


CR 2007/13 - Income tax: CVC Sustainable Investments Limited - proposed return of capital and stapling arrangement

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Class Ruling

Income tax: CVC Sustainable Investments Limited – proposed return of capital and stapling arrangement

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① This Ruling 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, we must apply the law to you in the way set out in the ruling (unless we are satisfied that the ruling is incorrect and disadvantages you, in which case we may apply the law in a way that is more favourable for you – provided we are 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 Class Ruling are:

- subsection 6(1) of the *Income Tax Assessment Act 1936* (ITAA 1936);
- section 45 of the ITAA 1936;
- section 45A of the ITAA 1936;
- section 45B of the ITAA 1936;
- section 45C of the ITAA 1936;
- Division 104 of the *Income Tax Assessment Act 1997* (ITAA 1997);
- section 104-10 of the ITAA 1997;
- section 104-135 of the ITAA 1997;

- section 104-135(4) of the ITAA 1997;
- section 108-5 of the ITAA 1997;
- section 109-5 of the ITAA 1997;
- section 112-20 of the ITAA 1997;
- section 118-13 of the ITAA 1997; and
- section 855-10 of the ITAA 1997.

Class of entities

3. The class of entities to which this Ruling applies is the shareholders of CVC Sustainable Investments Limited (CVCSI) who hold their shares on capital account and participate in the scheme that is the subject of this Ruling.

Qualifications

4. The Commissioner makes this Ruling 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 13 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.

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Date of effect

8. This Ruling applies from 25 January 2007 to 30 June 2007. However, the Ruling continues to apply after this date to all entities within the specified class who entered into the specified scheme during the term of the Ruling, subject to there being no change in the scheme or in the entities involved in the scheme.

9. The Ruling does not apply to a shareholder to the extent that it conflicts with the terms of settlement of a dispute agreed to before the date of issue of the Ruling. Furthermore, the Ruling only applies to the extent that:

- It is not later withdrawn by notice in the *Gazette*; or
- The relevant provisions are not amended.

10. If this Class Ruling is inconsistent with a later public or private ruling, the relevant class of entities may rely on either ruling which applies to them (item 1 of subsection 357-75(1) of Schedule 1 to the *Taxation Administration Act 1953* (TAA)).

11. If this Class Ruling is inconsistent with an earlier private ruling, the private ruling is taken not to have been made if, when the Class Ruling is made, the following two conditions are met:

- the income year or other period to which the rulings relate has not begun; and
- the scheme to which the rulings relate has not begun to be carried out.

12. If the above two conditions do not apply, the relevant class of entities may rely on either ruling which applies to them (item 3 of subsection 357-75(1) of Schedule 1 to the TAA).

Scheme

13. The following description of the scheme is based on information provided by the applicant. The scheme that is the subject of this Ruling is based on the following documents. These documents, or the relevant parts of them, as the case may be, form part of and are to be read in conjunction with this description.

14. The relevant documents or parts of documents, to be read in conjunction with this description are:

- the application for a Class Ruling (and appendices) dated 20 June 2006 on behalf of CVCSI by PKF Chartered Accountants & Business Advisers (PKF);
- correspondence providing further particulars dated from 5 September 2006 to 6 February 2007 from PKF;

- CVCSI Constitution;
- proposed replacement CVCSI Constitution, version 1.0;
- proposed CVC Sustainable Investments No. 2 Limited (CVCSI No. 2 Ltd) Constitution, version 1.0;
- proposed CVCSI Stapling Deed, version 1.0;
- CVCSI Financial Reports for the years ended 30 June 2006 and 30 June 2004, showing comparative 30 June 2005 and 30 June 2003 respectively; and
- CVCSI Prospectus dated 19 October 2005.

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

15. CVCSI is an unlisted public company, incorporated on 21 July 1999. CVCSI is a company that is a Pooled Development Fund (PDF) within the meaning of the *Pooled Development Funds Act 1992* (PDF Act).

16. CVCSI and the manner in which investments are undertaken are subject to the PDF Act.

17. CVCSI's management desires to expand the investment portfolio of CVCSI to non-eligible investments under the PDF Act. CVCSI incorporated CVCSI No. 2 Ltd on 7 December 2006 to undertake these investments, to be followed by the shares in CVCSI No. 2 Ltd then being 'stapled' to the shares of CVCSI. CVCSI is proposing to enter into the stapled security arrangement in order to promote its investment flexibility.

18. CVCSI proposes:

- to capitalise CVCSI No. 2 Ltd at \$4.5 million by acquiring \$4.5 million worth of shares;
- to undertake a return of capital to its shareholders, to be satisfied by an 'in specie distribution' of shares in CVCSI No. 2 Ltd; and
- immediately after the return of capital, to implement a Stapling Deed with CVCSI No. 2 Ltd, under which each original CVCSI share will be stapled to one CVCSI No. 2 Ltd share.

As part of the arrangement, CVCSI will adopt a new constitution.

19. CVCSI No. 2 Ltd will have the same number of shares on issue as CVCSI. Where options over CVCSI shares are unexercised, CVCSI No. 2 Ltd will issue options to CVCSI option holders.

20. The accounting entries CVCSI would make in regard to the capitalisation and proposed return of capital are:

- Debit Investment \$4.5 million, Credit Bank \$4.5 million; and
- Debit Share Capital \$4.5 million, Credit Investment \$4.5 million.

21. Immediately after the proposed return of capital and prior to the implementation of stapling, a shareholder will own their CVCSI shares and CVCSI No. 2 Ltd shares as separate and distinct assets.

22. After stapling, the CVCSI and CVCSI No. 2 Ltd shares remain separate and distinct assets; however, they can only be traded together as a CVCSI stapled security.

23. A condition precedent to the return of capital would be that shareholders accept the stapling arrangement or otherwise dissenting shareholders sell their shares to another entity.

24. The Pooled Development Fund Board, which regulates the PDF Act, has advised CVCSI that the investment in a subsidiary company, the in specie distribution of shares (that is, the return of capital) and the stapling proposal have received its conditional approval.

Other

25. CVCSI has advised that the share capital account is not tainted for the purposes of Subdivision 197-C of the ITAA 1997.

Ruling

Distribution not a dividend

26. As the proposed return of capital will be debited to CVCSI's share capital account, it will not be a dividend as defined within subsection 6(1) of the ITAA 1936.

Anti-avoidance provisions

27. Section 45 of the ITAA 1936 does not apply to the proposed return of capital to be received by a shareholder.

28. The Commissioner will not make a determination under section 45A of the ITAA 1936 or 45B of the ITAA 1936 that section 45C of the ITAA 1936 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

CVCSI shareholders

29. CGT Event G1 will happen when the proposed return of capital is paid to CVCSI's shareholders (section 104-135 of the ITAA 1997).

30. Under subsections 104-135(3) and (4) of the ITAA 1997, the cost base and reduced cost base of each CVCSI share will be reduced (but not below nil) by the amount of the proposed capital return. A CVCSI shareholder will make a capital gain from CGT event G1 happening to each share to the extent (if any) that the payment exceeds the share's cost base in accordance with subsection 104-135(3).

31. Any capital gain made by a CVCSI shareholder from the proposed return of capital will be disregarded (section 118-13 of the ITAA 1997).

Foreign resident CVCSI shareholders

32. A foreign resident CVCSI shareholder who receives the proposed return of capital will make a capital gain only if the shares in CVCSI are 'taxable Australian property' (section 855-10 of the ITAA 1997).

33. Any capital gain made by a foreign resident CVCSI shareholder from the proposed return of capital will be disregarded (section 118-13 of the ITAA 1997).

Dissenting CVCSI shareholders – sale of CVCSI shares to another entity

34. CGT event A1 will happen when a dissenting CVCSI shareholder sells their CVCSI shares to another entity (section 104-10 of the ITAA 1997). Any capital gain or capital loss made by a CVCSI shareholder will be disregarded (section 118-13 of the ITAA 1997).

Acquisition of CVC Stapled Ltd shares

35. A CVCSI shareholder will be taken to have acquired the CVCSI No. 2 Ltd shares on the day of the proposed return of capital (section 109-5 of the ITAA 1997).

36. The first element of the cost base and reduced cost base of each CVCSI No. 2 Ltd share is its market value at the time of the return of capital (section 112-20 of the ITAA 1997).

Two CGT assets after proposed return of capital

37. Each CVCSI share and CVCSI No. 2 Ltd share that makes up the CVCSI stapled security will be a separate CGT asset for the purposes of section 108-5 of the ITAA 1997.

Stapling of securities

38. No CGT event in Division 104 of the ITAA 1997 will happen as a result of the stapling of each CVCSI share to a CVCSI No. 2 Ltd share.

Commissioner of Taxation

21 February 2007

Appendix 1 – Explanation

① *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 not a dividend

39. Subsection 44(1) of the ITAA 1936 includes in a shareholder's assessable income a dividend, as defined in subsection 6(1) of the ITAA 1936, paid to the shareholder out of 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).

40. The term 'dividend' in subsection 6(1) of the ITAA 1936 includes any distribution made by a company to any of its shareholders. However, later paragraphs in this subsection exclude certain items from being a dividend for income tax purposes.

41. Relevantly, the specific exclusion in paragraph (d) of the definition of 'dividend' in subsection 6(1) of the ITAA 1936 provides:

moneys paid or credited by a company to a shareholder or any other property distributed by a company to shareholders (not being moneys or other property to which this paragraph, by reason of subsection (4), does not apply or moneys paid or credited, or property distributed for the redemption or cancellation of a redeemable preference share), where the amount of the moneys paid or credited, or the amount of the value of the property, is debited against an amount standing to the credit of the share capital account of the company.

42. The proposed return of capital will be debited against CVCSI's untainted share capital account. Therefore, paragraph (d) of the definition of 'dividend' in subsection 6(1) of the ITAA 1936 applies and the return of capital would not constitute a dividend.

Anti-avoidance provisions

Section 45 of the ITAA 1936

43. Section 45 of the ITAA 1936 applies to treat the value of certain bonus shares provided by a company to be unfranked dividends paid out of profits. Section 45 applies when, in the same or different years of income a company provides some of its shareholders with bonus shares whilst paying unfranked or minimally franked dividends to other shareholders. Both events must be present for the section to have any application.

44. CVCSI will not be returning bonus shares to its shareholders as part of the stapling proposal. The stapling proposal has CVCSI acquiring a shelf company and then capitalising that shelf company to the value of \$4.5 million. The stapling proposal then has CVCSI returning the capitalised amount to its shareholders as a return of capital. The return will be in the form of shares in the shelf company known as CVCSI No. 2 Ltd.

CVCSI will not be paying unfranked or minimally franked dividends to its shareholders as part of the stapling proposal. Shareholders not wishing to be a part of the stapling proposal are able to sell their shares in CVCSI. No dividends will be paid as part of the stapling proposal.

45. Section 45 of the ITAA 1936 has no application to the proposed capital return.

Sections 45A and 45B of the ITAA 1936

46. Sections 45A and 45B of the ITAA 1936 are anti-avoidance provisions which, if they apply, allow the Commissioner to make a determination that all or part of the proposed return of capital to be received by shareholders is to be treated as an unfranked dividend.

Section 45A of the ITAA 1936

47. Section 45A of the ITAA 1936 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 have received or would receive dividends (the disadvantaged shareholders).

48. CVCSI will provide shareholders with a 'capital benefit' (as defined in paragraph 45A(3)(b) of the ITAA 1936) under the proposed capital return. However, it remains that for section 45A of the ITAA 1936 to apply there must be both advantaged and disadvantaged shareholders as defined in subsection 45A(1) of the ITAA 1936. CVCSI will be returning capital to all shareholders. No dividends are payable as part of the stapling proposal and it cannot be said that advantaged and disadvantaged shareholders as defined in subsection 45A(1) exist within this arrangement.

49. Section 45A of the ITAA 1936 has no application to the proposed capital return.

Section 45B of the ITAA 1936

50. The purpose of section 45B is to ensure that the relevant amounts distributed to shareholders are treated as dividends for tax purposes if certain payments, allocations and distributions are made in substitution for dividends. Specifically, the provision applies where:

- there is a scheme under which a person is provided with a capital benefit by a company (paragraph 45B(2)(a) of the ITAA 1936);
- under the scheme a taxpayer, who may or may not be the person provided with the capital benefit, obtains a tax benefit (paragraph 45B(2)(b) of the ITAA 1936); 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 a purpose, (other than an incidental purpose) of enabling a taxpayer to obtain a tax benefit (paragraph 45B(2)(c) of the ITAA 1936).

51. The arrangement involving the proposed capital return by CVCSI will constitute a scheme for the purposes of section 45B of the ITAA 1936.

52. The phrase 'provided with a capital benefit' is defined in subsection 45B(5) of the ITAA 1936 and includes a distribution to a person of share capital. As the proposed capital return will be recorded by means of a debit to CVCSI's untainted share capital account, its shareholders would be taken to have been provided with a capital benefit as defined in paragraph 45B(5)(b) of the ITAA 1936.

53. For the purposes of paragraph 45B(2)(c) of the ITAA 1936, the Commissioner is required to consider the relevant circumstances (as outlined in subsection 45B(8) of the ITAA 1936) of the scheme with a view to determine whether it could be concluded that entities that entered into or carried out the scheme or any part of the scheme did so for a purpose (other than an incidental purpose), of enabling the relevant taxpayer to obtain a tax benefit. On the basis of the information surrounding the return of capital as described in the ruling application, the financial reports and further information, the Commissioner has formed the view that the capital benefits provided to the relevant taxpayers have not been made for a more than incidental purpose of obtaining a tax benefit.

54. Accordingly, the Commissioner will not make a determination pursuant to subsection 45B(3) of the ITAA 1936 that section 45C of the ITAA 1936 applies to the return of capital of CVCSI.

Section 45C of the ITAA 1936 – deeming dividends to be paid where determinations under sections 45A or 45B of the ITAA 1936 are made

55. As the Commissioner will not make a determination under subsections 45A(2) or 45B(3) of the ITAA 1936 in relation to the scheme as described, section 45C will not deem any part of the 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***

56. CGT event G1 (section 104-135 of the ITAA 1997) happens if a company makes a payment to a shareholder in respect of their shares in the company and some or all of that payment is not a dividend as defined in section 995-1 of the ITAA 1997 or an amount that is taken to be a dividend under section 47 of the ITAA 1936 (non-assessable payment). A payment can include the giving of property.

57. Where the payment is the giving of property, the amount of the payment is the market value of the property given (section 103-5 of the ITAA 1997).

58. The cost base and reduced cost base of each CVCSI share will be reduced (but not below nil) by the amount of the market value of the proposed return of capital, which will be in the form of CVCSI No. 2 Ltd shares transferred from CVCSI (subsections 104-135(3) and (4) of the ITAA 1997). A CVCSI shareholder will make a capital gain from CGT event G1 happening to each share to the extent (if any) that the payment exceeds the cost base of the share (subsection 104-135(3) of the ITAA 1997).

59. Any capital gain made by a CVCSI shareholder from the proposed return of capital will be disregarded (section 118-13 of the ITAA 1997). CGT event G1 will happen and may reduce the cost base of the CVCSI shares even though any capital gain will be disregarded.

Foreign resident CVCSI shareholders – Division 855 of the ITAA 1997

60. A foreign resident CVCSI shareholder will make a capital gain from the proposed return of capital only if their shares in CVCSI are 'taxable Australian property' (section 855-10 of the ITAA 1997). The term 'taxable Australian property' includes direct or indirect interests in Australian real property and the business assets of an Australian permanent establishment (section 855-15 of the ITAA 1997).

61. Any capital gain made by a non-resident CVCSI shareholder from the proposed return of capital will be disregarded (section 118-13 of the ITAA 1997).

Dissenting CVCSI shareholders – sale of CVCSI shares to another entity

62. Where CVCSI shareholders do not wish to participate in the proposed return of capital and the stapling arrangement, they may sell their shares to another entity.

63. The sale of CVCSI shares by a CVCSI shareholder to another entity constitutes the disposal of an asset; a CGT event A1 (section 104-10 of the ITAA 1997). The capital proceeds will be the amount paid by the other entity to the CVCSI shareholder. Any capital gain or capital loss from the sale of the shares in CVCSI, whilst CVCSI remains a PDF, is disregarded (section 118-13 of the ITAA 1997).

Acquisition of CVCSI No. 2 Ltd shares

64. Each CVCSI No. 2 Ltd share acquired under the proposed return of capital is taken to be acquired by the CVCSI shareholder at the time of the return of capital (section 109-5 of the ITAA 1997).

65. CVCSI shareholders will not incur any expenditure to acquire CVCSI No. 2 Ltd shares. The cost base of each CVCSI No. 2 Ltd share will be its market value at the time of the return of capital (section 112-20 of the ITAA 1997).

Two CGT Assets after proposed return of capital

66. After the proposed return of capital, a CVCSI shareholder will hold two CGT assets; the original CVCSI shares (with an adjusted cost base as a result of CGT event G1 happening) and the CVCSI No. 2 Ltd shares (section 108-5 of the ITAA 1997).

Stapling of securities

67. The effect of the proposed stapling arrangement is to apply restrictions to the transferability of the individual securities that together make up the CVCSI stapled security, such that they cannot be sold separately. Each individual security (that is, each CVCSI share and CVCSI No. 2 Ltd share) will retain its legal character without any change in beneficial ownership. There would be no variation to the rights or obligations attaching to, or the beneficial ownership of, the individual securities comprising the CVCSI stapled security as a consequence of stapling.

68. No CGT event in Division 104 of the ITAA 1997 happens as a consequence of the proposed stapling of each CVCSI share to the CVCSI No. 2 Ltd share.

Appendix 2 – Detailed contents list

69. The following is a detailed contents list for this ruling:

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References

Previous draft:

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- return of share capital
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- stapled companies
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- time of CGT event

- ITAA 1936 45B(2)(c)
- ITAA 1936 45B(3)
- ITAA 1936 45B(5)
- ITAA 1936 45B(5)(b)
- ITAA 1936 45B(8)
- ITAA 1936 45C
- ITAA 1936 47
- ITAA 1997 103-5
- ITAA 1997 Div 104
- ITAA 1997 104-10
- ITAA 1997 104-135
- ITAA 1997 104-135(3)
- ITAA 1997 104-135(4)
- ITAA 1997 108-5
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- ITAA 1997 118-13
- ITAA 1997 Subdiv 197-C
- ITAA 1997 Div 855
- ITAA 1997 855-10
- ITAA 1997 855-15
- ITAA 1997 995-1
- PDF Act 1992
- TAA 1953
- TAA 1953 Sch 1 357-75(1)
- Copyright Act 1968

Legislative references:

- ITAA 1936 6(1)
- ITAA 1936 44(1)
- ITAA 1936 45
- ITAA 1936 45A
- ITAA 1936 45A(1)
- ITAA 1936 45A(2)
- ITAA 1936 45A(3)(b)
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ATO references

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