

CR 2012/3 - Income tax: off-market share buy-back: Careers Australia Group Limited



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Class Ruling

Income tax: off-market share buy-back: Careers Australia Group Limited

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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 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 44(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 90 of the ITAA 1936;
- subsection 95(1) of the ITAA 1936;
- subsection 128B(1) of the ITAA 1936;
- section 159GZZZP of the ITAA 1936;
- section 6-5 of the *Income Tax Assessment Act 1997* (ITAA 1997);

- section 104-10 of the ITAA 1997;
- section 116-20 of the ITAA 1997;
- section 118-20 of the ITAA 1997;
- section 118-25 of the ITAA 1997;
- section 204-30 of the ITAA 1997; and
- section 855-10 of the ITAA 1997.

All 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 ordinary shareholders of Careers Australia Group Limited (CAG) who:

- (a) disposed of their ordinary shares in CAG under the CAG off-market share buy-back (the Buy-Back) which was approved by CAG shareholders on 13 July 2011 and which is described in the Scheme section of this Ruling; and
- (b) 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 CAG shares.

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

In this Ruling, the ordinary shareholders of CAG are collectively referred to as 'shareholders' or 'participating shareholders'.

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 9 to 21 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 2011 to 30 June 2012. The Ruling continues to apply after this date 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 dated 15 June 2011;
- Off-market buy-back Booklet dated 21 June 2011; and
- correspondence received from MHM Chartered Accountants on 15 August 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.

10. CAG is a resident unlisted company limited by shares.

11. As at 28 February 2011 the share capital of CAG comprised 103,504,686 fully paid ordinary shares.

12. The shareholders in CAG are a mix of individuals, companies, trusts, partnership and superannuation funds, some of whom are foreign residents. All shares were acquired after 19 September 1985.

13. Between 21 June 2011 and 12 July 2011 CAG undertook an off-market buy-back of its shares. During this period CAG bought back \$20 million of its ordinary shares at a price of \$0.66 per share, equalling a maximum of 30,303,030 shares representing approximately 29% of CAG's ordinary shares on issue.

14. The Buy-Back was conducted through a fixed price tender process during a specified tender period and was open to all shareholders, who were registered as such on the Record Date for the Buy-Back (21 June 2011), except for:

- shareholders whose ordinary shares were acquired after the Ex-entitlement Date ; and
- shareholders who are Excluded Foreign Persons (that is, shareholders in any countries where CAG is prohibited from paying money under Australian law and/or where the Buy-Back invitation cannot be legally made).

15. Participation in the Buy-Back was voluntary and therefore eligible shareholders who did not wish to participate were not required to do anything. Non-participating shareholders did not receive any property, dividends or distributions by way of compensation.

16. The Buy-Back tender period opened on 21 June 2011 (Opening Date) and closed on 12 July 2011 (Closing Date).

17. Under the tender process, shareholders were able to submit offers to sell up to 45% of their CAG ordinary shares at a fixed price of \$0.66 per share (the Purchase Price). CAG considered that the Purchase Price was a fair representation of the market value of a CAG ordinary share at the time of the Buy-Back tender period.

18. No minimum threshold applied to the Buy-Back. The exact number of Shares bought back depended on the level of shareholder participation. However, to the extent that shareholder participation in the Buy-Back would otherwise exceed the Buy-Back Limit, a scale back would apply on a pro-rata basis such that the maximum value of all shares bought back did not exceed \$20 million.

19. All shares bought back under the Buy-Back were cancelled.

20. Under the Buy-Back \$0.4791 per share (the Capital Component) was debited to CAG's untainted share capital account and the balance of the purchase price being \$0.1809 (the Dividend Component) was debited to CAG's retained earnings.

21. On 12 July 2011 CAG accepted the offers made by participating shareholders under the fixed price tender process. CAG announced on 8 August 2011 that it had successfully completed the off-market share Buy-Back of 30,303,030 CAG Shares.

Ruling

The Dividend Component

22. A participating CAG shareholder will be taken to have been paid a dividend of \$0.1809 (the Dividend Component) for each CAG share bought back under section 159GZZZP.

23. The Dividend Component of \$0.1809 is unfranked.

24. The difference between the Buy-Back Price and the Dividend Component is not a dividend for income tax purposes.

Assessability of the Dividend Component

Direct distributions

25. The Dividend Component of \$0.1809 per share is included in the assessable income of resident individual, superannuation fund and company shareholders who participate in the Buy-Back under subsection 44(1).

Indirect distributions

Partnerships

26. The Dividend Component of \$0.1809 per share is included in the assessable income of a partnership that participates in the Buy-Back for the purposes of computing the net income of the partnership under section 90.

Trusts

27. The Dividend Component of \$0.1809 per share is included in the assessable income of a trustee for the purposes of computing the net income of the trust under subsection 95(1).

Non-resident shareholders

28. As the Dividend Component is unfranked, participating non-resident shareholders are liable for Australian withholding tax under paragraph 128B(1).

Shares held on capital account

29. The shares are taken to have been disposed of for capital gains tax (CGT) purposes on 8 August 2011 pursuant to section 104-10 of the ITAA 1997 (CGT event A1).

30. The Sale Consideration of \$0.4791 per share represents the capital proceeds for CGT purposes pursuant to section 116-20 of the ITAA 1997. A shareholder will make a capital gain on a share if the Sale Consideration per share exceeds the cost base of that share. The capital gain is the amount of the excess. Similarly, a shareholder will make a capital loss on a share if the Sale Consideration per share is less than the reduced cost base of the share (subsection 104-10(4) of the ITAA 1997).

Shares held on revenue account

31. Where the shares are held as trading stock, the Sale Consideration of \$0.4791 per share is included in assessable income under section 6-5 of the ITAA 1997. Participating shareholders will also make a capital gain or capital loss calculated as per paragraph 30 of this Ruling. However, under section 118-25 of the ITAA 1997 any capital gain or capital loss a participating shareholder makes will be disregarded if at the time of the CGT event the shares were held as trading stock.

32. Where the shares are held as revenue assets, but are not trading stock, the amount by which the Sale Consideration of \$0.4791 cents per share exceeds the cost of each share is included in the shareholder's assessable income. Correspondingly, if the cost exceeds the Sale Consideration the difference is an allowable deduction. Where the Sale Consideration per share exceeds the cost base of that share these shareholders will also make a capital gain. However, under section 118-20 of the ITAA 1997 any capital gain a participating shareholder makes will be reduced if, because of the event, the capital proceeds have otherwise been included in assessable income. The capital gain is reduced by the amount of the Sale Consideration otherwise included in assessable income or to zero, whichever is the greater. (A corresponding rule applies to a partner of a partnership.)

Foreign resident shareholders: CGT consequences

33. Under section 855-10 of the ITAA 1997, foreign resident shareholders who participate in the Buy-Back will only have CGT consequences if their shares bought back under the Buy-Back are 'taxable Australian property'.

The anti-avoidance provisions

34. The Commissioner will not make a determination under subsection 45A(2) or 45B(3) that section 45C applies to the whole, or any part, of the Capital Component of the Buy-Back Price received by participating shareholders.

35. The Commissioner will not make a determination under paragraph 204-30(3)(c) of the ITAA 1997, as all of the participating shareholders will receive only an unfranked dividend.

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.*

The Dividend and Capital Components

36. The purchase price received by participating shareholders comprises two components:

- Dividend Component; and
- Capital Component.

The amount of each of these components is determined in accordance with sections 159GZZZP and 159GZZZQ, having regard to how the company accounts for the off-market share buy-back.

The Dividend Component

37. Section 159GZZZP provides that where the buy-back of a share is an off-market purchase, the difference between the purchase price and the part (if any) of the purchase price which is debited against the share capital account, is taken to be a dividend paid by the company to the seller on the day the buy-back occurs. In this case the purchase price was \$0.66 per share and \$0.4791 of this was debited to the share capital account (Capital Component). Therefore the Dividend Component is \$0.1809 per share.

38. The Dividend Component of \$0.1809 per share is unfranked.

Assessability of the Dividend Component

Direct distributions

39. In the case of Australian resident shareholders (other than a partnership or trust) who participate in the Buy-Back and who directly receive the Dividend Component, the Dividend Component is included in the assessable income of each shareholder under subsection 44(1).

Indirect distributions

40. The unfranked distribution may flow indirectly to a partner in a partnership or a beneficiary of certain trusts.

41. In general terms, the distribution will flow indirectly to a partner in a partnership where the partner has an individual interest in the partnership's net income that is covered by paragraph 92(1)(a) or 92(1)(b), or has an individual interest in a partnership loss of the partnership that is covered by paragraph 92(2)(a) or 92(2)(b).

42. In general terms, a distribution will flow indirectly to a beneficiary of a trust where the beneficiary has a share of the trust's net income that is covered by paragraph 97(1)(a) or has an individual interest in the trust's net income that is covered by paragraph 98A(1)(a) or 98A(1)(b) or paragraph 100(1)(a) or 100(1)(b).

43. In the case of partnerships and certain trusts that participate in the Buy-Back the following income tax consequences arise.

Partnerships

44. Pursuant to subsection 44(1), the Dividend Component is included in the assessable income of the partnership for the purposes of computing the net income of the partnership under section 90.

Trusts

45. Pursuant to subsection 44(1), the Dividend Component is included in the assessable income of a trustee for the purposes of computing the net income of the trust under subsection 95(1).

Non-resident shareholders

46. As the Dividend Component of the consideration received under the Buy-Back is unfranked, a non-resident shareholder is liable to Australian withholding tax on the Dividend Component (paragraph 128B(1)).

The Capital Component

Calculation of Sale Consideration

47. For the purposes of determining the amount of a capital gain or capital loss (where the shares are held on capital or revenue account) the consideration in respect of the disposal of a share, the Sale Consideration, under an off-market buy-back is determined in accordance with section 159GZZZQ.

48. Subsection 159GZZZQ(1) provides that a shareholder is taken to have received an amount equal to the purchase price (in this case the \$0.66) received for each share bought back as consideration in respect of the sale of the share bought back. However, this amount is reduced by the amount of the dividend component in accordance with subsection 159GZZZQ(4) in order to arrive at the Sale Consideration.

49. Participating shareholders are therefore taken to have disposed of those shares accepted under the Buy-Back for a Sale Consideration of \$0.4791 per share on 8 August 2011 (CGT event A1). The disposal may have different taxation implications for shareholders depending on how the shares were held, for instance:

- an investor who held their shares on capital account will be subject to the CGT provisions; and
- a share trader who held their shares on revenue account will be subject to the ordinary income provisions and the CGT provisions.

Shares held on capital account

50. The Sale Consideration of \$0.4791 represents the capital proceeds for CGT purposes pursuant to section 116-20 of the ITAA 1997. A shareholder will make a capital gain on a share if the Sale Consideration per share exceeds the cost base of that share. The capital gain is the amount of the excess. Similarly, a shareholder will make a capital loss on a share if the Sale Consideration per share is less than the reduced cost base of the share (subsection 104-10(4) of the ITAA 1997).

Shares held on revenue account

51. Where the shares are held as trading stock, the Sale Consideration of \$0.4791 is included in assessable income under section 6-5 of the ITAA 1997. These shareholders will also make a capital gain or capital loss. However, as the shares are held as trading stock, the capital gain or loss is disregarded under section 118-25 of the ITAA 1997.

52. Where the shares are held as revenue assets, but are not trading stock, the amount by which the Sale Consideration of \$0.4791 per share exceeds the cost of each share is included in the shareholder's assessable income. Correspondingly, if the cost exceeds the Sale Consideration of \$0.4791 per share the difference is an allowable deduction. Where the Sale Consideration per share exceeds the cost base of the share these shareholders will also make a capital gain. However, shareholders who hold their shares as revenue assets will have the amount of the capital gain reduced under the anti-overlap provisions contained in section 118-20 of the ITAA 1997.

Foreign resident shareholders: CGT consequences

53. Under subsection 855-10(1) of the ITAA 1997, an entity disregards a capital gain or capital loss 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 and the CGT event happens in relation to a CGT asset that is not 'taxable Australian property'.

54. The term 'taxable Australian property' is defined in the table in section 855-15 of the ITAA 1997. The table sets out these five categories of CGT assets:

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).

55. A foreign resident, or the trustee of a foreign trust for CGT purposes, just before CGT event A1 happened under the Buy-Back, cannot disregard under subsection 855-10(1) of the ITAA 1997 a capital gain or capital loss from CGT event A1 if:

- their share in CAG is an indirect Australian real property interest (item 2 of the table in section 855-15 of the ITAA 1997);
- their share in CAG has been used at any time by the foreign resident in carrying on a business through a permanent establishment in Australia (item 3 of the table in section 855-15); or
- their share in CAG is covered by subsection 104-165(3) of the ITAA 1997 (item 5 of the table in section 855-15).

The anti-avoidance provisions

Sections 45A and 45B

56. Sections 45A and 45B are two anti-avoidance provisions which, if they apply, allow the Commissioner to make a determination that section 45C applies. The effect of such a determination is that all or part of the distribution of capital received by the shareholder under the Buy-Back is treated as an unfranked dividend. Accordingly, the application of these two provisions to the Buy-Back must be considered.

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

58. Although a 'capital benefit' (as defined in paragraph 45A(3)(b)) is provided to participating shareholders under the Buy-Back, the circumstances of the Buy-Back indicate that there is no streaming of capital benefits to some shareholders and dividends to other shareholders. Accordingly, section 45A has no application to the Buy-Back.

59. Section 45B applies where certain capital payments are paid to shareholders in substitution for dividends. In broad terms, section 45B applies where:

- (a) there is a scheme under which a person is provided with a capital benefit by a company (paragraph 45B(2)(a));
- (b) under the scheme, a taxpayer (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
- (c) 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 a tax benefit (paragraph 45B(2)(c)).

60. In the case of the Buy-Back, whilst the conditions of paragraphs 45B(2)(a) and 45B(2)(b) have been met, the requisite purpose of enabling the shareholder to obtain a tax benefit – by way of capital distribution – was not present.

61. Accordingly, the Commissioner will not make a determination under subsection 45A(2) or 45B(3) that section 45C applies to the whole, or any part, of the Capital Component of the Buy-Back Price received by participating shareholders.

Section 204-30

62. Section 204-30 of the ITAA 1997 applies where a corporate tax entity streams the payment of dividends, or the payment of dividends and the giving of other benefits, to its members in such a way that:

- (a) an imputation benefit is, or apart from this section would be, received by a member of the entity as a result of the distribution or distributions (paragraph 204-30(1)(a));
- (b) the member would derive a greater benefit from franking credits than another member of the entity (paragraph 204-30(1)(b)); and
- (c) the other member of the entity will receive lesser imputation benefits, or will not receive any imputation benefits, whether or not the other member receives other benefits (paragraph 204-30(1)(c)).

63. As all of the participating shareholders will receive only an unfranked dividend, the Commissioner will not make a determination under section 204-30.

Appendix 2 – Detailed contents list

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References

Previous draft:

Not previously issued as a draft

Related Rulings/Determinations:

TR 2006/10

Subject references:

- dividend income
- dividend streaming arrangements
- share buy backs

Legislative References:

- ITAA 1936
- ITAA 1936 44(1)
- ITAA 1936 45A
- ITAA 1936 45A(2)
- ITAA 1936 45A(3)(b)
- ITAA 1936 45B
- ITAA 1936 45B(2)(a)
- ITAA 1936 45B(2)(b)
- ITAA 1936 45B(2)(c)
- ITAA 1936 45B(3)
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- ITAA 1936 90
- ITAA 1936 92(1)(a)
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- ITAA 1936 97(1)(a)
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- ITAA 1936 128B(1)
- ITAA 1936 159GZZZP
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- ITAA 1997 204-30(1)(a)
- ITAA 1997 204-30(1)(b)
- ITAA 1997 204-30(1)(c)
- ITAA 1997 204-30(3)
- ITAA 1997 204-30(3)(c)
- ITAA 1997 Div 230
- ITAA 1997 855-10
- ITAA 1997 855-10(1)
- ITAA 1997 855-15
- TAA 1953
- Copyright Act 1968

Other references:

- Law Administration Practice Statement PS LA 2007/9 Share Buy-Backs

ATO references

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ATOlaw topic: Income Tax ~~ Entity specific matters ~~ share buy-backs
Income Tax ~~ Capital Gains Tax ~~ capital proceeds
Income Tax ~~ Capital Gains Tax ~~ CGT event A1 – disposal of a CGT asset