Disclaimer:

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Overview

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  - Why Liquidate? (The Benefits)

• **Processes**
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• **Procedures**
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**The Basics**

**Purpose of the Appointment**

- To realise and collect assets, extinguishing creditors’ liabilities and distribution of surplus funds to shareholders

**Who appoints the Liquidator**

- Shareholders / Members
- Initiated by Board of Directors convening Meeting of Members (after Declaration of Solvency is issued by Directors and lodged with ASIC)

**Who is appointed**

- Title – Liquidator
- Section 532 (4) of the Corporations Act 2001
- Not required to be a registered liquidator
Why Liquidate

**Tax Benefits to shareholders where the company has:**
- Pre CGT Capital reserves;
- Active Asset Reserve:
  - Non-taxable gains resulting from small business CGT concessions;
- Shareholder loan accounts (Debit Loan Accounts);
- Debt forgiveness reserves;
- Tax sheltered gains where a pre-CGT asset of the company was deemed to become a post-CGT asset due to a majority change in ownership;
- Other non-taxed gains that are capital in nature.

**Other Benefits to shareholders:**
- The ability to distribute assets “in specie”;
- A liquidator will advertise for claims and call from Proof of Debts in order to provide certainty that the company’s liabilities have been addressed;
- Arrange Tax Clearance with ATO;
- Reduce costs of ongoing compliance by finalising a company’s affairs.
The Process

• To realise assets of the company and distribute those assets in the priorities set out in the Corporations Act.

• The Act requires that, in a Liquidation, a company’s liabilities are fully discharged prior to distributing the assets to shareholders.

• The shareholder receives a liquidator’s distribution in connection with the cancellation of their shares in the company. This receipt in the hands of the shareholder is distinctly capital in nature.

• A liquidator’s distribution is not a dividend under the ordinary tax definition specific rules were developed for distributions by liquidators.

The Process

• Under Section 47 of the Income Tax Assessment Act a liquidator’s distribution is deemed to be a dividend to the extent that it is from “income” of the company as follows:
  - ordinary income
  - statutory income
  - assessable capital gains

• A deemed dividend can only arise if the liquidator’s distribution includes one or more of these components.

• Any dividend cannot exceed the actual distribution by the liquidator. The ability of the liquidator to identify and specifically determine the composition of the distribution can be critical from a tax perspective.
The Archer Brothers
Principal

Provides guidance on how a liquidator can classify the components of a payment. The principle is summarised in ATO TD 95/10 as follows:

“By a proper system of book-keeping the liquidator, in the same way as the accountant of a private company which is a going concern, could so keep his accounts that these distributions could be made wholly and exclusively out of those particular profits or income.”

• Effectively a liquidator is required to maintain records that identify the specific source of funds from which a distribution is made.

• Prior to the appointment of a liquidator care should be taken to ensure that reserves (both Capital and Revenue) are correctly reflected in the accounts.

Archer Bros Pty Ltd (In Vol Liq) v. FCT (1952-53) 90 CLR 140

Tax considerations of the liquidator and company

The sale or transfer of the assets may result in a taxable gain. The liquidator is required to pay the tax and then distribute any cash or remaining assets to shareholders.

In-specie distributions of CGT assets to shareholders can result in a number of tax issues for the liquidator, including:
- The CGT implications of the transfer;
- The GST effect;
- The timing of tax payments and liabilities to ensure that dividends are franked to the maximum extent possible.

A liquidator can become liable for tax debts incurred after the appointment.
Returns to Shareholders

Dividends – franked and unfranked
• Shareholders are assessable on the dividend component of a liquidator’s distribution. Dividends may be franked or unfranked.

Pre-CGT shareholders
• Shareholders who acquired their shares before 20 September 1985 can potentially receive substantial tax-free capital gains on liquidation of a company. Naturally, pre-CGT shareholders are assessable on the dividend component of a liquidator’s distribution.

Differing share classes
• Management vs Equity interest issues relating to the entitlement to dividends.

Cancellation of shares
• On cancellation at completion of the liquidation, a capital gain or loss may occur. - (CGT event C2).
  • Occurs at the time the shares are cancelled which is generally 3 months after liquidator lodges the ASIC return for the holding of the final meeting of members.
  • Any assessable dividend distributed by a liquidator will form part of the proceeds for the share cancellation and can therefore reduce any capital loss.
  • The timing of dividends before or after the appointment of a liquidator can impact the availability of capital losses.
Small Business CGT Concessions

• The small business CGT concessions can substantially reduce the tax liability on sale of business assets for those taxpayers who qualify, and can be used to reduce the tax liability of shareholders on liquidation of the company.

• Shares in a company can be an active asset if the company has previously conducted a business. There are several conditions that will need to be satisfied:
  - $6 million net asset value test; or
  - $2 million turnover test.
  - Generally, the shares must have been an active asset for at least 7 years or half the ownership period.

50% active asset reduction

• Reduces the taxable capital gain by a further 50% after applying the general 50% discount (where applicable).

• The effective saving is therefore 25% of the original capital gain for an individual or trust (after applying the general 50% discount).

Retirement exemption

• up to $500,000 (lifetime limit) of the remaining taxable capital gain to be taken as a tax-free retirement benefit.

• The amount must be paid into a superannuation fund if the taxpayer is under 55 years.
Procedures
General steps

The general steps in Members Voluntary Liquidations are as follows:

Step 1: Obtain instruction and information from client
Step 2: Obtain specialist Capital Gains Tax and/or Income Tax advice, if necessary
Step 3: Obtain consent of Liquidator to act
Step 4: Meeting of directors held to initiate winding up and Declaration of Solvency lodged
Step 5: Meeting of members convened
Step 6: Meeting of members held and company placed into liquidation
Step 7: Statutory notifications and lodgements; assets realised; distributions to unpaid creditors
Step 8: Clearances from Australian Taxation Office and Office of State Revenue
Step 9: Distribution to members made
Step 10: Final meeting of members held and final returns lodged
Step 11: Company is deregistered three (3) months after the lodgement of final returns

What is Required of the Accountant

• In order to ensure an efficient, cost effective and timely winding up of the company and to provide the best outcome for the client it is helpful if the following documents are available:

- Memorandum and Articles of Association.
- Current financial statements.
- Financial statements and Income Tax Returns for a period of two (2) years preceding our engagement.
- BAS returns for a period of twelve (12) months preceding our engagement.
- Office of State Revenue (e.g. Payroll Tax) returns for a period of twelve (12) months preceding our engagement.

• Essential so that we can obtain the necessary clearances from the Australian Taxation Office and Office of State Revenue to finalise the winding-up.
The Alternative
Voluntary Deregistration

ASIC Form 6010 – Application for voluntary deregistration of a company

In order for a company to be deregistered the following circumstances need to apply:

• all members of the company agree to deregister
• the company is not conducting business
• the company's assets are worth less than $1000
• the company has no outstanding liabilities (e.g. unpaid employee entitlements)
• the company is not involved in any legal proceedings and
• the company has paid all fees and penalties payable to ASIC.

When a company is deregistered:

• Any property still owned by the company (excluding trust property) is vested in ASIC. Trust property is vested in the Commonwealth.
• Former officeholders lose any right to deal in the property that has now been vested.
• Any legal proceedings involving the company cannot continue, as the company no longer exists.
• This means it is important to finalise any of the company’s ongoing business before deregistration.
• The company directors (at the time of deregistration) must keep the company's books for at least three years from the date of deregistration.
Practical Examples

- The appointment process (when to date and lodge documents)
- Pre CGT Reserve
- Active Asset Reserve
- Correct distribution between share classes
- Completing final returns

Questions?

www.worrells.net.au
THANK YOU