to the acquisition of any investment assets such as property and shares, in view of the 50% Discount concession.

It hard enough to acquire wealth, and so to pay a larger portion of this in tax, which was avoidable, is not good commercial decision-making.