



Class Ruling

Income tax: off-market share buy-back: Collins Foods Holding Pty Ltd

Contents	Para
LEGALLY BINDING SECTION:	
What this Ruling is about	1
Date of effect	8
Scheme	9
Ruling	24
NOT LEGALLY BINDING SECTION:	
Appendix 1:	
Explanation	46
Appendix 2:	
Detailed contents list	103

ⓘ This publication provides you with the following level of protection:

This publication (excluding appendixes) is a public ruling for the purposes of the *Taxation Administration Act 1953*.

A public ruling is an expression of the Commissioner's opinion about the way in which a relevant provision applies, or would apply, to entities generally or to a class of entities in relation to a particular scheme or a class of schemes.

If you rely on this ruling, the Commissioner must apply the law to you in the way set out in the ruling (unless the Commissioner is satisfied that the ruling is incorrect and disadvantages you, in which case the law may be applied to you in a way that is more favourable for you – provided the Commissioner is not prevented from doing so by a time limit imposed by the law). You will be protected from having to pay any underpaid tax, penalty or interest in respect of the matters covered by this ruling if it turns out that it does not correctly state how the relevant provision applies to you.

What this Ruling is about

1. This Ruling sets out the Commissioner's opinion on the way in which the relevant provision(s) identified below apply to the defined class of entities, who take part in the scheme to which this Ruling relates.

Relevant provision(s)

2. The relevant provisions dealt with in this Ruling are:

- section 6 of the *Income Tax Assessment Act 1936* (ITAA 1936);
- subsection 44(1) of the ITAA 1936;
- section 45A of the ITAA 1936;
- section 45B of the ITAA 1936;
- section 45C of the ITAA 1936;
- subsection 95(1) of the ITAA 1936;
- paragraph 128B(3)(ga) of the ITAA 1936;
- section 159GZZZP of the ITAA 1936;
- section 159GZZZQ of the ITAA 1936;

- Division 1A of former Part IIIAA of the ITAA 1936;
- section 177EA of the ITAA 1936;
- section 6-5 of the *Income Tax Assessment Act 1997* (ITAA 1997);
- Division 67 of the ITAA 1997;
- section 104-10 of the ITAA 1997;
- section 116-20 of the ITAA 1997;
- section 118-20 of the ITAA 1997;
- section 118-25 of the ITAA 1997;
- section 202-5 of the ITAA 1997;
- section 202-40 of the ITAA 1997;
- section 204-30 of the ITAA 1997;
- section 207-20 of the ITAA 1997;
- section 207-45 of the ITAA 1997;
- section 855-10 of the ITAA 1997; and
- section 855-15 of the ITAA 1997.

All legislative references in this Ruling are to the ITAA 1936 unless otherwise indicated.

Class of entities

3. The class of entities to which this Ruling applies is the shareholders of Collins Foods Holding Pty Ltd (Collins Foods) who disposed of their ordinary shares in Collins Foods under the Collins Foods selective off-market share buy-back (Buy-Back) described in the Scheme part of this Ruling and are not subject to the taxation of financial arrangements rules in Division 230 of the ITAA 1997. In this Ruling, the shareholders of Collins Foods are referred to as 'shareholders' or 'participating shareholders'.

(Note – Division 230 will generally not apply to individuals, unless they have made an election for it to apply to them.)

Qualifications

4. The Commissioner makes this Ruling based on the precise scheme identified in this Ruling.

5. The class of entities defined in this Ruling may rely on its contents provided the scheme actually carried out is carried out in accordance with the scheme described in paragraphs 9 to 23 of this Ruling.

6. If the scheme actually carried out is materially different from the scheme that is described in this Ruling, then:

- this Ruling has no binding effect on the Commissioner because the scheme entered into is not the scheme on which the Commissioner has ruled; and
- this Ruling may be withdrawn or modified.

7. This work is copyright. Apart from any use as permitted under the *Copyright Act 1968*, no part may be reproduced by any process without prior written permission from the Commonwealth. Requests and inquiries concerning reproduction and rights should be addressed to:

Commonwealth Copyright Administration
Copyright Law Branch
Attorney-General's Department
National Circuit
Barton ACT 2600
or posted at: <http://www.ag.gov.au/ccca>

Date of effect

8. This Ruling applies from 1 July 2010 to 30 June 2011. The Ruling continues to apply after 30 June 2011 to all entities within the specified class who entered into the specified scheme during the term of the Ruling. However, this Ruling will not apply to taxpayers to the extent that it conflicts with the terms of a settlement of a dispute agreed to before the date of issue of this Ruling (see paragraphs 75 and 76 of Taxation Ruling TR 2006/10).

Scheme

9. The following description of the scheme is based on information provided by the applicant. The following documents or relevant parts of them form part of and are to be read with the description:

- Class Ruling application and annexures dated 20 August 2010 and
- Annual financial statements of Collins Foods for the years ended 27 April 2008, 3 May 2009 and 2 May 2010.

Note: certain information has been provided on a commercial-in-confidence basis and will not be disclosed or released under Freedom of Information legislation.

10. Collins Foods is the Australian resident head company of a consolidated group for Australian income tax purposes and is not listed on the Australian Securities Exchange.

11. Collins Foods' ordinary shares are comprised of
 - active ordinary shares;
 - active preferred ordinary shares;
 - passive ordinary shares; and
 - passive preferred ordinary shares.
12. As at 2 May 2010, Collins Foods had 53,377,485 fully paid active shares on issue which comprised of 35,998,970 active ordinary shares and 17,378,515 active preferred ordinary shares. Shares in Collins Foods are held by a mix of individuals and investment funds, some of whom are non-residents
13. The financial statements of Collins Foods as at 2 May 2010 show total share capital of \$53.62 million, nil reserves and retained earnings of \$9.01 million.
14. Following finalisation of its financial statements for the year ended 2 May 2010, Collins Foods proposed to undertake a Buy-Back of up to approximately 8.5% of Collins Foods' ordinary share capital. The Buy-Back took place on 23 September 2010 for a total consideration of approximately \$6.6m.
15. The Buy-Back was initiated to provide shareholders, many of whom had held their shares for a significant period of time, with an opportunity to obtain liquidity for their investment.
16. For each active ordinary share or each active preferred ordinary share bought back, Collins Foods acquired a further 100 passive ordinary shares or 100 passive preferred ordinary shares. Irrespective of the number of passive ordinary or passive preferred ordinary shares bought back, each shareholder was paid a total of one cent for the entire bundle of their passive ordinary or passive preferred ordinary shares bought back.
17. The Buy-Back tender period opened on 31 August 2010 and closed on 3 September 2010.
18. The Buy-Back was in the nature of an offer under which eligible shareholders were able to sell their shares at the price nominated by Collins Foods.
19. Participation in the Buy-Back was voluntary and therefore eligible shareholders who did not wish to participate were not required to return the Buy-Back Offer Acceptance Form. Due to restrictions imposed by external financiers a dividend could not be paid at this time and the investment fund shareholders were not able to participate in the Buy-Back. Non-participating shareholders did not receive any property, dividends or distributions by way of compensation for being unable to participate in the Buy-Back.
20. The Buy-Back Price was set at \$1.457 per active ordinary share or preferred ordinary share which Collins Foods considered represented the market value for those shares as at 23 September 2010.

21. As tenders were received for more than the number of ordinary shares Collins Foods proposed to buy-back, acceptances were scaled back on a pro-rata basis.
22. All shares bought under the Buy-Back were cancelled.
23. Under the Buy-Back, \$1.036 per share was debited to Collins Foods' untainted share capital account and the balance of the Buy-Back Price of \$0.421 was debited to Collins Foods' retained earnings and the maximum franking credit was allocated to the amount.

Ruling

The Dividend Component

24. Participating shareholders will be taken to have been paid a dividend of \$0.421 (the Dividend Component) for each active ordinary share and active preferred ordinary share bought back under section 159GZZP.
25. The Dividend Component is a frankable distribution pursuant to section 202-40 of the ITAA 1997 and is therefore capable of being franked in accordance with section 202-5 of the ITAA 1997.
26. The difference between the Buy-Back Price and the Dividend Component is not a dividend for income tax purposes.

Assessability of the Dividend Component and tax offset

Direct Distributions

27. The Dividend Component of \$0.421 and an amount equal to the franking credit on the Dividend Component (gross-up) is included in the assessable income of resident individual and company shareholders who participated in the Buy-Back under subsection 44(1) and subsection 207-20(1) of the ITAA 1997 respectively in the income year in which the Buy-Back occurred. These shareholders, subject to being a 'qualified person', will be entitled to a tax offset under subsection 207-20(2) of the ITAA 1997 equal to the amount of the franking credit on the Dividend Component.

Indirect distributions

Trusts

28. The Dividend Component of \$0.421 and an amount equal to the franking credit on the Dividend Component (gross-up) is included in the assessable income of a trustee for the purposes of computing the net income of the trust under subsection 95(1).

29. In a case where an individual beneficiary, corporate beneficiary, or a trustee beneficiary specified by paragraphs 207-45(c) or (d) of the ITAA 1997 (certain trustees, and certain superannuation funds, approved deposit funds and pooled superannuation trusts) is assessable in respect of a share of the net income of the trust, the beneficiary both includes an amount in its assessable income (the gross-up), and is entitled to a tax offset equal to the beneficiary's share of the franking credit on the Dividend Component, provided that the Dividend Component was taken into account in working out the whole or part of that share of the net income of the trust.

Refundable tax offset

30. The tax offsets may be refundable under Division 67 of the ITAA 1997. However, because of subsections 67-25(1A) to (1D), certain trustees and corporate tax entities are not entitled to refunds for the offsets.

Non-resident shareholders

31. Participating non-resident shareholders are not liable for Australian withholding tax because paragraph 128B(3)(ga) applies.

Sale Consideration

32. Participating shareholders are taken to have received \$1.036 as consideration in respect of each share bought back under the Buy-Back (Sale Consideration) on 23 September 2010 in accordance with section 159GZZZQ, unless the participating shareholder is a corporate tax entity to which subsections 159GZZZQ(8) and (9) apply.

33. If the Buy-Back Price for each share bought back under the Buy-Back was less than what would have been the market value of the share if the Buy-Back did not occur and was never proposed to occur then the market value rule in subsection 159GZZZQ(2) applies to the Buy-Back. The effect of this rule is that the difference between the Buy-Back Price and the market value will be included in the consideration received for the disposal of the share for ordinary income or capital gains tax (CGT) purposes, in addition to the capital amount of \$1.036 per share debited to the share capital account (Capital Component). No adjustment is required under the market value rule in paragraph 159GZZZQ(2) because the purchase price was equal to the market value. Accordingly, the Sale Consideration is \$1.036.

34. The treatment of the Sale Consideration amount for tax purposes will depend on whether the Collins Foods share is held on capital account or on revenue account.

Shares held on capital account

35. CGT event A1 happens when a participating Collins Foods shareholder disposes of their share under the Buy-Back (subsection 104-10(1) and (2) of the ITAA 1997).

36. The time of the CGT event is when the change of ownership occurs (subsection 104-10(3) of the ITAA 1997). This is when the Collins Foods shares are disposed of to Collins Foods and cancelled being 23 September 2010.

37. The Sale Consideration of \$1.036 represents the capital proceeds for CGT purposes pursuant to section 116-20 of the ITAA 1997. A participating Collins Foods shareholder makes a capital gain when CGT event A1 happens if the capital proceeds in respect of the disposal of their Collins Foods share is more than its cost base. A participating Collins Foods shareholder makes a capital loss if the capital proceeds in respect of the disposal of their Collins Foods share is less than its reduced cost base (subsection 104-10(4) of the ITAA 1997).

Foreign resident shareholders

38. A foreign resident Collins Foods shareholder who participates in the Buy-Back disregards any capital gain made when CGT event A1 happens if their share is not 'taxable Australian property' (section 855-10 of the ITAA 1997).

Shares held on revenue account

39. Where the shares are held as trading stock, the Sale Consideration of \$1.036 is included in assessable income under section 6-5 of the ITAA 1997. These shareholders will also make a capital gain or capital loss calculated as discussed above at paragraph 37 for those who held their shares on capital account. However, under section 118-25 of the ITAA 1997 any capital gain or capital loss a participating shareholder makes will be disregarded if at the time of the CGT event the shares are held by them as trading stock.

40. Where the shares are held as revenue assets, but are not trading stock, the amount by which the Sale Consideration of \$1.036 per share exceeds the cost of each share is included in the shareholder's assessable income. Correspondingly, if the cost exceeds the Sale Consideration of \$1.036 per share the difference is an allowable deduction. Where the Sale Consideration per share exceeds the cost base of that share these shareholders will also make a capital gain. However, under section 118-20 of the ITAA 1997 any capital gain a participating shareholder makes will be reduced to the extent that the capital proceeds have otherwise been included in assessable income.

Qualified persons

41. For the purposes of Division 1A of former Part IIIAA, participating shareholders will be considered to satisfy the holding period rule under former section 160APHO and therefore be qualified persons (as long as the related payments rule is also met) in relation to the Dividend Component received under the Buy-Back if:

- the shares sold via the Buy-Back were acquired on or before 8 August 2010; and
- during the period when the shares or interest in the shares were held, the shareholders had sufficient risks of loss or opportunities for gain in respect of the shares or interest in the shares (as defined in former section 160APHM) for a continuous period of at least 45 days. Neither the announcement of the Buy-Back, the making of an invitation to shareholders to offer to sell their Collins Foods shares nor the making of an offer by a shareholder to Collins Foods in respect of a Collins Foods share will affect whether the shares bought back under the Buy-Back were held 'at risk' for the purposes of Division 1A of former Part IIIAA.

42. A shareholder who acquired shares after 8 August 2010 that were subsequently accepted into the Buy-Back pursuant to the 'last-in first-out' rule is not a qualified person in relation to the Dividend Component under former section 160APHO unless certain exceptions are met.

The anti-avoidance provisions

43. The Commissioner will not make a determination under subsection 45A(2) or 45B(3) that section 45C applies to the whole, or any part, of the Capital Component of the Buy-Back Price received by participating shareholders.

44. The Commissioner will not make a determination under paragraph 177EA(5)(b) to deny the whole, or any part, of the imputation benefits received in relation to the Dividend Component of the Buy-Back Price by participating shareholders.

45. The Commissioner will not make a determination under paragraph 204-30(3)(c) of the ITAA 1997 to deny the whole, or any part, of the imputation benefits received in relation to the Dividend Component of the Buy-Back Price by participating shareholders.

Appendix 1 – Explanation

❶ *This Appendix is provided as information to help you understand how the Commissioner's view has been reached. It does not form part of the binding public ruling.*

The Dividend and Capital Components

46. The purchase price received by participating shareholders comprises two components:

- a Dividend Component; and
- a Capital Component.

47. The amount of each of these components is determined in accordance with sections 159GZZZP and 159GZZZQ, having regard to how the company accounts for the off-market share buy-back.

The Dividend Component

48. Section 159GZZZP provides that where the buy-back of a share is an off-market purchase, the difference between the purchase price and the part (if any) of the purchase price which is debited against the share capital account, is taken to be a dividend paid by the company to the seller on the day the buy-back occurs. For participating shareholders this was 23 September 2010. In this case the purchase price was \$1.457 per share and \$1.036 of this was debited to the share capital account. Therefore the Dividend Component is \$0.421 per share.

49. The Dividend Component of \$0.421 per share is frankable but only to the extent that the Buy-Back Price does not exceed the market value of the share at the time of the Buy-Back if the Buy-Back did not occur and was never proposed to occur (paragraph 202-45(c) of the ITAA 1997). In this case, the Buy-Back Price did not exceed the market value and consequently paragraph 202-45(c) of the ITAA 1997 does not apply to treat any of the Dividend Component as unfrankable. As the requirements of section 202-5 of the ITAA 1997 are met and the maximum franking credit was allocated to the amount, the distribution was fully franked.

50. Subsection 159GZZZP(2) provides that the difference between the Buy-Back Price and the Dividend Component is not a dividend for income tax purposes.

Assessability of the Dividend Component and tax offset

Direct distributions

51. In the case of Australian resident shareholders (other than a trust) who participate in the Buy-Back and who directly receive the Dividend Component:

- the Dividend Component is included in the assessable income of each shareholder under subsection 44(1); and
- subject to the 'qualified person' rule, an amount equal to the amount of the franking credit on the Dividend Component is included in the assessable income of each shareholder under subsection 207-20(1) of the ITAA 1997 (gross-up).

52. Subject to the 'qualified person' rule, these shareholders are entitled to a tax offset under subsection 207-20(2) of the ITAA 1997 equal to the amount of the franking credit on the Dividend Component.

Indirect distributions

Trusts

53. The franked distribution may flow indirectly to a beneficiary of certain trusts.

54. In general terms, pursuant to subsection 207-50(3) of the ITAA 1997, a franked distribution will flow indirectly to a beneficiary of a trust where the beneficiary:

- has a share of the trust's net income that is covered by paragraph 97(1)(a) or has an individual interest in the trust's net income that is covered by paragraph 98A(1)(a) or (b) or paragraph 100(1)(a) or (b); and
- has a share of the franked distribution under section 207-55 of the ITAA 1997 that is a positive amount.

55. In the case of certain trusts that participate in the Buy-Back the following income tax consequences arise.

56. Pursuant to subsection 44(1), the Dividend Component is included in the assessable income of a trustee for the purposes of computing the net income of the trust under subsection 95(1).

57. Subject to the 'qualified person' rule, pursuant to subsection 207-35(1) of the ITAA 1997, an amount equal to the amount of the franking credit on the Dividend Component is included in the assessable income of the trustee for the purposes of computing the net income of the trust under subsection 95(1) (gross-up).

58. In the case where an individual beneficiary, corporate beneficiary, or a trustee beneficiary specified by paragraph 207-45(c) or (d) of the ITAA 1997 (that is, trustees liable to be assessed under section 98, 99 or 99A, or certain superannuation funds, approved deposit funds and pooled superannuation trusts) has a share of the trust's net income that is covered by paragraph 97(1)(a) or has an individual interest in the trust's net income that is covered by paragraph 98A(1)(a) or (b) or paragraph 100(1)(a) or (b), and the beneficiary has a share of the Dividend Component under section 207-55 of the ITAA 1997 that is a positive amount, the beneficiary is, subject to the 'qualified person' rule, assessed on an amount equal to the beneficiary's share of the franking credit on the Dividend Component as calculated under section 207-57 of the ITAA 1997, and entitled to a tax offset of the same amount.

Refundable tax offset

59. The tax offsets are subject to the refundable tax offset rules in Division 67 of the ITAA 1997, provided the participating shareholders are not excluded by subsections 67-25(1A) to (1D) of the ITAA 1997.

Non-resident shareholders

60. As the Dividend Component of the consideration received under the Buy-Back is fully franked and no determination will be made in relation to the Dividend Component under either paragraph 204-30(3)(c) of the ITAA 1997 or paragraph 177EA(5)(b), a non-resident shareholder is not liable to Australian withholding tax on the Dividend Component (paragraph 128B(3)(ga)).

Sale consideration

Calculation of Sale Consideration

61. For the purpose of computing the amount of the gain or loss (on capital or revenue account) in these cases, the consideration in respect of the disposal of a share under a buy-back is determined in accordance with section 159GZZZQ.

62. Subsection 159GZZZQ(1) provides that the shareholder is taken to have received an amount equal to the purchase price (in this case the \$1.457 received for each share bought back) as consideration in respect of the sale of the share bought back. However, this amount is subject to certain adjustments in order to arrive at the Sale Consideration.

63. Subsection 159GZZZQ(2) is one of the adjusting provisions. It provides that if the purchase price is less than the market value of the share at the time of the buy-back if the buy-back did not occur and was never proposed to occur the shareholder is taken to have received an amount equal to the market value as consideration in respect of the sale of the share bought back.

64. The implied value of the ordinary share classes, referable to shadow equity issued, was the method proposed to determine the market value for the shares bought back. This method was accepted by the Commissioner as being appropriate for determining market value for the purposes of subsection 159GZZZQ(2).

65. Under this methodology, the market value of a share bought back under the Buy-Back was calculated to be \$1.457.

66. Pursuant to subsection 159GZZZQ(3), the deemed consideration of \$1.457 is reduced by a 'Reduction Amount'. The Reduction Amount is an amount calculated under subsection 159GZZZQ(4). In the circumstances of the Buy-Back, the Reduction Amount is equivalent to the Dividend Component, that is, \$0.421 unless the seller is a corporate tax entity to whom subsection 159GZZZQ(8) applies. Therefore, the Sale Consideration for each share disposed of under the Buy-Back is \$1.036 (\$1.457 less \$0.421).

67. However, it should be noted that where the participating shareholder is a corporate tax entity, which is entitled to a tax offset under Division 207 of the ITAA 1997 in respect of the Dividend Component, an adjustment may be made to the Sale Consideration. Under subsection 159GZZZQ(8) if that shareholder would otherwise incur either a capital loss or a deductible loss (or any increase in such a loss) in respect of the sale of a share bought back under the Buy-Back, the Sale Consideration is increased by an off-settable amount determined under subsection 159GZZZQ(9). The reduction amount is reduced by so much of the off-settable amount that does not exceed the capital loss or the deductible loss.

68. Participating shareholders are taken to have disposed of those shares accepted under the Buy-Back on 23 September 2010. The disposal may have different taxation implications for shareholders depending on how the shares were held, for instance:

- an investor who held their shares on capital account will be subject to the CGT provisions; and
- a share trader who held their shares on revenue account will be subject to the ordinary income provisions and the CGT provisions.

Shares held on capital account

69. CGT event A1 happens if there is a change in the ownership of an asset from one entity to another (section 104-10 of the ITAA 1997). This event happens when a contract to dispose of the asset is entered into or, if there is no contract, when the change of ownership occurs (subsection 104-10(3) of the ITAA 1997).

70. A Buy-Back does not involve a disposal of shares under a contract.

71. CGT event A1 happened when participating Collins Foods shareholders disposed of their Collins Foods shares pursuant to the Buy-Back. The disposal occurred on the date of the Buy-Back, being 23 September 2010 as this was the date that the change in ownership occurred (subsections 104-10(1) and (2) of the ITAA 1997).

72. The time when CGT event A1 happens determines the income year in which any capital gain or capital loss is made and whether the CGT discount applies to any capital gain.

73. A participating Collins Foods shareholder makes a capital gain from CGT event A1 happening if the capital proceeds from the disposal of their share exceeds its cost base. A participating Collins Foods shareholder makes a capital loss if the capital proceeds are less than the share's reduced cost base (subsection 104-10(4) of the ITAA 1997).

74. The Sale Consideration of \$1.036 represents the capital proceeds for CGT purposes pursuant to section 116-20 of the ITAA 1997. A shareholder will make a capital gain on a share if the Sale Consideration per share exceeds the cost base of that share. The capital gain is the amount of the excess. Similarly, a shareholder will make a capital loss on a share if the Sale Consideration per share is less than the reduced cost base of the share (subsection 104-10(4) of the ITAA 1997).

Foreign resident shareholders

75. Under subsection 855-10(1) of the ITAA 1997, an entity disregards a capital gain or capital loss from a CGT event if they are a foreign resident, or the trustee of a foreign trust for CGT purposes, just before the CGT event happens and the CGT event happens in relation to a CGT asset that is not 'taxable Australian property'.

76. The term 'taxable Australian property' is defined in the table in section 855-15 of the ITAA 1997. The table sets out these five categories of CGT assets:

Item 1	taxable Australian real property;
Item 2	an indirect Australian real property interest not covered by item 5;
Item 3	a CGT asset used at any time in carrying on a business through a permanent establishment in Australia and which is not covered by item 1, 2 or 5;
Item 4	an option or right to acquire a CGT asset covered by item 1, 2 or 3; and
Item 5	a CGT asset that is covered by subsection 104-165(3) of the ITAA 1997 (choosing to disregard a gain or loss on ceasing to be an Australian resident).

77. A foreign resident, or the trustee of a foreign trust for CGT purposes, just before CGT event A1 happened under the buy-back, can not disregard under subsection 855-10(1) of the ITAA 1997 a capital gain or capital loss from CGT event A1 if:

- their share in Collins Foods is an indirect Australian real property interest (item 2 of the table in section 855-15 of the ITAA 1997); or
- their share in Collins Foods has been used at any time by the foreign resident, or the trustee of a foreign trust for CGT purposes, in carrying on a business through a permanent establishment in Australia (item 3 of the table in section 855-15 of the ITAA 1997); or
- their share in Collins Foods is covered by subsection 104-165(3) of the ITAA 1997 (item 5 of the table in section 855-15 of the ITAA 1997).

Shares held on revenue account

78. Where the shares are held as trading stock, the Sale Consideration of \$1.036 is included in assessable income under section 6-5 of the ITAA 1997. These shareholders will also make a capital gain or capital loss. However, under section 118-25 of the ITAA 1997 any capital gain or capital loss a participating shareholder makes will be disregarded if at the time of the CGT event the shares are held by them as trading stock.

79. Where the shares are held as revenue assets, the amount by which the Sale Consideration of \$1.036 per share exceeds the cost of each share is included in the shareholder's assessable income. Correspondingly, if the cost exceeds the Sale Consideration of \$1.036 per share the difference is an allowable deduction. Where the Sale Consideration per share exceeds the cost base of that share these shareholders will also make a capital gain. However, shareholders who hold their shares as revenue assets will have the amount of the capital gain reduced under the anti-overlap provisions contained in section 118-20 of the ITAA 1997.

Qualified persons

80. Paragraph 207-145(1)(a) of the ITAA 1997 provides that in relation to a franked dividend made to an entity only a '...qualified person in relation to the distribution for the purposes of Division 1A of former Part IIIA...' is entitled to a franking credit or tax offset. Broadly speaking, to be a 'qualified person' in relation to the Dividend Component paid under the Buy-Back, the participating shareholder must satisfy both the holding period rule and the related payments rule.

81. Broadly, a shareholder will not satisfy the related payments rule if the shareholder, or associate of the shareholder, is under an obligation to make, or makes, a payment in respect of the dividend which effectively passes the benefit of the dividend to another person.

82. The holding period rule requires shareholders to hold the shares, or the interest in the shares, on which the dividend is paid at risk for a continuous period of at least 45 days if the shares are not preference shares or 90 days if the shares are preference shares. In determining whether a shareholder has satisfied the holding period rule, any days during which there is a materially diminished risk in relation to the relevant shares are not counted. The day of acquisition and the day of disposal of the relevant shares are also not counted.

83. Under former subsection 160APHM(2), a shareholder is taken to have materially diminished the risks of loss and opportunities for gain with respect to shares or interests in shares if the 'net position' of the shareholder results in the shareholder having less than 30% of the risks and opportunities relating to the shares or interest in shares.

84. In this case the Commissioner does not regard the announcement of the Buy-Back offer as affecting whether the shares or an interest in shares were held at risk or not.

85. There are 45 clear days between 8 August 2010 and 23 September 2010 that is, the date the offer was accepted. Therefore, a shareholder who acquired shares on or before 8 August 2010 satisfies the holding period rule as long as those shares were held at risk for at least 45 continuous days. A shareholder who acquired shares after 8 August 2010 that were subsequently bought back under the Buy-Back is not a qualified person in relation to the dividend paid under the Buy-Back for the purposes of Division 1A of former Part IIIAA.

86. Generally, under the holding period rule a shareholder will be deemed to have disposed of his or her most recently acquired shares first under former subsection 160APHI(4). The 45 day rule operates on a last-in first-out basis, so that shareholders will be deemed to have disposed of their most recently acquired shares first for the purposes of applying the 45 day rule. Accordingly, shareholders who, after 8 August 2010 acquired any additional Collins Foods shares which conferred an entitlement to participate in the Buy-Back, may not qualify for the franking credits attached to the dividends paid on some or all of their shares sold into the Buy-Back.

The anti-avoidance provisions

Sections 45A and 45B

87. Sections 45A and 45B are two anti-avoidance provisions which, if they apply, allow the Commissioner to make a determination that section 45C applies. The effect of such a determination is that all or part of the distribution of capital received by the shareholder under the Buy-Back is treated as an unfranked dividend. Accordingly, the application of these two provisions to the Buy-Back must be considered.

88. Section 45A is an anti-avoidance provision that applies in circumstances where capital benefits are streamed to certain shareholders (the advantaged shareholders) who derive a greater benefit from the receipt of share capital and it is reasonable to assume that the other shareholders (the disadvantaged shareholders) have received or will receive dividends.

89. Although a 'capital benefit' (as defined in paragraph 45A(3)(b)) is provided to participating shareholders under the Buy-Back, the circumstances of the Buy-Back indicate that there is no streaming of capital benefits to some shareholders and dividends to other shareholders. Accordingly, section 45A has no application to the Buy-Back.

90. Section 45B applies where certain capital payments are paid to shareholders in substitution for dividends. In broad terms, section 45B applies where:

- (a) there is a scheme under which a person is provided with a capital benefit by a company (paragraph 45B(2)(a));
- (b) under the scheme, a taxpayer (the 'relevant taxpayer'), who may or may not be the person provided with the capital benefit, obtains a tax benefit (paragraph 45B(2)(b)); and
- (c) having regard to the relevant circumstances of the scheme, it would be concluded that the person, or one of the persons, who entered into or carried out the scheme or any part of the scheme did so for a purpose (whether or not the dominant purpose but not including an incidental purpose), of enabling the relevant taxpayer to obtain a tax benefit (paragraph 45B(2)(c)).

91. In the case of the Buy-Back, whilst the conditions of paragraphs 45B(2)(a) and 45B(2)(b) have been met, the requisite purpose of enabling the shareholder to obtain a tax benefit – by way of capital distribution – was not present.

92. Having regard to the 'relevant circumstances' of the scheme (the Buy-Back), as set out in subsection 45B(8), it is apparent that the inclusion of a Capital Component as part of the Buy-Back Price was not inappropriate. Further, the Capital Component of the Buy-Back cannot be said to be attributable to the profits of the company, nor does the pattern of distributions indicate that the Capital Component is being paid in substitution for a dividend. Accordingly, section 45B has no application to the Buy-Back.

Section 177EA

93. Section 177EA is a general anti-avoidance provision that applies to a wide range of schemes to obtain a tax advantage in relation to imputation benefits. In essence, it applies to schemes for the disposition of shares or an interest in shares, where a franked distribution is paid or payable in respect of the shares or an interest in shares. This would include a buy-back with a franked dividend component.

94. Specifically, subsection 177EA(3) provides that section 177EA applies if:

- (a) there is a scheme for a disposition of membership interests, or an interest in membership interests, in a corporate tax entity; and
- (b) either:
 - (i) a frankable distribution has been paid, or is payable or expected to be payable, to a person in respect of the membership interests; or
 - (ii) a frankable distribution has flowed indirectly, or flows indirectly or is expected to flow indirectly, to a person in respect of the interest in membership interests, as the case may be; and
- (c) the distribution was, or is expected to be, a franked distribution or a distribution franked with an exempting credit; and
- (d) except for this section, the person (the 'relevant taxpayer') would receive, or could reasonably be expected to receive, imputation benefits as a result of the distribution; and
- (e) having regard to the relevant circumstances of the scheme, it would be concluded that the person, or one of the persons, who entered into or carried out the scheme or any part of the scheme did so for a purpose (whether or not the dominant purpose but not including an incidental purpose) of enabling the relevant taxpayer to obtain an imputation benefit.

95. In the present case the conditions of paragraphs 177EA(3)(a) to (d) are satisfied. Accordingly, the issue is whether, having regard to the relevant circumstances of the scheme, it would be concluded that, on the part of Collins Foods, its shareholders or any other relevant party, there is a purpose more than merely an incidental purpose of conferring an imputation benefit under the scheme. Under this arrangement the relevant taxpayer is the participating shareholder and the scheme comprises the circumstances surrounding the Buy-Back.

96. In arriving at a conclusion the Commissioner must have regard to the relevant circumstances of the scheme which include, but are not limited to, the circumstances set out in subsection 177EA(17). The relevant circumstances listed there encompass a range of circumstances which taken individually or collectively could indicate the requisite purpose. Due to the diverse nature of these circumstances some may not be present at any one time in any one scheme.

97. The Commissioner has come to the view that section 177EA applies to the Buy-Back. In coming to this conclusion the Commissioner had regard to all the relevant circumstances of the arrangement, as outlined in subsection 177EA(17). Among the circumstances of the Buy-Back reflected in those paragraphs are:

- the delivery of franking credits in excess of what would have otherwise been distributed in the ordinary course of dividend declaration;
- the greater attraction of the Buy-Back to resident shareholders who could fully utilise the franking credits than to non-resident shareholders who could not.

98. Where section 177EA applies the Commissioner has a discretion, pursuant to subsection 177EA(5) to make a determination to debit the company's franking account pursuant to paragraph 177EA(5)(a), or deny the imputation benefit to each shareholder pursuant to paragraph 177EA(5)(b). The Commissioner will exercise his discretion in such a way that he does not make a determination that the imputation benefit obtained by the participating shareholders be denied under paragraph 177EA(5)(b).

Section 204-30

99. Section 204-30 of the ITAA 1997 applies where a corporate tax entity streams the payment of dividends, or the payment of dividends and the giving of other benefits, to its members in such a way that:

- (a) an imputation benefit is, or apart from this section would be, received by a member of the entity as a result of the distribution or distributions (paragraph 204-30(1)(a) of the ITAA 1997);
- (b) the member would derive a greater benefit from franking credits than another member of the entity (paragraph 204-30(1)(b) of the ITAA 1997); and
- (c) the other member of the entity will receive lesser imputation benefits, or will not receive any imputation benefits, whether or not the other member receives other benefits (paragraph 204-30(1)(c) of the ITAA 1997).

100. Relevantly, if section 204-30 of the ITAA 1997 applies, the Commissioner is vested with a discretion under subsection 204-30(3) of the ITAA 1997 to make a determination in writing either:

- (a) that a specified franking debit arises in the franking account of the entity, for a specified distribution or other benefit to a disadvantaged member (paragraph 204-30(3)(a) of the ITAA 1997); or
- (b) that no imputation benefit is to arise in respect of any streamed distribution made to a favoured member and specified in the determination (paragraph 204-30(3)(c) of the ITAA 1997).

101. For section 204-30 of the ITAA 1997 to apply, members to whom distributions are streamed must derive a greater benefit from imputation benefits than the members who do not participate in the Buy-Back. The words 'derive a greater benefit from franking credits' (imputation benefits) are defined in subsection 204-30(8) of the ITAA 1997 by reference to the ability of the members to fully utilise imputation benefits.

102. A portion of Collins Foods shareholding was held by non-residents who do not fully benefit from franking, a feature of the Buy-Back, to the same extent as resident shareholders. Therefore, the conditions in subsection 204-30(1) of the ITAA 1997 for the provision to apply are met. However, the Commissioner will not make a determination under section 204-30 of the ITAA 1997.

Appendix 2 – Detailed contents list

103. The following is a detailed contents list for this Ruling:

	Paragraph
What this Ruling is about	1
Relevant provision(s)	2
Class of entities	3
Qualifications	4
Date of effect	8
Scheme	9
Ruling	24
The Dividend Component	24
Assessability of the Dividend Component and tax offset	27
<i>Direct Distributions</i>	27
<i>Indirect Distributions</i>	28
<i>Trusts</i>	28
<i>Refundable tax offset</i>	30
<i>Non-resident shareholders</i>	31
Sale Consideration	32
<i>Shares held on capital account</i>	35
<i>Foreign resident shareholders</i>	38
<i>Shares held on revenue account</i>	39
Qualified persons	41
The anti-avoidance provisions	43
Appendix 1 – Explanation	46
The Dividend and Capital Components	46
The Dividend Component	48
Assessability of the Dividend Component and tax offset	51
<i>Direct distributions</i>	51
<i>Indirect distributions</i>	53
<i>Trusts</i>	53
<i>Refundable tax offset</i>	59
<i>Non-resident shareholders</i>	60
Sale Consideration	61
<i>Calculation of Sale Consideration</i>	61

<i>Shares held on capital account</i>	69
<i>Foreign resident shareholders</i>	75
<i>Shares held on revenue account</i>	78
Qualified persons	80
The anti-avoidance provisions	87
<i>Sections 45A and 45B</i>	87
<i>Section 177EA</i>	93
<i>Section 204-30</i>	99
Appendix 2 – Detailed contents list	103

References

Previous draft:

Not previously issued as a draft

Related Rulings/Determinations:

TR 2006/10

Subject references:

- dividend income
- dividend streaming arrangements
- frankable dividends
- qualified person
- share buy backs

Legislative references:

- ITAA 1936 177EA(3)
- ITAA 1936 177EA(3)(a)
- ITAA 1936 177EA(3)(b)
- ITAA 1936 177EA(3)(c)
- ITAA 1936 177EA(3)(d)
- ITAA 1936 177EA(3)(e)
- ITAA 1936 177EA(5)
- ITAA 1936 177EA(5)(a)
- ITAA 1936 177EA(5)(b)
- ITAA 1936 177EA(17)
- ITAA 1997 6-5
- ITAA 1997 Div 67
- ITAA 1997 67-25(1A)
- ITAA 1997 67-25(1B)
- ITAA 1997 67-25(1C)
- ITAA 1997 67-25(1D)
- ITAA 1997 104-10
- ITAA 1997 104-10(1)
- ITAA 1997 104-10(2)
- ITAA 1997 104-10(3)
- ITAA 1997 104-10(4)
- ITAA 1997 104-165(3)
- ITAA 1997 116-20
- ITAA 1997 118-20
- ITAA 1997 118-25
- ITAA 1997 202-5
- ITAA 1997 202-40
- ITAA 1997 202-45(c)
- ITAA 1997 204-30
- ITAA 1997 204-30(1)
- ITAA 1997 204-30(1)(a)
- ITAA 1997 204-30(1)(b)
- ITAA 1997 204-30(1)(c)
- ITAA 1997 204-30(3)
- ITAA 1997 204-30(3)(a)
- ITAA 1997 204-30(3)(c)
- ITAA 1997 204-30(8)
- ITAA 1997 Div 207
- ITAA 1997 207-20
- ITAA 1997 207-20(1)
- ITAA 1997 207-20(2)
- ITAA 1997 207-35(1)
- ITAA 1997 207-45(c)
- ITAA 1997 207-45(d)
- ITAA 1997 207-50(3)
- ITAA 1997 207-55
- ITAA 1997 207-57
- ITAA 1997 207-145(1)(a)
- ITAA 1997 Div 230
- ITAA 1997 855-10
- ITAA 1997 855-15
- TAA 1953
- Copyright Act 1968
- ITAA 1936 6(1)
- ITAA 1936 6(1)(d)
- ITAA 1936 44(1)
- ITAA 1936 45A
- ITAA 1936 45A(2)
- ITAA 1936 45A(3)(b)
- ITAA 1936 45B
- ITAA 1936 45B(2)(a)
- ITAA 1936 45B(2)(b)
- ITAA 1936 45B(2)(c)
- ITAA 1936 45B(3)
- ITAA 1936 45B(8)
- ITAA 1936 45C
- ITAA 1936 95(1)
- ITAA 1936 97(1)(a)
- ITAA 1936 98
- ITAA 1936 98A(1)(a)
- ITAA 1936 98A(1)(b)
- ITAA 1936 99
- ITAA 1936 99A
- ITAA 1936 100(1)(a)
- ITAA 1936 100(1)(b)
- ITAA 1936 128B(3)(ga)
- ITAA 1936 159GZZZP
- ITAA 1936 159GZZZQ
- ITAA 1936 159GZZZQ(1)
- ITAA 1936 159GZZZQ(2)
- ITAA 1936 159GZZZQ(3)
- ITAA 1936 159GZZZQ(4)
- ITAA 1936 159GZZZQ(8)
- ITAA 1936 159GZZZQ(9)
- ITAA 1936 Pt IIIA Div 1A
- ITAA 1936 160APHI(2)
- ITAA 1936 160APHI(4)
- ITAA 1936 160APHM
- ITAA 1936 160APHM(2)
- ITAA 1936 160APHO
- ITAA 1936 177EA

Other references:

- Law Administration Practice
Statement PS LA 2007/9
-

ATO references

NO: 1-29M9WCA

ISSN: 1445-2014

ATOlaw topic: Income Tax ~~ Entity specific matters ~~ share buy-backs