



## Class Ruling

### Income tax: proposed return of capital: eBet Ltd

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#### **1 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

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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:
- subsection 6(1) 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
  - section 104-25 of the *Income Tax Assessment Act 1997* (ITAA 1997)
  - section 104-135 of the ITAA 1997
  - section 855-10 of the ITAA 1997, and

- section 855-15 of the ITAA 1997.

All subsequent legislative references are to the ITAA 1936 unless otherwise stated.

## **Class of entities**

3. The class of entities to which this Ruling applies is the holders of ordinary shares in eBet Ltd (eBet) who:

- (a) are registered on the eBet share registry on the Record Date, being the date for determining the entitlements under the proposed return of capital
- (b) hold their ordinary shares in eBet (eBet shares) on capital account, and
- (c) are not subject to the taxation of financial arrangement rules in Division 230 of the ITAA 1997 in relation to gains and losses on their eBet shares.

(Note - Division 230 of the ITAA 1997 will generally not apply to individuals unless they have made an election for it to apply to them).

In this Ruling, a person belonging to this class of entities is referred to as an 'eBet shareholder'.

## **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 8 to 25 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.

## **Date of effect**

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7. This Ruling applies from 1 July 2014 to 30 June 2015. The Ruling continues to apply after 30 June 2015 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).

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## Scheme

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8. 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 dated 27 August 2013
- additional information from the applicant dated 26 September 2013; 21 November 2013; 11 December 2013 and 13 January 2014
- Market Announcement dated 20 December 2012
- Market Announcement dated 26 February 2013
- Market Announcement dated 21 August 2013
- eBet Limited Annual Reports for the years ended 30 June 2012 and 30 June 2013, and
- Chairman and CEO addresses to the eBet Limited AGM dated 26 November 2013.

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

9. eBet was incorporated on 22 June 1992.

10. eBet was floated on the Australian Securities Exchange on 18 August 1999. eBet was floated on the New Zealand Stock Exchange on 22 September 1999.

11. eBet acts predominately as the holding company of the eBet group.

12. eBet is also the head company of the eBet tax consolidated group.

13. The eBet group develops and markets gaming system products and supports internet wagering systems with government sanctioned and licensed gaming operations located in regulated jurisdictions. eBet has operations and commercial arrangements in Australia, New Zealand, Singapore, Philippines, Vietnam, Korea, New Caledonia, Canada and the United States of America (US).

14. eBet has historically made losses in most years and it has substantial accumulated losses overall.

15. On 17 December 2012 eBet undertook a 15 for 1 share consolidation in order to give the company a more efficient share register.

16. In the year ended 30 June 2013 the eBet group made a profit from trading operations.

17. Also in the year ended 30 June 2013 eBet sold a 50% interest in eBet Online Inc, a US based joint venture which was formed in March 2008. Total consideration for the sale of the joint venture was US\$9.6 million. eBet recognised a net profit from the sale of A\$2.08 million.

18. The Market Announcement of the sale of eBet Online Inc, dated 20 December 2012, stated that despite significant growth in the business of eBet Online Inc since its formation, it contributed only 2% of eBet's total revenues and was not considered core to eBet's business. Further, the cash flow from the divestment allowed eBet to focus on extending its range of products and services in its core gaming markets and the company Board undertook to review the company's capital management options.

19. eBet paid a maiden dividend of 3.5 cents per share, totalling \$536,342 in the year ended 30 June 2013, which was partially franked (at 50%).

20. eBet has not previously made a return of capital.

21. eBet has confirmed that its share capital account is not presently tainted within the meaning of Division 197 of the ITAA 1997.

22. eBet currently has 15,324,047 ordinary shares on issue.

23. Following a recent review of its capital structure eBet is proposing to make a capital return to eBet shareholders of 6.5 cents per ordinary share, totalling \$996,063.05.

24. eBet is proposing to return the share capital without cancelling any ordinary shares. The whole amount of the proposed return of capital will be debited against eBet's share capital account.

25. eBet has confirmed that it does not own taxable Australian real property assets which equate to more than 50% of the market value of its assets.

## Ruling

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### **Distribution is not a dividend**

26. The proposed return of capital to eBet shareholders will not be a dividend as defined in subsection 6(1).

### **The application of sections 45A, 45B and 45C**

27. The Commissioner will not make a determination under subsection 45A(2) or subsection 45B(3) that section 45C applies to the proposed return of capital. Accordingly, no part of the proposed return of capital will be taken to be a dividend for income tax purposes.

**Capital gains tax (CGT) consequences**

28. CGT event G1 (section 104-135 of the ITAA 1997) will happen when eBet pays the proposed return of capital to an eBet shareholder in respect of an eBet share that they own at the Record Date and continue to own at the payment date.

29. CGT event C2 (section 104-25 of the ITAA 1997) will happen when eBet pays the proposed return of capital to an eBet shareholder in respect of an eBet share that they own at the Record Date but do not own at the payment date.

**Foreign resident shareholders**

30. An eBet shareholder who is a foreign resident, or the trustee of a foreign trust for CGT purposes, and who is paid the proposed return of capital, disregards any capital gain made when CGT event G1 happens to their eBet share if their eBet share is not 'taxable Australian property' (sections 855-10 and 855-15 of the ITAA 1997).

31. An eBet shareholder who is a foreign resident, or the trustee of a foreign trust for CGT purposes, who is paid the proposed return of capital and who owns an eBet share at the Record Date but not at the payment date, disregards any capital gain made when CGT event C2 happens to their right to receive the return of capital if their right to receive the proposed return of capital is not 'taxable Australian property' (sections 855-10 and 855-15 of the ITAA 1997).

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**Commissioner of Taxation**21 May 2014

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## 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.*

### **Distribution is not a dividend**

32. Subsection 44(1) includes in a shareholder's assessable income any dividends paid to the shareholder out of the profits derived by the company from any source (if the shareholder is a resident of Australia) and from an Australian source (if the shareholder is a non-resident of Australia).

33. The term 'dividend', as defined in subsection 6(1) includes any distribution made by a company to any of its shareholders. However, paragraph (d) of the definition of 'dividend' excludes a distribution from the meaning of 'dividend' if the amount of the distribution is debited against an amount standing to the credit of the company's share capital account.

34. The term 'share capital account' is defined in section 975-300 of the ITAA 1997 as an account which the company keeps of its share capital, or any other account created after 1 July 1998 where the first amount credited to the account was an amount of share capital.

35. Subsection 975-300(3) of the ITAA 1997 states that an account is not a share capital account, except for certain limited purposes, if it is tainted. Section 197-50 of the ITAA 1997 states that a share capital account is tainted if an amount to which Division 197 of the ITAA 1997 applies is transferred to the account and the account is not already tainted.

36. The proposed return of capital will be recorded as a debit to eBet's share capital account. As the share capital account of eBet is not tainted within the meaning of Division 197 of the ITAA 1997, paragraph (d) of the definition of 'dividend' in subsection 6(1) of the ITAA 1936 applies. Accordingly, the proposed return of capital will not be a dividend as defined in subsection 6(1) of the ITAA 1936.

### **Anti-avoidance provisions**

37. Sections 45A and 45B are two anti-avoidance provisions which, if they apply, allow the Commissioner to make a determination that section 45C applies to treat all or part of the return of capital amount received by shareholders as an unfranked dividend paid by a company out of profits to the shareholder.

**Section 45A – streaming of dividends and capital benefits**

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

39. A reference to the 'provision of a capital benefit to a shareholder in a company' is defined in paragraph 45A(3)(b) to include a distribution of share capital to a shareholder. eBet will provide its shareholders with a 'capital benefit' as defined in paragraph 45A(3)(b). This capital benefit will be provided to all of its shareholders in the same proportion as their shareholdings.

40. Therefore, section 45A will have no application in respect of the proposed return of capital. Accordingly, the Commissioner will not make a determination under subsection 45A(2) that section 45C applies in relation to the proposed return of capital to the shareholders of eBet.

**Section 45B – schemes to provide capital benefits**

41. Section 45B applies where certain capital payments are paid to shareholders. Subsection 45B(2) sets out the conditions under which the Commissioner may make a determination under subsection 45B(3) that section 45C applies. These conditions are that:

- there is a scheme under which a person is provided with a capital benefit by a company (paragraph 45B(2)(a))
- 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
- 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 the 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)).

**Scheme**

42. A 'scheme' for the purposes of section 45B is taken to have the same meaning as provided in subsection 177A(1) of Part IVA. That definition is widely drawn and includes any agreement, arrangement, understanding, promise, undertaking, scheme, plan or proposal.

43. The proposed return of capital by eBet will constitute a scheme for the purposes of paragraph 45B(2)(a).

## ***Capital benefit***

44. The phrase 'provided with a capital benefit' is defined in subsection 45B(5). It states that a person is provided with a capital benefit if:

- (a) an ownership interest in a company is issued to the person
- (b) there is a distribution to the person of share capital, or
- (c) the company does something in relation to an ownership interest that has the effect of increasing the value of the ownership interest (which may or may not be the same interest) held by that person.

45. Therefore, the proposed return of capital by eBet will constitute the provision of a capital benefit under paragraph 45B(5)(b).

## ***Tax benefit***

46. A taxpayer 'obtains a tax benefit', as defined in subsection 45B(9) if:

- the amount of tax payable, or
- any other amount payable under the ITAA 1936 or the ITAA 1997,

would, apart from the operation of section 45B:

- be less than the amount that would have been payable, or
- be payable at a later time than it would have been payable,

if the capital benefit had instead been a dividend.

47. On the basis of the information provided by eBet it is likely that its shareholders will obtain a tax benefit from the proposed return of capital. A dividend would generally be included in the assessable income of a resident shareholder, or in the case of a foreign resident, be subject to dividend withholding tax under section 128B of the ITAA 1936. However, generally, a return of capital would be subject to the CGT provisions of the income tax law. Unless the amount of the proposed return of capital exceeds the cost base of the shares, there will only be a cost base reduction under CGT event G1 (section 104-135 of the ITAA 1997). It is only to the extent (if any) that the return of capital exceeds the cost base of the shares that a capital gain arises.

48. Additionally, a capital gain may not arise at all for certain foreign resident shareholders.

***Relevant circumstances***

49. Under paragraph 45B(2)(c) the Commissioner is required to consider the 'relevant circumstances' of the scheme as set-out in subsection 45B(8) to determine whether any part of the scheme would be entered into for a purpose, other than an incidental purpose, of enabling a relevant taxpayer to obtain a tax benefit.

50. The test is objective, based on the facts of each case. The question is whether it would be concluded that a person who entered into or carried out the scheme did so for the purpose of obtaining a tax benefit for the relevant taxpayer in respect of the capital benefit. This purpose does not have to be the most influential or prevailing purpose but it must be more than an incidental purpose.

51. The relevant circumstances under subsection 45B(8) cover the circumstances of the company and the tax profile of the shareholders. In this instance the proposed return of capital is to be made to all shareholders of eBet regardless of individual shareholder circumstances. As such, paragraphs 45B(8)(c) to 45B(8)(h) do not incline for or against a conclusion as to purpose. The circumstances covered by paragraphs 45B(8)(i) and 45B(8)(j) pertaining to the provision of ownership interests and demerger respectively are also not relevant. In this case, the relevant matters are those covered by the circumstances described in paragraphs 45B(8)(a), 45B(8)(b) and 45B(8)(k).

52. Paragraph 45B(8)(a) refers to the extent to which the capital benefit is attributable to capital and profits (realised and unrealised) of the company or an associate (within the meaning of section 318) of the company.

53. On the basis of the information available to the Commissioner, it is considered that eBet has profits both from the disposal of part of its business and also from ongoing operations, as well as capital attributable to the joint venture sold. The company has already declared and paid a dividend to shareholders in September 2013.

54. In these circumstances, it is considered reasonable to regard the proposed return of capital to shareholders as attributable to capital and not to any realised or unrealised profits of eBet.

55. Paragraph 45B(8)(b) refers to the pattern of distributions made by a company or an associate (within the meaning of section 318) of the company.

56. eBet had never paid a dividend prior to 2013. A maiden dividend was declared in August 2013 and paid in September 2013. There have been no other distributions of profits or capital to shareholders. The proposed return of capital is in addition to the dividend of 3.5 cents per share paid in September 2013. This circumstance neither inclines for or against a conclusion as to purpose.

57. Paragraph 45B(8)(k) refers to matters in subparagraphs 177D(2)(b)(i) to 177D(2)(b)(viii). These are matters by reference to which a scheme is able to be examined from a practical perspective in order to identify and compare its tax and non-tax objectives. The matters include the manner in which the scheme is carried out, its form and substance, and its financial and other implications for the parties involved.

58. In this case the form and substance of eBet's proposed return of capital does not lead to a conclusion that the requisite purpose exists that the proposed scheme is carried out for the purpose of enabling a relevant taxpayer to obtain a tax benefit.

59. Accordingly, it cannot be concluded that eBet or participating eBet shareholders entered into or carried out the scheme for the purpose of enabling the shareholders to obtain a tax benefit. As such, the Commissioner will not make a determination under subsection 45B(3) that section 45C applies to the whole or any part of the proposed return of capital.

## **Section 45C – deeming dividends to be paid where determinations under sections 45A or 45B are made**

60. As the Commissioner will not make a determination under subsection 45A(2) or subsection 45B(3) in relation to the scheme as described, section 45C will not deem any part of the proposed return of capital to be an unfranked dividend for the purposes of the ITAA 1936 or the ITAA 1997.

## **Capital gains tax**

### ***CGT event G1 – section 104-135 of the ITAA 1997***

61. CGT event G1 will happen when eBet pays the proposed return of capital to an eBet shareholder in respect of a share that they own in eBet at the Record Date and continue to own at the payment date (section 104-135 of the ITAA 1997).

62. If the proposed return of capital (\$0.065 per share) is equal to or less than the cost base of the eBet share at the payment date, the cost base and reduced cost base of the share will be reduced by the amount of the payment (subsection 104-135(4) of the ITAA 1997).

63. An eBet shareholder will make a capital gain if the proposed return of capital is more than the cost base of the eBet share (subsection 104-135(3) of the ITAA 1997). The amount of the capital gain is equal to the excess amount.

64. If an eBet shareholder makes a capital gain when CGT event G1 happens, the cost base and the reduced cost base of the eBet share is reduced to nil. An eBet shareholder cannot make a capital loss when CGT event G1 happens (subsection 104-135(3) of the ITAA 1997).

65. A capital gain made when CGT event G1 happens will be eligible to be treated as a discount capital gain under Subdivision 115-A of the ITAA 1997 provided that the eBet share was acquired at least 12 months before the payment of the proposed return of capital (subsection 115-25(1) of the ITAA 1997) and the other conditions of that Subdivision are satisfied.

***CGT event C2 – section 104-25 of the ITAA 1997***

66. The right to receive the proposed return of capital is one of the rights inherent in an eBet share at the Record Date. If, after the Record Date but before the payment date, an eBet shareholder ceases to own an eBet share, the right to receive the proposed return of capital in respect of that share will be retained by the shareholder and is a separate CGT asset.

67. CGT event C2 (section 104-25 of the ITAA 1997) will happen when the proposed return of capital is paid. The right to receive the payment (being an intangible CGT asset) will end by the right being discharged or satisfied when the payment is made.

68. An eBet shareholder will make a capital gain if the capital proceeds from the ending of the right are more than its cost base. The capital gain is equal to the amount of the excess. An eBet shareholder will make a capital loss if the capital proceeds from the ending of the right are less than its reduced cost base. The capital loss is equal to the amount of the difference (subsection 104-25(3) of the ITAA 1997).

69. In working out the capital gain or capital loss made when CGT event C2 happens, the capital proceeds will be the amount of the proposed return of capital (subsection 116-20(1) of the ITAA 1997).

70. The cost base of the eBet shareholders right to receive the proposed return of capital is worked out under Division 110 of the ITAA 1997 (modified by Division 112 of the ITAA 1997). The cost base of the right does not include the cost base or reduced cost base of the share previously owned by an eBet shareholder that has been applied in working out a capital gain or capital loss made when a CGT event happened to the share – for example, when the eBet shareholder disposed of the share after the Record Date.

71. Therefore, if the full cost base or reduced cost base of the eBet share has been previously applied in working out a capital gain or capital loss made when a CGT event happened to that share, then the right to receive the proposed return of capital is likely to have a nil cost base. As a result, the eBet shareholder will generally make a capital gain equal to the amount of the proposed return of capital.

72. As the right to receive the payment of the proposed return of capital was inherent in the eBet share at the time it was owned, the right is considered to have been acquired at the time when the corresponding share was acquired (section 109-5 of the ITAA 1997). Accordingly, if the eBet share was acquired at least 12 months before the payment of the proposed return of capital, a capital gain made from the ending of the corresponding right will satisfy the requirements of section 115-25 of the ITAA 1997. Such a capital gain may be eligible to be treated as a discount capital gain under Subdivision 115-A of the ITAA 1997 provided the other conditions of that Subdivision are satisfied.

### Foreign resident shareholders

73. Under subsection 855-10(1) of the ITAA 1997, an entity disregards a capital gain or capital loss made 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 in relation to a CGT asset that is not 'taxable Australian property'.

74. Section 855-15 of the ITAA 1997 sets out five categories of CGT assets that are 'taxable Australian property':

|        |                                                                                                                                                                       |
|--------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 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 capital gain or capital loss on ceasing to be an Australian resident). |

75. Neither the eBet share nor the right to the payment is 'taxable Australian real property' or 'an indirect Australian real property interest'. However, a capital gain cannot be disregarded under subsection 855-10(1) of the ITAA 1997 if the eBet share or the right to the payment:

- (a) has been used at any time by the foreign resident eBet shareholder 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
- (b) is covered by subsection 104-165(3) of the ITAA 1997 (item 5 of the table in section 855-15 of the ITAA 1997).

## **Appendix 2 – Detailed contents list**

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

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## References

### *Previous draft:*

Not previously issued as a draft

### *Related Rulings/Determinations:*

TR 2006/10

### *Subject references:*

- anti avoidance
- Capital gains tax
- CGT events C1-C3 – end of a CGT asset
- CGT events G1-G3 – shares
- Distributions
- dividend streaming arrangements
- return of capital on shares
- share capital
- shareholder payments

### *Legislative references:*

- ITAA 1936
- ITAA 1936 6(1)
- ITAA 1936 44(1)
- ITAA 1936 45A
- ITAA 1936 45A(2)
- ITAA 1936 45A(3)(b)
- ITAA 1936 45B
- ITAA 1936 45B(2)(a)
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- ITAA 1936 45B(3)
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- ITAA 1936 45B(9)
- ITAA 1936 45C
- ITAA 1936 128B
- ITAA 1936 Part IVA
- ITAA 1936 177A(1)
- ITAA 1936 177D(2)(b)
- ITAA 1936 177D(2)(b)(i)
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- ITAA 1936 318
- ITAA 1997
- ITAA 1997 104-25
- ITAA 1997 104-25(3)
- ITAA 1997 104-35
- ITAA 1997 104-35(3)
- ITAA 1997 104-35(4)
- ITAA 1997 104-165(3)
- ITAA 1997 109-5
- ITAA 1997 Div 110
- ITAA 1997 Div 112
- ITAA 1997 Div 115
- ITAA 1997 Subdiv 115-A
- ITAA 1997 115-25
- ITAA 1997 115-25(1)
- ITAA 1997 116-20(1)
- ITAA 1997 Div 197
- ITAA 1997 197-50
- ITAA 1997 Div 230
- ITAA 1997 855-10
- ITAA 1997 855-10(1)
- ITAA 1997 855-25
- ITAA 1997 855-30
- ITAA 1997 975-300
- ITAA 1997 975-300(3)
- TAA 1953
- Copyright Act 1968

### ATO References

|               |                               |
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