


CR 2009/35 - Income tax: proposed return of capital: Rattoon Holdings Limited

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Class Ruling

Income tax: proposed return of capital: Rattoon Holdings Limited

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ⓘ 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:

- subsection 6(1) of the *Income Tax Assessment Act 1936* (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;
- Subdivision 725-B of the ITAA 1997;
- Division 727 of the ITAA 1997; and
- section 855-10 of the ITAA 1997.

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

Class of entities

3. The class of entities to which this Ruling applies is the ordinary shareholders of Rattoon Holdings Ltd (Rattoon) who are registered on the Rattoon share register on the Record Date, being the date for determining entitlements to the proposed return of capital and who receive distributions under the proposed return of capital as described in the Scheme in paragraphs 9 to 33 of this Ruling.

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 33 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 1 April 2009 to 30 June 2010. The Ruling continues to apply after 30 June 2010 to all entities within the specified class who entered into the specified scheme during the term of this 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 from PKF Chartered Accountants dated 29 October 2008;
- amended Class Ruling application (in the form of a draft ruling) from PKF Chartered Accountants which was submitted to the Commissioner on 19 March 2009;
- copy of Rattoon's half year financial report as at 31 December 2008;
- email from Applicant dated 19 June 2009; and
- email from Applicant dated 23 June 2009.

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.

Background

10. Rattoon is an investment company which listed on the Newcastle Stock Exchange on 21 June 2004.

11. As at 31 December 2008, Rattoon had 505,452,440 shares on issue. As at 19 June 2009, approximately 225,075,578 shares are shown in the share register as being held by shareholders with an overseas address. There is one class of share on issue, being ordinary shares.

12. Rattoon's shareholders are a mix of individuals, companies, superannuation funds, institutions and foreign residents.

13. Rattoon has advised that GPG Australia Nominees Ltd (GPG) currently owns approximately 44% of the shares of Rattoon. GPG holds these shares on behalf of a non-resident.

14. Decreases in the value of Rattoon's share investments (being most of its investment in Tatt's Group Ltd (Tatt's)) have resulted in Rattoon having substantial accumulated losses as at 31 December 2008. Rattoon reported a loss after tax of approximately \$63 million for the year ended 30 June 2008, predominantly attributable to a write-down of its investment in Tatt's as an impaired asset.

15. Between 30 June 2008 and 31 December 2008, Rattoon sold the bulk of its investments in order to reduce gearing levels and reduce ongoing exposure to the Tatt's share price. During this period, 62,914,587 shares in Tatt's were sold, yielding sale proceeds of \$160,643,528. Proceeds of \$81,411,365 were applied against Rattoon's margin loan account balance, repaying the balance in full. Rattoon has subsequently further reduced its shareholding in Tatt's.

Transaction history

16. In September 2006, Rattoon issued 432,962,732 ordinary shares for \$0.2694 per share. Also in 2006, Rattoon issued a further 29,695,633 ordinary shares at an issue price of approximately \$0.27. These share issues increased the issued capital of Rattoon significantly and accounted for at least 92% of the issued capital.

17. Between 1 July 1999 and 30 June 2006, Rattoon paid dividends totalling \$24,000.

18. In October 2005, Rattoon returned capital to its shareholders totalling \$1.88 million by way of an on-market share buyback.

19. In the 2007 financial year, Rattoon paid a dividend of \$0.006 per share totalling \$3.006 million and on 18 May 2007 it paid a dividend of \$0.015 per share totalling \$7.58 million. Although Rattoon had accumulated losses of \$5.698 million as at 30 April 2007, the dividends were paid out of Rattoon's current year profits that resulted from profits on the sale of shares and franked dividends.

20. In the 2008 financial year, Rattoon paid dividends totalling \$10.1 million. These dividends were paid out of profits which primarily resulted from dividends received from 'available for sale financial assets', profits from the disposal of 'available for sale financial investments' and option income earned. The dividends were paid prior to the write-down of the Rattoon investments which put Rattoon into an accumulated loss position as at 30 June 2008 of approximately \$89 million.

21. A dividend of \$0.02 per share, totalling approximately \$11.1 million, was paid in January 2009 out of Rattoon's 2009 year's earnings.

22. As at 31 December 2008, Rattoon's franking account had a credit balance of approximately \$7.4 million. After payment of the dividend in January 2009, the franking account balance was approximately \$2.6 million. A dividend of \$0.0065 per share, totalling approximately \$3,285,441, was declared on 24 June 2009 with an expected payment date of 29 June 2009. The dividend will be paid out of current period profits. Following the payment, Rattoon's franking account will have a credit balance of approximately \$1,265,934.

Proposed return of capital

23. Rattoon has no accumulated profits and no immediate need for its cash reserves. Accordingly, the Board of Rattoon has decided to provide a capital return and distribute in cash \$0.136 per share to Rattoon shareholders on a pro-rata basis based on the number of shares on issue at the Record Date.

24. There will be no change in either the number of ordinary shares held by each Rattoon shareholder or the proportionate interest of each shareholder in Rattoon as a result of the return of capital.

25. Following the return of capital there will be residual assets of approximately \$4.5 million left in Rattoon. This is predominantly cash and a small shareholding in Tatts and NSX Ltd with a combined market value of approximately \$700,000. Some of this residual will be applied by Rattoon towards the dividend declared on 24 June 2009.

26. Rattoon confirms that its share capital account as defined in section 975-300 of the ITAA 1997 is untainted.

27. Rattoon will account for the return of capital as follows:

DR Share Capital	\$68,741,532
CR Cash	\$68,741,532

28. As at 31 December 2008, Rattoon's assets comprised cash and cash equivalents, receivables and available for sale financial assets. As at 31 December 2008, the Available for Sale Financial Assets Reserve of Rattoon totalled \$4,318,862. No real property was held by Rattoon.

29. The remaining assets of Rattoon (estimated at approximately \$1.5 million to \$2 million) will be retained to act as a reserve and fund expenses. The board is looking to consider whether there are future investment opportunities for Rattoon. In the event that future investment opportunities are identified, Rattoon will consider its funding requirements and the possible need to raise fresh debt or equity. There are no further opportunities currently identified.

30. The Directors have proposed that the capital return will take place on 17 July 2009.

31. The proposed return of capital was approved at a General Meeting held on 29 June 2009.

32. At the Record Date, Rattoon had 505,452,440 ordinary shares on issue which were held by approximately 592 shareholders. Because Rattoon has no retained profits, Rattoon intends to fund the proposed return of capital, amounting to approximately \$66 million, by debiting its share capital account.

33. Rattoon does not know the cost base for each current shareholder. Rattoon is aware that the two major shareholders acquired most of their shareholding at a cost base of approximately \$0.27 and have not materially changed their shareholding. There have been limited share trades at a price below the amount expected to be provided under the proposed capital return of \$0.136. Accordingly, based on the limited movement of Rattoon's share register, it would be reasonable to expect that approximately 84% of Rattoon shares would still have a cost base of approximately \$0.27.

Ruling

Distribution is not a dividend

34. As the proposed return of capital will be debited to Rattoon's untainted share capital account, it will not be a dividend within the meaning of subsection 6(1).

Distribution will not be deemed a dividend under section 45C

35. 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. Consequently, section 45C of the ITAA 1936 will not deem any part of the proposed return of capital to be an unfranked dividend for the purposes of the ITAA 1936 or of the ITAA 1997.

Capital gains tax

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

37. CGT event C2 will happen when Rattoon pays the proposed return of capital to a Rattoon shareholder in respect of a Rattoon share they owned at the Record Date but which they ceased to own before the payment date (section 104-25 of the ITAA 1997).

Foreign resident shareholders

38. A foreign resident Rattoon shareholder who is paid the proposed return of capital disregards any capital gain made from CGT event G1 happening if their Rattoon shares are not 'taxable Australian property' (section 855-10 of ITAA 1997).

39. A foreign resident Rattoon shareholder who is paid the proposed return of capital disregards any capital gain or capital loss made from CGT event C2 happening if their right to receive the return of capital is not 'taxable Australian property' (section 855-10 of the ITAA 1997).

Value Shifting Issues

40. As the proposed return of capital will be made equally in respect of each share on issue, there will not be any value shifting issues in terms of Subdivision 725-B of the ITAA 1997.

41. Tax issues relevant to Division 727 of the ITAA 1997 have not been considered in this Ruling.

Commissioner of Taxation

15 July 2009

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

42. Subsection 44(1) includes in a shareholder's assessable income any dividends, as defined in subsection 6(1), 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).

43. The term 'dividend' in subsection 6(1) includes any distribution made by a company to any of its shareholders. However, this broad definition is confined by later paragraphs in the definition which expressly exclude certain items from being a dividend for income tax purposes.

44. Relevantly, paragraph (d) specifically excludes from the definition of 'dividend':

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.

45. '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.

46. Subsection 975-300(3) of the ITAA 1997 states that an account is not a share capital account 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.

47. The proposed return of capital will be debited against Rattoon's share capital account. There have been no amounts to which Division 197 of the ITAA 1997 applies that have been transferred to Rattoon's share capital account. Consequently, the share capital account remains untainted.

48. Therefore, paragraph (d) of the definition of 'dividend' in subsection 6(1) applies and the proposed return of capital would not constitute a dividend.

Anti-avoidance provisions

49. Sections 45A and 45B are two anti-avoidance provisions which, if they apply, allow the Commissioner to determine that all or part of a distribution is treated as an unfranked dividend that is paid by the company out of profits to the shareholder.

Streaming of dividends and capital benefits: section 45A

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

51. Ratoon will provide its shareholders with a 'capital benefit' as defined in paragraph 45A(3)(b). The capital benefit will be provided to all of the shareholders in the same proportion as their share holdings. Furthermore, the scheme does not involve the payment of a dividend. Consequently, the company cannot be said to be streaming the provision of benefits, so as to provide capital benefits to advantaged shareholders and dividends to disadvantaged shareholders.

52. Accordingly, section 45A does not apply to the proposed return of capital and the Commissioner will not make a determination under subsection 45A(2) that section 45C applies to the proposed return of capital to the shareholders of Ratoon.

Schemes to provide capital benefits in substitution for dividends: section 45B

53. The purpose of section 45B is to ensure that relevant amounts distributed to shareholders of a company are treated as dividends for tax purposes if certain payments, allocations and distributions are made in substitution for dividends.

54. Subsection 45B(2) sets out the conditions under which the Commissioner will 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 could 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)).

These conditions are considered in paragraphs 55 to 72 of this Ruling.

Scheme

55. A 'scheme' for the purposes of section 45B is taken to have the same meaning as provided in subsection 177A(1). That definition is widely drawn and includes:

- any agreement, arrangement, understanding, promise or undertaking, whether express or implied and whether or not enforceable, or intended to be enforceable, by legal proceedings; and
- any scheme, plan, proposal, action, course of action or course of conduct.

By virtue of this definition the proposed return of capital will constitute a scheme.

Tax benefit

56. A relevant 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,

by the relevant taxpayer 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.

57. Ordinarily, a return of capital would be subject to the CGT provisions of the income tax law. Unless the amount of the distribution 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 distribution exceeds the cost base of the shares that a capital gain arises. A capital gain may not arise at all for certain foreign resident shareholders: see paragraphs 87 to 90 of this Ruling. By contrast, 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.

58. Furthermore, based upon the available information, following the dividends paid in January 2009 and June 2009, the franking account of Rattoon will have a franking surplus of approximately \$1,265,934. Consequently, it will also be unlikely that Rattoon will be able to frank the proposed distribution, if paid as a dividend, to any meaningful extent. Therefore, the shareholders of Rattoon, as the relevant taxpayers in respect of the scheme, will obtain tax benefits from the proposed return of capital.

Relevant circumstances

59. Under paragraph 45B(2)(c) the Commissioner is required to consider the 'relevant circumstances' set out under subsection 45B(8) to determine whether it could be concluded that any part of the scheme would be entered into for a purpose, other than a merely incidental purpose, of enabling a relevant taxpayer to obtain a tax benefit. However, the list of relevant circumstances in subsection 45B(8) is not exhaustive and regard may be had to other circumstances on the basis of their relevance.

60. The test of purpose is an objective one. The question is whether, objectively, it would be concluded that a person who entered into or carried out the scheme did so for the purpose of securing a tax benefit for the relevant taxpayer. This purpose does not have to be the most influential or prevailing purpose but it must be more than a merely incidental purpose.

61. The relevant circumstances under subsection 45B(8) cover both the circumstances of the company and the shareholders. The matters sought to be covered by paragraphs 45B(8)(i) and (j), pertaining to the provision of ownership interests and demergers, are not in this instance relevant circumstances.

62. In this case, it is considered that the matters covered by paragraphs 45B(8)(a), (b), (c) (d), (e), (f), (h) and (k) are most relevant.

63. 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. The return of capital is not a distribution from Rattoon's current or previous profits. Rattoon has no realised or unrealised profits and has substantial accumulated losses following the large write-down of investments at 30 June 2008 and the subsequent sale of those investments at a loss. Although Rattoon has a current year profit as at 31 December 2008, the bulk of this has or will be paid out as dividends with the balance to be offset against accumulated losses. If there are further current year profits resulting from the revaluation or sale of Rattoon's remaining share investments and returns thereon, these will not affect paragraph 45B(8)(a). Given the potential volatility associated with the stock market, any unrealised gains may not be of a permanent nature. Further, these profits would be absorbed by the accumulated losses. Consequently, sourcing a dividend distribution in them would be commercially imprudent.

64. Paragraph 45B(8)(b) requires a consideration of the pattern of distributions made by a company or an associate (within the meaning of section 318) of the company. Since incorporation in December 1996, Rattoon paid dividends of approximately \$24,000 on 1 July 1999 and a total of approximately \$10.5 million in respect of the income year ended 30 June 2007 out of current year profits of approximately \$18 million. Dividends totalling \$10.1 million were paid during the income year ended 30 June 2008. Therefore, since its incorporation in 1996, it is only in the past two years that Rattoon has engaged in a consistent dividend policy of approximately \$0.02 per share. In respect of the income year ending 30 June 2009, an \$11.1 million dividend also at the rate of approximately \$0.02 cents per share was paid in January 2009 with a further small dividend being proposed. Consequently, it cannot be concluded that the proposed return of capital in any way interrupts an established pattern of distribution. The only return of capital previously undertaken by Rattoon was in October 2005 when it returned \$1.88m by way of an on-market share buyback.

65. Paragraph 45B(8)(c) requires a consideration of the capital losses available to the relevant taxpayers. In the present instance, whether the relevant taxpayers have capital losses available to them is not a material consideration as it is not expected that capital gains that may be sheltered by those losses will arise as a result of the proposed return of capital. The proposed return of capital per share (\$0.136) is expected to be less than the cost base of the vast majority of shares on issue. Consequently, the predominant effect of the capital return will be a reduction in the cost base of the shares on issue rather than the derivation of a capital gain that may be sheltered by available capital losses.

66. Paragraph 45B(8)(d) requires a consideration of the CGT status of the shares on issue. As Rattoon was incorporated on 4 December 1996, all shares on issue will be post-CGT shares.

67. Paragraph 45B(8)(e) requires a consideration of the extent to which the capital benefit will be derived by non-residents. The available information suggests that approximately 44% of Rattoon's shares are held by non-residents. Unless a foreign resident's shares in Rattoon are taxable Australian property, any capital gain will be disregarded. However, the proposed capital benefit of \$0.136 per share is less than what Rattoon reasonably assumes is the cost base of approximately 84% of the shares on issue. Therefore, it is submitted that the likely outcome is an adjustment to the cost base rather than the derivation of any capital gain that may be disregarded.

68. Paragraph 45B(8)(f) requires a consideration of the extent by which the relevant capital benefit exceeds the cost base of the shares. As discussed above, based upon the information available, approximately 84% of the shares on issue have a cost base of at least \$0.27. Consequently, the value of the proposed capital benefit of \$0.136 per share is expected to be less than the cost base, resulting in an adjustment to the cost base rather than the derivation of any capital gain.

69. As the capital reduction is to be effected proportionately across all shareholders, the proportionate interests of each shareholder in Rattoon will not vary and would remain the same as it would have been had an equivalent dividend been paid instead (paragraph 45B(8)(h)).

70. Paragraph 45B(8)(k) refers to the matters in subparagraphs 177D(b)(i) to (viii). Rattoon is presently un-leveraged without accumulated profits or an immediate need for its cash reserves. Accordingly, the Board wishes to undertake the pro-rata return of capital through the debiting of its share capital account.

71. A consequence of the scheme is that the proposed return of capital, expected to be \$0.136 per share, will result in an adjustment to the cost base of approximately 84% of the Rattoon shares on issue to relevant taxpayers.

72. Having regard to the relevant circumstances of the scheme, it could be concluded that any tax benefit that may be derived by the relevant taxpayers that participate in the proposed scheme will be merely incidental to the purpose of returning capital that Rattoon believes is surplus to its current requirements. Accordingly, the Commissioner will not make a determination pursuant to subsection 45B(3) that section 45C applies to the proposed return of capital.

Application of section 45C

73. 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 of the ITAA 1936 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.

CGT event G1: section 104-135

74. CGT event G1 will happen when Rattoon pays the proposed return of capital in respect of a share that a Rattoon shareholder owns in Rattoon at Record Date and continues to own at the payment date (section 104-135 of the ITAA 1997).

75. If the proposed return of capital amount is equal to or less than the cost base of the Rattoon share at the payment date, the cost base and reduced cost base of that Rattoon share is reduced (but not below nil) by the amount of the payment (subsection 104-135(4) of the ITAA 1997).

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

77. If a Rattoon shareholder makes a capital gain when CGT event G1 happens, the cost base and reduced cost base of the Rattoon share is reduced to nil.

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

79. A Rattoon shareholder cannot make a capital loss when CGT event G1 happens (subsection 104-135(3) of the ITAA 1997).

CGT event C2: section 104-25

80. The right to receive the proposed return of capital is one of the rights inherent in a Rattoon share at the Record Date. If, after the Record Date but before the payment date, a Rattoon shareholder ceases to own some, or all, of their shares in Rattoon, the right to receive the proposed return of capital in respect of those shares will be retained by the shareholder and is a separate CGT asset.

81. CGT event C2 will happen when the proposed return of capital is paid and the right to receive that payment ends (section 104-25 of the ITAA 1997).

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

83. 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).

84. The cost base of the Rattoon shareholder's 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). As the Rattoon shareholder has paid nothing for the right, the cost base of the right is nil. Therefore, the Rattoon shareholder will make a capital gain equal to the amount of the proposed return of capital.

85. As the right to receive the proposed return of capital amount was inherent in the Rattoon share during the time it was owned, the right is considered to have been acquired at the time when the share was acquired (section 109-5 of the ITAA 1997).

86. Consequently, if the Rattoon share to which the payment relates was originally acquired by the former Rattoon shareholder at least 12 months before the payment of the proposed return of capital, a capital gain made when CGT event C2 happens to the right may qualify as a discount capital gain under subsection 115-25(1) of the ITAA 1997 (provided the other conditions in Subdivision 115-A of the ITAA 1997 are satisfied).

Foreign Resident shareholders

87. A foreign resident disregards a capital gain or capital loss made from a CGT event that happens in relation to a CGT asset that is not 'taxable Australian property' (subsection 855-10(1) of the ITAA 1997). The term 'taxable Australian property' is defined in the table in section 855-15 of the ITAA 1997 and covers five categories of CGT assets.

88. Broadly, these CGT asset categories are:

- taxable Australian real property which is held directly;
- indirect Australian real property interests which are not covered by item 5 of the table;
- CGT assets used in carrying on a business through a permanent establishment in Australia, and which are not covered by item 1, 2 or 5 of the table;
- options or rights to acquire a CGT asset covered by item 1, 2 or 3 of the table; and
- CGT assets 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).

89. A foreign resident Rattoon shareholder who receives a payment of the proposed return of capital, and makes a capital gain when CGT event G1 happens to the Rattoon shares, will disregard the capital gain if the Rattoon shares are not 'taxable Australian property' (section 855-10 of the ITAA 1997).

90. A foreign resident Rattoon shareholder who has a right to the payment of the proposed return of capital, will disregard any capital gain or capital loss made when CGT event C2 happens to that right as the right is not 'taxable Australian property' (section 855-10 of the ITAA 1997).

Value shifting issues

91. Because the proposed return of capital will be made equally in respect of each share on issue, there will not be any value shifting issues in terms of Subdivision 725-B of the ITAA 1997. Tax issues relating to Division 727 of the ITAA 1997 have not been considered.

Appendix 2 – Detailed contents list

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References

<i>Previous draft:</i>	- ITAA 1936 45B(8)(j)
Not previously issued as a draft	- ITAA 1936 45B(8)(k)
	- ITAA 1936 45B(9)
<i>Related Rulings/Determinations:</i>	- ITAA 1936 45C
TR 2006/10	- ITAA 1936 128B
	- ITAA 1936 177A(1)
<i>Subject references:</i>	- ITAA 1936 177D(b)(i)
- capital gains tax	- ITAA 1936 177D(b)(ii)
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