


CR 2017/30 - Income tax: Tasmania Mines Limited - selective capital reduction and cancellation of shares

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Class Ruling

Income tax: Tasmania Mines Limited – selective capital reduction and cancellation of shares

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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.

Summary – 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
- Division 16K of Part III of the ITAA 1936
- section 177EA of the ITAA 1936
- section 204-30 of the *Income Tax Assessment Act 1997* (ITAA 1997)

- subsection 207-20(1) of the ITAA 1997
- subsection 207-20(2) of the ITAA 1997.

All subsequent references are to the ITAA 1936 unless otherwise indicated.

Class of entities

3. The class of entities to which this Ruling applies are the ordinary shareholders of Tasmania Mines Limited shares, other than Metroof Industries Pty Ltd (the 'Controlling Shareholder'), who:

- are listed on the share register of Tasmania Mines Limited as at 7:00pm (Sydney time) 19 April 2017, the Participation Record Time
- are residents of Australia as defined in subsection 6(1) at the record date
- participate in the selective capital reduction described in the Scheme part of this Ruling under which their shares will be cancelled, 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 Tasmania Mines Limited shares.

In this Ruling, a person belonging to this class of entities is referred to as an 'Exiting 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 23 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 2016 to 30 June 2017. The Ruling continues to apply after 30 June 2017 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.

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. Tasmania Mines Limited (Tasmania Mines) is an Australian resident public company listed on the ASX since 13 November 1969. It comprises Tasmania Mines and four wholly owned subsidiaries (the Tasmania Mines group).

10. The principal activities of the Tasmania Mines group are the mining and production of magnetite and scheelite including the operating of the crushing and concentrating mill at the Kara Mine in Tasmania, the sale of the group's products and the ongoing exploration and development of mining tenements.

11. The majority shareholder in the Tasmania Mines group of companies is Metroof Industries Pty Ltd (the 'Controlling Shareholder') an Australian resident company. The Controlling Shareholder is a foreign owned investment holding company.

12. The minority shareholders in the Tasmania Mines group of companies (the 'Exiting Shareholders') comprise a mix of individuals, companies and superannuation funds.

13. As at 30 June 2016, Tasmania Mines has 18,252,496 ordinary shares on issue, of which 14,459,910 are owned by the majority/Controlling Shareholder and 3,792,586 shares are owned by the minority (Exiting) shareholders.

14. Tasmania Mines has a single class share capital structure consisting of ordinary shares.

Selective capital reduction

15. On 7 November 2016 Tasmania Mines announced to the ASX its intention to seek shareholder approval to undertake a selective capital reduction in accordance with section 256B and 256C of the *Corporations Act 2001* (Corporations Act), by way of a cancellation of shares owned by the minority (Exiting) shareholders.

16. The selective capital reduction was proposed to be undertaken for the following reasons:

- the Controlling Shareholder wishes to privatise the company and delist it from the ASX, and
- to enable minority shareholders a mechanism to exit the company's share register at a premium to the recent share price.

17. Under the selective capital reduction Tasmania Mines cancelled the 3,792,586 shares owned by the Exiting Shareholders. Exiting Shareholders received consideration of \$1.80 (the Cancellation Payment) for the cancellation of each Tasmania Mines share held at the Participation Record Time which was 7:00pm (Sydney time) on 19 April 2017. Of this amount \$0.30 cents per share will be debited to the Tasmania Mine's share capital account (the 'Capital Component') and \$1.50 will be debited to the Tasmania Mine's retained earnings account (the 'Dividend Component'). The Dividend Component of the Cancellation Payment was a fully franked dividend, with a franking credit of \$0.64 attached.

18. The selective capital reduction has been partly funded by Tasmania Mines cash balance together with an existing undrawn loan facility and a new bank loan facility.

19. The selective capital reduction was subject to shareholder approval and was approved via a resolution passed at a general meeting of all Tasmania Mines shareholders on 21 February 2017 and via a special resolution at a special meeting of minority shareholders held immediately after.

20. On 7 April 2017, Tasmania Mines announced to the ASX that the securities of Tasmania Mines Limited were suspended from quotation at the close of trading on 7 April 2017, in connection with the selective reduction of capital. Following the announcement, Tasmania Mines has:

- successfully completed the selective capital reduction of 3,792,586 Tasmania Mines shares representing approximately 21% of its issued shares
- the final price for the Cancellation Payment was \$1.80 per share, and
- made an application for Tasmania Mines to be delisted from the ASX which is expected to occur by 31 May 2017.

Other matters

21. Tasmania Mines had issued capital of \$9,534,000 and retained earnings of \$48,042,000 as at 30 June 2016.
22. Tasmania Mines paid a yearly dividend of \$0.03 cents per share fully franked in each of the last three years.
23. Tasmania Mine's share capital account is not tainted, as defined in subsection 995-1(1) of the ITAA 1997.

Ruling

Division 16K

24. The selective capital reduction will not be treated as a buy-back for the purposes of Division 16K of Part III.

The Dividend and Capital Components

25. The consideration amount (Cancellation Payment) paid by Tasmania Mines to Exiting Shareholders in respect of the cancellation of a share under the selective capital reduction will be a distribution made by the company. The distribution will be a dividend to the extent that it is not debited to Tasmania Mine's share capital account (paragraphs (a) and (d) of the definition of a 'dividend' in subsection 6(1)). As \$0.30 of the consideration will be debited against Tasmania Mine's share capital account (the 'Capital Component'), the Exiting Shareholders will receive a dividend of \$1.50 (the Dividend Component) for each share cancelled.
26. The Dividend Component will be a frankable distribution pursuant to section 202-40(1) of the ITAA 1997 and will therefore be capable of being franked in accordance with section 202-5 of the ITAA 1997.

Assessability of the Dividend Component for Exiting Shareholders

27. The Dividend Component will be included in the assessable income of resident individual, company and superannuation fund Exiting Shareholders who held their shares on capital and revenue account and who participate in the selective capital reduction, under subsection 44(1).

Shares held on revenue account

28. Where the shares are held as revenue assets, the amount by which the Capital Component (\$0.30) exceeds the cost of each share will be included in the Exiting Shareholder's assessable income under section 6-5 of the ITAA 1997. Correspondingly, if the cost exceeds the Capital Component of \$0.30 per share the difference will be an allowable deduction under section 8-1 of the ITAA 1997.

29. Where the shares are held as trading stock, the Cancellation Payment of \$1.80 per share will be included in assessable income under section 6-5 of the ITAA 1997.

Gross-up and tax offset

30. An amount equal to the franking credit on the Dividend Component (gross-up) will be included in the assessable income of Exiting Shareholders under subsection 207-20(1) of the ITAA 1997.

31. Exiting Shareholders will be entitled to a tax offset under subsection 207-20(2) of the ITAA 1997 equal to the amount of the franking credit on the Dividend Component (tax offset), subject to being a 'qualified person': see paragraph 207-145(1)(a) of the ITAA 1997.

Qualified persons

32. For the purposes of Division 1A of former Part IIAA, Exiting Shareholders are considered to have satisfied the holding period rule under former section 160APHO and therefore be qualified persons (as long as the related payments rule is also met) in relation to the Dividend Component under the selective capital reduction if:

- the shares were acquired no less than 45 days prior to the date of cancellation of the shares under the selective capital reduction, not counting the date of acquisition and the date of disposal
- the Exiting Shareholder has no other positions (for example, an option) in relation to the shares cancelled under the selective capital reduction, and
- the Exiting Shareholder or an associate of the Exiting Shareholder has not made, is not under an obligation to make, nor is likely to make, any related payments.

Refundable tax offset

33. The tax offsets will be subject to the refundable tax offset rules in Division 67 of the ITAA 1997. Certain trustees and corporate tax entities are not entitled to a refundable tax offset because of subsections 67-25(1A) to (1DA) of the ITAA 1997.

Capital gains tax

34. CGT event C2 happens when an Exiting Shareholder's Tasmania Mines shares are cancelled under the selective capital reduction (paragraph 104-25(1)(a) and subsection 104-25(2) of the ITAA 1997).
35. The cancellation of the shares under the selective capital reduction did not happen under a contract. Accordingly, CGT event C2 happens when a Tasmania Mines share ended by being cancelled under the selective capital reduction.
36. The capital proceeds received by an Exiting Shareholder in respect of the cancellation of their Tasmania Mines shares is the Cancellation Payment of \$1.80 per share (subsection 116-20(1) of the ITAA 1997).
37. An Exiting Shareholder will make a capital gain if the capital proceeds for the cancellation of their shares are more than the cost base of their shares. The capital gain is equal to the amount of the excess (subsection 104-25(3) of the ITAA 1997).
38. An Exiting Shareholder will make a capital loss if the capital proceeds from the cancellation of their shares are less than the reduced cost base of their shares. The capital loss is equal to the amount of the difference (subsection 104-25(3) of the ITAA 1997).
39. Any capital gain made by an Exiting Shareholder when CGT event C2 happens is reduced (but not below zero) by the amount of the gain that was included in the assessable income of the shareholder under section 6-5 of the ITAA 1997 or as a dividend under subsection 44(1) (subsections 118-20(2) and 118-20(3) of the ITAA 1997).
40. A capital gain or capital loss made from the cancellation of the shares is disregarded if, at the time of the cancellation, the shares were trading stock (subsection 118-25(1) of the ITAA 1997).
41. Where an Exiting Shareholder acquired their share before 20 September 1985 and the share is not subject to CGT event K6 in section 104-230 of the ITAA 1997, any capital gain is disregarded under subsection 104-135(5) of the ITAA 1997.

The anti-avoidance provisions**Section 45A**

42. The Commissioner will not make a determination under subsection 45A(2) that section 45C of the ITAA 1936 applies to the whole, or any part, of the Capital Component of the Cancellation Payment received by Exiting Shareholders.

Section 45B

43. The Commissioner will not make a determination under subsection 45B(3) that section 45C applies to the whole, or any part, of the Capital Component of the Cancellation Payment received by Exiting Shareholders.

Section 177EA

44. The Commissioner will not make a determination under paragraph 177EA(5)(b) to deny the whole, or any part, of the imputation benefits received in relation to the Dividend Component of the received under the selective capital reduction by Exiting Shareholders.

Section 204-30

45. The Commissioner will not make a determination under subsection 204-30(3) of the ITAA 1997 to deny the whole, or any part, of the imputation benefits received in relation to the Dividend Component received under the selective capital reduction by Exiting Shareholders.

Commissioner of Taxation

17 May 2017

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.*

Division 16K

46. Division 16K of Part III provides for the taxation treatment of share buy-backs. A buy-back is defined as having the meaning given by paragraph 159GZZZK(a) which provides that a purchase is a buy-back where a company buys a share in itself from a shareholder in the company.

47. Tasmania Mines will not be buying back its shares from its Exiting Shareholders. Instead they will be cancelled in accordance with section 256 of the Corporations Act. Therefore, the selective capital reduction will not be treated as a buy-back for the purposes of Division 16K of Part III.

The Dividend and Capital Components

48. The Cancellation Payment received by Exiting Shareholders for each share cancelled under the selective capital reduction comprises two elements:

- A Dividend Component, and
- A Capital Component.

49. The amount of these components is determined in accordance with the definition of 'dividend' in subsection 6(1), having regard to how the company accounts for the selective capital reduction.

Assessability of the Dividend Component for Exiting Shareholders

50. 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) or from an Australian source (if the shareholder is a non-resident of Australia).

51. The definition of 'dividend' in subsection 6(1) has the effect that any distribution made by the company to any of its shareholders, whether in money or property, is a dividend except where the distribution is debited against an amount standing to the credit of the share capital account of the company (paragraphs (a) and (d) of the definition).

52. 'Share capital account' is defined in subsection 975-300(1) of the ITAA 1997 as an account which the 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.

53. Subsection 975-300(3) of the ITAA 1997 states that an account is taken not to be a share capital account if it is tainted. Subsection 197-50(1) 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.

54. The Cancellation Payment of \$1.80 per share is a distribution made by Tasmania Mines to its Exiting Shareholders. \$0.30 of the Cancellation Payment will be debited to Tasmania Mine's untainted 'share capital account'. As such it will not constitute a dividend as defined in subsection 6(1).

55. As the remainder of the Cancellation Payment will be debited to the retained profits account, the shareholders will have received a dividend of \$1.50 per share (Dividend Component).

Shares held on revenue account

56. Exiting Shareholders, who hold their shares as revenue assets, include the difference between the cost of a share and the Cancellation Payment as assessable income or allowable deduction under sections 6-5 and 8-1 of the ITAA 1997.

57. However, section 6-25 of the ITAA 1997 operates so that the Dividend Component (which is assessable under subsection 44(1) of the ITAA 1936) is brought to account once only. Accordingly, where the shares are held as revenue assets, the amount by which the Capital Component (\$0.30 per share) exceeds the cost of each share is included in the shareholder's assessable income under section 6-5 of the ITAA 1997. Correspondingly, if the cost exceeds the Capital Component of \$0.30 per share the difference is an allowable deduction.

58. Where the shares are held as trading stock, the Cancellation Payment of \$1.80 per share is included in assessable income under section 6-5 of the ITAA 1997.

Gross-up and tax offset

59. For all Exiting Shareholders, the Dividend Component will constitute a frankable distribution for the purposes of subsection 202-40(1) of the ITAA 1997, and is capable of being franked in accordance with section 202-5 of the ITAA 1997. Further, the Dividend Component will not be rendered an unfrankable distribution pursuant to the operation of section 202-45 of the ITAA 1997.

60. An amount equal to the franking credit on the Dividend Component (gross-up) will be included in the assessable income of Exiting Shareholders in the year in which the distribution is made under subsection 207-20(1) of the ITAA 1997.

61. Exiting Shareholders will be entitled to a tax offset under subsection 207-20(2) of the ITAA 1997 for the income year in which the distribution is made. The tax offset is equal to the franking credit on the Dividend Component, subject to the shareholder being a 'qualified person': see paragraph 207-145(1)(a) of the ITAA 1997.

Qualified Person

62. Paragraph 207-145(1)(a) of the ITAA 1997 provides that, an entity that is not a 'qualified person' in relation to a franked distribution for the purposes of Division 1A of former Part IIIAA is denied a gross-up and a tax offset. Broadly speaking, to be a 'qualified person' in relation to the dividend paid under the selective capital reduction, the shareholder must satisfy both the holding period rule and the related payments rule.

63. The holding period rule requires shareholders to hold the shares, or the interest in the shares, on which the dividend is paid at risk for a continuous period of at least 45 days. In determining whether a shareholder has satisfied the holding period rule, any days during which there is a materially diminished risk in relation to the relevant shares are not counted. The day of acquisition and the day of disposal of the relevant shares are also not counted.

64. Under former subsection 160APHM(2), a shareholder is taken to have materially diminished the risks of loss and opportunities for gain with respect to shares or interests in shares if the 'net position' of the shareholder results in the shareholder having less than 30% of the risks and opportunities relating to the shares or interest in the shares.

65. An Exiting Shareholder will be a qualified person in relation to the Dividend Component of the selective capital reduction amount if the shares were acquired not less than 45 days prior to the date of cancellation of the shares under the selective capital reduction, not counting the date of acquisition and the date of disposal and the eligible shareholder has no other positions in relation to the shares cancelled under the selective capital reduction.

66. An Exiting Shareholder who acquired shares that are subsequently cancelled under the selective capital reduction less than 45 days prior to the date of cancellation of the shares under the selective capital reduction will not be a qualified person under former section 160APHO in relation to the dividend paid under the selective capital reduction for the purposes of Division 1A of former Part IIIAA.

Refundable tax offset

67. The tax offsets will be subject to the refundable tax offset rules in Division 67 of the ITAA 1997. Certain trustees and corporate tax entities are not entitled to a refundable tax offset because of subsections 67-25(1A) to (1DA) of the ITAA 1997.

Capital gains tax

Time of the CGT event

68. The time of CGT event C2 is when you enter into the contract that results in the asset ending or if there is no contract, when the asset ends (subsection 104-25(2) of the ITAA 1997).

69. The cancellation of the shares under the selective capital reduction did not happen under a contract. Accordingly, CGT event C2 will happen when the shares end by being cancelled under the selective capital reduction.

Capital proceeds

70. The capital proceeds from a CGT event are determined under Division 116 of the ITAA 1997.

71. Subsection 116-20(1) of the ITAA 1997 provides that the capital proceeds from a CGT event are the total of the money received, or entitled to be received, and the market value of any property received, or entitled to be received, in respect of the CGT event happening.

72. The capital proceeds for the cancellation of the shares will be the Cancellation Payment Exiting Shareholders receive or will be entitled to receive in respect of the cancellation, that is, \$1.80 per share.

73. An Exiting Shareholder will make a capital gain if the Cancellation Payment is more than the cost base of their shares under subsection 104-135(3) of the ITAA 1997. The amount of the capital gain is equal to this excess. However, a capital gain is disregarded pursuant to subsection 104-135(5) of the ITAA 1997 if the Exiting Shareholder acquired the share before 20 September 1985, and the share is not subject to CGT event K6 in section 104-230 of the ITAA 1997.

74. The market value substitution rule in section 116-30 of the ITAA 1997 will not apply as the CGT event relates to a share in a company that has at least 300 members and is not an entity that is covered by section 116-35 of the ITAA 1997.

The anti-avoidance provisions

Section 45A

75. Section 45A is an anti-avoidance provision which, if it applies, allows 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 selective capital reduction is treated as an unfranked dividend. Accordingly, the application of this provision to the capital reduction must be considered.

76. 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.

77. Although there will have been a 'provision of capital benefit' (as defined in subsection 45A(3)) to shareholders under the selective capital reduction, the circumstances of the selective capital reduction indicate that there will be no streaming of capital benefits to some shareholders and of dividends to other shareholders. Accordingly, section 45A does not apply.

Section 45B

78. Section 45B applies where certain capital payments are made 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, 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 a taxpayer to obtain a tax benefit (paragraph 45B(2)(c)).

79. In the case of the selective capital reduction, whilst the conditions of paragraphs 45B(2)(a) and 45B(2)(b) will have been met, the requisite purpose of enabling the Exiting Shareholder to obtain a tax benefit – by way of capital distribution – will not be present.

80. Having regard to the relevant circumstances of the scheme, set out in subsection 45B(8), it is apparent that the inclusion of a capital element in the consideration for the selective capital reduction will be appropriate. Further, the Capital Component of the selective capital reduction amount cannot be said to be attributable to the profits of the company, nor does the pattern of distributions indicate that it will be paid in substitution for a dividend. Accordingly, section 45B does not apply.

Section 177EA

81. Section 177EA is a general anti-avoidance provision that applies to a wide range of schemes to obtain a tax advantage in relation to imputation benefits. In essence, it applies to schemes for the disposition of shares or an interest in shares where a franked distribution is paid or payable in respect of the shares or an interest in shares. This would include a capital reduction with a franked dividend component.

82. Specifically, subsection 177EA(3) provides that section 177EA applies if:

- (a) there is a scheme for a disposition of membership interests, or an interest in membership interests, in a corporate tax entity; and
- (b) either:
 - (i) a frankable distribution has been paid, or is payable or expected to be payable, to a person in respect of the membership interests, or
 - (ii) a frankable distribution has flowed indirectly, or flows indirectly or is expected to flow indirectly, to a person in respect of the interest in membership interests, as the case may be; and
- (c) the distribution was, or is expected to be, a franked distribution or a distribution franked with an exempting credit; and
- (d) except for this section, the person (the 'relevant taxpayer') would receive, or could reasonably be expected to receive, imputation benefits as a result of the distribution; and
- (e) 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 an imputation benefit.

83. In the present case the conditions of paragraphs 177EA(3)(a) to (d) are satisfied. Accordingly, the issue is whether, having regard to the relevant circumstances of the scheme, it would be concluded that, on the part of Tasmania Mines, its shareholders or any other person, there is a more than incidental purpose of conferring an imputation benefit under the scheme. Under this scheme the relevant taxpayer is an Exiting Shareholder and the scheme comprises the circumstances surrounding the Tasmania Mines selective capital reduction.

84. In arriving at a conclusion the Commissioner must have regard to the relevant circumstances of the scheme which include, but are not limited to, the circumstances set out in subsection 177EA(17). The relevant circumstances encompass a range of circumstances which, taken individually or collectively, could indicate the requisite purpose. Due to the diverse nature of these circumstances, some may not be present at any one time in any one scheme.

85. The purpose of the selective capital reduction in this case is to effectively privatise Tasmania Mines. The overriding purpose of the selective capital reduction is to cancel the interests held by the minority shareholders in order to privatise the company. Having regard to the relevant circumstances of the scheme, the Commissioner has come to the view that the requisite purpose is not present and accordingly will not make a determination under paragraph 177EA(5)(b).

Section 204-30

86. 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:

- an imputation benefit is, or apart from that section would be, received by a member of the entity as a result of the distribution or distributions (paragraph 204-30(1)(a) of the ITAA 1997)
- the member would derive a greater benefit from franking credits than another member of the entity (paragraph 204-30(1)(b) of the ITAA 1997), and
- 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) of the ITAA 1997).

87. Relevantly, if section 204-30 of the ITAA 1997 applies the Commissioner is vested with a discretion under subsection 204-30(3) to make a determination in writing either:

- that a specified franking debit arises in the franking account of the entity, for a specified distribution or

- other benefit to a disadvantaged member (paragraph 204-30(3)(a) of the ITAA 1997), or
- that no imputation benefit is to arise in respect of any streamed distributions made to a favoured member and specified in the determination (paragraph 204-30(3)(c) of the ITAA 1997).

88. For section 204-30 of the ITAA 1997 to apply, members to whom distributions are streamed must derive a greater benefit from imputation benefits than other members. The words 'derives a greater benefit from franking credits' (imputation benefits) are defined in subsection 204-30(8) by reference to the ability of the members to fully utilise imputation benefits.

89. Under the selective capital reduction, Exiting Shareholders will receive an imputation benefit as a result of the Dividend Component; the resident shareholder in the form of a tax offset (paragraph 204-30(6)(a) of the ITAA 1997) and the non-resident shareholders in the form of an exemption from dividend withholding tax (paragraph 204-30(6)(e) of the ITAA 1997). The resident members will derive a greater benefit from franking credits than the non-resident members. However, as the Dividend Component will be franked to the same extent and paid to all Exiting Shareholders and having regard to the profile of Tasmania Mine's shareholders, it is concluded that Tasmania Mines has not directed the flow of distributions in such a manner as to ensure that imputation benefits are derived by members who derive greater benefit from franking credits, while other members receive lesser or no imputation benefits.

90. Having regard to all of the relevant circumstances the Commissioner has formed the view that section 204-30 of the ITAA 1997 does not apply to the selective capital reduction.

Appendix 2 – Detailed contents list

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- Previous draft:*
- ITAA 1997 104-25(3)
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- ITAA 1997 104-230
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 - ITAA 1997 116-20(1)
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NO: 1-AOCS7JH
 ISSN: 2205-5517
 ATOLaw topic: Income tax ~~ Capital management ~~ Returning capital
 ~~ Share capital return

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