CR 2021/67 - Primewest (HICT) Pty Ltd - return of capital

Class Ruling

Primewest (HICT) Pty Ltd – return of capital

Relying on this Ruling

This publication (excluding appendix) is a public ruling for the purposes of the *Taxation Administration Act 1953*.

If this Ruling applies to you, and you correctly rely on it, we will apply the law to you in the way set out in this Ruling. That is, you will not pay any more tax or penalties or interest in respect of the matters covered by this Ruling.

Table of Contents	**Paragraph**

What this Ruling is about

1. This Ruling sets out the income tax consequences for shareholders of Primewest (HICT) Pty Ltd (PW-HICT) who received a return of capital from Home Investment Consortium Trust (HICT) on 8 January 2021 (Distribution Date) by way of a return of capital to its shareholders.

2. Full details of this scheme are set out in paragraphs 13 to 37 of this Ruling.

3. All legislative references in this Ruling are to provisions of the *Income Tax Assessment Act 1997,* unless otherwise indicated.

Who this Ruling applies to

4. This Ruling applies to you if you were a holder of ordinary shares in PW-HICT who received capital proceeds from the sale of the units in the HomeCo Daily Needs REIT (the REIT) as a return of capital. Specifically, the Ruling applies to shareholders who:

- were registered on the PW-HICT share register on 23 December 2020 (Record Date)
- held your PW-HICT shares on capital account; that is, you did not hold your shares in PW-HICT as revenue assets (as defined in section 977-50) or as trading stock (as defined in subsection 995-1(1)) on the Record Date
- received the return of capital payment of 0.2343 cents per PW-HICT share on the 8 January 2021 (Distribution Date), and

- were a resident of Australia, as defined in subsection 6(1) of the *Income Tax Assessment Act 1936* (ITAA 1936), on 8 January 2021.

5. This Ruling does not apply to anyone who is subject to the taxation of financial arrangements rules in Division 230 in relation to the scheme outlined in paragraphs 13 to 37 of this Ruling.

Note: Division 230 will not apply to individuals, unless they have made an election for it to apply.

When this Ruling applies

6. This Ruling applies from 1 July 2020 to 30 June 2021.

Ruling

Return of capital is not a dividend and therefore not assessable income

7. The return of capital is not a dividend as defined in subsection 6(1) of the ITAA 1936 and therefore not assessable income under subsection 44(1) of the ITAA 1936.

Sections 45A, 45B and 45C of the ITAA 1936 do not apply

8. The Commissioner will not make a determination under either subsection 45A(2) or 45B(3) of the ITAA 1936 that section 45C of the ITAA 1936 applies to treat the whole or any part of the capital benefit you received on the Distribution Date as an unfranked dividend.

Capital gains tax consequences

CGT event G1

9. CGT event G1 happened to your PW-HICT shares on the Distribution Date when PW-HICT made the return of capital to you in respect of each PW-HICT share you own (section 104-135).

10. You made a capital gain from CGT event G1 happening to your PW-HICT shares if the amount of the return of capital you received is more than the cost base of your shares. The capital gain is equal to the difference, and the cost base and reduced cost base of your PW-HICT shares is reduced to nil (subsection 104-135(3)). You cannot make a capital loss from CGT event G1 happening (Note 1 to subsection 104-135(3)).

11. If the amount of the return of capital you received is not more than the cost base of your shares, the cost base and reduced cost base of your shares is reduced by the amount of the return of capital (but not below nil) (subsection 104-135(4)).

Discount capital gain

12. You can treat a capital gain made when CGT event G1 happened in respect of the return of capital as a discount capital gain if you acquired your PW-HICT shares at least 12 months before the Distribution Date (subsection 115-25(1)), provided the other conditions in Subdivision 115-A are satisfied.

Scheme

13. The following description of the scheme is based on information provided by the applicant. If the scheme is not carried out as described, this Ruling cannot be relied upon.

Background

Primewest (Home Investment Consortium Trust) Pty Ltd

14. PW-HICT is an Australian-resident private company that was incorporated on 17 October 2016.

15. On incorporation, PW-HICT issued 19,750,000 ordinary shares ($1 per share) to investors and all the funds raised were utilised to acquire 7,500,000 units in HICT.

16. The original cost of the units in HICT was $18,750,000. PW-HICT also incurred $1 million worth of acquisition costs. Accordingly, the tax cost base of the units in HICT for PW-HICT totals $19,750,000.

17. PW-HICT currently has 50 shareholders, all of which are Australian residents.

18. PW-HICT's sole and principal activity is holding the investment in HICT. HICT held an investment in Home Consortium Limited (HCL), formerly named Hydrox Holdings Pty Ltd.

19. PW-HICT has not paid any dividends to its shareholders since its inception.

20. PW-HICT's retained profits for each income year since the date of incorporation were as follows:

Income Year	Retained Profit/(Loss)
2017	$7,527
2018	$3,133
2019	($404)
2020	$323,800

21. The profits for the 2020 income year are mainly attributable to a trust distribution from HICT totalling $327,660.99.

22. PW-HICT's franking account balance as at 30 June 2020 totalled $144,642.86.

Home Investment Consortium Trust

23. HICT is an Australian-resident unit trust of which PW-HICT holds 7,500,000 of the total units issued.

24. HICT was set up for the purpose of acquiring all of the shares in HCL. HCL owned the real property interests from the former Master Home Improvements businesses.

Home Consortium Group Limited – return of capital arrangement

25. HCL listed on the Australian Securities Exchange on 14 October 2019 as a stapled security.

26. As per paragraph 22 of Class Ruling CR 2021/2 *Home Consortium Group – return of capital by way of in specie distribution*, on 1 July 2020 HCL proposed to its stapled

security holders the establishment of the REIT. As a result of this proposal, the stapled security holders were to receive one unit in the REIT for every two HCL shares via a distribution in specie.

27. The proposal in CR 2021/2 was subsequently executed and, on 26 November 2020, HICT received a return of capital from HCL by way of in specie distribution of units in the REIT.

28. The ATO concluded in CR 2021/2:

- No part of the return of capital to HCL's shareholders (that is, HICT) by way of the in specie distribution of the units in the REIT is a 'dividend' as defined in section 6(1) of the ITAA 1936.
- The return of capital from HCL by way of the in specie distribution of the units in the REIT is not assessable as ordinary income under section 6-5.
- The Commissioner did not make a determination under either subsection 45A(2) or paragraph 45B(3)(b) of the ITAA 1936 that section 45C of the ITAA 1936 applied to any part of the return of capital.
- CGT event G1 happened to the HCL shares held by its shareholders (that is, HICT) when HCL made the return of capital to the shareholders by way of the in specie distribution in respect of each share held at the date the in specie distribution was made.

29. At the date of the in specie distribution the cost base for each REIT unit was $1.3722 per unit.

Transfer of HomeCo Daily Needs REIT units from Home Investment Consortium Trust to Primewest (HICT) Pty Ltd

30. Immediately after the execution of the arrangement in paragraph 25 to 29 of this Ruling, HICT distributed the REIT units received from HCL to its unitholders (that is, PW-HICT) by way of an in specie capital distribution.

31. PW-HICT received 3,750,852 units in the REIT by way of an in specie capital distribution with a cost allocation of $1.3722 per unit as per paragraph 15 of CR 2021/2. As a result, the cost base of the REIT units held by PW-HICT as at 26 October 2020 totalled $5,138,667.

32. As the investment in the REIT was not in line with PW-HICT's investment strategy, the units in the REIT were sold on market. Between 11 December 2020 and 23 December 2020, a total of 3,750,852 units were sold for net capital proceeds received (meaning net of transaction costs; that is, brokerage fees and GST charged) totalling $4,625,469.81.

33. PW-HICT's cost base for the units in the REIT ($5,138,667) exceeded the net capital proceeds received ($4,625,469.81) and, accordingly, PW-HICT realised a capital loss on the sale of the units of $513,197.19.

Return of capital

34. The Directors of PW-HICT determined that the capital proceeds received from disposal of the REIT units were in surplus to the operational needs of PW-HICT and consequently distributed capital proceeds totalling $4,627,130 as a return of capital to its shareholders on 8 January 2021 (Distribution Date). The distribution differed from the capital proceeds received due to a manual error regarding brokerage fees on the sale of a portion of the REIT units.

35. The capital proceeds distributed were debited in full against PW-HICT's untainted share capital account.

36. PW-HICT continues to own 7,500,000 units in HICT, which have a current market value of $29,775,000 and a cost base for CGT purposes of $14,611,333. The cost base for CGT purposes takes into account the occurrence of CGT event E4 as a result of trust capital distribution from HICT by way of in specie distribution of the units in the REIT.

Other matters

37. PW-HICT is not able to dispose of its units in HICT until October 2021 due to an escrow arrangement. This was not known at the time of preparing the Information Memorandum that was issued to prospective shareholders of PW-HICT.

Commissioner of Taxation
13 October 2021

Appendix – Explanation

This Explanation 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.

Table of Contents **Paragraph**

Return of capital not a dividend

38. Subsection 44(1) of the ITAA 1936 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.

39. The term 'dividend' is defined in subsection 6(1) of the ITAA 1936 and 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.

40. The term 'share capital account' is defined within section 975-300 as an account that 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.

41. Further, subsection 975-300(3) states that an account is generally not taken to be a share capital account if it is tainted. PW-HICT has confirmed that its share capital account is not tainted within the meaning of Division 197.

42. As the capital proceeds have been debited directly against PW-HICT's untainted share capital account, the amounts do not satisfy the definition of a dividend in accordance with paragraph (d) of subsection 6(1) of the ITAA 1936. Accordingly, the capital proceeds of $4,627,130 will not be included as assessable income of PW-HICT by operation of subsection 44(1) of the ITAA 1936.

Sections 45A, 45B and 45C do not apply

43. Sections 45A and 45B of the ITAA 1936 are integrity provisions which, if they apply, allow the Commissioner to make a determination that section 45C of the ITAA 1936 applies. If the Commissioner were to make a determination under section 45C of the ITAA 1936, then part of or all of the return of capital received by the shareholders of PW-HICT is treated as an unfranked dividend paid by PW-HICT out of profits.

Section 45A – streaming of dividends and capital benefits

44. Section 45A of the ITAA 1936 applies in circumstances where capital benefits are streamed to shareholders (the advantaged shareholders) who would, in the year of income in which the capital benefits are provided, derive a greater benefit from the capital benefits streamed compared to other shareholders (the disadvantaged shareholders) who would receive, or have received, dividends.

45. As the capital proceeds have been distributed as a return of capital in direct proportion to their individual shareholding in PW-HICT on the Distribution Date, there was no streaming of capital benefits to some shareholders and not to other shareholders.

46. Further, when the return of capital was distributed on the Distribution Date, there were no shareholders that had circumstances that would have allowed them to derive a greater benefit from the provision of the capital benefit from other shareholders.

47. Accordingly, the Commissioner will not make a determination pursuant to subsection 45A(2) of the ITAA 1936 that section 45C of the ITAA 1936 applies to the capital benefit.

Section 45B – scheme to provide capital benefits

48. 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 capital benefit by a company (paragraph 45B(2)(a) of the ITAA 1936)
- under the scheme, a taxpayer (a relevant taxpayer), who may or may not be the person provided with the capital benefit, obtains a tax benefit (paragraph 45B(2)(b) of the ITAA 1936), and
- having regard to the relevant circumstances of the scheme, it would be concluded that the person, or one of the persons, who entered into or carried out the scheme or any part of the scheme did so for a purpose (whether or not the dominant purpose but not including an incidental purpose) of enabling a relevant taxpayer to obtain a tax benefit (paragraph 45B(2)(c) of the ITAA 1936).

49. The arrangement involving the return of capital to PW-HICT shareholders constitutes a scheme for the purposes of section 45B of the ITAA 1936.

50. The return of capital was recorded as a debit to PW-HICT's share capital account and PW-HICT shareholders received a distribution of capital proceeds totalling $4,627,130. Therefore, PW-HICT shareholders were provided with a capital benefit (paragraph 45B(5)(b) of the ITAA 1936).

51. A taxpayer 'obtains a tax benefit' where the amount of tax payable would, apart from the operation of section 45B of the ITAA 1936, be less than the amount that would be payable, or would be payable at a later time, if the distribution had instead been a dividend (subsection 45B(9) of the ITAA 1936).

52. As a return of capital will generally result in a lesser amount of tax payable than a dividend, PW-HICT shareholders will obtain a tax benefit.

53. Paragraph 45B(2)(c) of the ITAA 1936 sets out an objective purpose test for the Commissioner to consider having regard to the 'relevant circumstances' of the scheme set out in subsection 45B(8) of the ITAA 1936.

54. Having regard to the relevant circumstances of the scheme set out in subsection 45B(8) of the ITAA 1936, it cannot be concluded that the scheme was entered into or carried out for a more than incidental purpose of enabling PW-HICT shareholders to obtain a tax benefit.

55. Accordingly, the Commissioner will not make a determination under subsection 45B(3) of the ITAA 1936 that section 45C of the ITAA 1936 applies to the whole, or part, of the payment of the return of capital.

Capital gains tax consequences

CGT event G1

56. CGT event G1 happens if:

- a company makes a payment to a shareholder in respect of a share they own in the company
- some or all of the payment (the non-assessable part) is not a dividend, or an amount that is taken to be a dividend under section 47 of the ITAA 1936, and
- the payment is not included in the shareholder's assessable income (section 104-135).

57. CGT event G1 happened to your PW-HICT shares when you received the return of capital in respect of your PW-HICT shares (section 104-135).

58. You made a capital gain when CGT event G1 happened if the amount of the return of capital you received exceeded the cost base of your PW-HICT shares. If so, the capital gain is equal to the amount of the excess and the cost base and reduced cost base of the shares is reduced to nil (subsection 104-135(3)). You cannot make a capital loss when CGT event G1 happens (Note 1 to subsection 104-135(3)).

59. If the amount of the return of capital you received is less than the cost base of your PW-HICT shares, you reduce both the cost base and reduced cost base of the shares (but not below nil) by the amount of the return of capital (subsection 104-135(4)).

References

Previous draft:

Not previously issued as a draft

Related Rulings/Determinations:

CR 2021/2

Legislative references:

- ITAA 1936 6(1)
- ITAA 1936 44(1)
- ITAA 1936 45A
- ITAA 1936 45A(2)
- ITAA 1936 45B
- ITAA 1936 45B(2)
- ITAA 1936 45B(2)(a)
- ITAA 1936 45B(2)(b)
- ITAA 1936 45B(2)(c)
- ITAA 1936 45B(3)
- ITAA 1936 45B(3)(b)
- ITAA 1936 45B(5)(b)
- ITAA 1936 45B(8)
- ITAA 1936 45B(9)
- ITAA 1936 45C
- ITAA 1936 47
- ITAA 1997 6-5
- ITAA 1997 104-135
- ITAA 1997 104-135(3)
- ITAA 1997 104-135(4)
- ITAA 1997 Subdiv 115-A
- ITAA 1997 115-25(1)
- ITAA 1997 Div 197
- ITAA 1997 Div 230
- ITAA 1997 975-300
- ITAA 1997 975-300(3)
- TAA 1953

ATO references

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