


# ***CR 2017/82 - Income tax: return of capital: Whitehaven Coal Limited***

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## Class Ruling

### Income tax: return of capital: Whitehaven Coal 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.

## Summary – what this ruling is about

1. This Ruling sets out the Commissioner's opinion on the way in which the relevant provisions identified below apply to the defined class of entities, who take part in the scheme to which this Ruling relates.

### Relevant provisions

2. The relevant provisions dealt with in this ruling are:

- subsection 6(1) of the *Income Tax Assessment Act 1936* (ITAA 1936)
- subsection 44(1) of the 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 legislative references are to the ITAA 1936 unless otherwise stated.

## **Class of entities**

3. The class of entities to which this Ruling applies are the holders of ordinary shares in Whitehaven Coal Limited (Whitehaven) who:

- were registered on Whitehaven's share register on 13 November 2017 at 7:00pm AEDT (the Record Date)
- held their fully paid ordinary Whitehaven shares on capital account, and
- are not subject to the taxation of financial arrangement rules in Division 230 of the ITAA 1997 in relation to gains and losses on their Whitehaven shares.

In this Ruling, a person belonging to this class of entities is referred to as a 'Whitehaven Shareholder'.

## **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 8 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.

## **Date of effect**

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7. This Ruling applies from 1 July 2017 to 30 June 2018. The Ruling continues to apply after 30 June 2018 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).

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## Scheme

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8. 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.

9. Whitehaven is an Australian resident company that has been listed on the Australian Securities Exchange (ASX) since 1 June 2007.

10. Whitehaven is the holding company of the Whitehaven group of companies and the head company of the Whitehaven tax consolidated group.

11. Whitehaven's primary business activity is coal mining.

12. Since its listing on the ASX in 2007, Whitehaven has issued capital to fund new opportunities for bolt-on acquisitions, increase working capital to manage volatile cash flows arising from fluctuations in commodity prices, to strengthen its balance sheet and to improve liquidity to meet the objectives of ASX 200 inclusion.

### Return of capital

13. On 16 August 2017, Whitehaven announced its intention to make a distribution of \$0.20 per Whitehaven share (the Distribution), subject to shareholder approval. The distribution would consist of a return of capital of \$0.14 per share and an unfranked dividend of \$0.06 per share.

14. Whitehaven proposed the return of capital as it considered that it had capital surplus to its business requirements and sought to return capital to its shareholders.

15. The Capital Return was undertaken by way of an equal reduction of capital of \$140,000,000 under section 256B of the *Corporations Act 2001* (Corporations Act) and required shareholder approval by ordinary resolution under section 256C of the Corporations Act. Shareholder approval was granted at the Annual General Meeting of Whitehaven shareholders held on 25 October 2017.

16. Whitehaven made a return of \$200,000,000 to Whitehaven Shareholders (\$0.20 per share). This consisted of a share capital component of \$140,000,000 (\$0.14 per share) (Capital Return), and an unfranked dividend component of \$60,000,000 (\$0.06 per share) (Dividend).

17. The Capital Return was debited to Whitehaven's share capital account.

18. The Distribution was paid to each Whitehaven Shareholder, in proportion to their shareholdings, who were registered on the Whitehaven share register on the Record date. The payment date for the Distribution was 28 November 2017 (the Payment Date).

19. The Capital Return did not result in the cancellation or variation of shares, and the number of shares held by shareholders did not change as a result of the Capital Return.

## **Other relevant matters**

20. As at the Record Date:

- Whitehaven's paid up share capital was \$3,136,941,000
- Whitehaven had 1,026,045,885 fully paid ordinary shares on issue
- as at 30 June 2017, Whitehaven had a retained earnings balance of \$146,246,000, and
- Whitehaven had a nil franking account balance.

21. Since its listing in 2007, Whitehaven has returned nil capital to its shareholders.

22. Whitehaven's dividend policy provides that the dividend payouts through the business cycle will be in the range of 20% to 50% of net profit after tax before significant items.

23. Whitehaven's share capital account (as defined in section 975-300 of the ITAA 1997) is not tainted within the meaning of Division 197 of the ITAA 1997.

24. As at 30 June 2017, approximately 56% of Whitehaven's shares were beneficially held by foreign resident shareholders.

25. The market value of Whitehaven's taxable Australian real property (TARP assets) exceeds the market value of its non-taxable Australian real property (non-TARP assets).

## **Ruling**

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### **Capital Return is not a dividend**

26. No part of the Capital Return from Whitehaven to the Whitehaven Shareholders is a dividend as defined in subsection 6(1) of the ITAA 1936, and is therefore not included in the assessable income of the Whitehaven Shareholders pursuant to subsection 44(1) of the ITAA 1936.

27. The remainder of the Distribution, being the Dividend, will be included in the assessable income of Whitehaven Shareholders pursuant to subsection 44(1) of the ITAA 1936.

28. The Dividend paid to foreign resident Whitehaven Shareholders will be subject to dividend withholding tax under section 128B of the ITAA 1936 and will not be included in the assessable income of foreign resident Whitehaven Shareholders.

**Anti-avoidance provisions will not apply**

29. The Commissioner will not make a determination under section 45A or section 45B of the ITAA 1936 that section 45C applies to the Capital Return.

**Capital gains tax**

30. CGT event G1 (section 104-135 of the ITAA 1997) happened when Whitehaven paid the Capital Return to a Whitehaven shareholder in respect of a Whitehaven share that they owned at the Record Date and continue to own at the Payment date.

31. CGT event C2 (section 104-25 of the ITAA 1997) happened when Whitehaven paid the Capital Return to a Whitehaven Shareholder in respect of a Whitehaven share they owned at the Record Date but ceased to own at the Payment Date.

**Foreign resident shareholders**

32. A foreign resident Whitehaven Shareholder who receives the Capital Return will disregard a capital gain or capital loss in accordance with section 855-10 of ITAA 1997 where it is not in respect of 'taxable Australian property'.

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**Commissioner of Taxation****6 December 2017**

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## 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.*

### **Capital Return is not a dividend**

33. Subsection 44(1) of the ITAA 1936 includes in a shareholder's assessable income any dividends, as defined in subsection 6(1) of the ITAA 1936, paid to the shareholders 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).

34. The term 'dividend' in subsection 6(1) of the ITAA 1936 includes any distribution made by a company to any of its shareholders. However paragraph (d) of the definition of dividend in subsection 6(1) of the ITAA 1936 specifically 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.

35. 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 after 1 July 1998 where the first amount credited to the account was an amount of share capital.

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

37. The Capital Return was debited against an amount standing to the credit of Whitehaven's share capital account.

38. As the share capital account of Whitehaven 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 and the Capital Return does not constitute a dividend under subsection 6(1) of the ITAA 1936.

39. The remainder of the Distribution, being the Dividend of \$0.06 per share was debited to the retained earnings account of Whitehaven. As such, this amount will be included in the assessable income of a Whitehaven shareholder.

40. A foreign resident shareholder receiving the Dividend will not be required to include the Dividend in its assessable income pursuant to section 128D of the ITAA 1936.

**Anti-avoidance provisions will not apply****Section 45A of the ITAA 1936**

41. Section 45A of the ITAA 1936 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.

42. Although Whitehaven has provided its shareholders with a 'capital benefit', as defined in paragraph 45A(3)(b) of the ITAA 1936, the capital benefit has been provided to all Whitehaven Shareholders in direct proportion to their shareholding. The circumstances of the scheme do not indicate that there is a 'streaming' of capital benefits to advantaged shareholders and of dividends to disadvantaged shareholders.

43. Accordingly, section 45A of the ITAA 1936 does not apply to the Capital Return. The Commissioner will not make a determination under subsection 45A(2) of the ITAA 1936 that section 45C of the ITAA 1936 applies in relation to the whole, or a part, of the capital benefit.

**Section 45B of the ITAA 1936**

44. Section 45B of the ITAA 1936 is an anti-avoidance provision that allows the Commissioner to make a determination that section 45C of the ITAA 1936 applies to treat all or part of a return of capital amount as an unfranked dividend if certain conditions are satisfied.

45. Section 45B of the ITAA 1936 applies where certain capital payments are made to shareholders in substitution for dividends. Specifically, the provision applies where:

- there is a scheme under which a person is provided with a demerger benefit or a capital benefit by a company
- under the scheme, a taxpayer (the *relevant taxpayer*), who may or may not be the person provided with the demerger benefit or the capital benefit, obtains a tax benefit, 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 (the *relevant taxpayer*) to obtain a tax benefit.



## *Scheme*

46. Subsection 45B(10) of the ITAA 1936 provides that 'scheme' in section 45B of the ITAA 1936 has the same meaning as provided in subsection 995-1(1) of the ITAA 1997. That definition is widely drawn and includes any arrangement, scheme, plan proposal, action course of action or course of conduct, whether unilateral or otherwise.

47. The Capital Return as described in paragraphs 8 to 25 of this Ruling constitutes a scheme for the purposes of section 45B of the ITAA 1936.

## *Capital Benefit*

48. The phrase 'provided with a capital benefit' is defined in subsection 45B(5) of the ITAA 1936. It states that a person is provided with a capital benefit if:

- an ownership interest in a company is issued to the person
- there is a distribution to the person of share capital, or
- the company does something in relation to the ownership interest that has the effect of increasing the value of the ownership interest (which may or may not be the same interest) held by that person.

49. As the Capital Return was debited to Whitehaven's share capital account, Whitehaven is taken to have provided each Whitehaven Shareholder with a capital benefit under paragraph 45B(5)(b) of the ITAA 1936 in the form of a Capital Return.

50. A relevant taxpayer 'obtains a tax benefit' as defined in subsection 45B(9) of the ITAA 1936, if:

- the amount of tax payable, or
- any other amount payable under the ITAA 1936 or the ITAA 1997

would, apart from the operation of section 45B of the ITAA 1936:

- 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 an assessable dividend.

51. A return of capital would ordinarily be subject to the CGT provisions of the income tax law. Unless the amount of the return of capital exceeds the cost base of the shares, there will only be a cost base reduction under CGT event G1 (section 104-135). It is only to the extent (if any) that the return of capital exceeds the cost base of the shares that a capital gain arises. 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. Therefore, if the return of capital did represent a dividend rather than a capital benefit, it is likely that a Whitehaven Shareholder would incur a greater tax liability. Whitehaven Shareholders therefore obtain a tax benefit from the Capital Return.

#### *Relevant circumstances*

52. For the purposes of paragraph 45B(2)(c) of the ITAA 1936, the Commissioner is required to consider the 'relevant circumstances' set out in subsection 45B(8) of the ITAA 1936 to determine whether any part of the scheme was entered into for a purpose, other than an incidental purpose, of enabling a relevant taxpayer to obtain a tax benefit.

53. 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 or any part of the scheme did so for the purpose of obtaining a tax benefit for the relevant taxpayer. The purpose does not have to be the most influential or prevailing purpose, but it must be more than an incidental purpose.

54. Having regard to the relevant circumstances of the scheme to return capital to Whitehaven Shareholders, it cannot be concluded that the scheme was entered into or carried out for a more than incidental purpose of enabling Whitehaven Shareholders to obtain a tax benefit. In particular, having regard to the overall commercial circumstances of Whitehaven the capital and dividend components of the distribution were considered reasonable.

55. Accordingly, the Commissioner will not make a determination under subsection 45B(3) that section 45C applies to the Capital Return.

#### **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 when a company makes a payment to a shareholder in respect of a share they own (and neither CGT event A1 or C2 happens in relation to the share), some or all of the payment (the non-assessable part) is neither a dividend nor an amount that is taken to be a dividend under section 47 of the ITAA 1936, and the payment is not included in their assessable income.

57. CGT event G1 happened when Whitehaven paid the Capital Return to a Whitehaven Shareholder in respect of a Whitehaven share that they owned at the Record Date and continued to own at the Payment Date.

58. A Whitehaven Shareholder makes a capital gain if the Capital Return amount is more than the cost base of the shareholder's Whitehaven share. The amount of the capital gain is equal to that excess (subsection 104-135(3) of the ITAA 1997).

59. If a Whitehaven Shareholder makes a capital gain from CGT event G1 happening, the cost base and reduced cost base of the Whitehaven share is reduced to nil. A Whitehaven Shareholder cannot make a capital loss from CGT event G1 happening (subsection 104-135(3) of the ITAA 1997).

60. If the Capital Return amount is equal to or less than the cost base of the Whitehaven share at the Payment Date, the cost base and reduced cost base of the Whitehaven share will be reduced by the amount of the Capital Return (subsection 104-135(4) of the ITAA 1997).

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

## ***CGT Event C2 – section 104-25 of the ITAA 1997***

62. The right to receive the payment of the Capital Return is one of the rights of a holder of a Whitehaven share at the Record Date. If, after the Record Date but before the Payment Date, a Whitehaven shareholder ceases to own some, or all, of their shares, the right to receive the payment of the return of capital in respect of each of the shares disposed is retained by the shareholder and is a separate CGT asset.

63. CGT event C2 (section 104-25 of the ITAA 1997) happens when the Capital Return is paid. The right to receive the payment (being an intangible CGT asset) ended by the right being discharged or satisfied when the payment was made.

64. A Whitehaven Shareholder will make a capital gain if the capital proceeds from the ending of the right are more than the cost base of the right. A Whitehaven Shareholder will make a capital loss if the capital proceeds from the ending of the right are less than the reduced cost base of the right (subsection 104-25(3) of the ITAA 1997).

65. In working out the capital gain or capital loss made from CGT event C2, the capital proceeds will be the amount of the Capital Return (subsection 116-20(1) of the ITAA 1997).

66. The cost base of a Whitehaven Shareholder's right to receive the Capital Return 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 Whitehaven 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, if the Whitehaven Shareholder disposed of the share after the Record Date but before Payment Date.

67. Therefore if the full cost base or reduced cost base of a Whitehaven share has been previously applied in working out a capital gain or capital loss made when a CGT event happens to that share, the right to receive the Capital Return has a nil cost base. Therefore, a capital gain will equal the amount received (\$0.14 per share).

68. As the right to receive the Capital Return is inherent in the Whitehaven share during the time it is owned, the right is considered to be acquired at the time when the share was acquired (section 109-5 of the ITAA 1997).

69. If the Whitehaven share to which the Capital Return relates was originally acquired by a Whitehaven Shareholder at least 12 months before the payment, a capital gain from CGT event C2 happening 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 were or will be satisfied.

### **Foreign resident shareholders**

70. Under subsection 855-10(1) of the ITAA 1997, an entity disregards a capital gain or capital loss 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'.

71. The term 'taxable Australian property' is defined in the table in section 855-15 of the ITAA 1997. The table sets out 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) (choosing to disregard a gain or loss on ceasing to be an Australian resident).              |

72. Under subsection 855-10(1) of the ITAA 1997, an entity disregards a capital gain or capital loss 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'.

***Indirect Australian real property interest***

73. Subsection 855-25(1) of the ITAA 1997 provides that a membership interest held by an entity in another entity at a time, is an indirect Australian real property interest at that time if the interest satisfies both:

- the non-portfolio test in section 960-195 of ITAA 1997 at either time specified in subparagraphs 855-25(1)(a)(i) and 855-25(1)(a)(ii), and
- the principal asset test in section 855-30 of ITAA 1997 at that time.

74. Subsection 855-30(2) of the ITAA 1997 provides that a membership interest held by the holding entity in the test entity passes the principal asset test if the sum of the market values of the test entity's assets that are TARP assets exceeds the sum of the market values of its assets that are non-TARP assets.

75. The market value of Whitehaven's TARP assets exceeds the market value of its non-TARP assets. Therefore the principal asset test is satisfied.

76. Section 960-195 of ITAA 1997 provides that an interest held by an entity in another entity passes the non-portfolio interest test at a time if the sum of the direct participation interests held by the holding entity and its associates in the test entity at that time is 10% or more.

77. The interest is an indirect Australian real property interest if the non-portfolio test is passed either at that time (being the time the Capital Return is paid) or if it is passed throughout a 12 month period that began no earlier than 24 months before that time and ended no later than that time under subparagraphs 855-25(1)(a)(i) or 855-25(1)(a)(ii) of the ITAA 1997.

78. A Whitehaven Shareholder, being a non-resident, or the trustee of a non-resident trust for CGT purposes, cannot disregard a capital gain or capital loss made when CGT event G1 happened to their Whitehaven share under subsection 855-10(1) if:

- their Whitehaven share was an indirect Australian real property interest (item 2 of the table in section 855-15 of the ITAA 1997), having satisfied the non-portfolio test in section 960-195 of the ITAA 1997 at the time the Capital Return is paid, or throughout a 12 month period that began no earlier than 24 months before the Capital Return is paid and ended no later than that time

- their Whitehaven share had been used at any time by them in carrying on a business through a permanent establishment in Australia (item 3 of the table in section 855-15 of the IATA 1997), or
- their Whitehaven share was covered by subsection 104-165(3) of the ITAA 1997 (item 5 of the table in 855-15 of ITAA 1997).

A Whitehaven Shareholder, being a non-resident, or the trustee of a non-resident trust for CGT purposes, can disregard a capital gain or loss made when CGT event G1 happened to their Whitehaven share provided it does not fall into any of the above categories.

79. A Whitehaven Shareholder, being a non-resident, or the trustee of a non-resident for CGT purposes, cannot disregard a capital gain or capital loss made when CGT event C2 happened to their right to receive a return of share capital if:

- the right had been used at any time by them in carrying on a business through a permanent establishment in Australia (item 3 of the table in section 855-15 of ITAA 1997), or
- the right was covered by subsection 104-165(3) of ITAA 1997 (item 5 of the table in section 855-15 of ITAA 1997).

## Appendix 2 – Detailed contents list

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

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## References

### *Previous draft:*

Not previously issued as a draft

### *Related Rulings/Determinations:*

TR 2006/10

### *Legislative references:*

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- ITAA 1936 6(1)
- ITAA 1936 44(1)
- ITAA 1936 45A
- ITAA 1936 45A(3)(b)
- ITAA 1936 45A(2)
- ITAA 1936 45B
- ITAA 1936 45B(2)
- ITAA 1936 45B(2)(c)
- ITAA 1936 45B(3)
- ITAA 1936 45B(5)
- ITAA 1936 45B(5)(b)
- ITAA 1936 45B(8)
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- ITAA 1997 855-10(1)
- ITAA 1997 855-15
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- ITAA 1997 975-300
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- Corporations Act 2001
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### ATO references

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 Income tax ~~ Capital management ~~ Assessability of distribution

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