


# ***CR 2007/61 - Income tax: off-market share buy-back: Gotalk Limited***

 This cover sheet is provided for information only. It does not form part of *CR 2007/61 - Income tax: off-market share buy-back: Gotalk Limited*



## Class Ruling

### Income tax: off-market share buy-back: Gotalk Limited

---

Contents	Para
<b>LEGALLY BINDING SECTION:</b>	
<b>What this Ruling is about</b>	<b>1</b>
<b>Date of effect</b>	<b>8</b>
<b>Scheme</b>	<b>13</b>
<b>Ruling</b>	<b>26</b>
<b>NOT LEGALLY BINDING SECTION:</b>	
<b>Appendix 1:</b>	
<b>Explanation</b>	<b>35</b>
<b>Appendix 2:</b>	
<b>Detailed contents list</b>	<b>48</b>

#### **ⓘ 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, 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 Ruling are:

- section 45A of the *Income Tax Assessment Act 1936* (ITAA 1936);
- section 45B of the ITAA 1936;
- section 45C of the ITAA 1936;
- section 159GZZZP of the ITAA 1936;
- section 159GZZZQ of the ITAA 1936;
- section 6-5 of the *Income Tax Assessment Act 1997* (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 855-15 of the ITAA 1997;
- section 855-30 of the ITAA 1997; and
- section 960-195 of the ITAA 1997.

## Class of entities

3. The class of entities to which this Ruling applies is the ordinary shareholders of Gotalk Limited (Gotalk) who disposed of their shares to Gotalk under the Gotalk off-market share buy-back (Buy-Back) announced on 11 April 2007 and described in the Scheme part of this Ruling. In this Ruling, the shareholders of Gotalk are collectively referred to as 'shareholders' or 'participating shareholders'.

## 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 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.

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  
Attorney General's Department  
Robert Garran Offices  
National Circuit  
Barton ACT 2600

or posted at: <http://www.ag.gov.au/cca>

---

## Date of effect

---

8. This Ruling applies from 1 July 2006 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 taxpayers 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 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 Ruling is inconsistent with an earlier private ruling, the private ruling is taken not to have been made if, when the 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 a number of documents provided to the Commissioner.

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

14. Gotalk is an Australian incorporated unlisted public company. On 11 April 2007 Gotalk announced its intention to undertake an off-market buy-back of its own shares. Gotalk would buy-back shares via a tender process that determined the shares to be bought back (though not their price). Gotalk would buy-back \$4.5 million worth of its ordinary shares up to a maximum of 18,000,000 shares. Gotalk announced that the buy-back price would be set at 25 cents per share.

15. Shareholders could sell a nominated number of their shares up to a Priority Parcel of 375,000 shares. Shareholders with less than 100,000 shares had to offer to sell all of their shares if they wished to participate in the Buy-Back. The tender process opened on 12 April 2007 and closed on 26 April 2007.

16. Under the terms of the Gotalk Shareholders' Agreement, any shares tendered were first offered to all existing shareholders to purchase. The pre-emptive right expired on 25 May 2007. Any shares tendered that were not purchased by other shareholders by that date formed the basis for the Buy-Back.

17. As at 31 March 2007, Gotalk's Share Capital comprised 134,372,140 full paid ordinary shares. The unaudited consolidated balance sheet of Gotalk at 31 December 2006 disclosed total shareholders' equity of \$10.516 million, consisting of \$15.562 million contributed share capital, reserves of \$0.439 million and accumulated losses of \$5.485 million.

18. The shareholders in Gotalk are a mix of individuals, companies, trusts, partnerships and superannuation funds, some of whom are non-residents. All shares were acquired after 19 September 1985.

19. The Buy-Back forms part of Gotalk's aim of facilitating a reduction in the size of its share register to less than 50 shareholders. The Buy-Back would achieve a return of excess capital to shareholders, provide liquidity to shareholders in the short term and provide shareholders with a relatively small number of shares with an opportunity to exit their holdings.

20. The Buy-Back was implemented through a fixed price tender offer process and participation by shareholders was voluntary. Shareholders not wishing to participate in the Buy-Back were not required to do anything.

21. Where the number of shares for which acceptances were received exceeded the number of shares Gotalk determined to buy-back, a scale back mechanism applied. The Priority Parcel was bought back from each tendering shareholder with the balance of tenders being scaled back on a pro-rata basis dependent on respective shareholdings held prior to the Buy-Back.

22. All shares bought back under the Buy-Back were cancelled. This excludes shares acquired under the pre-emptive right entitlement, which does not form part of the Buy-Back.

23. Under the Buy-Back, \$0.25 per share was debited to Gotalk's untainted share capital account.

24. On 31 May 2007 Gotalk shareholders approved the off-market share buy-back.

25. On 4 June 2007 Gotalk confirmed:
- it had successfully completed the off-market share Buy-Back of 18,000,000 Gotalk shares, representing 13% of the issued capital of Gotalk;
  - the total amount of capital repurchased under the Buy-Back was \$4.5 million; and
  - a scale-back mechanism was applied, subject to paragraph 21 of this Ruling.

## **Ruling**

---

26. Section 159GZZZP of the ITAA 1936 will not apply to treat any part of the buy-back purchase price as a dividend paid to participating shareholders on the day of the buy-back.

27. Participating shareholders are taken to have received \$0.25 as consideration in respect of the sale of each of their shares on 31 May 2007 pursuant to section 159GZZZQ of the ITAA 1936.

28. The treatment of the consideration amount for tax purposes will depend on whether the sale is on capital account (where the shares are held for investment) or on revenue account.

### **Shares held on capital account**

29. The Sale Consideration of \$0.25 represents the capital proceeds for capital gains tax 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 if the Sale Consideration is less than the reduced cost base of a share.

30. The shares are taken to have been disposed of for capital gains tax purposes on 31 May 2007 pursuant to section 104-10 of the ITAA 1997.

### **Shares held on revenue account**

31. Where the shares are held as trading stock, the Sale Consideration of \$0.25 per share is included in assessable income under section 6-5 of the ITAA 1997. Where the shares are held as revenue assets, the amount by which the Sale Consideration of \$0.25 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 \$0.25 per share the difference is an allowable deduction.

## Foreign resident shareholders

32. A foreign resident shareholder that participates in the Buy-Back can disregard any capital gain or capital loss made in respect of a share bought back under the Buy-Back if the share is not taxable Australian property under the tests in section 855-15 of the ITAA 1997. Generally, a Gotalk share that is disposed into the Buy-Back will only be taxable Australian property if:

- it is an indirect Australian real property interest (see item 2 of the table in section 855-15 of the ITAA 1997); or
- it has been used at any time by a foreign resident in carrying on a business through a permanent establishment in Australia (item 3 of the table in section 855-15 of the ITAA 1997).

33. A Gotalk share that is disposed into the Buy-Back will only be an indirect Australian real property interest at the time that the share is disposed into the Buy-Back if the share passes both the principal asset test (see section 855-30 of the ITAA 1997), and the non-portfolio interest test (see section 960-195 of the ITAA 1997). Gotalk have advised that Gotalk's foreign shareholders all hold less than 10% of Gotalk's shares. Therefore, none of the Gotalk shares disposed into the Buy-Back pass the non-portfolio interest test.

## The anti-avoidance provisions

34. The Commissioner will not make a determination under section 45A or 45B of the ITAA 1936 that section 45C of the ITAA 1936 applies to the whole, or any part, of the Buy-Back price received by participating shareholders.

---

**Commissioner of Taxation**

27 June 2007

---

## 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.*

35. This Ruling does not deal with the taxation consequences of shares sold or acquired under the pre-emptive right entitlement. That is, this Ruling only applies to entities whose shares were purchased by Gotalk under the Buy-Back.

36. Participating shareholders are taken to have disposed of those shares accepted under the Buy-Back on 31 May 2007. 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 capital gains tax provisions; and
- a share trader who held their shares on revenue account will be subject to the ordinary income provisions.

37. It should be noted that shareholders who have both an income tax and a capital gains tax liability will generally have the amount of the capital gain reduced under the anti-overlap provisions contained in section 118-20 of the ITAA 1997. If the shares are held as trading stock the capital gain or loss is disregarded under section 118-25 of the ITAA 1997.

38. Section 159GZZZP of the ITAA 1936 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 in respect of the buy-back of the share which is debited against amounts standing to the credit of the company's share capital account, is taken to be a dividend paid by the company to the seller as a shareholder in the company.

39. As Gotalk debited the whole amount of the Buy-Back Price to its untainted share capital account, section 159GZZZP of the ITAA 1936 will not apply to treat any part of that purchase price as a dividend paid to participating shareholders on the day of the Buy-Back.

40. Subsection 159GZZZQ(1) of the ITAA 1936 provides that the shareholder is taken to have received an amount equal to the purchase price (in this case \$0.25 received for each share bought back) as consideration in respect of the sale of the share bought back.

41. The Commissioner accepts that the market value of each Gotalk share was \$0.25, which accorded with the consideration received by participating shareholders.



**The anti-avoidance provisions*****Sections 45A and 45B***

42. Sections 45A and 45B of the ITAA 1936 are two anti-avoidance provisions which, if they apply, allow the Commissioner to make a determination that section 45C of the ITAA 1936 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.

43. Section 45A of the ITAA 1936 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.

44. Although a 'capital benefit' (as defined in paragraph 45A(3)(b) of the ITAA 1936) 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.

45. Section 45B of the ITAA 1936 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) of the ITAA 1936);
- (b) 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
- (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 a taxpayer to obtain a tax benefit (paragraph 45B(2)(c) of the ITAA 1936).

46. In the case of the Buy-Back, whilst the conditions of paragraphs 45B(2)(a) and 45B(2)(b) of the ITAA 1936 have been met, the requisite purpose of enabling the shareholder to obtain a tax benefit – by way of capital distribution – was not present.

47. Having regard to the 'relevant circumstances' of the scheme (the Buy-Back), as set out in subsection 45B(8) of the ITAA 1936, it is apparent that there was no requisite purpose, by way of capital distribution, of enabling the shareholders to obtain a tax benefit. Further, the Buy-Back consideration cannot be said to be attributable to the profits of the company, nor does the pattern of distributions by Gotalk indicate that it is paid in substitution for a dividend.

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

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

	<b>Paragraph</b>
<b>What this Ruling is about</b>	<b>1</b>
Relevant provision(s)	2
Class of entities	3
Qualifications	4
<b>Date of effect</b>	<b>8</b>
<b>Scheme</b>	<b>13</b>
<b>Ruling</b>	<b>26</b>
Shares held on capital account	29
Shares held on revenue account	31
Foreign resident shareholders	32
The anti-avoidance provisions	34
<b>Appendix 1 – Explanation</b>	<b>35</b>
The anti-avoidance provisions	42
<i>Sections 45A and 45B</i>	42
<b>Appendix 2 – Detailed contents list</b>	<b>48</b>

## References

---

*Previous draft:*

Not previously issued as a draft

*Subject references:*

- arrangements
- share buy-backs

*Legislative references:*

- ITAA 1936 45A
  - 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(8)
  - ITAA 1936 45C
  - ITAA 1936 159GZZZP
  - ITAA 1936 159GZZZQ
  - ITAA 1936 159GZZZQ(1)
  - ITAA 1997 6-5
  - ITAA 1997 104-10
  - ITAA 1997 116-20
  - ITAA 1997 118-20
  - ITAA 1997 118-25
  - ITAA 1997 855-15
  - ITAA 1997 855-30
  - ITAA 1997 960-195
  - TAA 1953
  - TAA 1953 Sch 1 357-75(1)
  - Copyright Act 1968
- 

ATO references

NO: 2007/9945

ISSN: 1445-2014

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