

CR 2016/51 - Income tax: Return of Capital and Scheme of Arrangement - Unity Mining Limited

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Class Ruling

Income tax: Return of Capital and Scheme of Arrangement – Unity Mining 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 45B of the ITAA 1936
- section 45C of the ITAA 1936
- section 104-10 of the *Income Tax Assessment Act 1997* (ITAA 1997)
- section 104-25 of the ITAA 1997, and
- section 116-20 of the ITAA 1997.

Class of entities

3. The class of entities to which this Ruling applies is the holders of ordinary shares in Unity Mining Limited (Unity), excluding Diversified Minerals Pty Ltd (DM) and any associate of DM that is a Unity shareholder, who:

- are residents of Australia for tax purposes as defined in subsection 6(1) of the ITAA 1936
- acquired their Unity shares on or after 20 September 1985
- held their Unity shares neither 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 broadly held their Unity shares on capital account
- participated in the return of capital (ROC) and the scheme of arrangement between Unity and its shareholders excluding Diversified Minerals Pty Ltd (DM) and any associate of DM that is a Unity shareholder (Scheme of Arrangement)
- held their Unity shares continuously from the record date being 7:00pm Melbourne time on 31 May 2016 (Record Date) to the scheme implementation date being 1 June 2016 (Scheme Implementation Date), and
- were not subject to the taxation of financial arrangements rules in Division 230 of the ITAA 1997 in relation to the gains and losses on their Unity 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.)

4. In this Ruling, a person belonging to this class of entities is referred to as a 'Unity Scheme Shareholder'.

Qualifications

5. The Commissioner makes this Ruling based on the precise scheme identified in this Ruling.

6. 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 29 of this Ruling.

7. 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

8. 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

9. The following description of the scheme is based on information 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.

10. Unity was incorporated in 1980 and listed on the Australian Securities Exchange in 1985.

11. Unity is an Australian resident company for income tax purposes and is the head company of a tax consolidated group.

12. As at 16 February 2016, Unity had approximately 1,140 million ordinary shares on issue.

13. As at 7 March 2016, DM (and its associates) was the largest shareholder of Unity, holding approximately 13.69% of all ordinary shares in Unity.

14. On 6 December 2015, Unity executed a scheme implementation agreement with DM (SIA). This SIA was amended on 7 April 2016 and 19 April 2016 (both times to increase the consideration payable under the Scheme). Under the terms of the amended SIA, it was proposed that:

- (a) Unity would make a ROC of \$0.01 per Unity share to its shareholders.

- (b) Diversified Minerals Management Pty Ltd (DMM) (a wholly owned subsidiary of DM) would then acquire all of the issued ordinary shares in Unity, not already owned or controlled by DM and any associates of DM, for \$0.023 per Unity share (Scheme Consideration) under the Scheme of Arrangement.

15. The ROC was approved by Unity shareholders at the special general meeting of Unity held on 20 May 2016.

16. At the scheme meeting held on 20 May 2016 immediately after the special general meeting, Unity Scheme Shareholders approved the Scheme of Arrangement.

17. The Scheme of Arrangement became effective on 26 May 2016 (Effective Date) when Unity lodged an official copy of the court order approving the Scheme of Arrangement and scheme documents with the Australian Securities and Investments Commission.

18. On 1 June 2016 (the Scheme Implementation Date), all of the Unity Shares held on the Record Date by the Unity Scheme Shareholders were transferred to DMM.

19. On 2 June 2016 (the Payment Date), Unity made the payment of the ROC of \$0.01 per Unity share to all of its shareholders.

20. On the Payment Date, payment of the Scheme Consideration was made by Unity to the Unity Scheme Shareholders.

Other information

21. Unity's income was primarily derived from the Henty Gold Mine. With the mine generating minimal profits and annual gold production decreasing, operations at the mine have ceased. The Henty Gold mine has been placed into care and maintenance by Unity.

22. The announcement in respect of the Scheme of Arrangement followed a detailed strategic review undertaken by Unity to examine all alternatives to maximise shareholders value.

23. Neither DM nor any associate of DM that is a Unity shareholder was in a position to control or influence Unity in respect of the ROC, though they were entitled to vote on the ROC like any other Unity shareholder.

24. The ROC was paid by Unity out of available cash. The ROC was recorded on the books by crediting cash and debiting Unity's share capital account.

25. Unity's share capital account is not tainted within the meaning of section 197-50 of the ITAA 1997.

26. Unity's consolidated statement of financial position as at 31 December 2015 discloses issued capital of approximately \$450 million, reserves of approximately \$2.4 million and accumulated losses of approximately \$425 million. The total equity of the company is approximately \$28 million.

27. Unity raised capital by the issuance of ordinary shares in the 2006, 2007 and 2014 income years.

28. Unity paid unfranked final dividends of \$0.005 per share for the years ended 30 June 2009 and 30 June 2010.

29. The transfer of Unity shares from the Unity Scheme Shareholder to DMM under the Scheme of Arrangement occurred at a price substantially aligned with the accounting net asset value of Unity (following the ROC).

Ruling

Return of capital is not a dividend

30. The ROC paid by Unity to the Unity Scheme Shareholders is not a dividend as defined in subsection 6(1) of the ITAA 1936.

The application of section 45B

31. The Commissioner will not make a determination under subsection 45B(3) of the ITAA 1936 that section 45C applies in relation to the ROC received by Unity Scheme Shareholders.

Capital Gains Tax (CGT) consequences

CGT event C2

32. CGT event C2 (section 104-25 of the ITAA 1997) happens when Unity pays the ROC to a Unity Scheme Shareholder in respect of a Unity ordinary share they owned at the Record Date, but ceased to own before the Payment Date.

CGT event A1

33. CGT event A1 (section 104-10 of the ITAA 1997) happens when a Unity Scheme Shareholder disposed of each of their Unity share to DMM under the Scheme of Arrangement.

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34. The capital proceeds received by a Unity Scheme Shareholder is the money received or entitled to receive in respect of the event happening (subsection 116-20(1) of the ITAA 1997). The capital proceeds received by a Unity Scheme Shareholder in respect of CGT event A1 happening is \$0.023 per Unity share.

Commissioner of Taxation

13 July 2016

Appendix 1 – Explanation

ⓘ *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 a dividend

35. The term 'dividend' is defined in subsection 6(1) of the *Income Tax Assessment Act 1936* (ITAA 1936) and includes any distribution made by a company to any of its shareholders. However, paragraph (d) of the definition of 'dividend' excludes a distribution from the meaning of 'dividend' if the amount of the distribution is debited against an amount standing to the credit of the share capital account of the company.

36. 'Share capital account' is defined in section 975-300 of the *Income Tax Assessment Act 1997* (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.

37. Subsection 975-300(3) of the ITAA 1997 broadly states that if a company's share capital account is tainted, that account is taken not to be a share capital account for the purposes of the ITAA 1936 and ITAA 1997 (subject to certain exceptions).

38. The ROC by Unity to the Unity Scheme Shareholders was wholly debited to Unity's share capital account. As Unity's share capital account is not tainted within the meaning of section 197-50 of the ITAA 1997, paragraph (d) of the definition of 'dividend' in subsection 6(1) of the ITAA 1936 applies. Accordingly, the ROC of \$0.01 per Unity share paid to the Unity Scheme Shareholder is not a dividend as defined in subsection 6(1) of the ITAA 1936.

Section 45B – scheme to provide capital benefits

39. Section 45B of the ITAA 1936 is an anti-avoidance provision which, if it applies, allows the Commissioner to make a determination that section 45C applies to treat all or part of the ROC received by a Unity Scheme Shareholder as an unfranked dividend, paid by the company out of profits.

40. Section 45B of the ITAA 1936 applies where certain capital payments are made to shareholders in substitution for dividends. Specifically, the provision applies if:

- (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)).

41. While the ROC satisfies the conditions in paragraphs 45B(2)(a) and 45B(2)(b) of the ITAA 1936, paragraph 45B(2)(c) 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 was entered into or carried out for a more than incidental purpose of enabling the Unity shareholders to obtain a tax benefit.

42. Accordingly, the Commissioner will not make a determination, under subsection 45B(3) of the ITAA 1936, that section 45C applies to the whole, or a part, of the payment of the ROC.

Capital Gains Tax (CGT) consequences

CGT event C2

43. CGT event C2 happens when the ROC is paid to a Unity shareholder that held the Unity share at the Record Date but no longer owned the Unity share at the Payment Date (section 104-25 of the ITAA 1997).

44. All Unity Scheme Shareholders ceased to own their Unity shares in respect of which the ROC was payable on the Scheme Implementation Date of 1 June 2016, prior to the Payment Date of 2 June 2016.

45. As a Unity Scheme Shareholder ceased to own a Unity share in respect of which the ROC was payable, the right to receive the ROC was retained by that shareholder and constituted a separate CGT asset.

46. The right to receive the ROC ended by the right being discharged or satisfied when the payment was made.

47. A Unity Scheme 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. A Unity Scheme Shareholder makes a capital loss if the capital proceeds from the ending of the right are less than the reduced cost base of the right. The capital loss is equal to the amount of the difference (subsection 104-25(3) of the ITAA 1997).

48. In working out the capital gain or capital loss made when CGT event C2 happens, the capital proceeds will be the amount of the ROC paid by Unity, that is, \$0.01 per Unity share (subsection 116-20(1) of the ITAA 1997).

49. The cost base of the Unity Scheme Shareholder's right to receive the ROC 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 Unity 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 Unity Scheme Shareholder disposed of it after the Record Date.

50. Therefore, if the full cost base or reduced cost base of the Unity 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 ROC will generally have a nil cost base. As a result, the Unity Scheme Shareholder will generally make a capital gain equal to the amount of the ROC.

51. As a right to receive the ROC was inherent in the Unity 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).

52. Accordingly, if the Unity share was acquired at least 12 months before the payment of the ROC, 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 may be eligible to be treated as a discount capital gain under Division 115 of the ITAA 1997, provided other conditions of that Division are satisfied.

CGT event A1

53. CGT event A1 happens when a Unity Scheme Shareholder disposed of their Unity shares to DMM under the Scheme of Arrangement (subsections 104-10(1) and 104-10(2) of the ITAA 1997).

54. Under paragraph 104-10(3)(b) of the ITAA 1997, the time of CGT event A1 happening was when DMM became the owner of the relevant Unity shares (that is the Scheme Implementation Date).

55. The capital proceeds received by a Unity Scheme Shareholder is the money received or entitled to receive in respect of the event happening (subsection 116-20(1) of the ITAA 1997). The capital proceeds received by a Unity Scheme Shareholder in respect of CGT event A1 happening is the Scheme Consideration of \$0.023 per Unity share.

56. Under subsection 104-10(4) of the ITAA 1997, a Unity Scheme Shareholder makes a capital gain from CGT event A1 happening if the capital proceeds from the disposal of a Unity share exceeds its cost base. A Unity Scheme Shareholder makes a capital loss if those capital proceeds were less than their Unity share's reduced cost base.

57. A capital gain made when CGT event A1 happens, will be eligible to be treated as a discount capital gain under Division 115 of the ITAA 1997, provided that the Unity share was acquired at least 12 months before the Scheme Implementation Date (subsection 115-25(1) of the ITAA 1997) and the other conditions of that Division are satisfied.

Appendix 2 – Detailed contents list

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References

- Previous draft:*
- Not previously issued as a draft
- Related Rulings/Determinations:*
- TR 2006/10
- Legislative references:*
- ITAA 1936
 - ITAA 1936 6(1)
 - ITAA 1936 45B
 - ITAA 1936 45B(2)(a)
 - ITAA 1936 45B(2)(b)
 - ITAA 1936 45B(2)(c)
 - ITAA 1936 45B(3)
 - ITAA 1936 45B(8)
 - ITAA 1936 45C
 - ITAA 1997
 - ITAA 1997 104-10
 - ITAA 1997 104-10(1)
 - ITAA 1997 104-10(2)
 - ITAA 1997 104-10(3)(b)
 - ITAA 1997 104-10(4)
 - ITAA 1997 104-25
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