

CR 2002/41 - Income tax: Return of Capital by Bligh Ventures Ltd

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Class Ruling

Income Tax: Return of Capital by Bligh Ventures Ltd.

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Preamble

*The number, subject heading, and the **What this Class Ruling is about** (including **Tax law(s)**, **Class of persons and Qualifications sections**), **Date of effect**, **Withdrawal**, **Arrangement** and **Ruling** parts of this document are a 'public ruling' in terms of Part IVAAA of the **Taxation Administration Act 1953**. CR 2001/1 explains **Class Rulings** and **Taxation Rulings TR 92/1** and **TR 97/16** together explain when a Ruling is a public ruling and how it is binding on the Commissioner.*

What this Class Ruling is about

1. This Ruling sets out the Commissioner's opinion on the way in which the 'tax law(s)' identified below apply to the defined class of persons, who take part in the arrangement to which this Ruling relates.

Tax law(s)

2. This Ruling relates to the application of the following provisions of the *Income Tax Assessment Act 1936* ('ITAA 1936') and the *Income Tax Assessment Act 1997* ('ITAA 1997'):

- Section 6(1) ITAA 1936;
- Section 6(4) ITAA 1936;
- Section 6D ITAA 1936;
- Section 160ARDM ITAA 1936;
- Section 995(1) ITAA 1997;
- Section 44 ITAA 1936;
- Section 45 ITAA 1936;
- Section 45A ITAA 1936;
- Section 45B ITAA 1936;
- Section 45C ITAA 1936;
- Section 104-135 ITAA 1997.

Class of persons

3. The class of persons to whom this Ruling applies are all shareholders in Bligh Ventures Ltd ('BVL') who receive a return of share capital consisting of cash and an in specie distribution of shares in Techniche Ltd ('Techniche') under the arrangement as described below.

Qualifications

4. The Commissioner makes this Ruling based on the precise arrangement identified in this Ruling.

5. The class of persons defined in this Ruling may rely on its contents provided the arrangement actually carried out in accordance with the arrangement described below at paragraphs 10 to 18 in this Ruling.

6. If the arrangement actually carried out is materially different from the arrangement described in this ruling:

- (a) this Ruling has no binding effect on the Commissioner because the arrangement entered into is not the arrangement on which the Commissioner has ruled; and
- (b) this Ruling may be withdrawn or modified.

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Date of effect

8. This Class Ruling applies to the year ended 30 June 2002 or 30 June 2003 dependent upon the income tax year in which the return of share capital is made. However, this Ruling does not apply to taxpayers to the extent that it conflicts with the terms of settlement of a dispute agreed to before the date of issue of this Ruling (see paragraphs 21 to 22 of Taxation Ruling TR 92/20). Furthermore this

Ruling applies to the extent that the relevant tax laws are not amended.

Withdrawal

9. This Class Ruling is withdrawn and ceases to have effect after the date on which shareholders receive the proceeds of the capital return or 30 June 2003, which ever is earlier. However, the Ruling continues to apply after its withdrawal in respect of the tax laws ruled upon, to all persons within the specified class who enter into the specified arrangement during the term of the Ruling, subject to there being no change in the arrangement or in the persons' involvement in the arrangement.

Arrangement

10. The arrangement that is the subject of the Ruling is described below. This description is based on the application for class ruling dated 26 March 2002, including all attachments, in relation to the proposal by BVL to return capital to all ordinary shareholders. This document, or relevant parts of it, as the case may be, forms part of and are to be read with this description.

Note: certain information received from BVL has been provided on a commercial-in-confidence basis and will not be disclosed or released under the *Freedom of Information Act 1982*.

11. BVL has been in existence for over 30 years and has been listed on the Australian Stock Exchange since May 1987. BVL's principal activities include the provision of management services and capital to business enterprises and petroleum companies, acting as a holding company as well as limited share trading.

12. As at 30 June 2001 BVL's financial statements disclosed share capital of \$4,751,463 and retained profits of \$(4,671,776). As at 26 March 2002 there were 7,204,523 fully paid and 150,000 partly paid ordinary shares on issue. There are no other types of shares on issue.

13. At this time BVL's long term investments comprised shares in two companies being Techniche, and Jtec Pty Ltd (Jtec). Jtec is a private company in which Techniche holds a 96.01% interest and BVL a 3.99% interest. Pursuant to a contract dated 19 March 2002 between BVL and Techniche, BVL sold its 3.99% interest in Jtec in exchange for 1,000,000 shares in Techniche at a market value of \$80,000. This increased BVL's holding of Techniche shares to 1,925,281.

14. The interest in Jtec was sold at a loss. Further, the share price of Techniche has fallen significantly since 30 June 2000 with the effect that BVL has had to write down the carrying value of both investments in the 2001 annual financial statements and the 31 December 2001 half year financial statements.

15. BVL is proposing to return share capital to its shareholders by way of a combination of cash and shares in Techniche (a publicly listed company on the ASX). The amount of share capital to be returned will be calculated on the basis of a cash component of approximately \$2,750,000 and 1,925,281 shares in Techniche. The actual amount to be returned will depend upon the market value of the Techniche shares at the date the distribution is made.

16. Since listing on the ASX, BVL has not paid any dividends. However, in August 2000 BVL returned share capital to its shareholders in the form of an in specie distribution of shares in one of its non-technology investments, Bligh Oil and Minerals NL. The return of share capital was undertaken primarily for the purpose of making BVL more attractive as a target for takeover. Subsequently, in September 2000 Techniche announced a takeover offer to acquire all the issued capital in BVL. The offer was subject to a number of conditions being satisfied, including an acceptance level of 90% of issued shares. This condition was not fulfilled.

17. As a result of the failed takeover offer by Techniche, the Board of BVL ('the Board') is now of the view that there is no possibility of BVL being purchased as it currently exists. Furthermore, the Board is generally of the opinion that BVL no longer serves the purposes for which it was established. The Board is of the view that it would not be in the interests of BVL shareholders for BVL to be wound up as it may be able to sell the ASX listed shell and produce additional value for shareholders. Accordingly, the Board is considering ways of rationalising and winding down BVL's operations so that BVL is attractive to a purchaser wishing to acquire an ASX listed company.

18. The current proposal forms part of the rationalisation process. The return of share capital will reduce BVL's capital base and make BVL more attractive to another company wanting an interest only in an ASX listed company.

Ruling

Distribution is not a dividend

19. The return of share capital does not constitute a dividend for the purposes of the ITAA 1936 and ITAA 1997.

The anti avoidance provisions

20. Section 45 of the ITAA 1936 does not apply to the return of share capital received by an ordinary shareholder.

21. The Commissioner will not make a determination (under section 45A or 45B of the ITAA 1936) that section 45C of the ITAA 1936 applies to the whole or any part, of the return of share capital received by an ordinary shareholder.

Explanations**Distribution is not a dividend**

22. Broadly, section 44 of the ITAA 1936 requires a shareholder in a company to include in its assessable income any dividends paid to the shareholder by a company out of profits derived by the company from any source (if resident in Australia) and from an Australian source (if non-resident). In order for section 44 to have application, the amount paid must constitute a 'dividend'.

23. 'Dividend' is defined in subsection 6(1) of the ITAA 1936 to include 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.

24. One such specific exclusion is paragraph (d) of the definition of dividend which provides:

'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.'

25. As the return of capital will be debited against BVL's share capital account, paragraph (d) of the definition of dividend applies to exclude the distribution from falling within the definition of dividend. Accordingly, the return of capital will not be regarded as a dividend unless some other more specific provision in either the ITAA 1936 or ITAA 1997 operates to make it a dividend.

26. For instance, if BVL's share capital account was tainted, any distribution debited to that account will be treated as a dividend. However, BVL's share capital account is not tainted for the purposes

of section 160ARDM of the ITAA 1936, as no amounts have been transferred to its share capital account from any of its other accounts other than the share premium account (which was permitted under the transitional provisions). Accordingly, the share capital account satisfies section 6D of the ITAA 1936 and is available to fund capital distributions that will not be treated as dividends under the section 6(1) definition.

27. Another such provision is subsection 6(4) of the ITAA 1936 which provides that paragraph (d) of the definition of dividend does not apply if the capital distribution forms part of an arrangement where the company raises share capital from certain shareholders and then makes a capital distribution to other shareholders. However, from the information provided it appears that BVL has no plans to undertake a corresponding raising of share capital and therefore subsection 6(4) does not apply to the return of capital.

The anti avoidance provisions

A. Section 45

28. Section 45 applies where a company streams the provision of bonus shares and the payment of minimally franked dividends, in such a way that shares are received by some but not all shareholders and some or all of the shareholders who do not receive the shares receive minimally franked dividends. If it applies, the value of the shares are taken to be an unfranked and non-rebatable dividend that is paid by the company out of profits to the shareholder at the time of provision. Section 45 does not apply to the return of capital as the arrangement described does not involve the distribution of minimally franked dividends and there is no proposal for dividends to be paid.

B. Sections 45A and 45B

29. Sections 45A and 45B of the 1936 Act are two anti-avoidance provisions which, if they apply, allow the Commissioner to make a determination under section 45C of the 1936 Act that all or part of the capital distribution is treated as an unfranked and non-rebatable dividend. Accordingly, the application of these two provisions to the return of capital must also be considered.

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

31. Although BVL will be providing shareholders with a 'capital benefit' (as defined in paragraph 45A(3)(b)) the capital benefit is to be

provided to all the shareholders in BVL at that time. Accordingly, there is no 'streaming' of capital benefits to some shareholders and dividends to other shareholders and section 45A has no application to the return of capital.

32. Section 45B applies where certain capital payments are paid to shareholders in substitution for dividends. Specifically, the provision applies where:

- a) there is a scheme under which a person is provided with a capital benefit by a company (paragraph 45B(2)(a));
- b) 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
- c) having regard to the relevant circumstances of the scheme, it would be concluded that the person, or one of the persons, entered into the scheme or carried out the scheme or any part of the scheme for a purpose, other than an incidental purpose, of enabling a taxpayer to obtain a tax benefit (paragraph 45B(2)(c)).

33. In this case, whilst the conditions of paragraphs 45B(2)(a) and (b) are met, the requisite purpose of enabling the shareholder to obtain a tax benefit – by way of a capital distribution – is not present.

34. Having regard to the relevant circumstances of the scheme - set out in subsection 45B(5) – it is apparent that the substantial purpose of the arrangement is the return of share capital and not the provision of capital benefits to shareholders. The purpose of the arrangement is to reduce the company's capital base as part of winding down its activities and whilst it may have the effect of providing capital benefits to some shareholders, any benefit is merely incidental.

35. In this regard, it cannot be said that the return of capital is attributable to the profits of the company, nor do the pattern of distributions indicate that it is being paid in substitution for a dividend. The conclusion that the distribution is demonstrably not attributable to profits of BVL or an associate of BVL follows from the fact that BVL has no profits and that, in the circumstances, the return of capital could not reasonably be regarded as other than the share capital invested in Techniche. Rather, BVL is likely to incur a substantial capital loss on disposal of its investment in Techniche.

Detailed contents list

36. Below is a detailed contents list for this Class Ruling:

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Commissioner of Taxation

17 July 2002

<i>Previous draft:</i>	- ITAA 1936 44
Not previously issued in draft form	- ITAA 1936 45
	- ITAA 1936 45A
	- ITAA 1936 45A(3)(b)
<i>Related Rulings/Determinations:</i> CR 2001/1; TR 92/1; TR 97/16	- ITAA 1936 45B
	- ITAA 1936 45B(2)(a)
	- ITAA 1936 45B(2)(b)
	- ITAA 1936 45B(2)(c)
<i>Subject references:</i>	- ITAA 1936 45B(5)
	- ITAA 1936 45C
	- ITAA 1997 995(1)
<i>Legislative references:</i>	- TAA 1953 Part IVA
	- ITAA 1936 6(1)
	- ITAA 1936 6(4)
	- ITAA 1936 6D
	- ITAA 1936 160ARDM

ATO References

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