



CR 2006/90 - Income tax: Miller's Retail Limited: proposed return of capital and share consolidation

 This cover sheet is provided for information only. It does not form part of *CR 2006/90 - Income tax: Miller's Retail Limited: proposed return of capital and share consolidation*

 This document has changed over time. This is a consolidated version of the ruling which was published on *20 September 2006*



Class Ruling

Income tax: Miller's Retail Limited: proposed return of capital and share consolidation

Contents	Para
LEGALLY BINDING SECTION:	
What this Ruling is about	1
Date of effect	8
Withdrawal	12
Scheme	13
Ruling	24
NOT LEGALLY BINDING SECTION:	
Appendix 1:	
Explanation	29
Appendix 2:	
Detailed contents list	59

① 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, we must apply the law to you in the way set out in the ruling (or in a way that is more favourable for you if we are satisfied that the ruling is incorrect and disadvantages you, and we are 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); and
- section 104-135 of the ITAA 1997.

All references are to the ITAA 1936 unless otherwise stated.

Class of entities

3. The class of entities to which this Ruling applies is the owners of ordinary shares in Miller's Retail Limited (MRL) who are registered on the MRL Share Register on the Record Date, being the date for determining entitlements to the proposed return of capital, and who receive the capital distribution, hold their shares in MRL on capital account and are residents of Australia within the meaning of subsection 6(1). In this ruling, those entities are referred to as 'MRL shareholders'.

Qualifications

4. The Commissioner makes this Ruling based on the precise scheme identified in the 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 13 to 23 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.

7. This work is copyright. Apart from any use as permitted under the *Copyright Act 1968*, no part may be reproduced by any process without prior written permission from the Commonwealth. Requests and inquiries concerning reproduction and rights should be addressed to:

Commonwealth Copyright Administration
Attorney General's Department
Robert Garran Offices
National Circuit
Barton ACT 2600

or posted at: <http://www.ag.gov.au/cca>

Date of effect

8. This Ruling applies from 20 September 2006. However, the 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 the Ruling. Furthermore, the Ruling only applies to the extent that:

- it is not later withdrawn by notice in the *Gazette*; or
- the relevant provisions are not amended.

9. If this Class Ruling is inconsistent with a later public or private ruling, the relevant class of entities may rely on either ruling which applies to them (item 1 of subsection 357-75(1) of Schedule 1 to the *Taxation Administration Act 1953* (TAA)).

10. If this Class Ruling is inconsistent with an earlier private ruling, the private ruling is taken not to have been made if, when the Class Ruling is made, the following two conditions are met:

- the income year or other period to which the rulings relate has not begun; and
- the scheme to which the rulings relate has not begun to be carried out.

11. If the above two conditions do not apply, the relevant class of entities may rely on either ruling which applies to them (item 3 of subsection 357-75(1) of Schedule 1 to the TAA).

Withdrawal

12. This Ruling is withdrawn and ceases to have effect after 30 June 2007. However, the Ruling continues to apply after its withdrawal in respect of the relevant provisions ruled upon, to all entities within the specified class who entered into the specified scheme during the term of the Ruling, subject to there being no change in the scheme or in the entities involved in the scheme.

Scheme

13. The scheme that is the subject of the Ruling is described below. This description is based on, and includes reference to, the following documents:

- application for Class Ruling from Greenwoods & Freehills dated 29 June 2006; and
- emails from Greenwoods & Freehills from 12 July 2006 to 4 September 2006.

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

14. MRL, which along with its subsidiary members elected to form a tax consolidated group with effect from 1 July 2003, is an Australian resident public company listed on the Australian Stock Exchange and primarily conducts business as a retailer of women's clothing.

15. During the 2000, 2001 and 2002 years of income, MRL acquired a number of discount retail and wholesale businesses (referred to collectively as the Discount Variety Division) at no less than their market value.

16. MRL used a combination of cash, sourced through external debt financing, and scrip to acquire the Discount Variety Division.

17. In November 2005, MRL agreed to sell the Discount Variety Division to a third party for cash consideration of approximately \$120 million. In doing so, MRL generated a loss on the sale.

18. As a result of the sale of the Discount Variety Division, MRL has released capital which it has determined is surplus to its needs.

19. MRL, which has only ordinary shares on issue, proposes to return approximately \$50 million of this surplus capital to its shareholders.

20. MRL also proposes to reduce the number of shares on issue by way of a 10 for 8 share consolidation in accordance with section 254H of the *Corporations Act 2001*.

21. MRL's purpose in making the return of capital and share consolidation is to achieve the following commercial objectives:

- to return surplus capital equitably to all shareholders; and
- to facilitate an increase in earnings per share which may lead to an increase in share price.

22. The return of capital is subject to shareholder approval at a general meeting of shareholders to be held on 26 October 2006. All ordinary shareholders registered on the Record Date will be entitled to the return of capital. The Record Date and Payment Date will be 2 November 2006 and 10 November 2006, respectively.

23. MRL will debit the return of capital against its share capital account. MRL confirms that there have been no transfers to its share capital account, as defined in section 975-300 of the ITAA 1997, from any of its other accounts.

Ruling

Is the return of capital a dividend as defined in subsection 6(1)?

24. The proposed return of capital will not be a dividend as defined in subsection 6(1).

The application of sections 45A, 45B and 45C to the proposed return of capital

25. Subject to the qualifications in paragraphs 4 to 6 of this Ruling, 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 under section 45C.

Capital gains tax consequences of the return of capital and share consolidation

26. CGT event G1 will happen to a MRL shareholder when the return of capital is paid (section 104-135 of the ITAA 1997).
27. CGT event C2 will happen to a MRL shareholder receiving the return of capital who ceases to own their MRL shares after the Record Date but before the Payment Date (section 104-25 of the ITAA 1997).
28. CGT event C2 will not be triggered as a result of the share consolidation.

Commissioner of Taxation20 September 2006

Appendix 1 – Explanation

1 *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.*

Dividends

29. Subsection 44(1) includes in a shareholder's assessable income any dividends, as defined in subsection 6(1), paid to the shareholder out of profits derived by the company from any source (if a resident of Australia) and from an Australian source (if non-resident).

30. The term 'dividend' in subsection 6(1) includes any distribution made by a company to any of its shareholders. However, later paragraphs in this subsection exclude certain items from being a dividend for income tax purposes.

31. Relevantly, the specific exclusion in paragraph (d) of the definition of 'dividend' in subsection 6(1) provides:

Money 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 6(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.

32. The return of capital will be debited against MRL's share capital account. There have been no transfers into MRL's share capital account as defined in section 975-300 of the ITAA 1997 from any of MRL's other accounts. Therefore, paragraph (d) of the definition of 'dividend' in subsection 6(1) applies and the return of capital would not constitute a dividend.

Anti-avoidance provisions

33. Sections 45A and 45B are two anti-avoidance provisions which, if they apply, allow the Commissioner to determine that all or part of a distribution is treated as an unfrankable dividend that is paid by the company out of profits to the shareholder.

Section 45A – streaming of dividends and capital benefit

34. Section 45A applies in circumstances where capital benefits are streamed to advantaged shareholders who would derive a greater capital benefit than the other shareholders (the disadvantaged shareholders) who would receive dividends.

35. MRL will provide all of its shareholders with a 'capital benefit' (as defined in paragraph 45A(3)(b)), and the capital benefit is to be provided to all shareholders in direct proportion to their individual shareholding. As all shareholders benefit equally from the return of capital, there is no indication of 'streaming' of capital benefits to some shareholders and not to other shareholders. Accordingly, section 45A will not apply to the return of capital, and the Commissioner will not make a determination under subsection 45A(2) that section 45C applies to the return of capital.

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

36. Section 45B applies where capital benefits are provided to shareholders in substitution for dividends.

37. Subsection 45B(2) sets out the conditions under which the Commissioner will make a determination under subsection 45B(3) that section 45C applies. These conditions are that:

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

38. Therefore, the following elements need to be satisfied before section 45B will apply to the arrangement:

- the return of capital is a 'scheme' within the broad meaning of that term;
- the shareholders will be 'provided with a capital benefit' as defined in subsection 45B(2) by MRL under the proposed return of capital. The definition includes a distribution of share capital; and
- the shareholders will obtain a tax benefit under the arrangement.

39. A shareholder 'obtains' a 'tax benefit', as defined in subsection 45B(9), where:

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

by the taxpayer would, apart from the operation of section 45B:

- 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 a dividend.

40. Ordinarily, a return of capital would be subject to the CGT provisions of the income tax law. Unless the amount of the distribution exceeds the cost base of the share there will only be a cost base reduction under CGT event G1 (section 104-135 of the ITAA 1997). It is only to the extent (if any) that the distribution exceeds the cost base of the share that a capital gain is made. A dividend would generally be included in the assessable income of a resident shareholder. Therefore, MRL shareholders will obtain tax benefits from the return of capital.

Relevant circumstances

41. For the purposes of paragraph 45B(2)(c) the Commissioner is required to consider the 'relevant circumstances' set out in subsection 45B(8) to determine whether any part of the scheme would be entered into for a purpose, other than an incidental purpose, of enabling a relevant taxpayer to obtain a tax benefit. However, the list of relevant circumstances in subsection 45B(8) is not exhaustive and regard may be had to other circumstances on the basis of their relevance.

42. The test of purpose is an objective one. The question is whether it would be concluded that a person who entered into or carried out the scheme did so for the purpose of obtaining a tax benefit for the relevant taxpayer in respect of the capital benefit. The requisite purpose does not have to be the most influential or prevailing purpose but it must be more than an incidental purpose.

43. The purpose which causes section 45B to apply may be the purpose of any party to the scheme. In this case, however, the Commissioner is concerned only with the purpose of MRL. The Commissioner cannot at this stage apprehend the purposes of MRL's numerous shareholders, all of whom are eligible to vote on the return of capital under section 256C of the *Corporations Act 2001* and all of whom would participate in the return of capital should the proposal be approved. Nevertheless, in a case such as this, an objective conclusion as to the purpose of the company should, generally speaking, not be inconsistent with an objective conclusion as to the purpose of the shareholders, in particular those shareholders who vote in favour of the proposal.

44. The relevant circumstances under subsection 45B(8) cover the circumstances of the company and the tax profile of the shareholders. In this instance, as the return of capital is made to all shareholders of MRL regardless of individual shareholder circumstances, paragraphs 45B(8)(c) to (h) do not incline for or against a conclusion as to purpose. The circumstances covered by paragraphs 45B(8)(i) and (j), pertaining to the provision of ownership interests and a demerger respectively, are not relevant. In this case, the relevant matters are those covered by the circumstances described in paragraphs 45B(8)(a), (b) and (k).

45. Paragraph 45B(8)(a) refers to the extent to which the capital benefit is attributable to capital and profits (realised and unrealised) of the company or an associate (within the meaning of section 318) of the company. It is stated that in this case, the underlying purpose of MRL in seeking to make the capital distribution is to return the capital which was raised for the specific purpose of the acquisition of the Discount Variety Division. The return of capital is referable to surplus capital released from the sale of the Discount Variety Division. These funds cannot be described as profits, as no profit was made on the sale of the Discount Variety Division or through other trading activities of MRL. It will be part of the residual amount remaining after the debt used to acquire the Discount Variety Division has been repaid, all of which is surplus to the operation of the company's business, that will be returned to the MRL shareholders. In these circumstances, the capital benefit is not attributable to profits, realised or unrealised.

46. It is anticipated that the share consolidation, which is to be undertaken immediately after the return of capital, will assist in bolstering the earnings-per-share ratio of MRL shares. As a flow on effect, it is anticipated that the price of MRL shares will increase.

47. Paragraph 45B(8)(b) refers to the pattern of distributions made by a company or an associate (within the meaning of section 318) of the company. Although MRL states that it would prefer to proceed by way of payment of a fully franked dividend, which would assist in maintaining a stable distribution pattern as preferred by shareholders, there are no profits from which a distribution could be made. It is noted that while MRL did not pay any dividends during the 2005 and 2006 years of income it paid fully franked dividends during the previous 4 years of income. MRL has not made any capital distributions in recent years.

48. Paragraph 45B(8)(k) refers to the matters in subparagraphs 177D(b)(i) to (viii). These are matters by reference to which a scheme is able to be examined from a practical perspective in order to identify and compare its tax and non-tax objectives. The matters include the manner in which the scheme is carried out, the timing of the scheme, its form and substance, and the financial and other implications for the parties involved. MRL has demonstrated that the scheme, being a return of capital to its shareholders followed by a share consolidation, involves a legitimate return of surplus capital.

Section 45C – deeming dividends to be paid where determination made under sections 45A or 45B

49. As the Commissioner will not make a determination under subsection 45A(2) or subsection 45B(3) in relation to the scheme as described, section 45C will not apply.

CGT event G1: section 104-135 of the ITAA 1997

50. CGT event G1 (section 104-135 of the ITAA 1997) will happen if a company makes a payment to a shareholder in respect of a share they own in the company and some or all of the payment is not a dividend as defined in subsection 995-1 of the ITAA 1997, or an amount that is taken to be a dividend under section 47 of the ITAA 1997.

51. A shareholder will make a capital gain if the return of capital by the company in relation to a share exceeds the cost base of the share (subsection 104-135(3) of the ITAA 1997). A shareholder cannot make a capital loss under CGT event G1.

52. The cost base and reduced cost base of each MRL share will be reduced (but not below nil) by the amount of the return of capital (subsections 104-135(3) and (4) of the ITAA 1997). If the share was acquired by the shareholder at least 12 months before the Payment Date, a capital gain made from the share may qualify as a discount capital gain (subsection 115-25(1) of the ITAA 1997) if the other conditions in Subdivision 115-A of the ITAA 1997 are satisfied. As the return of capital is expected to be 20 cents per share, it is not likely to result in any capital gains for MRL shareholders.

CGT event C2: section 104-25 of the ITAA 1997

53. If, after the Record Date but before the Payment Date, a person who is a registered ordinary shareholder of MRL ceases to own some or all of their MRL shares in respect of which the proposed 2006 return of capital is payable, the right to receive the payment in respect of each of the shares disposed of is considered to be a separate CGT asset. That right is one of the rights inherent in the share on the Record Date and is retained by the shareholder when the share is sold.

54. CGT event C2 (section 104-25 of the ITAA 1997) will happen when the return of capital is paid and the right to payment ends. A capital gain will result if the capital proceeds for the event are more than the cost base of the right. The capital proceeds will be the amount of the proposed 2006 return of capital from MRL. The cost base of the MRL shareholder's right to receive a payment under the scheme is worked out in accordance with Division 110 of the ITAA 1997. However, the cost base (or reduced cost base) of the right is likely to be nil because the full cost base (or reduced cost base) of the share previously held by the shareholder has been applied in working out the capital gain or loss when a CGT event happened to the share – for example the shareholder disposed of the share.

55. The right to payment from the company was inherent in the share during the time that it was owned. Therefore, for the purposes of Subdivision 109-A of the ITAA 1997 the right is considered to have been acquired at the time when the share was acquired. Consequently, if the share was originally acquired by the former shareholder at least 12 months before the payment, a capital gain from 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 are satisfied).

Share consolidation

56. As the share consolidation will be undertaken in accordance with section 254H of the *Corporations Act 2001*, no ordinary shares in MRL will be cancelled as a result of the proposed share consolidation. The shareholders of the MRL shares will not receive any capital proceeds consequent to the reduction in the number of shares on issue.

57. The share consolidation will not result in any change to MRL's share capital. Further, there will be no change to the proportionate interests held by each shareholder.

58. Accordingly, no CGT event will happen as a result of the share consolidation.

Appendix 2 – Detailed contents list

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

	Paragraph
What this Ruling is about	1
Relevant provision(s)	2
Class of entities	3
Qualifications	4
Date of effect	8
Withdrawal	12
Scheme	13
Ruling	24
Is the return of capital a dividend as defined in subsection 6(1)?	24
The application of sections 45A, 45B and 45C to the proposed return of capital	25
Capital gains tax consequences of the return of capital and share consolidation	26
Appendix 1 – Explanation	29
Dividends	29
Anti-avoidance provisions	33
Section 45A – streaming of dividends and capital benefit	34
Section 45B – schemes to provide capital benefits in substitution for dividends	36
<i>Relevant circumstances</i>	41
Section 45C – deeming dividends to be paid where determination made under sections 45A or 45B	49
CGT event G1: section 104-135 of the ITAA 1997	50
CGT event C2: section 104-25 of the ITAA 1997	53
Share consolidation	56
Appendix 2 – Detailed contents list	59

References

Previous draft:

Not previously issued as a draft

Subject references:

- capital reduction
- reduction of share capital
- return of share capital
- share capital

Legislative references:

- Copyright Act 1968
- Corporations Act 2001 254H
- Corporations Act 2001 256C
- ITAA 1936 6(1)
- ITAA 1936 6(1)(d)
- ITAA 1936 6(4)
- ITAA 1936 44(1)
- ITAA 1936 45A
- ITAA 1936 45A(2)
- ITAA 1936 45A(3)(b)
- ITAA 1936 45B
- ITAA 1936 45B(2)
- ITAA 1936 45B(2)(c)
- ITAA 1936 45B(3)
- ITAA 1936 45B(8)
- ITAA 1936 45B(8)(a)
- ITAA 1936 45B(8)(b)
- ITAA 1936 45B(8)(c)
- ITAA 1936 45B(8)(d)
- ITAA 1936 45B(8)(e)
- ITAA 1936 45B(8)(f)

- ITAA 1936 45B(8)(g)
- ITAA 1936 45B(8)(h)
- ITAA 1936 45B(8)(i)
- ITAA 1936 45B(8)(j)
- ITAA 1936 45B(8)(k)
- ITAA 1936 45B(9)
- ITAA 1936 45C
- ITAA 1936 47
- ITAA 1936 177D(b)(i)
- ITAA 1936 177D(b)(ii)
- ITAA 1936 177D(b)(iii)
- ITAA 1936 177D(b)(iv)
- ITAA 1936 177D(b)(v)
- ITAA 1936 177D(b)(vi)
- ITAA 1936 177D(b)(vii)
- ITAA 1936 177D(b)(viii)
- ITAA 1936 318
- ITAA 1997 104-25
- ITAA 1997 104-135
- ITAA 1997 104-135(3)
- ITAA 1997 104-135(4)
- ITAA 1997 Subdiv 109-A
- ITAA 1997 Div 110
- ITAA 1997 Subdiv 115-A
- ITAA 1997 115-25(1)
- ITAA 1997 975-300
- ITAA 1997 995-1(1)
- TAA 1953
- TAA 1953 Sch 1 357-75(1)

ATO references

NO: 2006/16951

ISSN: 1445-2014

ATOlaw topic: Income Tax ~~ Return of capital
 Income Tax ~~ Capital Gains Tax ~~ CGT events G1 to G3 - shares
 Income Tax ~~ Capital Gains Tax ~~ CGT events C1 to C3 - end of a CGT asset