


CR 2009/56 - Income tax: partial repayment of principal of Debenture Stock: Hastings Capital Limited (Receivers and Managers appointed) (in liquidation)

 This cover sheet is provided for information only. It does not form part of *CR 2009/56 - Income tax: partial repayment of principal of Debenture Stock: Hastings Capital Limited (Receivers and Managers appointed) (in liquidation)*



Class Ruling

Income tax: partial repayment of principal of Debenture Stock: Hastings Capital Limited (Receivers and Managers appointed) (in liquidation)

Contents	Para
LEGALLY BINDING SECTION:	
What this Ruling is about	1
Date of effect	8
Scheme	9
Ruling	23
NOT LEGALLY BINDING SECTION:	
Appendix 1:	
Explanation	27
Appendix 2:	
Detailed contents list	50

❶ 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, the Commissioner must apply the law to you in the way set out in the ruling (unless the Commissioner is satisfied that the ruling is incorrect and disadvantages you, in which case the law may be applied to you in a way that is more favourable for you – provided the Commissioner is 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:

- section 26BB of the *Income Tax Assessment Act 1936* (ITAA 1936);
- section 6-5 of the *Income Tax Assessment Act 1997* (ITAA 1997);
- Division 104 of the ITAA 1997; and
- Division 110 of the ITAA 1997.

All legislative references in this Ruling are to the ITAA 1997 unless otherwise stated.

Class of entities

3. The class of entities to which this Ruling applies consists of:
- (a) the holders of Debenture Stock issued by Hastings Capital Limited (Receivers and Managers appointed) (in liquidation) (HCL); and
 - (b) who hold their HCL Debenture Stock on capital account.

In this Ruling, a person belonging to this class of entities is referred to as a 'Debenture holder'.

Qualifications

4. The Commissioner makes this Ruling based on the precise scheme 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 9 to 22 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
Copyright Law Branch
Attorney-General's Department
National Circuit
Barton ACT 2600

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

Date of effect

8. This Ruling applies from 17 December 2008 to 30 June 2012. 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. However, this Ruling will not apply to taxpayers to the extent that it conflicts with the terms of a settlement of a dispute agreed to before the date of issue of this Ruling (see paragraphs 75 and 76 of Taxation Ruling TR 2006/10).

Scheme

9. The following description of the scheme is based on information provided by the applicant. The following documents, or relevant parts of them, form part of and are to be read with the description:

- Class Ruling application including attachments;
- Correspondence from the applicant dated 17 July 2009; and
- McGrathNicol, Update to Debenture Holders, 22 June 2009.

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

10. HCL is an Australian resident company limited by shares. Its business consists of raising funds and advancing those funds to third party borrowers for business and investment purposes (principally property development).

11. On 6 June 2002, HCL and Permanent Nominees (Australia) Limited (the Trustee) entered into a trust deed (the Trust Deed). The Trust Deed sets out the terms and conditions upon which HCL may issue Debenture Stock and the powers, rights and responsibilities of the Trustee.

12. HCL issued various tranches of Debenture Stock that were governed by the Trust Deed and charges granted in favour of the Trustee. Following a default by HCL under the terms of the Trust Deed, Joseph Hayes and Tony McGrath of McGrathNicol were appointed by the Trustee as Receivers and Managers (the Receivers) of HCL on 20 August 2008.

13. The time during which the Receivers are in office, in relation to the default that led to the appointment on 20 August 2008, is referred to in this Ruling as 'the period of Receivership'.

14. At the date of appointment of the Receivers, all interest payments and redemptions relating to the Debenture Stock were frozen so that the assets of HCL could be realised and the proceeds distributed rateably to the holders of HCL Debenture Stock.

15. On 24 October 2008, the Receivers estimated that, having regard to the financial position of HCL, the holders of HCL Debenture Stock would not receive repayment of their principal in full. As at 17 July 2009, the Receivers have not had cause to revise this estimate and consider it very unlikely that they will do so. This Ruling is prepared on the basis that the total amount a Debenture holder will receive will not exceed the principal they subscribed for their Debenture Stock.

16. On 17 December 2008, a repayment of 10 cents for each dollar outstanding on the Debenture Stock was made to each holder of HCL Debenture Stock out of the assets of HCL. The repayment was made by HCL under the control of the Receivers. The Trustee authorised the Receivers to make the payment, as allowed for in the Trust Deed, rather than pay the money to the Trustee for distribution.

17. On 3 April 2009, HCL was placed into liquidation. The Receivers continue to retain control of HCL's affairs on behalf of the holders of HCL Debenture Stock.

18. On 22 June 2009, a further repayment of 4 cents for each dollar outstanding on the Debenture Stock was made to each holder of HCL Debenture Stock. This repayment was also made by HCL under the control of the Receivers. The Receivers also obtained authorisation from the Trustee for this repayment.

19. The amount of each repayment, 10 cents and 4 cents in the dollar, is a proportion of the total debts owing to the holders of HCL Debenture Stock on the date of the Receivers' appointment, that is, the sum of principal and accrued interest owing under the Debenture Stock on 20 August 2008. However, the Receivers have determined that each repayment was a repayment of principal only.

20. The principal owing to each holder of HCL Debenture Stock was reduced by the amount of each repayment. No Debenture Stock was cancelled or redeemed as a result of the repayments.

21. HCL will not redeem, cancel or otherwise extinguish the Debenture Stock during the period of Receivership. The Receivers will not repay the face value of any Debenture Stock on the maturity dates specified in the debenture certificates.

22. Where future repayments of principal are made, they will be made on the same basis as the two repayments described in paragraphs 10 to 21 of this Ruling.

Ruling

Ordinary income

23. To the extent that the sum of all repayments does not exceed the face value of the Debenture Stock, no part of the repayments will be assessable as ordinary income of the Debenture holders under section 6-5.

Traditional security

24. Section 26BB of the ITAA 1936 will not apply to include any part of the repayments in the assessable income of the Debenture holders.

Capital gains tax

25. A CGT event under Division 104 will not happen as a result of the repayments. Therefore, the Debenture holders will not make a capital gain or capital loss as a result of the repayments.

26. However, the cost base and reduced cost base of each Debenture holder's Debenture Stock will be reduced by the amount of each repayment (subsections 110-45(3) and 110-55(6)).

Commissioner of Taxation

30 September 2009

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.*

Ordinary income

27. Under subsection 6-5(1), the assessable income of a taxpayer includes income according to ordinary concepts (ordinary income). Interest received is an example of ordinary income. On the other hand, a repayment of the principal of a debt is generally a capital receipt and is not assessable as ordinary income.

28. HCL, under the control of the Receivers, made two repayments to the Debenture holders for the amount outstanding on the Debenture Stock. The amount of each repayment, 10 cents and 4 cents in the dollar, is a repayment of principal only.

29. Therefore, the two repayments of 10 cents and 4 cents in the dollar will not be assessable as ordinary income of the Debenture holders under section 6-5.

30. To the extent that the sum of all repayments made does not exceed the face value of the Debenture Stock, no part of the repayments will be included in the assessable income of the Debenture holders under section 6-5.

Traditional security

31. Subsection 26BB(1) of the ITAA 1936 defines a 'traditional security' as a security held by the taxpayer that:

- (a) was acquired by the taxpayer after 10 May 1989;
- (b) does not have an eligible return or has an eligible return that meets certain conditions;
- (c) is not a prescribed security within the meaning of section 26C of the ITAA 1936; and
- (d) is not trading stock of the taxpayer.

32. The term 'security' is defined by reference to subsection 159GP(1) of the ITAA 1936. The Debenture Stock held by a Debenture holder satisfies the definition of a 'security' within that subsection. All of the Debenture Stock was acquired by the Debenture holders after 10 May 1989. The Debenture Stock, being issued by HCL and not the Commonwealth, is not a prescribed security within the meaning of section 26C of the ITAA 1936.

33. A security will have an eligible return where, at the time of issue of the security, it is reasonably likely that the sum of all payments under the security, other than periodic interest, will exceed the issue price of the security (subsection 159GP(3) of the ITAA 1936). As no payments are liable to be made on the Debenture Stock other than principal repayments equal to its issue price and periodic interest, the Debenture Stock does not have an eligible return.

34. Therefore, the Debenture Stock is a traditional security for those holders of HCL Debenture Stock who do not hold the Debenture Stock as trading stock.

35. Under subsection 26BB(2) of the ITAA 1936, where a taxpayer disposes of a traditional security or a traditional security of a taxpayer is redeemed, the amount of any gain on the disposal or redemption shall be included in the assessable income of the taxpayer of the year of income in which the disposal or redemption takes place.

36. The repayments that are the subject of this Ruling do not constitute a disposal or redemption of the Debenture Stock. No Debenture Stock was cancelled or redeemed as a result of the repayments. Furthermore, HCL will not redeem, cancel or otherwise extinguish the Debenture Stock during the period of Receivership.

37. Accordingly, section 26BB of the ITAA 1936 will not apply to include any part of the repayments in the assessable income of the Debenture holders.

Capital gains tax

38. The Debenture Stock that is owned by Debenture holders is a CGT asset (section 108-5). A taxpayer can make a capital gain or capital loss only if a CGT event happens (section 102-20). The CGT events that may happen to a Debenture holder are discussed in paragraphs 39 to 43.

39. CGT event A1 happens if you dispose of a CGT asset (section 104-10). You dispose of a CGT asset if a change of ownership occurs from you to another entity, whether because of some act or event or by operation of law. The repayments that are the subject of this Ruling do not constitute, involve or require a disposal of any Debenture Stock by any of the Debenture holders.

40. CGT event C2 happens, insofar as it is relevant to the Debenture Stock, if your ownership of an intangible CGT asset ends by the asset:

- (a) being redeemed or cancelled;
- (b) being released, discharged or satisfied;
- (c) expiring; or
- (d) being abandoned, surrendered or forfeited.

(section 104-25)

No Debenture Stock was cancelled or redeemed as a result of the repayments. HCL will not redeem, cancel or otherwise extinguish the Debenture Stock during the period of Receivership.

41. CGT event G3 happens if:

- you own, amongst other things, financial instruments (including the Debenture Stock) issued by a company; and
- a liquidator or administrator of the company declares in writing that they have reasonable grounds to believe (as at the time of the declaration) that, for financial instruments, the instruments have no value or have only negligible value (section 104-145).

A liquidator or administrator of HCL has not made such a written declaration.

42. CGT event H2 happens if an act, transaction or event occurs in relation to a CGT asset that you own, and it does not result in an adjustment being made to the asset's cost base or reduced cost base (section 104-155). Each repayment is an act, transaction or event that occurs in relation to the Debenture Stock, but it will result in an adjustment being made to the asset's cost base or reduced cost base under subsections 110-45(3) and 110-55(6), respectively (see paragraphs 44 to 49 of this Ruling).

43. Therefore, no CGT event under Division 104 will happen as a result of the repayments that are the subject of this Ruling. Accordingly, the Debenture holders will not make a capital gain or capital loss as a result of the repayments.

44. Subsection 110-45(3) provides that expenditure does not form part of any element of the cost base of a CGT asset to the extent of any amount you have received as 'recoupment' of it, except so far as the amount is included in your assessable income.

Subsection 110-55(6) similarly provides that expenditure does not form part of the reduced cost base of a CGT asset to the extent of any amounts you have received as 'recoupment' of it, except to the extent that the amounts are included in your assessable income.

45. Under subsection 995-1(1), 'recoupment' has the meaning given by section 20-25. Under subsection 20-25(1), recoupment of an outgoing (such as expenditure) includes any kind of recoupment, reimbursement, refund, insurance, indemnity or recovery, however described.

46. Each repayment of the principal owing to Debenture holders under the Debenture Stock is a recoupment, refund or recovery of the expenditure previously incurred to acquire the Debenture Stock. Therefore, it is a 'recoupment' within the meaning of section 20-25.

47. No part of a repayment of the principal is included in the assessable income of a Debenture holder.

48. Therefore, the amount of each repayment is a recoupment of expenditure in relation to the Debenture Stock for the purposes of subsections 110-45(3) and 110-55(6).

49. Accordingly, the cost base and the reduced cost base of the Debenture Stock held by each Debenture holder must be reduced by the amount of each repayment that is the subject of this Ruling.

Appendix 2 – Detailed contents list

50. 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
Scheme	9
Ruling	23
Ordinary income	23
Traditional security	24
Capital gains tax	25
Appendix 1 – Explanation	27
Ordinary income	27
Traditional security	31
Capital gains tax	38
Appendix 2 – Detailed contents list	50

References

Previous draft:

Not previously issued as a draft

Related Rulings/Determinations:

TR 2006/10

Subject references:

- capital gains
- CGT cost base
- CGT reduced cost base
- traditional securities

Legislative references:

- ITAA 1936 26BB
- ITAA 1936 26BB(1)
- ITAA 1936 26BB(2)
- ITAA 1936 26C
- ITAA 1936 159GP(1)
- ITAA 1936 159GP(3)

- ITAA 1997
 - ITAA 1997 6-5
 - ITAA 1997 6-5(1)
 - ITAA 1997 20-25
 - ITAA 1997 20-25(1)
 - ITAA 1997 102-20
 - ITAA 1997 Div 104
 - ITAA 1997 104-10
 - ITAA 1997 104-25
 - ITAA 1997 104-145
 - ITAA 1997 104-155
 - ITAA 1997 108-5
 - ITAA 1997 Div 110
 - ITAA 1997 110-45(3)
 - ITAA 1997 110-55(6)
 - ITAA 1997 995-1(1)
 - TAA 1953
 - Copyright Act 1968
-

ATO references

NO: 2009/9766

ISSN: 1445-2014

ATOlaw topic: Income Tax ~~ Capital Gains Tax ~~ cost base and reduced cost base