


CR 2011/60 - Income tax: return of capital - Australian Pipeline Trust

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Class Ruling

Income tax: return of capital – Australian Pipeline Trust

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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, 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 provisions identified below apply to the defined class of entities, who take part in the scheme to which this Ruling relates.

Relevant provisions

2. The relevant provisions dealt with in this Ruling are:

- subsection 6(1) of the *Income Tax Assessment Act 1936* (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);
- section 104-135 of the ITAA 1997; and
- section 855-10 of the ITAA 1997.

All subsequent legislative references in this Ruling are to the ITAA 1936 unless otherwise indicated.

Class of entities

3. The class of entities to which this Ruling applies is the owners of units in Australian Pipeline Trust (APT) who:

- are unitholders who participate in the scheme that is the subject of this Ruling (APT unitholders);
- hold their units on capital account; and
- are not subject to the taxation of financial arrangements rules in Division 230 of the ITAA 1997 in relation to gains and losses on their APT units.

(Note – Division 230 will generally not apply to individuals, unless they have made an election for it to apply to them.)

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 10 to 20 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 2010 to 30 June 2011. The Ruling continues to apply after 30 June 2011 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).

Previous Rulings

9. Class Ruling CR 2007/60 Income tax: stapling of units in Australian Pipeline Trust with the units in Australian Pipeline Trust Investment Trust.

Scheme

10. The following description of the Scheme is based on information provided to the Commissioner. The following documents or relevant parts of them, as the case may be, form part of and are to be read with this description. The documents include:

- application for Class Ruling (including Appendices), dated 25 February 2011;
- Australian Pipeline Trust Interim Financial Report for the Half Year ended 31 December 2010;
- correspondence from the applicant dated 24 March 2011, 28 March 2011 and 29 April 2011.

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

Background

11. APA Group (APA), comprising APT and the APT Investment Trust (APTIT), owns Australia's largest gas distribution and storage infrastructure network.

12. APT is a unit trust. Each APT unit is stapled to a unit of the APT Investment Trust (APTIT) and traded on the Australian Securities Exchange (ASX). The two units are collectively referred to as the APA Group stapled security.

13. APT was listed on the ASX in 2000 and is an Australian resident public trading trust.

14. APT is the head entity of a tax consolidated group and is treated as a company for income tax purposes. APT holds either directly or through interposed companies a number of corporate subsidiaries that are subject to the *Corporations Act 2001*.

15. On 17 December 2010, APT announced its intention to increase distributions in the 2011 financial year by at least 5%, with distributions fully covered by operating cash flow.

Interim distribution

16. In December 2010, APT declared an interim distribution (being 12.0128 cents per unit) with a Record Date of 31 December 2010 and a Payment Date of 17 March 2011. This formed part of the APA Group's interim distribution of 16.5 cents per APA Group stapled security.

17. APT's interim distribution had two components:

- an amount (being 9.5490 cents per unit) paid out of accounting profits and treated as a dividend for income tax purposes; and
- an amount (being 2.4638 cents per unit) paid in excess of available accounting profits and treated as a return of capital.

Other matters

18. APT's Trust Deed authorises the trustee to distribute income or capital pro-rata to unitholders.

19. APT's accounting share capital in its subsidiaries is share capital within the meaning of the ITAA 1936 and is not tainted within the meaning of Division 197 of the ITAA 1997.

20. This Ruling only deals with the income tax treatment of the part of APT's interim distribution, which was paid by APT on 17 March 2011, that comprised the return of capital (being 2.4638 cents per unit).

Ruling

Distribution is not a dividend

21. The payment of the return of capital to APT unitholders was not a dividend, as defined in subsection 6(1).

The application of sections 45B and 45C

22. The Commissioner will not make a determination under section 45B that section 45C applies to the whole, or any part, of the payment of the return of capital.

Capital gains tax

23. CGT event G1, in section 104-135 of the ITAA 1997, happened when APT paid the return of capital in respect of a unit that a unitholder owned at the Record Date and continued to own at the time of the payment.

24. CGT event C2, in section 104-25 of the ITAA 1997, happened when APT paid the return of capital to an APT unitholder in respect of an APT unit that they owned at the Record Date but ceased to own before the time of the payment.

Foreign resident shareholders

25. A foreign resident APT unitholder who was paid the return of capital disregards any capital gain made when CGT event G1 happened if their APT unit was not 'taxable Australian property' (section 855-10 of the ITAA 1997).

26. A foreign resident APT unitholder who was paid the return of capital disregards any capital gain or capital loss made when CGT event C2 happened if their right to receive the return of capital was not 'taxable Australian property' (section 855-10 of the ITAA 1997).

Commissioner of Taxation22 June 2011

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.*

Unit trust considerations

27. As a consequence of the consolidation rules in Division 713 of the ITAA 1997, section 45B of the ITAA 1936 can apply to particular types of trusts. This is due to the fact that as per subdivision 713-C of the ITAA 1997, certain corporate unit trusts and public trading trusts are treated like a company for tax purposes when they elect to become the head company of a consolidated group. For these trusts, the modifications to the applied law pursuant to section 713-140 of the ITAA 1997 provide that a reference to a dividend in both the ITAA 1936 and ITAA 1997 includes a reference to a distribution from the trust out of profits and a reference to a share capital account includes a reference to the amount of the trust estate that is not attributable to profits.

28. In the present circumstances, these modifications will result in the distribution from the trust out of profits being treated as a dividend as defined in the ITAA 1936 and ITAA 1997. Further, it will result in an amount of the trust estate that is not attributable to profits being treated in the same way as a share capital account.

29. Sections 713-130, 713-135 and 713-140 of the ITAA 1997 provide that the applied law involves corresponding treatment of analogous characteristics, things and persons relating to a trust to those of a company. For the purposes of simplicity, this Ruling will use the terminology that applies to companies where the trust has engaged in an equivalent transaction but will retain the distinction that unit holders, rather than shareholders, will receive the payment.

Distribution is not a dividend

30. 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 the shareholder is a resident of Australia).

31. 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 tax purposes.

32. Paragraph (d) of subsection 6(1) specifically excludes from the definition of 'dividend' an amount of the distribution debited against an amount standing to the credit of a company's share capital account.

33. The term 'share capital account' is defined in section 975-300 of the ITAA 1997 as an account that a company keeps of its share capital, or any other account created on or after 1 July 1998 where the first amount credited to the account was an amount of share capital.

34. Subsection 975-300(3) of the ITAA 1997 states that an account is not a share capital account, except for certain purposes, if it is tainted. Section 197-50 of the ITAA 1997 states that a share capital account is tainted if an amount to which Division 197 of the ITAA 1997 applies is transferred to the account and the account is not already tainted.

35. As the return of capital will be wholly debited against an amount standing to the credit of APT's share capital account, paragraph (d) of the definition of 'dividend' in subsection 6(1) will apply and the return of capital will not constitute a dividend.

Anti-avoidance provision

Section 45B – Scheme to provide capital benefits

36. Section 45B is an anti-avoidance provision which if it applies, will allow the Commissioner to make a determination that section 45C applies to treat all or part of the return of capital amount received by the unitholders as an unfranked dividend.

37. Section 45B applies where certain capital payments are made to shareholders in substitution for dividends. Specifically, the provision will apply where:

- there is a scheme under which a person is 'provided with a capital benefit' by a company (paragraph 45B(2)(a));
- under the scheme a taxpayer (the 'relevant taxpayer'), who may or may not be the person provided with the capital benefit obtains a tax benefit (paragraph 45B(2)(b)); 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 the scheme or carried out the scheme or any part of the scheme did so for a purpose, other than the incidental purpose of enabling the relevant taxpayer to obtain a tax benefit (paragraph 45B(2)(c)).

38. The phrase 'provided with a capital benefit' is defined in subsection 45B(5) of the ITAA 1936 and includes a 'distribution to the person of share capital'. Under the present Scheme, APT will make a distribution of capital to all of its ordinary unitholders, which will constitute the provision of a capital benefit.

Tax benefit

39. A relevant taxpayer 'obtains a tax benefit' as defined in subsection 45B(9), if an amount of tax or other amount payable under the income tax laws is less than the amount that would have been payable or would be payable at a later time if the capital benefit had instead been an assessable dividend.

40. These conditions are satisfied in the present Scheme as the return of capital to ordinary unitholders will be assessed under the CGT provisions of the income tax law rather than being immediately assessed as a dividend.

Relevant circumstances

41. Paragraph 45B(2)(c) sets out an objective purpose test, having regard to 'the relevant circumstances of the scheme' as set out in subsection 45B(8). The test will be satisfied for any non-incidental purpose.

42. Subsection 45B(8) lists factors in paragraphs (a) through (k) that are relevant circumstances in determining whether a person entered into or carried out a scheme for a more than incidental purpose of enabling a taxpayer to obtain a tax benefit. The list of factors is not exclusive and not all factors listed will be relevant to every scheme.

43. In the present Scheme, the return of capital will be made to all ordinary unit holders. Therefore, the factors within paragraphs 45B(8)(c) to 45B(8)(f) do not incline for or against a conclusion as to purpose, rather, the relevant factors are those covered by the circumstances described in paragraphs 45B(8)(a), 45B(8)(b) and 45B(8)(k).

44. Paragraph 45B(8)(a) refers to the extent to which a capital benefit is attributable to realised and unrealised profits of the company and its associates (which includes APT's subsidiaries). As most of the profits of APT have been and are expected to be distributed to the ordinary unit holders as dividends, the return of capital is not attributable to the profits of APT.

45. Paragraph 45B(8)(b) refers to the pattern of distribution of dividends, bonus shares and returns of paid up capital of APT or its associates. APT has confirmed that it has regularly made distributions of trust income and intends to continue to do so. In these circumstances, the return of trust capital to the ordinary unitholders under this Scheme does not incline to the conclusion that it is being made in substitution for dividends.

46. Paragraph 45B(8)(k) refers to the matters in subparagraphs 177D(b)(i) to 177D(b)(viii) of the ITAA 1936. These are matters by reference to which a scheme is examined from a practical perspective to compare its tax and non tax objectives. These matters include, among other things, the form and substance of the scheme and its financial implications for the parties to it.

47. In considering the Scheme, the return of capital by APT to the ordinary unitholders is consistent with it being, in form and substance, a return of capital. The Scheme does not lead to the conclusion that the requisite purpose exists and that the Scheme was carried out for the purpose of enabling the relevant taxpayer to obtain a tax benefit.

48. It cannot be concluded that ATP or the ordinary unitholders entered into or carried out the Scheme for the purpose of enabling the unitholders to obtain a tax benefit. Accordingly, the Commissioner will not make a determination under subsection 45B(3) that section 45C will apply to the whole or any part of the return of capital.

Section 45C

49. As the Commissioner will not make a determination under subsection 45B(3) in relation to the capital benefit, section 45C will not deem the return of capital to be an unfranked dividend for the purposes of the ITAA 1936 or the ITAA 1997.

Capital gains tax

CGT event G1 – section 104-135

50. CGT event G1 happened when APT paid the return of capital to an APT unitholder in respect of a unit that they owned in APT at the Record Date and continued to own at the Payment Date (section 104-135(1) of the ITAA 1997).

51. An APT unitholder made a capital gain if the return of capital amount was more than the cost base of their APT unit. In which case the amount of the capital gain was equal to the excess (subsection 104-135(3) of the ITAA 1997).

52. If an APT unitholder made a capital gain, the cost base and reduced cost base of the APT unit is reduced to nil. It is not possible to make a capital loss when CGT event G1 happens (subsection 104-135(3) of the ITAA 1997).

53. If the return of capital was equal to or less than the cost base of the APT unit at the time of the payment, the cost base and reduced cost base of the APT unit is reduced (but not below nil) by that amount of the return of capital (subsection 104-135(4) of the ITAA 1997).

54. If the APT unit was acquired by the unitholder at least 12 months before the payment of the return of capital, a capital gain from CGT event G1 happening may qualify as a discount capital gain under subsection 115-25(1) of the ITAA 1997 (provided the other conditions in Division 115 of the ITAA 1997 are satisfied).

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

55. The right to receive the return of capital is one of the rights inherent in an APT unit at the Record Date. If, after the Record Date but before the Payment Date, an APT unitholder ceased to own an APT unit, the right to receive the return of capital in respect of that unit was retained by the unitholder and forms a CGT asset separate from the APT unit to which the right relates.

56. CGT event C2 happened when the return of capital was paid on the Payment Date. The right to receive the payment came to an end by the right being discharged or satisfied when the payment was made (section 104-25 of the ITAA 1997).

57. An APT unitholder made a capital gain if the capital proceeds from the ending of the right were more than its cost base. In which case the capital gain was equal to the amount of the excess. An APT unitholder made a capital loss if the capital proceeds from the ending of the right were less than its reduced cost base. In which case the capital loss was equal to the amount of the difference (subsection 104-25(3) of the ITAA 1997).

58. In working out the capital gain or capital loss made when CGT event C2 happened, the capital proceeds were the amount of the return of capital (subsection 116-20(1) of the ITAA 1997).

59. The cost base of an APT unitholder's right to receive the return of capital is worked out under Division 110 of the ITAA 1997 (modified by Division 112 of the ITAA 1997). The cost base of the right does not include the cost base or reduced cost base of the APT unit to which the right relates. The right to receive the return of capital should have a nil cost base.

60. As the right to receive the return of capital was inherent in the APT unit during the time it was owned, the right is considered to have been acquired at the time when the corresponding unit was acquired (section 109-5 of the ITAA 1997). Accordingly, if the APT unit was acquired at least 12 months before the return of capital, a capital gain made from the ending of the corresponding right will satisfy the requirements of section 115-25 of the ITAA 1997. Such a capital gain will be eligible to be treated as a discount capital gain under Division 115 of the ITAA 1997 provided the other conditions of that Division are satisfied.

Foreign resident shareholders

61. Under subsection 855-10(1) of the ITAA 1997, an entity disregards a capital gain or capital loss made from a CGT event if they are a foreign resident, or the trustee of a foreign trust for CGT purposes, just before the CGT event happens in relation to a CGT asset that is not 'taxable Australian property'.

62. Section 855-15 of the ITAA 1997 sets out when a CGT asset is 'taxable Australian property':

Item 1	taxable Australian real property;
Item 2	an indirect Australian real property interest not covered by item 5;
Item 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 item 1, 2, or 5;
Item 4	an option or right to acquire a CGT asset covered by item 1, 2 or 3; and
Item 5	a CGT asset that is covered by subsection 104-165(3) of the ITAA 1997 (choosing to disregard a gain or loss on ceasing to be an Australian resident).

63. Neither the APT unit nor the right to receive a return of capital payment was 'taxable Australian real property', as per section 855-20 of the ITAA 1997 or 'an indirect Australian real property interest' under section 855-25 of the ITAA 1997. However, a capital gain cannot be disregarded under subsection 855-10(1) of the ITAA 1997 if the APT unit or the right to payment:

- (a) had been used at any time by the foreign resident APT unitholders in carrying on a business through a permanent establishment in Australia (item 3 of the table in section 855-15) of the ITAA 1997; or
- (b) was covered by subsection 104-165(3) of the ITAA 1997 (item 5 of the table in section 855-15 of the ITAA 1997).

Appendix 2 – Detailed contents list

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References

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- ITAA 1936 177D(b)(i)
- Not previously issued as a draft
- ITAA 1936 177D(b)(ii)
 - ITAA 1936 177D(b)(iii)
- Related Rulings/Determinations:*
- TR 2006/10
- ITAA 1936 177D(b)(iv)
 - ITAA 1936 177D(b)(v)
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- Subject references:*
- capital benefit
 - capital gains tax
 - CGT cost base
 - dividend income
 - shareholder payments
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 - stapled structure
 - return of capital on shares
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ATO references

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