


CR 2015/63 - Income tax: return of capital: Ambre Energy Limited

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Class Ruling

Income tax: return of capital: Ambre Energy Limited

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① 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 provision(s)

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

- subsection 6(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 104-25 of the *Income Tax Assessment Act 1997* (ITAA 1997)
- section 104-35 of the ITAA 1997, and
- section 855-10 of the ITAA 1997.

Class of entities

3. The class of entities to which this Ruling applies are the holders of ordinary shares in Ambre Energy Limited (AEL) who:

- were registered on the AEL share register on 7 July 2015, the date for determining entitlement to the return of capital (Record Date)
- held their fully paid ordinary shares in AEL (AEL ordinary shares) 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 AEL ordinary shares.

(Note: Division 230 of the ITAA 1997 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 an AEL 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 33 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:

- Application for class ruling dated 11 June 2015,
- Notice of annual general meeting held on 22 December 2014, dated 26 November 2014
- Notice of annual general meeting held on 30 June 2015, dated 4 June 2015,
- Top 20 shareholders percentage of issued capital as per AEL's share register as at 16 March 2015, and
- Correspondence from 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.

Background

9. AEL is an unlisted public company incorporated in New South Wales in 2005 and the head company of an income tax consolidated group.

10. AEL has been engaged in an integrated coal mining, infrastructure and alternative fuels business.

11. AEL's principal business activities consisted of three key divisions being:

- Coal – including the operation and management of thermal coal mines, coal exploration and development of coal resources, and the development and acquisition of coal mines.
- Infrastructure – including the operation of a bulk materials terminal and the development and eventual operation of port facilities for the shipping of coal in the United States of America (US).
- Alternative fuels – including the development of oil shale resources in the US.

12. AEL was headquartered in Brisbane, Australia with its US operations managed from Salt Lake City, Utah. AEL's business was predominantly undertaken in the US through its former US subsidiary with development assets also held in Australia.

Assets divestments

13. In 2014, AEL's Board of Directors decided to divest AEL of its major assets due to adverse market conditions and depleted cash reserves. Each asset was sold at a loss. The assets sold were:

- Common stock of a former US subsidiary
- Oil shale leases in Utah, US
- Felton properties located in Queensland.

14. As a result of the asset divestments, AEL no longer engages in any significant business activities in the US or Australia.

15. Following the asset divestments, AEL's only material asset is non-voting B class common stock in a former US subsidiary.

Sale of the former US subsidiary

16. Prior to the asset divestment, AEL's coal and infrastructure businesses were conducted by a former wholly owned US subsidiary.

17. All of the common stock in the former US subsidiary was held by an AEL wholly owned Australian subsidiary (AEL Australian subsidiary).

18. By term sheet dated 28 August 2014 and as subsequently recorded in an agreement dated 11 November 2014, AEL agreed to sell the common stock in the former US subsidiary to a related party and its associated entity.

19. AEL shareholders approved the sale at AEL's annual general meeting on 22 December 2014.

20. Details of the transactions involved with the sale of the former US subsidiary were set out in the Notice of annual general meeting dated 26 November 2014. The sale occurred as follows:

- The AEL Australian subsidiary made an *in specie* distribution of 26.41% of class A common stock in the former US subsidiary as consideration for the buy-back of 121,625,000 AEL ordinary shares (representing 26.41% of the shares in AEL) to the related party – valued at approximately A\$7,956,387,
- The associated entity of the related party made a cash payment of approximately A\$20,406,417 for 73.59% of class A common stock in the former US subsidiary,
- The AEL Australian subsidiary was issued with 80,000 non-voting, class B common stock of the former US subsidiary – valued at approximately A\$1,870,842, and
- All loans from the former US subsidiary to the AEL group were forgiven – valued at approximately A\$12,561,959.

21. The total loss arising from the sale of the common stock in the former US subsidiary was A\$89,361,061.

Sale of the oil shale lease assets

22. On 31 October 2014, AEL through another US subsidiary, entered into an asset purchase agreement to sell all the oil shale leases held by its US subsidiary for US\$4,000,000. The sale was completed on 20 November 2014.

23. The total loss arising from the sale of the oil shale lease assets was US\$16,281,000.

Sale of the Felton properties

24. Since December 2013, AEL's Felton properties were actively marketed for sale.

25. On 25 February 2015, AEL through one of its Australian subsidiaries, entered into contracts of sale of the Felton properties for total of A\$1,801,000, which settled on 27 March 2015.

26. The total loss arising from the sale of the Felton properties was A\$2,762,498.

Return of capital to AEL shareholders

27. As a result of the asset divestments, AEL had funds in excess of its working capital requirements.

28. At AEL's annual general meeting held on 30 June 2015, AEL shareholders approved a return of capital of up to A\$5,423,168 (A\$0.016 per share) by way of an equal share capital reduction.

29. The return of capital was conducted pursuant to section 256B of the *Corporations Act 2001*.

30. The return of capital of A\$0.016 per share was made to all AEL shareholders on 24 July 2015 (Payment Date).

31. The return of capital was debited to AEL's share capital account and sourced entirely from AEL's cash reserves.

AEL's capital structure

32. As at 11 June 2015, AEL had 338,948,009 ordinary shares on issue.

33. AEL has a diverse shareholder base comprising approximately 69% Australian residents and 31% foreign residents. All foreign resident shareholders hold minority stakes in AEL (i.e. less than 10% shareholding each).

34. After the return of capital, each AEL shareholder's proportionate interest in AEL remained the same.

Other matters

35. AEL's share capital account is not tainted within the meaning of Division 197 of the ITAA 1997.

36. Prior to the return of capital, AEL had issued capital of US\$199,380,000 and accumulated losses of US\$186,512,000.

37. AEL has been in accumulated loss position since incorporation.

38. AEL has never paid any dividends to its shareholders and does not anticipate paying a dividend to shareholders in the near future.

39. Prior to the return of capital, AEL had approximately A\$7,000,000 cash on hand.

40. After the return of capital, AEL has issued share capital of approximately US\$194,940,000 and cash on hand of approximately A\$1,300,000 to A\$1,500,000.

Ruling

Return of capital is not a dividend

41. The return of capital paid to AEL shareholders is not a dividend as defined in subsection 6(1) of the ITAA 1936.

The application of sections 45A, 45B and 45C

42. The Commissioner does not make a determination under subsection 45A(2) of the ITAA 1936 or subsection 45B(3) of the ITAA 1936 that section 45C of the ITAA 1936 applies to the return of capital. Accordingly, the return of capital is not taken to be a dividend for income tax purposes.

Capital gains tax (CGT) consequences

CGT event G1

43. CGT event G1 (section 104-135 the ITAA 1997) happened when AEL paid the return of capital of A\$0.016 per share to an AEL shareholder in respect of an AEL ordinary share that they owned at 7 July 2015 (Record Date) and continued to own at 24 July 2015 (Payment Date).

CGT event C2

44. CGT event C2 (section 104-25 of the ITAA 1997) happened when AEL paid the return of capital of A\$0.016 per share to an AEL shareholder in respect of an AEL ordinary share that they owned at 7 July 2015 (Record Date), but ceased to own before 24 July 2015 (Payment Date).

Foreign resident shareholders

45. Foreign resident AEL shareholders disregard any capital gain or capital loss made from CGT event G1 and CGT event C2, if their AEL ordinary shares or right to receive the relevant return of capital is not 'taxable Australian property' under section 855-10 of the ITAA 1997.

Commissioner of Taxation

12 August 2015

Appendix 1 – Explanation

① *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.*

Return of capital is not dividend

46. The term 'dividend' is defined in subsection 6(1) of the ITAA 1936 and includes a 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.

47. '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.

48. Subsection 975-300(3) of the ITAA 1997 states that an account is generally taken not to be a share capital account if it is tainted.

49. The return of capital was recorded as being entirely debited to AEL's share capital account. As AEL's 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 return of capital of A\$0.016 per share is not a dividend as defined in subsection 6(1).

The application of sections 45A, 45B and 45C

50. Sections 45A and 45B of the ITAA 1936 are two anti-avoidance provisions which, if they apply, allow the Commissioner to make a determination that section 45C of the ITAA 1936 applies to treat all or part of the return of share capital received by AEL's shareholders as an unfranked dividend paid by the company out of profits.

Section 45A – streaming of dividends and capital benefits

51. Section 45A of the ITAA 1936 applies in circumstances where capital benefits are streamed to some shareholders (the advantaged shareholders) who would derive a greater benefit from the capital benefits than the other shareholders (the disadvantaged shareholders) and it is reasonable to assume that the disadvantaged shareholders have received, or will receive, dividends.

52. Although AEL provided its shareholders with a 'capital benefit' (as defined in paragraph 45A(3)(b) of the ITAA 1936), the circumstances of the return of capital do not indicate that there is a streaming of capital benefits to advantaged shareholders and dividends to disadvantaged shareholders.

53. Accordingly, the Commissioner does not make a determination under subsection 45A(2) of the ITAA 1936 that section 45C of the ITAA 1936 applies to the return of capital to the AEL shareholders.

Section 45B – scheme to provide capital benefits

54. Section 45B of the ITAA 1936 applies where certain 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), and
- 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).

55. The arrangement involving the return of capital to AEL shareholders constitutes a scheme for the purposes of section 45B of the ITAA 1936.

56. The return of capital was debited to the share capital account and AEL shareholders received a distribution of share capital of A\$0.016 per share. Therefore, AEL shareholders were provided with a capital benefit under paragraph 45B(5)(b) of the ITAA 1936.

57. Paragraph 45B(2)(c) of the ITAA 1936 sets out an objective purpose test for the Commissioner to consider having regard to the 'relevant circumstances' of the scheme as set out in subsection 45B(8) of the ITAA 1936.

58. The asset divestments resulted in the cessation of a significant portion of AEL's business and the realisation of losses to AEL. Further, there were no retained earnings available in the AEL group from which a dividend could be paid. Therefore, the return of capital cannot be attributed to AEL's profits.

59. Based on the evidence, the return of capital reflects circumstances where the share capital distributed was genuinely surplus to AEL's needs. The divestments resulted in a release of share capital which became available to be returned to AEL shareholders.

60. Having regard to the relevant circumstances, it could not be concluded that the scheme was entered into or carried out for a more than incidental purpose of enabling AEL shareholders to obtain a tax benefit.

61. Accordingly, the Commissioner does not make a determination under subsection 45B(3) of the ITAA 1936 that section 45C of the ITAA 1936 applies to the payment for the return of capital.

CGT consequences

CGT event G1 – section 104-135

62. CGT event G1 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) of the ITAA 1997 or an amount that is taken to be a dividend under section 47 of the ITAA 1936.

63. Accordingly, CGT event G1 happened when AEL paid the return of capital amount to an AEL shareholder in respect of an AEL ordinary share they owned at the Record Date (7 July 2015) and continued to own at the Payment Date (24 July 2015).

64. An Australian resident AEL shareholder makes a capital gain if the return of capital is more than the cost base of the shareholder's AEL ordinary share. The amount of the capital gain is equal to the excess (subsection 104-135(3) of the ITAA 1997).

65. If the Australian resident AEL shareholder makes a capital gain when CGT event G1 happens, the cost base and reduced cost base of the AEL ordinary share is reduced to nil. An Australian resident AEL shareholder cannot make a capital loss when CGT event G1 happens (subsection 104-135(3) of the ITAA 1997).

66. If the return of capital is equal to or less than the cost base of the AEL ordinary share at the Payment Date (24 July 2015), the cost base and reduced cost base of the share is reduced 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 is eligible to be treated as a discount capital gain under Division 115 of the ITAA 1997 provided that the AEL ordinary share was acquired at least 12 months before the payment of the return of capital (subsection 115-25(1) of the ITAA 1997) and the other conditions of that Division are satisfied.

CGT event C2 – section 104-25

68. CGT event C2 happened when the return of capital was paid to AEL shareholders that held the AEL ordinary share at the Record Date (7 July 2015) but no longer owned the AEL share at the Payment Date (24 July 2015) (section 104-25 of the ITAA 1997).

69. The right to receive the return of capital is one of the rights inherent in the AEL ordinary share at 7 July 2015 (the Record Date). If, after 7 July 2015 (the Record Date) but before 24 July 2015 (the Payment Date), an AEL shareholder ceased to own an AEL ordinary share in respect of which the return of capital was paid, the right to receive the payment in respect of that share is retained by the shareholder and is a separate CGT asset.

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

71. An Australian resident AEL shareholder makes a capital gain if the capital proceeds from the ending of the right are more than the cost base of the right. The capital gain is equal to the amount of the excess. An Australian resident AEL shareholder makes a capital loss if the capital proceeds from the ending of the right are 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).

72. In working out the capital gain or capital loss made when CGT event C2 happened, the capital proceeds is the amount of the return of capital received by the AEL shareholder (subsection 116-20(1) of the ITAA 1997).

73. The cost base of the 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 share previously owned by the AEL shareholder that has been applied in working out a capital gain or capital loss made when a CGT event happened to the share, for example, when the AEL shareholder disposed of the share after 7 July 2015 (the Record Date).

74. Therefore, if the full cost base or reduced cost base of the AEL ordinary share was applied in working out a capital gain or capital loss when a CGT event happened to that share, then the right to receive the return of capital is likely to have a cost base of nil. As a result, the AEL shareholder generally makes a capital gain equal to the amount of the return of capital received.

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

76. Accordingly, if the AEL ordinary share was acquired at least 12 months before the payment of the return of capital, a capital gain made from the ending of the corresponding right satisfies the requirements of section 115-25 of the ITAA 1997. Such a capital gain may 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

77. Under subsection 855-10(1) of the ITAA 1997, an entity disregards a capital gain or capital loss made from a CGT event if:

- just before the CGT event happened, the entity is a foreign resident, or the trustee of a foreign trust for CGT purposes, and
- the CGT event happens in relation to a CGT asset that is not 'taxable Australian property'.

78. 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).

79. Items 1 and 2 of the table in section 855-15 of the ITAA 1997 do not apply to AEL ordinary shares.

80. At the time the return of capital was made to the AEL shareholders, AEL did not hold any interests in real property and accordingly AEL ordinary shares do not constitute taxable Australian real property. Further, AEL ordinary shares held by an AEL shareholder who was a foreign resident are not an indirect Australian real property interest in AEL at the time the CGT event happened as the AEL ordinary shares do not pass the principal asset test (section 855-30 of the ITAA 1997).

81. Accordingly, a foreign resident, or the trustee of a foreign resident trust for CGT purposes, disregards a capital gain or capital loss made when CGT event G1 or CGT event C2 happened to their AEL ordinary share or right to receive the capital return under section 855-10 of the ITAA 1997 unless their share or right:

- had been used at any time by them 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
- 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

Previous draft:

Not previously issued as a draft

Related Rulings/Determinations:

TR 2006/10

Subject references:

- capital benefit
- capital reductions
- CGT event C1-C3 - end of a CGT asset
- CGT event G1-G3 – shares
- return of capital on shares
- share capital
- shareholder payments

Legislative references:

- | | |
|-----------------------|------------------------------|
| - ITAA 1936 | - ITAA 1936 45C |
| - ITAA 1936 6(1) | - ITAA 1936 47 |
| - ITAA 1936 45A | - ITAA 1997 |
| - ITAA 1936 45A(2) | - ITAA 1997 104-25 |
| - ITAA 1936 45A(3)(b) | - ITAA 1997 104-25(3) |
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