


CR 2008/50 - Income tax: Distribution of VISA proceeds by Cuscal Limited via the issuance of a special class of share

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Class Ruling

Income tax: Distribution of VISA proceeds by Cuscal Limited via the issuance of a special class of share

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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, we must apply the law to you in the way set out in the ruling (unless we are satisfied that the ruling is incorrect and disadvantages you, in which case we may apply the law in a way that is more favourable for you – provided 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 tax laws dealt with in this Class Ruling are:
- Section 45A of the *Income Tax Assessment Act 1936* (ITAA 1936);
 - Section 45B of the ITAA 1936;
 - Section 45C of the ITAA 1936;
 - Part IVA of the ITAA 1936;
 - Subdivision 204-D of the *Income Tax Assessment Act 1997* (ITAA 1997); and
 - Division 725 of the ITAA 1997.

Class of entities

3. The class of entities to which this Ruling applies is the shareholders of Cuscal Limited (Cuscal) who are issued with Class B shares in Cuscal under the scheme.

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 13 to 30 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.

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Date of effect

8. This Ruling applies from 1 July 2008 to 30 June 2012. However, the Ruling continues to apply after 30 June 2012 to all entities within the specified class who entered into the specified scheme during the term of the Ruling.

9. 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.

10. If this 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)).

11. If this Ruling is inconsistent with an earlier private ruling, the private ruling is taken not to have been made if, when the 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.

12. 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).

Scheme

Background

13. Cuscal is a service organisation providing various wholesale banking services primarily to its shareholders (as customers). Cuscal is also an Authorised Deposit-taking Institution (ADI) regulated by the Australian Prudential Regulatory Authority (APRA).

14. Cuscal is a principal member of VISA and through Cuscal's principal membership a number of its customers are associate VISA members (called VISA Issuing Credit Unions or VICUs). The VISA membership allows Cuscal and the VICUs to issue VISA debit and credit cards.

15. The VICUs generate VISA transactions through their own business and Cuscal facilitates/processes these transactions as part of its wholesale banking business. As a principal member of VISA, Cuscal also acts as the link between VISA and Cuscal's shareholders/customers in respect of product and policy development.

16. Of Cuscal's 119 members, 75 members are VICUs and collectively they own approximately 94.5% of the ordinary shares in Cuscal. The remaining 44 members, who did not issue VISA cards, own the remaining ordinary shares.

17. Cuscal has approximately 149.5 million ordinary shares on issue as at 30 June 2008 and these are the only equity interests (within the meaning of Division 974 of the ITAA 1997) on issue.

18. All of Cuscal's shareholders are Australian residents and, except for one, are credit unions. The largest shareholding that a single entity has in Cuscal is 15.18%, and this ownership stake is subject to the voting limitation of 15% as generally applies to ADIs regulated by APRA.

Proceeds from VISA restructure

19. Since late 2007, VISA has been restructuring itself from a member-owned organisation into a US corporation in preparation for public listing. In consequence of this restructure Cuscal was allocated a number of Class C shares in the newly-formed VISA Inc in consequence of its principal membership with VISA. Cuscal's entitlement to shares was based on the revenue and transaction volumes generated by the VICUs and Cuscal over the period from 1 October 2001 to 31 December 2007. The VICUs, as associate members of VISA, were not entitled to any VISA shares.

20. A portion of Cuscal's VISA shares were sold into the initial public offering (IPO) of VISA Inc on 19 March 2008 and Cuscal received \$A37.3 million in cash proceeds. This sale was compulsory and the portion of shares sold was determined by VISA.

21. Cuscal continues to hold 621,704 of the Class C shares in VISA. These shares become convertible, on a one-for-one basis, to listed VISA shares three years after the IPO (that is, in March 2011) and are in escrow until the expiration of this three year period.

22. Cuscal will pay tax (at the normal corporate rate) in its assessment for the year ended 30 June 2008 as a consequence of the VISA restructure.

Rationale for the transaction

23. Cuscal has no obligation to pay any amount of the proceeds from the VISA IPO to the VICUs or any other party, and intends to retain an amount that recognises its role in the processing of VISA transactions and member coordination of the VICUs.

24. However, Cuscal recognises that the profit that has arisen from the VISA restructure and IPO is partially due to the revenue and transactions generated from VISA cards issued by the VICUs to their customers. The relative contribution of the VICUs to the gain is not the same as their level of ordinary shareholding in Cuscal.

Mechanics of the transaction

25. Cuscal proposes to issue 10,000 Class B shares to the VICUs based on the revenues generated to Cuscal by each VICU in respect of VISA products during the period from 1 July 2004 to 31 December 2007. This allocation formula broadly reflects the formula under which Cuscal became entitled to its VISA shares.

26. The shares will be issued to each VICU for nominal consideration of \$0.60 each, and are equity interests in accordance with Division 974 of the ITAA 1997.

27. Dividends on the Class B shares will not exceed the after-tax proceeds Cuscal receives from the disposal of the shares acquired through the VISA IPO. These dividends will be fully franked.

28. The Class B shares will have restricted rights and limitations:

- they will have a right to dividends, but only to the extent (if any) that dividends are declared by Cuscal from time to time;
- they will have only limited voting rights (on matters that affect them as a class) and no rights to participate in any capital distribution (subject to Corporations Act requirements);
- they will only be transferable by the holder to its direct successor organisation as the result of a merger, demutualisation, takeover, amalgamation or other corporate restructure approved by APRA, and such transfer will also be subject to the approval of the Cuscal Board;
- they will not be disposed under any other circumstances;
- should a Class B shareholder enter into any arrangement which does not result in the existence of a direct successor, including receivership, administration or liquidation and subject to any laws applicable to insolvency, the holder's Class B shares will be cancelled and the application monies received will be returned;
- the term will be no later than 30 June 2012; and
- they will be cancelled after all the remaining VISA shares have been sold and all relevant dividends have been paid.

29. Cuscal's ordinary shares will continue to exist, and the VICUs will continue to hold their ordinary shares in Cuscal in addition to their new Class B shares.

30. Cuscal will continue its policy of fully franking regular bi-annual dividend payments on ordinary shares.

Ruling

31. The Commissioner will not make a determination under subsection 45A(2) or subsection 45B(3) of the ITAA 1936 that section 45C of the ITAA 1936 applies in relation to the scheme.

32. The Commissioner will not make a determination pursuant to subsection 204-30(3) of the ITAA 1997 to deny the imputation benefits received by shareholders in relation to the scheme.

33. The direct value shifting provisions in Division 725 of the ITAA 1997 do not apply to the scheme.

34. The Commissioner will not make a determination under paragraph 177EA(5)(b) of the ITAA 1936 to deny the whole, or any part, of the imputation benefits received by the shareholders under the scheme.

35. Having regard to the scheme as described, Part IVA of the ITAA 1936 does not apply.

Commissioner of Taxation

23 July 2008

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.*

Section 45A

36. Section 45A of the ITAA 1936 is an anti-avoidance provision which applies to capital streaming arrangements in which capital benefits are provided to some shareholders, and, generally, less than fully franked dividends are provided to other shareholders. Where it applies, the capital benefits provided are treated as unfranked dividends paid from the profits of the company pursuant to section 45C of the ITAA 1936.

37. Subsection 45A(1) of the ITAA 1936 provides that section 45A of the ITAA 1936 applies where a company streams the provision of capital benefits and the payment of dividends to its shareholders in such a way that:

- the shareholders that receive the capital benefits are those that would derive a greater benefit from the capital benefits than the other shareholders (paragraph 45A(1)(a) of the ITAA 1936); and
- it is reasonable to assume that the other shareholders (the disadvantaged shareholders) have received, or will receive, dividends (paragraph 45A(1)(b) of the ITAA 1936).

38. Although a 'capital benefit' (as defined in paragraph 45A(3)(a) of the ITAA 1936) is provided to Class B shareholders under Cuscal's scheme, there is no provision of dividends to disadvantaged shareholders (as required under paragraph 45A(1)(b) of the ITAA 1936), other than those paid to all ordinary shareholders via Cuscal's regular bi-annual fully franked dividends. Accordingly, section 45A of the ITAA 1936 has no application to the Cuscal scheme.

Section 45B

39. Section 45B of the ITAA 1936 is an anti-avoidance provision which functions to ensure that certain payments that are paid in substitution for dividends are treated as dividends for tax purposes. Following the requirements of subsection 45B(2) of the ITAA 1936, section 45B 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, 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, 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) of the ITAA 1936).

Scheme

40. 'Scheme' is not defined in relation to section 45B of the ITAA 1936. However, the issue of Class B shares followed by the distribution of a significant portion of the realised VISA proceeds will constitute a 'scheme' for the purposes of section 45B.

Capital benefit

41. Following paragraph 45B(5)(a) of the ITAA 1936, providing a capital benefit includes the provision of ownership interests in a company. As such, the issue of the Class B shares will constitute the provision of a capital benefit.

Tax benefit

42. The shareholder 'obtains a tax benefit', as defined in subsection 45B(9) of the ITAA 1936, where the amount of tax payable or any other amount payable under the ITAA 1936 or the ITAA 1997 by the shareholder 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 a dividend.

43. Here, no tax benefit arises as:

- the issue of the Class B shares will be for nominal consideration. This means that the Class B shareholders will have a nominal cost base in the shares, and as such no capital loss should arise to the VICUs when the Class B shares are eventually redeemed;

- the advantage provided by the receipt of the capital benefit (the Class B shares) could be seen to be the future right to the fully franked dividends payable on the Class B shares. However, this would not be a 'tax benefit' for the purposes of subsection 45B(9) of the ITAA 1936 as the amount of tax payable by the shareholders here would be exactly the same as if the payment had been a dividend; and
- tax payable by the Class B shareholders on dividends attached to Class B shares will be exactly the same as tax payable on dividends attached to ordinary shares in Cuscal.

44. As such, no 'tax benefit' arises here for the purposes of paragraph 45B(2)(b) of the ITAA 1936 and accordingly section 45B of the ITAA 1936 does not apply.

Streaming distributions – application of Subdivision 204-D

45. Subdivision 204-D of the ITAA 1997 relates to the Commissioner's power to make a determination in circumstances where distributions with attached imputation benefits are streamed to members of a corporate tax entity. An 'imputation benefit' is defined in subsection 204-30(6) of the ITAA 1997 to include a franking credit arising in the franking account of the respective member as a result of the distribution.

46. Streaming is not defined for the purposes of Subdivision 204-D of the ITAA 1997, however it is understood to refer to a company selectively directing the flow of franked distributions to those members who can most benefit from the imputation credits: refer to paragraph 3.28 of the Explanatory Memorandum to the New Business Tax System (Imputation) Bill 2002. A frankable distribution is a necessary prerequisite for the operation of section 204-30 of the ITAA 1997.

47. Section 204-30 of the ITAA 1997 applies in respect of a company which streams distributions and the giving of other benefits in such a way that some shareholders receive imputation benefits (the favoured members), and other shareholders receive lesser or no imputation benefits (the disadvantaged members) regardless of whether or not they receive other benefits.

48. If section 204-30 of the ITAA 1997 is found to have application the Commissioner may make a determination under subsection 204-30(3) of the ITAA 1997 that, among other things, no imputation benefit is to arise in respect of the distributions made to those favoured members.

49. For section 204-30 of the ITAA 1997 to apply there must be a streaming of imputation benefits to advantaged members who derive a greater benefit from the franking credits received than disadvantaged members. The words 'derives a greater benefit from franking credits' are defined in subsection 204-30(8) of the ITAA 1997 by reference to the ability of members to fully utilise the franking credits received.

50. The dividends to be paid by Cuscal on the Class B shares will be fully franked, and Cuscal also intends that the dividends paid on its ordinary shares to all shareholders will continue to be fully franked. As such, there is no evidence that the requisite element of streaming exists in relation to the franked distributions to be paid by Cuscal on its Class B shares.

51. Accordingly, based on the information provided, the Commissioner will not make a determination applying Subdivision 204-D of the ITAA 1997 to the scheme.

Value shifting – application of Division 725

52. Division 725 of the ITAA 1997 may apply where there is a direct value shift under a scheme involving equity or loan interests in an entity (the target entity). For Division 725 to have any possible consequences, paragraph 725-50(b) of the ITAA 1997 requires that a 'controlling entity test' be satisfied.

53. The 'controlling entity test' is satisfied if an entity controls (for value shifting purposes) the target entity at some time during the 'scheme period' starting when the scheme involving equity or loan interests is entered into and ending when that scheme has been carried out: section 725-55 of the ITAA 1997.

54. Subdivision 727-E of the ITAA 1997 sets out the circumstances in which an entity will be regarded as controlling an entity for value shifting purposes. Section 727-355 of the ITAA 1997 contains the relevant tests for whether an entity controls a company. On the basis of the information provided regarding the share capital structure of Cuscal, including the fact that the largest shareholding a single entity has in Cuscal is 15.18%, and that none of the 75 shareholders in Cuscal are 'associates' as defined in subsection 318(2) of the ITAA 1936, there is no entity that would control (for value shifting purposes) Cuscal at any time during the scheme period. Accordingly, there are no direct value shifting consequences in respect of the scheme.

Section 177EA

55. Section 177EA of the ITAA 1936 is a general anti-avoidance provision that applies to a wide range of schemes to obtain a tax advantage in relation to imputation benefits. In essence, it applies to schemes for the disposition of shares or an interest in shares, where a franked distribution is paid or payable in respect of the shares or an interest in shares. This would include the issue of a new class of share upon which franked distributions are paid.

56. Specifically, subsection 177EA(3) of the ITAA 1936 provides that section 177EA of the ITAA 1936 applies if the following conditions are satisfied:

- (a) there is a scheme for a disposition of membership interests, or an interest in membership interests, in a corporate tax entity; and
- (b) either:
 - (i) a frankable distribution has been paid, or is payable or expected to be payable, to a person in respect of the membership interests; or
 - (ii) a frankable distribution has flowed indirectly, or flows indirectly or is expected to flow indirectly, to a person in respect of the interest in membership interests, as the case may be; and
- (c) the distribution was, or is expected to be, a franked distribution or a distribution franked with an exempting credit; and
- (d) except for this section, the person (the relevant taxpayer) would receive, or could reasonably be expected to receive, imputation benefits as a result of the distribution; and
- (e) 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 the relevant taxpayer to obtain an imputation benefit.

57. It is considered that the conditions in paragraphs 177EA(3)(a) to (d) of the ITAA 1936 are satisfied because:

- (a) paragraph 177EA(14)(a) provides that a scheme for disposition of membership interests includes the issuing of membership interests. As Cuscal's issue of Class B shares will be regarded as membership interests for tax purposes the scheme involves a disposition of membership interests in a corporate tax entity;
- (b) the distributions are expected to be frankable distributions;
- (c) the distributions are expected to be franked; and
- (d) it is reasonable to expect that an imputation benefit will be received by the Class B shareholders as a result of the distributions made.

58. Accordingly, the issue is whether having regard to the relevant circumstances of the scheme, it would be concluded that on the part of Cuscal, its shareholders or any other relevant party, there is a purpose more than merely an incidental purpose of enabling the relevant taxpayer to obtain an imputation benefit under the scheme. Under this arrangement the relevant taxpayers are the Class B shareholders.

59. In arriving at a conclusion the Commissioner must have regard to the relevant circumstances of the scheme which include, but are not limited to, the circumstances set out in subsection 177EA(17) of the ITAA 1936. The relevant circumstances listed there encompass a range of circumstances which taken, individually or collectively, could indicate the requisite purpose. Due to the diverse nature of these circumstances, some may not be present at any one time in any one scheme.

60. Based on the information provided, and having regard to the assumptions and qualifications set out in this Ruling and the relevant circumstances of the scheme, it would not be reasonable to conclude that in entering into the scheme, Cuscal, its shareholders or any other relevant party demonstrate the objective purpose of securing imputation benefits for the Class B shareholders. To the extent that any imputation benefits are secured, those benefits are considered to be incidental to the more significant objective purposes of sharing the gains from the VISA restructure amongst those ordinary shareholders that were responsible for generating it, in proportion to those efforts.

61. Accordingly, the Commissioner will not make a determination under paragraph 177EA(5)(b) of the ITAA 1936 to deny imputation benefits to the Class B shareholders.

Part IVA (not including section 177EA)

62. For the general provisions of Part IVA of the ITAA 1936 to apply, there must be a 'scheme', a tax benefit and a sole or dominant purpose of entering into the scheme to obtain a tax benefit. The issuing of the Class B shares and subsequent payment of franked dividends will constitute a scheme.

63. Based on the information provided, and having regard to the qualifications set out in this Ruling and the matters set out in section 177D of the ITAA 1936, it would not be reasonable to conclude that in entering into or carrying out the scheme, Cuscal, its shareholders or any other relevant party demonstrate a dominant purpose of securing a tax benefit for the Class B shareholders.

64. Furthermore, based on the information provided, and having regard to the qualifications set out in this Ruling, it would not be reasonable to conclude that the scheme is a dividend stripping scheme or a scheme having substantially that effect within the meaning of section 177E of the ITAA 1936.

65. Accordingly, the Commissioner will not make a determination to apply Part IVA of the ITAA 1936 to the scheme.

Appendix 2 – Detailed contents list

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

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References

Previous draft:

Not previously issued as a draft

Subject references:

- anti avoidance measures
- capital benefit
- direct value shifts
- dividend streaming arrangements
- franking credits

Legislative references:

- ITAA 1936
- ITAA 1936 45A
- ITAA 1936 45A(1)
- ITAA 1936 45A(1)(a)
- ITAA 1936 45A(1)(b)
- ITAA 1936 45A(2)
- ITAA 1936 45A(3)(a)
- 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(5)(a)
- ITAA 1936 45B(9)
- ITAA 1936 45C
- ITAA 1936 177D
- ITAA 1936 177E
- ITAA 1936 177EA

- ITAA 1936 177EA(3)
- ITAA 1936 177EA(3)(a)
- ITAA 1936 177EA(3)(b)
- ITAA 1936 177EA(3)(c)
- ITAA 1936 177EA(3)(d)
- ITAA 1936 177EA(5)(b)
- ITAA 1936 177EA(14)(a)
- ITAA 1936 177EA(17)
- ITAA 1936 Pt IVA
- ITAA 1936 318(2)
- ITAA 1997
- ITAA 1997 Subdiv 204-D
- ITAA 1997 204-30
- ITAA 1997 204-30(3)
- ITAA 1997 204-30(6)
- ITAA 1997 204-30(8)
- ITAA 1997 Div 725
- ITAA 1997 725-50(b)
- ITAA 1997 725-55
- ITAA 1997 Subdiv 727-E
- ITAA 1997 727-355
- ITAA 1997 Div 974
- TAA 1953
- TAA 1953 Sch 1 357-75(1)
- Copyright Act 1968

Other references:

- Explanatory Memorandum to the New Business Tax System (Imputation) Bill 2002

ATO references

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ATOlaw topic: Income Tax ~~ Return of capital
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