


CR 2010/67 - Income tax: return of capital: Centrepont Alliance Limited

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Class Ruling

Income tax: return of capital: Centrepont Alliance 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;
- section 855-10 of the ITAA 1997.

All subsequent legislative references in this Ruling are to the ITAA 1936, unless stated otherwise.

Class of entities

3. The class of entities to which this Ruling applies consists of the holders of fully paid ordinary shares in the capital of Centrepont Alliance Limited (Centrepont) who:

- (a) are registered on the Centrepont share register on the Record Date, being the date for determining entitlements under the proposed return of capital as described in paragraphs 10 to 24 of this Ruling;
- (b) hold their Centrepont shares on capital account, and
- (c) are not subject to the taxation of financial arrangements rules in Division 230 of the ITAA 1997 in relation to gains and losses on their Centrepont shares.

(Note – Division 230 will generally not apply to individuals, unless they have made an election for it to apply to them.)

4. Partly paid Centrepont shares and employee share plan shares are not the subject of this Ruling.

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

Qualifications

6. 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 10 to 24 of this Ruling.

7. 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

9. This Ruling applies from 1 July 2010 to 30 June 2011. The Ruling continues to apply after 30 June 2011 to all entities within the specified class who entered into the specified scheme during the term of the Ruling. However, this Ruling will not apply to taxpayers to the extent that it conflicts with the terms of a settlement of a dispute agreed to before the date of issue of this Ruling (see paragraphs 75 and 76 of Taxation Ruling TR 2006/10).

Scheme

10. The following description of the scheme is based on information provided by the applicant.

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

11. The proposed return of capital of 2.5 cents per share is to all shareholders.

12. The return of capital will be paid entirely from Centrepoint's share capital account and not from any other account.

13. The rights and interests held by shareholders after the return of capital will be the same as those that would have been held had an equivalent dividend been paid instead of the return of capital. The return of capital will not alter the original rights and interests of shareholders.

Background

14. Centrepoint was formed in October 2005 and is a listed public company on the Australian Stock Exchange. It specialises in insurance premium funding, primarily for business clients. Centrepoint is a resident for Australian tax purposes and became the head of a tax consolidated group with effect from 1 July 2007.

15. Following the global financial crisis in the 2009 financial year, Centrepoint now operates on a smaller scale. The business model was also streamlined resulting in the discontinuation of Centrepoint's commercial financial business.

16. Centrepoint has recently announced its intention to merge with Professional Investment Holdings Ltd (PIH) in accordance with its aim to diversify and re-establish a profitable business. Centrepoint will be the parent entity.

17. Centrepont made an accounting loss for the year ended 30 June 2009 primarily as a result of an impairment adjustment of goodwill and intangibles. Centrepont expects to make a small profit for the year ended 30 June 2010.

18. The financial position of Centrepont at 30 June 2010, relevant to the proposed return of capital is as follows:

- Negative retained earnings of \$33,817,000 (largely due to the significant write down of goodwill and intangible assets of approximately \$28,343,000 in the year ended 30 June 2009);
- Cash reserves of \$25,593,000; and
- Ordinary share capital of \$63,069,00. The share capital account is untainted.

19. Centrepont has large accumulated accounting losses and has not paid a dividend to ordinary shareholders since October 2007, with no ordinary dividends paid in the 2008, 2009 or 2010 financial years.

Return of capital

20. Centrepont currently holds cash surplus to requirements. \$8,000,000 capital was raised from shareholders in December 2009 in anticipation of a business acquisition and also to fund organic growth in the insurance premium funding business. However, Centrepont has found organic growth in the insurance premium funding market more difficult to achieve than originally anticipated and the business transaction with PIH will be for scrip only.

21. The \$8,000,000 raised in December 2009 was deposited into Centrepont's bank account along with other monies and not in a separate bank account. However, the cash balance of the company has consistently been in excess of \$8,000,000 since the capital raising.

22. Accordingly, the Directors believe it is appropriate to return a portion of the excess capital to shareholders prior to the upcoming merger with PIH.

23. For holders of fully paid Centrepont shares, the return of capital will be allocated on a cash basis of 2.5 cents per share, resulting in a gross return of capital of \$4,098,046

24. Centrepont's proposed return of capital of \$4,098,046 represents a return of a portion of this capital raised in December 2009.

Ruling

Distribution is not a dividend

25. The return of capital to Centrepont shareholders will not be a dividend, as defined in subsection 6(1).

Distribution will not be deemed a dividend under section 45C

26. The Commissioner will not make a determination under sections 45A or 45B that section 45C applies to the return of capital. Accordingly, no part of the return of capital will be taken to be a dividend for income tax purposes.

Capital gains tax

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

28. CGT event C2 will happen when Centrepoint pays the return of capital to a Centrepoint shareholder in respect of a Centrepoint share that they own at the Record Date but cease to own before the time of the payment (section 104-25 of ITAA 1997).

Foreign resident shareholders

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

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

Commissioner of Taxation24 November 2010

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

31. Subsection 44(1) includes in a shareholder's assessable income any dividends 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).

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

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

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

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

Anti-avoidance provisions

Sections 45A and 45B

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

Section 45A – streaming of dividends and capital benefits

37. Section 45A applies where capital benefits are streamed to some shareholders (the Advantaged Shareholders), who would derive a greater benefit from the capital benefits than other shareholders (the Disadvantaged Shareholders) and these Disadvantaged Shareholders receive, or are likely to receive, dividends.

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

39. Therefore, section 45A will have no application in respect of the return of capital. Accordingly, the Commissioner will not make a determination under subsection 45A(2) that section 45C applies in relation to the whole, or a part, of the capital benefit.

Section 45B – schemes to provide capital benefits in substitution for dividends

40. Section 45B applies where certain capital payments are paid to shareholders in substitution for dividends. It allows the Commissioner to make a determination that section 45C applies to a capital benefit. The effect of such a determination is that all or part of the distribution of capital received by the shareholder under the return of capital is treated as an unfranked dividend.

41. In broad terms, section 45B applies where:

- 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, who may or may not be the person provided with the capital benefit, obtains a tax benefit (paragraph 45B(2)(b)); and
- having regard to the relevant circumstances of the scheme, it would be concluded that the person, or one of the persons, who entered into or carried out the scheme or any part of the scheme did so for 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)).

42. Under the present scheme, Centrepont proposes a distribution of 2.5 cents per share, paid out of its untainted share capital account, in respect of each share held by Centrepont shareholders. This will constitute the provision of a capital benefit in accordance with paragraph 45B(5)(b).

43. Pursuant to subsection 45B(9), it is likely that each of the Centrepont shareholders to which this Ruling applies will obtain a tax benefit due to the capital benefit being assessed at a later time via the CGT regime rather than being assessed immediately under subsection 44(1) as a dividend.

44. However, having regard to the relevant circumstances of the scheme (defined to include the circumstances set out in subsection 45B(8)), it cannot be concluded that either Centrepont or the Centrepont shareholders will enter into or carry out the scheme for the purpose of enabling the Centrepont shareholders to obtain a tax benefit. Given the circumstances outlined in paragraphs 14 to 19 of this Ruling, it cannot be said that the return of capital is a disguised distribution of profits, nor does Centrepont's pattern of distributions indicate that the return of capital is being made in substitution for dividends. Similarly, the manner in which the scheme is to be carried out, and the form and substance of the scheme, do not indicate that the capital return will be made in substitution for dividends.

45. Accordingly, the Commissioner will not make a determination under subsection 45B(3) that section 45C applies to the whole, or a part of the return of capital.

46. As the Commissioner will not make a determination under subsection 45A(2) of the ITAA 1936 or subsection 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 return of capital to be an unfranked dividend for the purposes of the ITAA 1936 or of the ITAA 1997.

Capital gains tax

CGT event G1 – section 104-135

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

48. If the return of capital (2.5 cents per share) is equal to or less than the cost base of the Centrepont share at the time of payment, the cost base and reduced cost base of the share will be reduced (but not below nil) by the amount of the payment (subsection 104-135(4) of the ITAA 1997).

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

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

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

CGT event C2 – section 104-25

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

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

54. A Centrepoint 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 Centrepoint 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.

55. In working out the capital gain or capital loss made when CGT event C2 happens, the capital proceeds will be the amount of the return of capital (2.5 cents per share) (subsection 116-20(1) of the ITAA 1997).

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

57. Therefore, if the full cost base or reduced cost base of a Centrepoint share has been previously applied in working out a capital gain or capital loss made when a CGT event happened to that share, the right to receive the return of capital will have a nil cost base.

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

Foreign resident shareholders

59. An entity disregards a capital gain or capital loss made from a CGT event if they are a foreign resident, or the trustee of a foreign trust for CGT purposes, just before the CGT event happens and the CGT event happens in relation to a CGT asset that is not 'taxable Australian property', under subsection 855-10(1) of the ITAA 1997.

60. The term 'taxable Australian property' is defined in the table in section 855-15 of the ITAA 1997. The table sets out these five categories of CGT assets:

Item 1	taxable Australian real property;
Item 2	an indirect Australian real property interest not covered by item 5;
Item 3	a CGT asset used at any time in carrying on a business through a permanent establishment in Australia and which is not covered by item 1, 2 or 5;
Item 4	an option or right to acquire a CGT asset covered by item 1, 2 or 3; and
Item 5	a CGT asset that is covered by subsection 104-165(3) of the ITAA 1997 (choosing to disregard a gain or loss on ceasing to be an Australian resident).

61. A foreign resident Centrepont shareholder who is paid the proposed return of capital disregards any capital gain made when CGT event G1 happens if their Centrepont share is not 'taxable Australian property' (section 855-10 of the ITAA 1997)

62. A foreign resident Centrepont shareholder who is paid the proposed return of capital disregards any capital gain made when CGT event C2 happens when the right ends if their right is not 'taxable Australian property' (section 855-10 of the ITAA 1997)

Appendix 2 – Detailed contents list

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References

Previous draft:

Not previously issued as a draft

Related Rulings/Determinations:

TR 2006/10; CR 2010/2

Subject references:

- capital benefit
- capital gains tax
- capital reductions
- CGT events C2 – end of a CGT asset
- CGT events G1 – shares
- dividends
- return of capital on shares
- share capital

Legislative references:

- ITAA 1936
 - ITAA 1936 6(1)
 - ITAA 1936 6(1)(d)
 - ITAA 1936 44(1)
 - ITAA 1936 45A
 - ITAA 1936 45A(2)
 - 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(3)
 - ITAA 1936 45B(5)(b)
 - ITAA 1936 45B(8)
 - ITAA 1936 45B(9)
 - ITAA 1936 45C
 - ITAA 1997
 - ITAA 1997 104-25
 - ITAA 1997 104-25(3)
 - ITAA 1997 104-135
 - ITAA 1997 104-135(3)
 - ITAA 1997 104-135(4)
 - ITAA 1997 104-165(3)
 - ITAA 1997 109-5
 - ITAA 1997 Div 110
 - ITAA 1997 Div 112
 - ITAA 1997 Subdiv 115-A
 - ITAA 1997 115-25
 - ITAA 1997 115-25(1)
 - ITAA 1997 116-20(1)
 - ITAA 1997 Div 197
 - ITAA 1997 197-50
 - ITAA 1997 855-10
 - ITAA 1997 855-10(1)
 - ITAA 1997 855-15
 - ITAA 1997 975-300
 - ITAA 1997 975-300(3)
 - ITAA 1997 995-1(1)
 - TAA 1953
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ATO references

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