


CR 2015/101 - Income tax: Qantas Airways Limited - capital return and share consolidation

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Class Ruling

Income tax: Qantas Airways Limited – capital return and share consolidation

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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 6(1) of the *Income Tax Assessment Act 1936* (ITAA 1936)
- subsection 44(1) of the 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)
- section 104-135 of the ITAA 1997
- section 112-25 of the ITAA 1997
- section 855-15 of the ITAA 1997

Class of entities

3. The class of entities to which this ruling applies is the ordinary shareholders of Qantas Airways Limited (Qantas) who:

- (a) are registered on the Qantas share register on 29 October 2015 (Record Date)
- (b) do not hold their Qantas ordinary shares as revenue assets (as defined in section 977-50 of the ITAA 1997) nor as trading stock (as defined in subsection 995-1(1) of the ITAA 1997) – that is, they will hold their Qantas shares on capital account, and
- (c) are not subject to the taxation of financial arrangements rules in Division 230 in relation to gains and losses on their Qantas 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, a person belonging to this class of entities is referred to as a 'Qantas Shareholder'.

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 8 to 32 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.

Date of effect

7. This Ruling applies from 1 July 2015 to 30 June 2016. The Ruling continues to apply after 30 June 2016 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

8. 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:

- Qantas's proposed capital return, ATO Presentation Deck dated 13 July 2015
- draft application for a Class Ruling received on 13 July 2015
- final application for a Class Ruling received on 17 July 2015, and
- other information and documents provided by the applicant.

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

9. Qantas is a resident of Australia for income tax purposes.

10. As at 30 June 2015, Qantas had 2,196,330,250 fully paid-up ordinary shares on issue.

11. Under the Qantas Sale Act, Qantas can have a maximum foreign ownership of 49%. As at 30 June 2015, Qantas shareholders included approximately 39.7% foreign residents.

Qantas' share capital

12. Qantas raised \$761.6 million share capital in 2009 during the global financial crisis through share placements and use of dividend reinvestment plans. The stated purpose for the capital raising was 'to enhance financial flexibility and support the fleet renewal program, increase diversity of funding, reduce net debt and support Qantas investment grade credit rating'.

13. Of the \$761.6 million capital raised, Qantas returned \$99.6 million through on-market share buybacks in the income year ended 30 June 2014.

14. As at 30 June 2015, Qantas' share capital balance was \$4,630 million.

15. Qantas' share capital account is not tainted (within the meaning of Division 197 of the ITAA 1997).

Qantas' financial position

16. On 20 August 2015, the Qantas consolidated group announced:

- an after tax profit of approximately \$560 million for the financial year ended 30 June 2015, and
- a retained loss balance of approximately \$1,115 million as at 30 June 2015.

17. No profit reserves have been created in the Qantas consolidated group as at 30 June 2015.

18. Qantas does not anticipate that it will pay a fully franked dividend prior to 31 December 2015, but it intends to return to the payment of dividends as soon as appropriate having regard to relevant commercial and legal restrictions.

19. Qantas advises that they had approximately \$2.8 billion in carried forward tax losses as at 30 June 2015.

Capital return

20. On 23 October 2015, Qantas obtained shareholder approval in the Qantas Annual General Meeting to reduce its share capital by returning a total of approximately \$505 million or \$0.23 per fully paid ordinary share.

21. The capital return was affected by way of an equal reduction of capital under section 256B of the *Corporations Act 2001*.

22. The capital return was paid equally to each holder of a Qantas share who was registered on the Qantas share register on the Record Date. The payment to be made on 6 November 2015 (the Payment Date).

23. The capital return was debited to Qantas' share capital account.

24. The capital return represented a return of the capital that was raised by Qantas in 2009 to Qantas Shareholders, and took into account the impacts of the following factors which include:

- the fundamentally different market conditions and operating environment (between 2009 and now)
- the structural changes to the business from the implementation of the Qantas Transformation Program to date, including more streamlined operations and a lower commitment to capital expenditure on its fleet
- improving credit rating metrics within investment grade credit rating thresholds
- revised assessment of liquidity requirements/risks (including working capital peaks and troughs, crisis reserve, collateral risk, and requirements to support transformation projects), and
- application of a targeted debt to capital range determined to achieve the lowest weighted average cost of capital for Qantas.

Share consolidation

25. On 23 October 2015, Qantas also obtained shareholder approval to undertake a share consolidation through a conversion of every one share into approximately 0.939 of a share (based on a share price of \$3.77).

26. The share consolidation will result in the reduction in the number of shares on issue from approximately 2,196 million to approximately 2,062 million, representing a 6.1 per cent reduction in the number of shares on issue.

27. The share consolidation will be applied to all ordinary shares and it will occur after the capital return.

28. After the share consolidation, Qantas Shareholders will own fewer shares that are proportionately higher priced. The share consolidation will have no effect on the value of each shareholder's shares relative to the total market value of Qantas.

29. The share consolidation will be undertaken in accordance with section 254H of the *Corporations Act 2001* such that:

- a shareholder's original shares will not be cancelled or redeemed
- there will be no change in the total amount allocated to the Qantas share capital account, and
- the proportion of equity owned by each shareholder in the share capital account will be maintained.

Other matters

30. As at 30 June 2015, Qantas had:

- A franking account balance of approximately \$84 million, and
- A conduit foreign income balance of approximately \$150 million.

31. A Qantas ordinary share is not an 'indirect Australian real property interest' as defined in section 855-25 of the ITAA 1997.

32. For the year ended 30 June 2015, Qantas did not make any significant disposals of non-core assets.

Ruling**Capital return is not a dividend**

33. The capital return by Qantas will not be a dividend under subsection 6(1) of the ITAA 1936 and it will not form part of a Qantas Shareholder's assessable income under subsection 44(1) of the ITAA 1936.

The anti-avoidance provisions

34. The Commissioner will not make a determination under subsections 45A(2) or 45B(3) of the ITAA 1936 that section 45C of the ITAA 1936 applies to the whole, or any part, of the capital return received by Qantas Shareholders.

Capital gains tax (CGT) consequences

CGT event C2

35. CGT event C2 (section 104-25 of the ITAA 1997) happened when Qantas paid the capital return of \$0.23 per share to a Qantas Shareholder in respect of a Qantas ordinary share they owned at the Record Date, but cease to own before the Payment Date.

CGT event G1

36. CGT event G1 (section 104-135 of the ITAA 1997) happened when Qantas paid the \$0.23 per share capital return to a Qantas Shareholder in respect of a Qantas ordinary share that they owned at the Record Date and continued to own at the Payment Date.

Foreign resident shareholders

37. A foreign resident Qantas Shareholder who was paid the capital return may disregard any capital gains made when CGT event G1 happened as their Qantas share did not constitute 'taxable Australian property' (section 855-10 of the ITAA 1997).

38. A foreign resident Qantas Shareholder who was paid the capital return may disregard any capital gains made when CGT event C2 happened as their right to receive the capital return was not 'taxable Australian property' (section 855-10 of the ITAA 1997).

Share consolidation

39. The consolidation of Qantas' ordinary shares will not result in a CGT event happening (section 112-25 of the ITAA 1997).

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.*

Capital return is not a dividend

40. Under subsection 44(1) of the ITAA 1936, the assessable income of a shareholder in a company includes any dividends, as defined in subsection 6(1) of the ITAA 1936, paid to the shareholders out of profits derived by the company from any source (if the shareholder is a resident of Australia) and from an Australian source (if the shareholder is a non-resident of Australia).

41. The term 'dividend' in subsection 6(1) of the ITAA 1936 includes any distribution made by a company to any of its shareholders. However, paragraph (d) of the definition of 'dividend' excludes a distribution that is debited against an amount standing to the credit of the share capital account of the company.

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

43. 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.

44. The total amount of capital return has been debited to Qantas' share capital account. As Qantas' share capital account is not tainted within the meaning of Division 197 of the ITAA 1997, paragraph (d) of the definition of 'dividend' in subsection 6(1) of the ITAA 1936 applies. Accordingly, the capital return of \$0.23 per ordinary share does not constitute a dividend under subsection 6(1) of the ITAA 1936. Therefore, it will not be required to be included in the assessable income of a Qantas Shareholder under subsection 44(1) of the ITAA 1936.

The anti-avoidance provisions

Section 45A of the ITAA 1936

45. Section 45A of the ITAA 1936 applies where a company streams 'capital benefits' to 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.

46. Although Qantas has provided its shareholders with a 'capital benefit' (as defined in paragraph 45A(3)(b) of the ITAA 1936), the capital benefit was provided to all Qantas Shareholders in direct proportion to their individual shareholding. The circumstances of the scheme do not indicate that there is a 'streaming' of capital benefits to advantaged shareholders and of dividends to disadvantaged shareholders.

47. Accordingly, section 45A of the ITAA 1936 will not apply to the capital return and the Commissioner will not make a determination under subsections 45A(2) of the ITAA 1936 that section 45C of the ITAA 1936 applies to the whole, or any part, of the capital return to the Qantas Shareholders.

Section 45B of the ITAA 1936

48. Section 45B of the ITAA 1936 is an anti-avoidance provision that allows the Commissioner to make a determination that section 45C of the ITAA 1936 applies to treat all or part of a capital return amount as an unfranked dividend if certain conditions are satisfied.

49. Section 45B of the ITAA 1936 applies where certain capital payments are made to shareholders in substitution for dividends. Specifically, the provision 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 (the relevant 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, 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 (the relevant taxpayer) to obtain a tax benefit (paragraph 45B(2)(c) of the ITAA 1936).

50. The capital return to Qantas Shareholders will constitute a scheme under which the Qantas Shareholders are provided with a capital benefit by Qantas (paragraph 45B(5)(b) of the ITAA 1936).

51. While the capital return by Qantas satisfies the conditions in paragraphs 45B(2)(a) and (b), paragraph 45B(2)(c) of the ITAA 1936 is not satisfied. Having regard to the relevant circumstances of the scheme set out in subsection 45B(8) of the ITAA 1936, it cannot be concluded that the scheme is to be entered into or carried out for a more than incidental purpose of enabling Qantas Shareholders to obtain a tax benefit. In particular, the capital that was raised by Qantas in 2009 was in response to the occurrence of an unprecedented global event which caused significant disruption to the financial markets. Those circumstances which necessitated the raising of additional capital no longer exist today.

52. Accordingly, the Commissioner will not make a determination under paragraph 45B(3)(b) of the ITAA 1936 that section 45C of the ITAA 1936 applies to treat the whole or any part of the capital return of \$0.23 per ordinary share paid by Qantas as an unfranked dividend in the hands of the Qantas Shareholders.

CGT consequences

CGT event C2

53. CGT event C2 happened when the capital return of \$0.23 per ordinary share was paid to a Qantas Shareholder that held the share at the Record Date but no longer owned the ordinary share at the Payment Date (section 104-25 of the ITAA 1997).

54. The right to receive the capital return was one of the rights inherent in a Qantas share held at the Record Date. If, after the Record Date but before the Payment Date, a Qantas Shareholder ceased to own a Qantas ordinary share in respect of which the capital return was payable, the right to receive the capital return was retained by that shareholder and constitutes a separate CGT asset.

55. The right to receive the capital return ended by the right being discharged or satisfied when the payment was made.

56. A Qantas Shareholder will make a capital gain if the capital proceeds from the ending of the right were more than the cost base of the right. The capital gain is equal to the amount of the excess. A Qantas Shareholder will make a capital loss if the capital proceeds from the ending of the right were less than its reduced cost base. The capital loss is equal to the amount of the difference (subsection 104-25(3) of the ITAA 1997).

57. In working out the capital gain or capital loss made when CGT event C2 happened, the capital proceeds will equal the amount of the capital return (\$0.23 per ordinary share) received by a Qantas Shareholder (subsection 116-20(1) of the ITAA 1997).

58. The cost base of the Qantas Shareholder's right to receive the capital return 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 share previously owned by a Qantas Shareholder that has been applied in working out a capital gain or capital loss made when a CGT event happens to the share, for example, when the Qantas Shareholder disposed of the share after the Record Date.

59. Therefore, as the full cost base or reduced cost base of the Qantas share was applied in working out a capital gain or capital loss made when a CGT event happens to that share, the right to receive the capital return will generally have a nil cost base. As a result, the Qantas Shareholder will generally make a capital gain equal to the amount of the capital return.

60. As the right to receive the capital return was inherent in the Qantas ordinary share during the time it was owned, the right is considered to have been acquired at the time when the corresponding ordinary share was acquired (section 109-5 of the ITAA 1997).

61. Accordingly, if the Qantas ordinary share was acquired at least 12 months before the capital return was paid, a capital gain made from the ending of the corresponding right might be eligible to be treated as a discount capital gain under Division 115 of the ITAA 1997, provided other conditions of that Division were satisfied.

CGT event G1

62. CGT event G1 (section 104-135 of the ITAA 1997) happens when a company makes a payment to a shareholder in respect of a share they own and some or all of the payment (the non-assessable part) is not a dividend (as defined in subsection 995-1(1)) or an amount that is taken to be a dividend under section 47 of the ITAA 1936 and the payment is not included in the shareholder's assessable income.

63. No part of the capital return to a Qantas Shareholder is a dividend, nor is included in a Qantas Shareholder's assessable income. Accordingly, CGT event G1 happened when Qantas paid the capital return to a Qantas Shareholder in respect of a Qantas ordinary share that they owned at the Record Date and continue to own at the Payment Date.

64. A Qantas Shareholder will make a capital gain if the capital return amount was more than the cost base of the Qantas ordinary share, with the amount of the capital gain being equal to that excess (subsection 104-135(3) of the ITAA 1997).

65. If a Qantas Shareholder makes a capital gain from CGT event G1 happening, the cost base and reduced cost base of the Qantas ordinary share is reduced to nil. A Qantas Shareholder cannot make a capital loss from CGT event G1 (subsection 104-135(3) of the ITAA 1997).

66. If the capital return is equal to or less than the cost base of the Qantas ordinary share at the Payment Date, the cost base and reduced cost base of the Qantas ordinary share will be reduced (but not below nil) by the amount of the non-assessable part of the payment (subsection 104-135(4) of the ITAA 1997).

67. A capital gain made when CGT event G1 happens will be eligible to be treated as a discount capital gain under Division 115 of the ITAA 1997 provided that the Qantas ordinary share was acquired at least 12 months before the payment of the return of share capital (subsection 115-25(1) of the ITAA 1997) and the other conditions of that Division are satisfied.

Foreign resident shareholders

68. 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'.

69. The term 'taxable Australian property' is defined in the table in section 855-15 of the ITAA 1997. The table sets out the 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) (choosing to disregard a gain or loss on ceasing to be an Australian resident).

70. Neither the Qantas ordinary shares nor a Qantas Shareholder's right to the capital return is an 'indirect Australian real property interest' as defined in section 855-25 of the ITAA 1997, and therefore not taxable Australian property.

71. A foreign resident who is a Qantas Shareholder who received the capital return payment will disregard any capital gain made when CGT event G1 happened and disregard any capital gain or capital loss if CGT event C2 happened.

Share consolidation

72. Under section 112-25 of the ITAA 1997, a CGT event will not happen if a company converts its shares into a larger or smaller number of shares (the converted shares).

73. While there is a change in the form of the original shares, there is no change in their beneficial ownership.

74. The converted shares will have the same date of acquisition as the original shares to which they relate.

75. Where the original shares were acquired on or after 20 September 1985, subsection 112-25(4) provides that each element of the cost base and reduced cost base of the converted shares is the sum of the corresponding elements of each original share.

Appendix 2 – Detailed contents list

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References

<i>Previous draft:</i>	- ITAA 1997 104-25(3)
Not previously issued as a draft	- ITAA 1997 104-135
	- ITAA 1997 104-135(3)
<i>Related Rulings/Determinations:</i>	- ITAA 1997 104-135(4)
TR 2006/10	- ITAA 1997 104-165(3)
	- ITAA 1997 109-5
<i>Legislative references:</i>	- ITAA 1997 Div 110
- ITAA 1936	- ITAA 1997 Div 112
- ITAA 1936 6(1)	- ITAA 1997 112-25
- ITAA 1936 44(1)	- ITAA 1997 112-25(4)
- ITAA 1936 45A	- ITAA 1997 Div 115
- ITAA 1936 45A(2)	- ITAA 1997 115-25(1)
- ITAA 1936 45A(3)(b)	- ITAA 1997 116-20(1)
- ITAA 1936 45B	- ITAA 1997 Div 230
- ITAA 1936 45B(2)(a)	- ITAA 1997 855-10
- ITAA 1936 45B(2)(b)	- ITAA 1997 855-10(1)
- ITAA 1936 45B(2)(c)	- ITAA 1997 855-15
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- ITAA 1936 45C	- Corporations Act 2001
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ATO references

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