

CR 2022/83 - Prospect Resources Limited - return of capital and special dividend



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Class Ruling

Prospect Resources Limited – return of capital and special dividend

❶ 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.

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What this Ruling is about

1. This Ruling sets out the income tax consequences for shareholders of Prospect Resources Limited (Prospect) who received the return of capital payment of 17c per ordinary Prospect share and the unfranked special dividend of 79c per ordinary Prospect share on 4 August 2022 (Payment Date).
2. Details of this return of capital and special dividend are set out in paragraphs 21 to 43 of this Ruling.
3. All legislative references in this Ruling are to the *Income Tax Assessment Act 1997*, unless otherwise indicated.

Who this Ruling applies to

4. This Ruling applies to you if you:
 - were registered on the Prospect share register on 28 July 2022 (Record Date)
 - held your Prospect shares on capital account on the Record Date; that is, you did not hold your Prospect shares as revenue assets (as defined in section 977-50) or as trading stock (as defined in subsection 995-1(1)), and
 - received the return of capital payment of 17c per Prospect share and the unfranked special dividend of 79c per Prospect share on the Payment Date.

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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 21 to 43 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 2022 to 30 June 2023.

Ruling

Return of capital is not a dividend

7. No part of the return of capital paid to you by Prospect on the Payment Date is a dividend as defined in subsection 6(1) of the *Income Tax Assessment Act 1936* (ITAA 1936).

8. No part of the return of capital is included in your assessable income as a dividend under section 44 of the ITAA 1936.

Special dividend and the assessability of the special dividend

9. The unfranked special dividend of 79c per Prospect share is a 'dividend' as defined in subsection 6(1) of the ITAA 1936.

10. If you are a resident of Australia as defined in subsection 6(1) of the ITAA 1936, you include the special dividend in your assessable income under paragraph 44(1)(a) of the ITAA 1936.

11. If you are a foreign resident, the special dividend is non-assessable non-exempt income and not included in your assessable income as the whole dividend was declared by Prospect in the distribution statement to be conduit foreign income (paragraph 802-15(1)(a)). You are also not liable to pay withholding tax in respect of the special dividend (paragraph 802-15(1)(b)).

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

12. The Commissioner will not make a determination under paragraph 45B(3)(b) of the ITAA 1936 that section 45C of the ITAA 1936 applies to any part of the return of capital of 17c per Prospect share you received on the Payment Date.

Capital gains tax consequences

CGT event G1

13. CGT event G1 happened on the Payment Date when Prospect paid you the return of capital of 17c for each Prospect share you owned on the Record Date and continued to own on the Payment Date (section 104-135).

14. You made a capital gain when CGT event G1 happened if the return of capital of 17c per Prospect share you received was more than the share's cost base. The capital

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gain is equal to the difference, and the cost base and reduced cost base of your Prospect share 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)).

15. If the return of capital of 17c per Prospect share you received was equal to or less than the cost base of the share, the cost base and reduced cost base of each share is reduced by the amount of the return of capital (subsection 104-135(4)).

CGT event C2

16. CGT event C2 happened on the Payment Date when Prospect paid you the return of capital of 17c for each Prospect share you owned on the Record Date but ceased to own before the Payment Date (section 104-25).

17. You made a capital gain under CGT event C2 if the capital proceeds from the ending of your right to receive the return of capital were more than the cost base of the right. (subsection 104-25(3)).

18. In working out the capital gain when CGT event C2 happened, the capital proceeds are equal to the amount of the return of capital of 17c for each share you owned on the Record Date but ceased to own before the Payment Date (subsection 116-20(1)).

Discount capital gain

19. You can treat a capital gain made when CGT event G1 or C2 happened as a discount capital gain under Subdivision 115-A if you acquired your Prospect share at least 12 months before the Payment Date (subsection 115-25(1)) and the other conditions in Subdivision 115-A are satisfied.

Foreign-resident shareholders may disregard capital gains tax

20. If you were a foreign resident or the trustee of a foreign trust for CGT purposes as defined in subsection 995-1(1), you disregard any capital gain you made from CGT event G1 or any capital gain from CGT event C2 under subsection 855-10(1), provided that:

- you did not use the Prospect share, or your right to receive the return of capital, at any time in carrying on a business through a permanent establishment in Australia (table item 3 of section 855-15), or
- the Prospect share, or your right to receive the return of capital, was not covered by subsection 104-165(3) about individuals who choose to disregard capital gains upon ceasing to be Australia residents (table item 5 of section 855-15).

Scheme

21. 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.

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Background

22. Prospect is an Australian-resident company and is the head company of the Prospect income tax consolidated group, which was formed on 1 July 2016.
23. Prospect is publicly listed on the Australian Securities Exchange, where its shares have traded since December 2009.
24. Prospect is a battery minerals mining company with a focus on lithium assets located in Zimbabwe.
25. Prospect's main flagship project was the Arcadia Project located in Zimbabwe, which was held through Prospect's 87% interest in foreign-resident company Prospect Lithium Zimbabwe Pvt Ltd (PLZ).

The disposal

26. On 23 December 2021, Prospect announced it would sell its 87% interest in PLZ to Huayou Cobalt Co Limited for consideration of US\$377.9 million.
27. On 20 April 2022, Prospect announced that the sale of its 87% interest in PLZ was completed and that it intended to return a substantial portion of the net proceeds to shareholders.

The return of capital and special dividend

28. On 11 July 2022, Prospect announced that it would distribute to its shareholders an amount of 96c per Prospect share equating to \$443,769,083. The distribution will consist of a return of capital of 17c per share equating to \$78,584,108 and the balance being an unfranked dividend of 79c per share equating to \$365,184,975.
29. Prospect shareholders approved the return of capital and special dividend by way of ordinary resolution at the extraordinary general meeting held on 22 July 2022. The return of capital and special dividend were paid to shareholders on 4 August 2022.
30. The return of capital constituted an equal reduction of Prospect's share capital for the purposes of the *Corporations Act 2001*.
31. All Prospect shareholders received the return of capital and special dividend on the same terms irrespective of their tax profile.
32. No shares were cancelled in connection with the return of capital and no fractional entitlements arose.
33. Prospect did not raise any share capital as part of the return of capital.
34. Prospect did not provide ownership interests as part of the return of capital to Prospect shareholders.
35. The total amount of the return of capital of \$78,584,108 was debited against the contributed equity account of Prospect, which is a 'share capital account' as defined in section 975-300.
36. The special dividend was not debited against the contributed equity account of Prospect. The special dividend was debited against Prospect's accumulated profits. The total amount of accumulated profits paid for the special dividend was \$365,184,975.
37. The entire special dividend was unfranked and declared by Prospect to be conduit foreign income pursuant to section 802-15 in the distribution statement provided to Prospect shareholders on or before the Payment Date.

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Other matters

38. On the Record Date, Prospect had 462,259,462 fully paid ordinary shares on issue and Prospect only had ordinary shares on issue.
39. On the Record Date, Prospect had a contributed equity account balance of \$105,229,731.
40. Prospect's contributed equity account is not tainted within the meaning in section 197-50.
41. On the Record Date, Prospect had approximately 2,800 shareholders consisting of approximately 27% Australian-resident shareholders and 73% foreign-resident shareholders.
42. Prospect had a conduit foreign income balance of \$456,916,634 at 30 June 2022.
43. On the Record Date, the sum of the market values of the assets of Prospect and its subsidiaries that are taxable Australian real property did not exceed the sum of the market values of their other assets for the purposes of section 855-30.

Commissioner of Taxation

14 September 2022

Appendix – Explanation

❶ *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.*

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Return of capital is not a dividend

44. 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 and from sources in Australia if the shareholder is a non-resident.

45. 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, whether in money or other property, but excludes a distribution debited against an amount standing to the credit of the company's share capital account.

46. As the return of capital was debited against Prospect's untainted contributed equity account, the return of capital is not a dividend and is not included in your assessable income under subsection 44(1) of the ITAA 1936.

Anti-avoidance provisions

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

47. Section 45B of the ITAA 1936 is an anti-avoidance provision which, if it applied, allows the Commissioner to make a determination that section 45C of the ITAA 1936 applies. The effect of such a determination is that all or part of a return of capital received by Prospect shareholders is treated as an unfranked dividend paid out of profits of the company.

48. Section 45B of the ITAA 1936 generally applies where, having regard to the relevant circumstances of the scheme (as set out in subsection 45B(8) of the ITAA 1936), a company provided certain capital payments to its shareholders for a more than incidental purpose of enabling a taxpayer to obtain a demerger benefit or a tax benefit.

49. Having regard to the relevant circumstances of the scheme, it cannot be concluded that the scheme was entered into or carried out for a more than incidental purpose of enabling the Prospect shareholders to obtain a tax benefit.

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50. Therefore, the Commissioner will not make a determination under paragraph 45B(3)(b) of the ITAA 1936, that section 45C of the ITAA 1936 applies in relation to the whole or any part of the return of capital received by Prospect shareholders.

Capital gains tax consequences

CGT event G1

51. CGT event G1 happens if:

- a company makes a payment to a shareholder in respect of a share they own in that 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).

52. CGT event G1 happened when Prospect made the return of capital payment to you in respect of Prospect shares you owned at the Record Date and continued to own at the Payment Date (section 104-135).

53. You made a capital gain when CGT event G1 happened if the amount of the return of capital of 17c per Prospect share you received was more than the cost base of your Prospect share. The capital gain is equal to the amount of any excess and you reduce both the cost base and reduced cost base of the Prospect share to nil (subsection 104-135(3)). No capital loss can be made when CGT event G1 happens (Note 1 to subsection 104-135(3)).

54. If the amount of the return of capital of 17c you received per Prospect share was not more than the cost base of your Prospect share, you reduce both the cost base and reduced cost base of your share (but not below nil) by the amount of the return of capital (subsection 104-135(4)).

CGT event C2

55. If, after the Record Date but before the Payment Date, you ceased to own a Prospect share in respect of which the return of capital was payable, the right to receive the return of capital in respect of that share is retained by you and is a separate CGT asset from the Prospect share.

56. CGT event C2 happened when the return of capital is made. The right to receive the return of capital, being an intangible asset, ended by the right being discharged or satisfied when the return of capital was made (section 104-25).

57. You will make a capital gain under CGT event C2 if the capital proceeds from the ending of the right are more than the cost base of the right. The capital gain is equal to the amount of any excess. You 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. The cost base is equal to the amount of any difference (subsection 104-25(3)).

58. In working out the capital gain when a CGT event C2 happens, the capital proceeds are equal to the amount of the return of capital, being 17c per Prospect share that you owned on the Record Date but ceased to own before the Payment Date (subsection 116-20(1)).

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59. The cost base of your right to receive each return of capital is worked out under Division 110 (modified by Division 112). The cost base of the right does not include the cost base or reduced cost base of the share previously owned by you to the extent that it was applied in working out a capital gain or capital loss made when a CGT event happened to the share; for example, when you disposed of the share after the Record Date and before the Payment Date. Therefore, if the cost base or reduced cost base of the share previously owned by you has been fully applied in working out a capital gain or capital loss on the share, the right to receive the return of capital will have a nil cost base. As a result, you will, in those circumstances, make a capital gain equal to the capital proceeds, being 17c per Prospect share owned at the Record Date.

60. For the purposes of Subdivision 109-A, you are considered to have acquired the right at the time when you acquired your Prospect share. Therefore, you can treat a capital gain made when CGT event C2 happened to your right to the payment of the return of capital as a discount capital gain under Subdivision 115-A if you acquired your Prospect share at least 12 months before the Payment Date (subsection 115-25(1)) provided the other conditions in Subdivision 115-A are satisfied.

Foreign-resident shareholders are able to disregard capital gains

61. You disregard a capital gain or capital loss you made from a CGT event if:

- just before the CGT event happened, you were a foreign resident or a trustee of a foreign trust for CGT purposes as defined in subsection 995-1(1), and
- the CGT event happens in relation to a CGT asset that is not taxable Australian property (subsection 855-10(1)).

62. The table in section 855-15 sets out the 5 categories of CGT assets that are taxable Australian property:

Table 1: Categories of CGT assets that are taxable Australian property

Item	Description
1	Taxable Australian real property
2	An indirect Australian real property interest not covered by table item 5
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 table items 1, 2, or 5
4	An option or right to acquire a CGT asset covered by table items 1, 2 or 3
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)

63. The only relevant category of taxable Australian property is table item 2 of section 855-15. Shares in Prospect will be 'an indirect Australian real property interest' if (among other things) they pass the principal asset test in section 855-30. The principal asset test is passed in the case of shares in a company if the sum of the market values of the company's assets that are taxable Australian real property exceed the sum of the market values of the company's other assets.

64. Prospect advised that the total market value of its assets that are not taxable Australian real property is greater than the market value of its taxable Australian real property assets. Accordingly, the principal asset test in section 855-30 will not be satisfied.

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65. Therefore, if you were a foreign resident or the trustee of a foreign trust for CGT purposes, you disregard any capital gain you made from CGT event G1 or any capital gain from CGT event C2 under subsection 855-10(1), provided that:

- you did not use the Prospect share, or your right to receive the return of capital, at any time in carrying on a business through a permanent establishment in Australia (table item 3 of section 855-15), or
- the Prospect share, or your right to receive the return of capital, was not covered by subsection 104-165(3) about individuals who choose to disregard capital gains upon ceasing to be Australia residents (table item 5 of section 855-15).

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References

Legislative references:

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 - ITAA 1936 44
 - ITAA 1936 44(1)
 - ITAA 1936 44(1)(a)
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