

CR 2020/51 - Consolidated Financial Holdings Limited - return of capital



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Class Ruling

Consolidated Financial Holdings Limited – return of capital

❶ Relying on this Ruling

This publication (excluding appendix) is a public ruling for the purposes of the *Taxation Administration Act 1953*.

If this Ruling applies to you, and you correctly rely on it, we will apply the law to you in the way set out in this Ruling. That is, you will not pay any more tax or penalties or interest in respect of the matters covered by this Ruling.

Further, if we think that this Ruling disadvantages you, we may apply the law in a way that is more favourable to you.

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What this Ruling is about

1. This Ruling sets out the income tax consequences for shareholders of Consolidated Financial Holdings Limited (CFH Ltd) (previously Chant West Holdings Limited) at 3 September 2020 (Record Date) who received a return of capital payment of 11 cents per ordinary CFH Ltd share on 8 September 2020 (Payment Date).
2. Full details of this return of capital arrangement are set out in paragraphs 13 to 37 of this Ruling.
3. All legislative references in this Ruling are to provisions of the *Income Tax Assessment Act 1997* unless otherwise indicated.

Who this Ruling applies to

4. This Ruling applies to you if you:
 - were registered on the CFH Ltd share register on the Record Date, and
 - held your CFH Ltd shares on capital account. That is, you did not hold your CFH Ltd shares as revenue assets (as defined in section 977-50) or as trading stock (as defined in subsection 995-1(1)) on the Record Date.

5. This Ruling does not apply to you if you are subject to the taxation of financial arrangements rules in Division 230 in relation to the scheme outlined in paragraphs 13 to 37 of this Ruling.

Note: Division 230 will not apply to you if you are an individual, unless you have made an election for it to apply.

When this Ruling applies

6. This Ruling applies from 1 July 2020 to 30 June 2021.

Ruling

Return of capital is not a dividend

7. No part of the return of capital payment will be included in your assessable income as a dividend under section 44 of the *Income Tax Assessment Act 1936* (ITAA 1936).

Sections 45A, 45B and 45C of the ITAA 1936 do not apply

8. The Commissioner will not make a determination under either subsection 45A(2) of the ITAA 1936 or paragraph 45B(3)(b) of the ITAA 1936 that section 45C of the ITAA 1936 applies to any part of the return of capital CFH Ltd paid to you on the Payment Date.

Capital gains tax consequences

CGT event G1

9. CGT event G1 (section 104-135) happened on the Payment Date when CFH Ltd paid you the return of capital of 11 cents per share in respect of the CFH Ltd shares you owned at the Record Date and continued to own at the Payment Date.

CGT event C2

10. CGT event C2 (section 104-25) happened when CFH Ltd paid you a return of capital of 11 cents per share in respect of CFH Ltd shares you owned at the Record Date and ceased to own before the Payment Date.

Discount capital gain

11. You can treat a capital gain made when CGT event G1 or CGT event C2 happened to your CFH share as a discount capital gain if you acquired the CFH share at least 12 months before the Payment Date (subsection 115-25(1)), provided the other conditions in Subdivision 115-A are satisfied.

Foreign resident shareholders are able to disregard capital gains tax

12. You can disregard any capital gain made from CGT event G1 or capital gain or capital loss made from CGT event C2, where you are a foreign resident and your CFH Ltd shares or right to receive the relevant return of capital is not taxable Australian property (section 855-10).

Scheme

13. The following description of the scheme is based on information provided by the applicant. If the scheme is not carried out as described, this Ruling cannot be relied upon.

Background

14. Chant West Holdings Limited was incorporated in Australia in 2006 and was listed on the Australian Securities Exchange (ASX) in 2007.

15. Chant West Holdings Limited changed its name to CFH Ltd on 1 July 2020.

16. CFH Ltd provided research, consulting and software services to the superannuation and financial planning industries through two core businesses operated through its wholly-owned subsidiaries:

- Chant West Pty Ltd, a superannuation research and consultancy business, and
- Enzumo Corporation Pty Ltd and Enzumo Consulting Pty Ltd, a consulting and software business that conducted in-depth analysis for superannuation and financial planning businesses and creates tailored technology solutions to help them operate efficiently and compliantly.

17. As at 31 December 2019, CFH Ltd's share capital was made up entirely of 123,923,798 fully-paid ordinary shares. Subsequent to this, CFH Ltd issued 2,904,000 ordinary shares to performance rights holders on 24 February 2020, bringing the total number of ordinary shares on issue to 126,827,798.

18. As at 11 March 2020, the top 20 shareholders held 67.11% of the shares on issue and a minority group of non-residents held 1.7% of the shares on issue.

19. On 22 July 2020, CFH Ltd cancelled one million ordinary shares, which were inadvertently issued on 24 February 2020 to a director as the result of a drafting error, reducing the number of ordinary shares on issue to 125,827,798.

Return of capital payment

20. On 18 February 2020, CFH Ltd announced to the ASX its proposal to sell the assets and business operated by Chant West Pty Ltd (the Chant West sale) to a wholly-owned subsidiary of Zenith Investment Partners Pty Ltd (the Buyer).

21. The Buyer agreed to purchase Chant West Pty Ltd for the headline purchase price of \$12 million less working capital adjustments (as defined under the business sale agreement).

22. CFH Ltd obtained shareholder approval for the Chant West sale at an extraordinary general meeting on 31 March 2020.

23. The Chant West sale was completed under the business sale agreement on 30 June 2020.

24. CFH Ltd used net funds of \$11,008,060 from the Chant West sale, and surplus cash of \$2,832,998 retained as working capital, to return capital to its shareholders. CFH Ltd paid a return of capital of 11 cents per share on the Payment Date, amounting to a total return of capital to shareholders of \$13,841,058.

25. All shareholders listed on CFH Ltd's share register on the Record Date, including non-resident shareholders, were permitted to participate in the return of capital.

26. The return of capital was distributed to shareholders on an equal basis. CFH Ltd did not cancel the shares of its shareholders.

27. The total amount of the return of capital payment of \$13,841,058 was debited against CFH Ltd's share capital account and was funded entirely from existing cash reserves.

28. There was no change in either the number of CFH Ltd shares on issue or the proportionate interest of each shareholder in CFH Ltd.

Other matters

29. CFH Ltd's half-yearly report for the half-year ended 31 December 2019 disclosed:

- a net profit of \$146,620
- issued capital of \$21,733,287
- accumulated losses of \$13,699,007, and
- total equity of \$8,391,765.

30. On 17 June 2020, CFH Ltd sold all its shares in Enzumo Corporation Pty Ltd and Enzumo Consulting Pty Ltd to Centrepont Alliance Limited (the Enzumo sale) for \$1.5 million (subject to a working capital adjustment).

31. Net proceeds from the Enzumo sale were \$1.325 million. Surplus funds from the Enzumo sale were used for the settlement sum for the Chant West sale and working capital.

32. CFH Ltd's quarterly activities report at 30 June 2020 disclosed a cash balance of approximately \$16 million. CFH Ltd received a net cash inflow of \$11.4 million from the Chant West sale and Enzumo sale, including \$1.1 million of deal costs associated with the sales paid in the June 2020 quarter.

33. CFH Ltd made a net profit of approximately \$6 million from the Chant West sale, reducing its accumulated losses to \$7.7 million.

34. CFH Ltd has not made any returns of capital or declared any dividends since its listing on the ASX.

35. CFH Ltd's share capital account, as defined in section 975-300, is not tainted within the meaning of Division 197.

36. After the Chant West sale and the Enzumo sale, CFH Ltd has no active business. CFH Ltd's assets include cash and an Australian Financial Services License.

37. On the Record Date, the sum of the market values of the assets of CFH Ltd and its subsidiaries that are taxable Australian real property did not exceed the sum of the market values of their other assets for the purposes of section 855-30.

Appendix – Explanation

❶ *This Explanation 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.*

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Return of capital is not a dividend

38. Subsection 44(1) of the ITAA 1936 includes in a shareholder's assessable income any dividends paid to the shareholder out of profits derived by the company from any source if the shareholder is a resident of Australia.

39. The term 'dividend' is defined in subsection 6(1) of the 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 company's share capital account.

40. The term 'share capital account' is defined in section 975-300 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.

41. Subsection 975-300(3) provides that an account is generally taken not to be a share capital account if it is tainted. CFH Ltd has confirmed that its share capital account is not tainted within the meaning of Division 197.

42. The return of capital was recorded as a debit to CFH Ltd's untainted share capital account. As such, paragraph (d) of the definition of dividend in subsection 6(1) of the ITAA 1936 applies and the return of capital is not a dividend.

Sections 45A, 45B and 45C of the ITAA 1936 do not apply

43. 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. The effect of such a determination is that all or part of the distribution of capital received under the return of capital is treated as an unfranked dividend.

44. Section 45A of the ITAA 1936 applies when a company streams the provision of 'capital benefits' to shareholders who would derive a greater benefit from the capital benefits than other shareholders who received, or are likely to receive, dividends. Paragraph 45A(3)(b) of the ITAA 1936 provides that capital benefits include the distribution of share capital.

45. Although a capital benefit was provided to CFH Ltd shareholders, the circumstances of the return of capital indicate that there was no streaming of capital benefits to some CFH Ltd shareholders and dividends to other CFH Ltd shareholders.

46. Accordingly, the Commissioner will not make a determination under subsection 45A(2) of the ITAA 1936 that section 45A of the ITAA 1936 applies in relation to the whole, or a part, of the return of capital.

47. Section 45B of the ITAA 1936 applies where certain capital payments are made to shareholders in substitution for dividends. In broad terms, section 45B of the ITAA 1936 applies where:

- there is a scheme under which a person is provided with a capital benefit by a company
- under the scheme, a taxpayer (relevant taxpayer), who may or may not be the person provided with the capital benefit, obtains a tax benefit, 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 relevant taxpayer to obtain a tax benefit.

48. The return of capital satisfies the first two conditions. However, having regard to the relevant circumstances of the scheme, it cannot be concluded that the scheme was entered into or carried out for a more than incidental purpose of enabling CFH Ltd shareholders to obtain a tax benefit.

49. Accordingly, the Commissioner will not make a determination under subsection 45B(3) of the ITAA 1936 that section 45C of the ITAA 1936 applies in relation to the whole, or a part, of the return of capital.

CGT events G1 or C2 happened

CGT event G1

50. CGT event G1 happens if a company makes a payment to a shareholder in respect of a share they own in the company, some or all of the payment (the non-assessable part) is not a dividend, 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 (section 104-135).

51. CGT event G1 happened when CFH Ltd made the return of capital to you in respect of CFH Ltd shares you owned at the Record Date and continued to own at the Payment Date (section 104-135).

52. You will make a capital gain from CGT event G1 happening if the amount of the return of capital of 11 cents per share is more than the cost base of your CFH Ltd share. If so, the capital gain is equal to the amount of the excess and the cost base and reduced cost base of the CFH Ltd share is reduced to nil (subsection 104-135(3)). No capital loss can be made from CGT event G1 (Note 1 to subsection 104-135(3)).

53. If the amount of the return of capital of 11 cents per share is not more than the cost base of your CFH Ltd share, the cost base and reduced cost base of the share are reduced (but not less than nil) by the amount of the return of capital (subsection 104-135(4)).

CGT event C2

54. If, after the Record Date but before the Payment Date, you ceased to own a CFH Ltd share in respect of which the return of capital was payable, the right to receive the return of capital in respect of that share is retained by you and is a separate CGT asset from the CFH Ltd share.

55. CGT event C2 happened when the return of capital was made. The right to receive the return of capital, being an intangible asset, ended by the right being discharged or satisfied when the return of capital was made (section 104-25).

56. You will make a capital gain under CGT event C2 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. You will make 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)).

57. In working out the capital gain or capital loss when CGT event C2 happens, the capital proceeds are equal to the amount of the return of capital (11 cents per share) (subsection 116-20(1)).

58. The cost base of your right to receive each return of capital is worked out under Division 110 (modified by Division 112). The cost base of the right does not include the cost base or reduced cost base of the share previously owned by you to the extent that it was applied in working out a capital gain or capital loss made when a CGT event happened to the share, for example, when you disposed of the share after the Record Date and before the Payment Date. Therefore, if the cost base or reduced cost base of the share previously owned by you has been fully applied in working out a capital gain or capital loss on the share, the right to receive the return of capital will have a nil cost base. As a result, you will, in those circumstances, make a capital gain equal to the capital proceeds, being 11 cents per CFH Ltd share owned at the Record Date.

59. For the purposes of Subdivision 109-A, you are considered to have acquired the right at the time when you acquired your CFH Ltd share. Therefore, you can treat a capital gain made when CGT event C2 happened to your CFH Ltd share if you acquired your CFH Ltd share at least 12 months before the Payment Date (subsection 115-25(1)) provided the other conditions in Subdivision 115-A are satisfied.

Foreign resident shareholders able to disregard capital gains tax

60. Under subsection 855-10(1), 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.

61. The term 'taxable Australian property' is defined in the table in section 855-15. The table sets out 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 items 1, 2 or 5
Item 4	an option or right to acquire a CGT asset covered by items 1, 2 or 3
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)

62. If you are a foreign resident, or the trustee of a foreign resident trust for CGT purposes, you can disregard a capital gain made when CGT event G1 happened to your CFH Ltd share under subsection 855-10(1) because your CFH Ltd share was not an indirect Australian real property interest, provided also that your CFH Ltd share:

- had not been used at any time by you in carrying on a business through a permanent establishment in Australia (table item 3 of section 855-15), or
- was not covered by subsection 104-165(3) (table item 5 of section 855-15, about individuals choosing to disregard capital gains upon ceasing to be Australian residents).

63. If you are a foreign resident, or the trustee of a foreign resident trust for CGT purposes, you cannot disregard a capital gain or capital loss made when CGT event C2 happened to your right to receive the return of capital if the right:

- had been used at any time by you in carrying on a business through a permanent establishment in Australia (table item 3 of section 855-15), or
- was covered by subsection 104-165(3) (table item 5 of section 855-15, about individuals choosing to disregard capital gains upon ceasing to be Australian residents).

References*Previous draft:*

Not previously issued as a draft

- ITAA 1997 104-165(3)
- ITAA 1997 Div 110
- ITAA 1997 Div 112
- ITAA 1997 Subdiv 115-A
- ITAA 1997 115-25(1)
- ITAA 1997 116-20(1)
- ITAA 1997 Div 197
- ITAA 1997 Div 230
- ITAA 1997 855-10
- ITAA 1997 855-10(1)
- ITAA 1997 855-15
- ITAA 1997 855-30
- ITAA 1997 975-300
- ITAA 1997 975-300(3)
- ITAA 1997 977-50
- ITAA 1997 995-1(1)
- TAA 1953

Legislative references:

- ITAA 1936 6(1)
- ITAA 1936 44
- ITAA 1936 44(1)
- ITAA 1936 45A
- ITAA 1936 45A(2)
- ITAA 1936 45A(3)(b)
- ITAA 1936 45B
- ITAA 1936 45B(3)
- ITAA 1936 45B(3)(b)
- ITAA 1936 45C
- ITAA 1936 47
- ITAA 1997 104-25
- ITAA 1997 104-25(3)
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- ITAA 1997 104-135(3)
- ITAA 1997 104-135(4)

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NO: 1-L4LKL3N

ISSN: 2205-5517

BSL: PGI

ATOlaw topic: Income tax ~~ Assessable income ~~ Dividend income ~~ Dividend income
Income tax ~~ Capital gains tax ~~ CGT events ~~ CGT events C1 to C3 –
end of a CGT asset

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