



Status: **legally binding**

Class Ruling

Digital Surge Pty Ltd – voluntary administration

❶ Relying on this Ruling

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

If this Ruling applies to you, and you correctly rely on it, we will apply the law to you in the way set out in this Ruling. That is, you will not pay any more tax or penalties or interest in respect of the matters covered by this Ruling.

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What this Ruling is about

1. This Ruling sets out the income tax consequences for the customers of Digital Surge Pty Ltd (Digital Surge) on 8 December 2022, that result from Digital Surge entering into voluntary administration on that date and from subsequent events.
2. Details of this scheme are set out in paragraphs 15 to 33 of this Ruling.
3. All legislative references in this Ruling are to the *Income Tax Assessment Act 1997*, unless otherwise indicated.

Who this Ruling applies to

4. This Ruling applies to you if you:
 - were a Participating Creditor (defined in paragraph 25 of this Ruling) at any point during the period to which this Ruling applies
 - held your interest against Digital Surge Pty Ltd on capital account, and
 - during the entire period you were a Participating Creditor, you were either a
 - resident of Australia as defined by subsection 6(1) of the *Income Tax Assessment Act 1936*, or
 - resident trust for capital gains tax (CGT) purposes as defined by subsection 995-1(1).

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5. This Ruling does not apply to anyone who is subject to the taxation of financial arrangements rules in Division 230 in relation to the scheme outlined in paragraphs 15 to 33 of this Ruling.

Note: Division 230 will not apply to individuals unless they have made an election for it to apply.

When this Ruling applies

6. This Ruling applies from 1 July 2022 to 30 June 2028.

Ruling

Administration

7. The following did not result in income tax consequences for Participating Creditors:

- the appointment of administrators to Digital Surge
- the execution of the Deed of Company Arrangement (DOCA)
- the settlement of the Creditors' Trust.

CGT event C2

8. Under section 104-25, CGT event C2 happened:

- on the termination of the DOCA
- when the Creditors' Trust made a full payment of the Claim (defined in paragraph 25 of this Ruling) of an Eligible Priority Customer Creditor (defined in at paragraph 25 of this Ruling)
- when the Creditors' Trust made a partial payment of the Claim of an Eligible Customer Creditor (defined in paragraph 25 of this Ruling).

9. CGT event C2 will also happen when the Creditors' Trust makes any further payments to an Eligible Customer Creditor.

Capital gain or capital loss

10. A capital gain under CGT event C2 is made if the capital proceeds from the ending of the asset are more than the asset's cost base. You make a capital loss if the capital proceeds are less than the asset's reduced cost base (subsection 104-25(3)).

Capital proceeds

11. The capital proceeds from the CGT event C2 that happened on termination of the DOCA is the market value of the Claim released against Digital Surge at the time the CGT event happened (subsection 116-20(1)). That market value is calculated as if the CGT event C2 had not occurred and was never proposed to occur (subsection 116-30(3A)).

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12. Under subsection 116-20(1), the capital proceeds from CGT event C2 that happens as a result of the Creditors' Trust paying any amount to a Participating Creditor will be the total of any of the following paid to them:

- Australian dollar equivalent of fiat currency
- market value of any property.

Cost base

13. Under Division 110, the cost base of each CGT asset will depend on the individual circumstances of the Participating Creditor. However, the first element of the cost base of the Claim against the Creditors' Trust will include the market value of the Claim against Digital Surge (subsection 110-25(2)).

14. Where CGT event C2 happens as a result of the Creditors' Trust making a payment to an Eligible Customer Creditor, the cost base will be proportionate to the cost base of the original Claim against the Creditors' Trust multiplied by the percentage of that Claim satisfied by the payment (subsection 112-30(3)).

Scheme

15. The following description of the scheme is based on information provided by the applicant. If the scheme is not carried out as described, this Ruling cannot be relied upon.

Background

16. Digital Surge is an Australian proprietary company limited by shares. The company operates digital asset and fiat currency broker accounts for third parties (Customers).

17. Customers sign up to access services offered by Digital Surge and contribute digital assets and fiat currency to accounts held and maintained by Digital Surge.

18. In order to create an account with Digital Surge, users are required to sign up through the company's website. In doing so, they agree to be bound by terms and conditions (T&Cs).

19. The T&Cs provide that Digital Surge does not act in the capacity of a trustee or custodian with respect to digital assets or fiat currency received from Customers. The T&Cs provide that Digital Surge becomes the legal owner of any assets received from Customers, and that they are not required to hold digital assets or fiat currency in segregated accounts for each Customer.

20. The T&Cs provide that, on demand, Digital Surge is to pay an amount to a Customer equal to the value credited to that Customer's account. Whether this payment is in the form of fiat currency or digital asset is at the discretion of Digital Surge.

Administration

21. Under a broker agreement, Digital Surge transferred assets into the control of FTX Trading Ltd (Bahamas) and FTX Australia Pty Ltd.

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22. On 11 November 2022, FTX Trading Ltd was placed into bankruptcy in the United States and FTX Australia Pty Ltd was placed into voluntary administration. On 8 December 2022, Digital Surge was placed into voluntary administration.

23. On 24 January 2023, at the second creditors meeting, it was resolved that Digital Surge would enter into a DOCA.

24. On 15 February 2023:

- the DOCA was executed
- the Creditors' Trust was then settled, and
- the DOCA terminated.

Deed of Company Arrangement

25. The following relevant definitions are contained within the DOCA:

- Claim – any claim against Digital Surge (present or future, certain or contingent, ascertained or sounding only in damages, in its own right or in its trustee capacity) that would be admissible to proof against Digital Surge in accordance with the winding up provisions if Digital Surge were in liquidation and the 'relevant date' were the Appointment Date
- Participating Claim – a Claim that is not a Secured Claim or an Employee Entitlement
- Appointment Date – 8 December 2022
- Account – the account held by a Creditor on the Digital Surge platform as at the Appointment Date with a balance denominated in either digital currency or fiat currency or a mixture of both
- Creditor – any creditor of Digital Surge with a valid Claim
- Participating Creditor – a Creditor in respect of a Participating Claim
- Eligible Customer Creditors – those Participating Creditors who held an Account with Digital Surge on the Appointment Date but who are not Eligible Priority Customer Creditors
- Eligible Priority Customer Creditors – those Participating Creditors who held an Account with Digital Surge on the Appointment Date with a value on that date equal to or less than A\$250, whether such balance was in fiat currency, or digital assets or a mixture of both
- Trust Fund – the fund held in trust by the Trustees pursuant to the terms and conditions of the Creditors' Trust Deed (the Deed).

26. The key terms of the DOCA are:

- that on termination of the DOCA, Digital Surge is released from all Claims by Participating Creditors
- on release of all Claims against Digital Surge, each Creditor becomes entitled to make a claim against the Creditors' Trust
- that the parties to the DOCA will agree to the terms of the Deed which will be executed by the relevant parties

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- that Digital Surge pay certain amounts into the Trust Fund of the Creditors' Trust
- that Digital Surge will comply with obligations under the Deed to continue to make payments into the Trust Fund
- that once all conditions precedent are effected the DOCA will terminate.

Creditors' Trust Deed

27. The relevant definitions contained in the DOCA set out at paragraph 25 of this Ruling have the same meaning in the Deed.

28. Additionally, the following relevant definition is contained within the Deed:

- Net Profit – the net profit of Digital Surge calculated on an accrual basis, being the revenue of Digital Surge for the relevant quarter less reasonable expenses incurred in the relevant quarter and taking into account any prior quarter's loss.

29. The key terms of the Deed are that:

- the trustees must determine what Claims are eligible to receive distribution out of the Trust Fund
- the trustees must apply the Trust Fund in accordance with the Deed
- Digital Surge will pay Eligible Priority Customer Creditors, on behalf of the Creditors' Trust, an amount equivalent to their Claim
- subsequent to receiving that payment, Eligible Priority Customer Creditors will no longer have a claim against Digital Surge or the Creditors' Trust, and will no longer be entitled to claim distributions from the Trust Fund
- after making the payment to Eligible Priority Customer Creditors, Digital Surge pay Eligible Customer Creditors, on behalf of the Creditors' Trust, a proportionate amount based on the remaining digital assets and fiat currency available to the Creditors' Trust
- within 60 days of each calendar quarter, Digital Surge will pay its Net Profit to Eligible Customer Creditors on a *pari passu* basis
- upon being paid their Participating Claim in full, Eligible Customer Creditors will no longer have a claim against Digital Surge or the Creditors' Trust.

Post administration

30. The effect of the actions described in paragraph 24 of this Ruling were that:

- the administration of Digital Surge ended
- Digital Surge was released from any Claims
- Participating Creditors received a Claim against the Creditors' Trust equivalent to that which they previously held against Digital Surge.

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31. On 17 February 2023, Digital Surge made the following payments on behalf of the Creditors' Trust to:

- Eligible Priority Customer Creditors in the amount of their entire Claim against the Creditors' Trust
- Eligible Customer Creditors equivalent to 57% of the amount of their Claim against the Creditors' Trust.

32. The payments made on 17 February 2023, were made either in digital currency, fiat currency or a mixture of both.

When this Ruling does not apply

33. This Ruling will not apply to an entity if they are not an Eligible Priority Customer Creditor or Eligible Customer Creditor.

Commissioner of Taxation

14 August 2024

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Appendix – Explanation

❶ *This Explanation 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.*

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Nature of claims

34. A CGT asset is any kind of property, or a legal or equitable right that is not property.¹

35. The result of the T&Cs is that the Customer ceases to be the legal owner of the fiat currency or digital asset received by Digital Surge. In turn, the Customer obtains a right to demand repayment. That right is a CGT asset.²

36. The Claim that a Participating Creditor has against the Creditors' Trust is similarly a defined right to payment (albeit subject to the availability of amounts to make that payment).³

Administration

37. Once appointed, administrators have control of the company and are able to perform the functions that the company or any of its officers could perform but for it being in administration.⁴

38. The appointment of administrators does not affect the CGT asset in the hands of the Customers. While Part 5.3A of the *Corporations Act 2001* may temporarily place restrictions on their ability to exercise their rights, it does not affect them in a way that causes any CGT event to happen.

39. Part 5.3A of the *Corporations Act 2001* similarly binds the creditors to act in accordance with the terms of the DOCA once it is executed. However, the DOCA does not affect the CGT asset held by the Participating Creditors in any way that would cause a CGT event to happen prior to its termination.

40. CGT event E1 does not happen for the Participating Creditors on settlement of the Creditors' Trust because they are not the ones who created the trust by deed or settlement.⁵

¹ Subsection 108-5(1).

² Note 1 to section 108-5.

³ The Participating Creditor is taken to acquire this asset at the time the right to payment is created in accordance with subsection 109-5(1).

⁴ Section 437A of the *Corporations Act 2001*.

⁵ Subsection 104-55(1).

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Deed of Company Arrangement termination

41. When the DOCA is terminated, Digital Surge is released from all Claims held by Participating Creditors.⁶ As a result, CGT event C2 happens for the Participating Creditors.⁷

42. The capital proceeds from a CGT event are the total of any money received in respect of the event happening, and the market value of any other property received in respect of the event happening.⁸

43. There is no determinative test for identifying a proprietary right. It is necessary to consider a range of factors while treating none as determinative. Factors that should be considered include (but are not limited to)⁹:

- whether a right is definable, identifiable and capable of assumption by third parties, and permanent or stable to some degree¹⁰
- whether it is possible to exclude others from the right in question
- whether something is treated in commerce as a valuable proprietary right, and
- enforceability against third parties generally.

44. In weighing the relevant factors, it is considered that the Claims against Digital Surge and the Creditors' Trust are property within the meaning of Part 3-1.

45. As the Claim against the Creditors' Trust is property, its market value forms part of the capital proceeds received by Participating Creditors when the DOCA terminated.

46. If the market value of the Claim against Digital Surge at the time the DOCA terminated was more or less than those capital proceeds, the Participating Creditors' capital proceeds are replaced with the market value¹¹ of the Claim against Digital Surge.¹²

47. The value of a Participating Creditor's Claim against Digital Surge will form part of the first element of cost of the Claim they receive against the Creditors' Trust.¹³

48. Whether any other amounts form part of the cost base of this CGT asset will depend on the individual circumstances of the Participating Creditor.

Payments

49. When an Eligible Priority Customer Creditor received a payment in the amount of the entirety of their Claim against the Creditors' Trust, their right to payment by the Creditors' Trust was satisfied in full and CGT event C2 happened.¹⁴

⁶ Clause 5.1 of the DOCA.

⁷ Paragraph 104-25(1)(b).

⁸ Subsection 116-20(1).

⁹ Taxation Determination TD 2014/26 *Income tax: is bitcoin a 'CGT asset' for the purposes of subsection 108-5(1) of the Income Tax Assessment Act 1997?* articulates the various approaches taken by the courts in determining whether something is 'property' at paragraphs 7 and 8 of this Ruling.

¹⁰ The factors in this dot point are collectively known as the 'Ainsworth test' – provided in *National Provincial Bank Ltd v. Ainsworth* [1965] AC 1175 at [1247-1248], approved in, for example, *R v. Toohey; Ex parte Meneling Station Pty Ltd* [1982] HCA 69.

¹¹ The market value of the Claim is to be calculated as if the CGT event C2 had not occurred and was never proposed to occur in accordance with subsection 116-30(3A). This process occurs for each CGT event C2 where the market value substitution rule applies.

¹² Subparagraph 116-30(2)(b)(ii).

¹³ Subsection 110-25(2).

¹⁴ Paragraph 104-25(1)(b).

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50. Where an Eligible Customer Creditor receives a payment that partially satisfies their right to payment from the Creditors' Trust, CGT event C2 happens.¹⁵ In this situation, the cost base of the asset to which CGT event C2 happens is determined proportionately in accordance with the formula in subsection 112-30(3).

51. Where an Eligible Customer Creditor receives a payment that completely satisfies their right to payment from the Creditors' Trust, CGT event C2 happens.¹⁶ The cost base will be the amount of the cost base that has not been apportioned to any previous partial payments.¹⁷

¹⁵ Paragraph 104-25(1)(b).

¹⁶ Paragraph 104-25(1)(b).

¹⁷ Subsection 112-30(4).

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References

Related Rulings/Determinations:
TD 2014/26

Legislative references:

- ITAA 1936 6(1)
- ITAA 1997 Pt 3-1
- ITAA 1997 104-25
- ITAA 1997 104-25(1)(b)
- ITAA 1997 104-25(3)
- ITAA 1997 104-55(1)
- ITAA 1997 108-5
- ITAA 1997 108-5(1)
- ITAA 1997 109-5(1)
- ITAA 1997 Div 110
- ITAA 1997 110-25(2)
- ITAA 1997 112-30(3)
- ITAA 1997 112-30(4)

- ITAA 1997 116-20(1)
- ITAA 1997 116-30(2)(b)(ii)
- ITAA 1997 116-30(3A)
- ITAA 1997 Div 230
- ITAA 1997 995-1(1)
- Corporations Act 2001 Pt 5.3A
- Corporations Act 2001 437A

Cases relied on:

- National Provincial Bank Ltd v Ainsworth [1965] AC 1175
- R v Toohey; Ex parte Meneling Station Pty Ltd [1982] HCA 69; (1982) 158 CLR 327; (1982) 57 ALJR 59; (1982) 44 ALR 63

ATO references

NO: 1-10QTVQ2U

ISSN: 2205-5517

BSL: PW

ATO law topic: Capital gains tax ~~ Capital proceeds ~~ Event-specific rules
Capital gains tax ~~ Cost base / reduced cost base
Capital gains tax ~~ CGT events ~~ C1 to C3 - end of a CGT asset

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