


CR 2015/38 - Income tax: CIC Australia Limited off-market share buy-back

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Class Ruling

Income tax: CIC Australia Limited off-market share buy-back

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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 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 44(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 90 of the ITAA 1936
- subsection 95(1) of the ITAA 1936
- paragraph 128B(3)(ga) of the ITAA 1936
- Division 16K of the ITAA 1936
- Division 1A of former Part IIIA of the ITAA 1936

- Section 177EA of the ITAA 1936
- section 6-5 of the *Income Tax Assessment Act 1997* (ITAA 1997)
- Division 67 of the ITAA 1997
- section 104-10 of the ITAA 1997
- subsection 104-165(3) of the ITAA 1997
- subsection 106-5 of the ITAA 1997
- section 116-20 of the ITAA 1997
- section 118-20 of the ITAA 1997
- section 118-25 of the ITAA 1997
- section 202-5 of the ITAA 1997
- section 202-40 of the ITAA 1997
- section 202-45 of the ITAA 1997
- subsection 204-30(3)(c) of the ITAA 1997
- Division 207 of the ITAA 1997
- section 855-10 of the ITAA 1997
- section 855-15 of the ITAA 1997
- section 855-25 of the ITAA 1997, and
- section 960-195 of the ITAA 1997.

All legislative references in this Ruling are to the ITAA 1997 unless otherwise stated.

Class of entities

3. The class of entities to which this ruling applies is the shareholders of CIC Australia Limited (CIC) who:

- (a) are either:
 - (i) 'resident of Australia' as the term is defined in subsection 6(1) of the ITAA 1936 (Resident Shareholder), or
 - (ii) 'non-resident of Australia' as that term is defined in subsection 6(1) of the ITAA 1936 who do not hold their CIC Shares through an Australian permanent establishment of that shareholder (Non-Resident Shareholder)
- (b) disposed of their ordinary shares (CIC Shares) under the CIC off-market share buy-back which was announced by CIC on 25 February 2015 (the Buy-Back) as part of the Scheme of Arrangement, and

- (c) are not subject to the taxation of financial arrangements rules in Division 230 in relation to gains and losses on their CIC Shares.

(Note – Division 230 will generally not apply to individuals, unless they have made an election for it to apply to them)

In this Ruling, these ordinary shareholders of CIC (other than Peet Limited (Peet)) are referred to 'Participating Shareholders'.

Qualifications

4. 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 7 to 27 of this Ruling.

5. 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

6. This Ruling applies from 1 July 2014 to 30 June 2015. The Ruling continues to apply after 30 June 2015 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

7. 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:

- CIC Australian Securities Exchange (ASX) Announcement made on 25 February 2015
- The application for a Class Ruling received on 11 March 2015
- The Independent Expert's Report received on 20 March 2015, and

- CIC Scheme Booklet received on 8 April 2015.

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

8. CIC is a public company listed on the ASX and is a resident of Australia for the purposes of subsection 6(1) of the ITAA 1936.
9. As at 31 October 2014, CIC had:
 - 126,991,118 ordinary shares on issue
 - \$62,629,669 in share capital, and
 - \$41,890,557 in retained earnings.
10. The shareholders of CIC (Shareholders) include a mixture of Resident Shareholders and Non-Resident Shareholders. Non-Resident Shareholders account for less than 1% of total CIC shareholders.
11. The majority shareholder of CIC is Peet which holds approximately 86% of the CIC Shares.
12. Notwithstanding that CIC is currently listed on the ASX, it is considered to be an illiquid stock. Given the low level of trading in the CIC Shares, CIC has been considering whether it would be appropriate to delist CIC from the ASX to reduce holding and compliance costs.

The Buy-Back

13. On 25 February 2015, CIC announced its proposal to enter into a Scheme of Arrangement (SOA) pursuant to *Corporations Act 2001* with the Participating Shareholders for the selective off-market buy-back and cancellation of the CIC Shares acquired by the company from them.
14. Peet was not entitled to vote on the Buy-Back pursuant to the SOA.
15. It was expected that the delisting of CIC will occur following the Buy-Back.
16. CIC anticipated that the Buy-Back will:
 - provide a liquidity mechanism for the Participating Shareholders to exit their investment
 - allow Participating Shareholders to exit their investment on the same terms (thereby not providing any preferential treatment to any particular Shareholders who wish to exit), and
 - allow Participating Shareholders to exit their investment by way of a streamlined process.

17. Under the Buy-Back, Participating Shareholders were entitled to receive a cash payment of \$0.827 (Buy-Back Price) for each CIC Share held at the Record Date (7:00pm on 21 May 2015). This amount consisted of:

- A return of capital \$0.49 per share which will be debited to CIC's share capital account, and
- A fully franked dividend of \$0.337 per share which will be debited to CIC's retained earnings account.

18. The Buy-Back Price represented the approximate net tangible assets per CIC Share as set out in the CIC financial statements for the half-year ended 31 December 2014.

19. The company applied the average capital per share method in determining the proportion of share capital represented by the Buy-Back Price.

20. All shares bought back under the Buy-Back will be cancelled.

21. Any Shareholder who did not participate in the Buy-Back will not receive any other dividend or distribution by way of compensation for not participating in the Buy-Back.

22. The Buy-Back will be funded by CIC from borrowings.

Other matters

23. CIC did not buy back shares at a Buy-Back price that exceeded the market value of a CIC Share or at discount greater than 14% to the market value of a CIC Share.

24. On 26 May 2015, CIC announced that:

- it had successfully completed the Buy-Back of 17,717,732 CIC Shares, and
- the total amount of capital repurchased under the Buy-Back was \$14,652,564.36 representing 13.95 % of the issued share capital of CIC.

25. CIC's dividend policy was not affected by the Buy-Back.

26. CIC's share capital account is not (and has never been) tainted for the purposes of the ITAA 1997.

27. The closing balance of CIC's franking account on 31 December 2014 was \$22,200,277.

Ruling

Off-market purchase

28. For the purposes of Division 16K of the ITAA 1936, the Buy-Back is an off-market purchase within the meaning given by paragraph 159GZZZK(d) of the ITAA 1936.

The Dividend Component

29. Participating Shareholders are taken to have been paid a dividend of \$0.337 (the Dividend Component) out of the profits of CIC on 26 May 2015 for each CIC Share bought back under section 159GZZZP of the ITAA 1936.

30. The Dividend Component is a frankable distribution pursuant to section 202-40, and is capable of being franked in accordance with section 202-5.

31. The difference between the purchase price and the Dividend Component is not a dividend for income tax purposes (subsection 159GZZZP(2) of the ITAA 1936).

The Capital Component

32. For the purposes of subsection 159GZZZP(1) of the ITAA 1936, the amount of \$0.49 will represent the Capital Component of the purchase price for each CIC Share bought back.

Assessability of the Dividend Component and tax offset

Direct distributions

33. The Dividend Component of \$0.337 and, subject to being a 'qualified person', the amount of the franking credit on the Dividend Component, is included in the assessable income of Australian resident individual and corporate shareholders, and trustees of resident complying superannuation funds who participated in the Buy-Back in the income year in which the Buy-Back occurred (subsection 44(1) of the ITAA 1936 and subsection 207-20(1)).

34. Participating Shareholders will be entitled to a tax offset under subsection 207-20(2) equal to the amount of the franking credit attached to the Dividend Component, subject to being a 'qualified person'.

Indirect distributions

Partnerships

35. The Dividend Component of \$0.337 per share and, subject to being a qualified person, the amount of the franking credit attached to the Dividend Component is included in the assessable income of a Participating Shareholder that is a partnership for the purposes of computing the net income of the partnership under section 90 of the ITAA 1936.

Trusts

36. The Dividend Component of \$0.337 per share and, subject to being a qualified person, the amount of the franking credit attached to the Dividend Component is included in the assessable income of a Participating Shareholder that is a trustee of a trust for the purposes of computing the net income of the trust under subsection 95(1) of the ITAA 1936.

Partners and Beneficiaries

37. Subsections 207-35(3) to (6) set out the circumstances in which a partner or beneficiary to whom a franked distribution flows indirectly is required to gross up their assessable income for their share of the franking credit on the franked distribution.

38. Where the franked distribution flows indirectly (within the meaning of Subdivision 207-B) through a trust or partnership to a resident that is an individual, a corporate tax entity (at the time the distribution flows indirectly to it) or a trustee mentioned in paragraphs 207-45(c), (ca) or (d), the entity will, subject to the qualified person rule, be entitled to a tax offset equal to the entity's share of the franking credit on the franked distribution (section 207-45).

Refundable tax offset

39. The tax offsets are subject to the refundable tax offset rules in Division 67. Certain trustees and corporate tax entities are not entitled to the refundable tax offset rules in accordance with subsections 67-25(1A) to (1D).

Non-resident Participating Shareholders

40. As the Dividend Component is fully franked, non-resident Participating Shareholders are not liable for Australian withholding tax on the Dividend Component (paragraph 128B(3)(ga) of the ITAA 1936).

Sale Consideration

41. A Participating Shareholder is taken to have received \$0.49 as the consideration in respect of each CIC Share bought back under the Buy-Back (Sale Consideration) on 26 May 2015 in accordance with section 159GZZZQ of the ITAA 1936, unless the Participating Shareholder is a corporate tax entity to which subsections 159GZZZQ(8) and (9) of the ITAA 1936 apply.

42. The income tax treatment of the Sale Consideration for a Participating Shareholder will depend on whether the sale is on capital account or on revenue account.

Shares held on capital account

43. The shares are taken to have been disposed of for CGT purposes on 26 May 2015 pursuant to section 104-10 (CGT event A1).

44. The Sale Consideration of \$0.49 per share represents the capital proceeds for CGT purposes pursuant to section 116-20. A Participating Shareholder (other than a partnership) will make a capital gain when CGT event A1 happens if the Sale Consideration per share exceeds the cost base of that share. The capital gain is the amount of the excess. Similarly, a Participating Shareholder (other than a partnership) will make a capital loss if the Sale Consideration per share is less than the reduced cost base of the share (subsection 104-10(4)).

45. Each partner in a partnership has a separate cost base and reduced cost base for the partner's interest in each CIC Share sold into the Buy-Back by the partnership (subsection 106-5(2)). Each partner is allocated an appropriate share of the Sale Consideration received by the partnership for the disposal of CIC Shares into the Buy-Back.

Shares held on revenue account

46. Where shares were held as trading stock, the Sale Consideration of \$0.49 per share is included in assessable income of a Participating Shareholder under section 6-5. Participating Shareholders (other than partnerships) who held shares as trading stock will also make a capital gain or capital loss calculated as discussed at paragraph 45 of this Ruling. However, under section 118-25 any capital gain or capital loss these Participating Shareholders make will be disregarded if at the time of the CGT event the shares are held by them as trading stock. There is a similar exemption for partners in partnerships (paragraph 118-25(1)(b)).

47. Where shares were held as revenue assets, but were not trading stock, the amount by which the Sale Consideration of \$0.49 per share exceeds the cost of each share is included in the Participating Shareholder's assessable income. Correspondingly, if the cost exceeds the Sale Consideration of \$0.49 per share the difference is an allowable deduction. Where the Sale Consideration per share exceeds the cost base of that share, the Participating Shareholders (other than partnerships) will also make a capital gain.

48. However, under section 118-20 any capital gain the Participating Shareholders make will be reduced if, because of the event, an amount has otherwise been included in assessable income. The capital gain will be reduced to zero if the capital gain does not exceed the amount otherwise included in assessable income (subsection 118-20(2)).

49. If the capital gain exceeds the amount otherwise included in assessable income, the capital gain will be reduced by the amount otherwise included in assessable income (subsection 118-20(3)). There is a similar reduction for partners in partnerships (paragraph 118-20(1)(b), paragraph 118-20(2)(b) and subsection 118-20(3)).

Foreign resident Participating Shareholders: CGT consequences

50. A Participating Shareholder who was a foreign resident, or the trustee of a foreign trust for CGT purposes, just before CGT event A1 happened will disregard a capital gain or capital loss made from CGT event A1, unless the CIC Share:

- has been used at any time by the Participating Shareholder in carrying on a business through a permanent establishment in Australia (item 3 of the table in section 855-15), or
- is covered by subsection 104-165(3) (item 5 of the table in section 855-15).

Qualified persons

51. For the purposes of paragraph 207-145(1)(a) which refers to Division 1A of former Part IIIAA of the ITAA 1936, Participating Shareholders in the Buy-Back under the SOA will be considered to satisfy the holding period rule under former section 160APHO of the ITAA 1936, and be qualified persons (as long as the related payments rule is also met) in relation to the Dividend Component received under the Buy-Back, if:

- the shares sold into the Buy-Back were acquired on or before 10 April 2015, and
- during the period when the shares were held the Participating Shareholders had sufficient risks of loss or opportunities for gain in respect of the shares (as defined in former section 160APHM of the ITAA 1936) for a continuous period of at least 45 days. Neither the announcement of the Buy-Back, the making of an invitation to shareholders to offer to sell their CIC Shares nor the making of an offer by a shareholder to CIC in respect of a CIC Share will affect whether the shares bought back under the Buy-Back are held 'at risk' for the purposes of Division 1A of former Part IIIAA.

The anti-avoidance provisions

52. The Commissioner will not make a determination under subsections 45A(2) or 45B(3) of the ITAA 1936 that section 45C, of the ITAA 1936, applies to the whole, or any part, of the Capital Component of the Buy-Back Price received by Participating Shareholders. Accordingly, no part of the Capital Component will be taken to be a dividend for income tax purposes.

53. The Commissioner will not make a determination under paragraph 177EA(5)(b) of the ITAA 1936 to deny the whole, or any part, of the imputation benefits received in relation to the Dividend Component of the Buy-Back Price by Participating Shareholders.

54. The Commissioner will not make a determination under paragraph 204-30(3)(c) to deny the whole, or any part, of the imputation benefits received in relation to the Dividend Component of the Buy-Back Price by Participating Shareholders.

Commissioner of Taxation

10 June 2015

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.*

Off-market purchase

55. For the purposes of Division 16K of the ITAA 1936, where a company buys a share in itself from a shareholder the purchase is a 'buy-back' (paragraph 159GZZZK(a) of the ITAA 1936).

56. Division 16K of the ITAA 1936 categorises a buy-back as either an 'on-market purchase' or an 'off-market purchase'.

57. A buy-back is an on-market purchase if the share bought back is listed for quotation in the official list of a stock exchange in Australia or elsewhere, and the buy-back is made in the ordinary course of trading on that stock exchange (paragraph 159GZZZK(c) of the ITAA 1936). A buy-back that is not an on-market purchase is an off-market purchase (section 159GZZZK(d) of the ITAA 1936).

58. Although CIC's ordinary shares are listed for quotation in the official list of the ASX, the Buy-Back was not made in the ordinary course of trading on the ASX. As a result, for the purposes of Division 16K of the ITAA 1936, the Buy-Back is an off-market purchase within the meaning given by paragraph 159GZZZK(d) of the ITAA 1936.

The Dividend and Capital Components

59. The Buy-Back Price received by Participating Shareholders comprises two components:

- a Dividend Component, and
- a Capital Component.

60. The amount of each of these components is determined in accordance with sections 159GZZZP and 159GZZZQ of the ITAA 1936, and has regard to how CIC accounted for the Buy-Back.

The Dividend Component

61. Section 159GZZZP of the ITAA 1936 applies to off-market purchases such as the Buy-Back.

62. Broadly, under subsection 159GZZZP(1) of the ITAA 1936 the difference between the purchase price and the part (if any) of the purchase price which is debited against amounts standing to the credit of the company's share capital account (paragraph 159GZZZP(1)(b) of the ITAA 1936) is taken to be a dividend paid by the company to the seller on 26 May 2015 being the day the Buy-Back occurred.

63. The Buy-Back Price was \$0.827 per share, of which \$0.49 (the Capital Component) was debited against amounts standing to the credit of CIC's share capital account. As a result, the Dividend Component is taken to be \$0.337 per share. The Dividend Component of \$0.337 per share is frankable, but only to the extent that the Buy-Back Price does not exceed the market value of a CIC share at the time of the Buy-Back if the Buy-Back did not occur and was never proposed to occur (paragraph 202-45(c)). In respect of the Buy-Back, the entire Dividend Component is frankable.

Assessability of the Dividend Component and tax offset

Direct distributions

64. For Participating Shareholders who are Australian residents (other than a partnership or a trustee of a trust) and who directly received the Dividend Component:

- the Dividend Component is included in the assessable income of each Participating Shareholder under subsection 44(1) of the ITAA 1936, and
- subject to the 'qualified person' rule, the amount of the franking credit on the Dividend Component is included in the assessable income of each Participating Shareholder under subsection 207-20(1).

65. Subject to the 'qualified person' rule, these Participating Shareholders are entitled to a tax offset under subsection 207-20(2) equal to the amount of the franking credit on the Dividend Component.

Indirect distributions

Partnerships

66. Pursuant to subsection 44(1) of the ITAA 1936, the Dividend Component is included in the assessable income of the partnership for the purposes of computing the net income of the partnership under section 90 of the ITAA 1936.

67. Subject to the 'qualified person' rule, pursuant to subsection 207-35(1), the amount of the franking credit on the Dividend Component is included in the assessable income of the partnership for the purposes of computing the net income of the partnership under section 90 of the ITAA 1936.

Trusts

68. Pursuant to subsection 44(1) of the ITAA 1936, the Dividend Component is included in the assessable income of the trustee for the purposes of computing the net income of the trust under subsection 95(1) of the ITAA 1936.

69. Subject to the 'qualified person' rule, pursuant to subsection 207-35(1), the amount of the franking credit on the Dividend Component is included in the assessable income of the trustee for the purposes of computing the net income of the trust under subsection 95(1) of the ITAA 1936.

Partners and Beneficiaries

70. Subsections 207-35(3) to (6) set out the circumstances in which a partner or beneficiary to whom a franked distribution flows indirectly is required to gross up their assessable income for their share of the franking credit on the franked distribution.

71. Where the franked distribution flows indirectly (within the meaning of Subdivision 207-B) through a trust or partnership to a resident that is an individual, a corporate tax entity (at the time the distribution flows indirectly to it) or a trustee mentioned in paragraphs 207-45(c), (ca) or (d), the entity will, subject to the qualified person rule, be entitled to a tax offset equal to the entity's share of the franking credit on the franked distribution (section 207-45).

Refundable tax offset

72. The tax offsets are subject to the refundable tax offset rules in Division 67, provided they are not excluded from the refundable tax offset rules by subsections 67-25(1A) to (1DA).

Non-resident Participating Shareholders

73. As the Dividend Component of the Buy-Back Price is fully franked, and no determination will be made in respect of the Dividend Component under either paragraph 204-30(3)(c) or paragraph 177EA(5)(b) of the ITAA 1936, a non-resident Participating Shareholder is not liable to Australian withholding tax on the Dividend Component (paragraph 128B(3)(ga) of the ITAA 1936).

The Capital Component

Calculation of Sale Consideration

74. For the purposes of determining the amount of gain or loss (where the CIC Shares are held on revenue or capital account) the consideration in respect of the disposal of a share under a Buy-Back (the Sale Consideration) is determined in accordance with section 159GZZZQ of the ITAA 1936.

75. Subsection 159GZZZQ(1) of the ITAA 1936 provides that a shareholder is taken to have received an amount equal to the purchase price (in this case the Buy-Back price of \$0.827 received for each CIC Share bought back) as consideration in respect of the sale of the share bought back. However, this amount is subject to certain adjustments in order to arrive at the Sale Consideration.

76. Subsection 159GZZZQ(3) of the ITAA 1936 is one of those provisions. Pursuant to that subsection, the deemed consideration of \$0.827 is reduced by a 'Reduction Amount'. The Reduction Amount is an amount calculated pursuant to subsection 159GZZZQ(4) of the ITAA 1936. In the circumstances of the Buy-Back, the Reduction Amount is equivalent to the Dividend Component of \$0.337, unless the Participating Shareholder is a corporate tax entity to whom subsection 159GZZZQ(8) of the ITAA 1936 applies (see paragraph 77 of this Ruling). As a result, the Sale Consideration for each CIC Share disposed of under the Buy-Back is \$0.49 (being \$0.827 less \$0.337).

77. However, where the Participating Shareholder is a corporate tax entity which is entitled to a tax offset under Division 207 in respect of the Dividend Component, a further adjustment may be made to the Sale Consideration. Under subsection 159GZZZQ(8) of the ITAA 1936, if such a Participating Shareholder would also make either a capital loss or a deductible loss (or any increase in such a loss) in respect of the sale of a CIC Share bought back under the Buy-Back, the Sale Consideration is increased by an off-settable amount determined under subsection 159GZZZQ(9) of the ITAA 1936. The Reduction Amount (being the Dividend Component) is itself reduced by so much of the off-settable amount that does not exceed the capital loss or the deductible loss.

78. Participating Shareholders are taken to have disposed of their shares accepted under the Buy-Back on 26 May 2015 (CGT event A1). The disposal may have different taxation implications for Participating Shareholders depending on how the shares were held, for instance:

- an investor who held their shares on capital account will be subject to the CGT provisions, and
- a share trader who held their shares on revenue account will be subject to the ordinary income provisions and the CGT provisions.

Shares held on capital account

79. The Sale Consideration of \$0.49 per share represents the capital proceeds for CGT purposes pursuant to section 116-20. A Participating Shareholder (other than a partnership) will make a capital gain in respect of the disposal of a share if the Sale Consideration per share exceeds the cost base of the share. The capital gain is the amount of the excess. Similarly, a Participating Shareholder (other than a partnership) will make a capital loss in respect of the disposal of a share if the Sale Consideration per share is less than the reduced cost base of the share (subsection 104-10(4)).

80. Where the Participating Shareholder is a partnership, any capital gain or loss will be made by the partners individually (subsection 106-5(1)). Each partner in a partnership has a separate cost base and reduced cost base for the partner's interest in each CIC Share sold into the Buy-Back by the partnership (subsection 106-5(2)). Each partner is allocated an appropriate share of the Sale Consideration received by the partnership for the disposal of CIC Shares into the Buy-Back.

Shares held on revenue account

81. Where shares were held as trading stock, the Sale Consideration of \$0.49 per share is included in assessable income under section 6-5. Participating Shareholders (other than partnerships) who disposed of shares held as trading stock will also make a capital gain or capital loss. However, as the shares were held as trading stock, the capital gain or loss is disregarded under section 118-25. There is a similar exemption for partners in partnerships (paragraph 118-25(1)(b)).

82. Where shares were held as revenue assets, but were not trading stock, the amount by which the Sale Consideration of \$0.49 per share exceeds the cost of each share is included in assessable income. Correspondingly, if the cost exceeds the Sale Consideration of \$0.49 per share the difference is an allowable deduction. Where the Sale Consideration per share exceeds the cost base of the share these Participating Shareholders (other than partnerships) will also make a capital gain. However, Participating Shareholders who held their shares as revenue assets will have the amount of the capital gain reduced under the CGT anti-overlap provisions contained in section 118-20. There is a similar reduction for partners in partnerships (paragraph 118-20(1)(b), paragraph 118-20(2)(b) and subsection 118-20(3)).

Foreign resident Participating Shareholders: CGT consequences

83. Under subsection 855-10(1), a Participating Shareholder or entity disregards a capital gain or capital loss from a CGT event if they are a foreign resident, or the trustee of a foreign trust for CGT purposes, just before the CGT event happens and the CGT event happens in relation to a CGT asset that is not 'taxable Australian property'.

84. The term 'taxable Australian property' is defined in the table in section 855-15. The table sets out these 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 an which is not covered by item 1, 2 or 5;
Item 4	An option or right to acquire a CGT asset covered by item 1, 2 or 3; and
Item 5	A CGT asset that is covered by subsection 104-165(3) (choosing to disregard a gain or loss on ceasing to be an Australian resident).

85. Items 1 and 4 of the table in section 855-15 do not apply to a CIC Share.

86. Item 2 of the table in section 855-15 also does not apply to a CIC Share as the Company has advised that at the time of the Buy-Back, the CIC Shares held by participating non-residents were not 'indirect Australian real property interests' as defined in section 855-25 due to the CIC Shares not passing the non-portfolio interest test under section 960-195 at that time, or throughout the period prescribed by subparagraph 855-25(1)(a)(ii).

87. However, a CIC Share that is disposed of in the Buy-Back will constitute taxable Australian property if the share:

- was used by the foreign resident in carrying on a business through a permanent establishment in Australia (Item 3 of the table in section 855-15), or
- is 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 – Item 5 of the table in section 855-15).

Qualified persons

88. Paragraph 207-145(1)(a) provides that in relation to a franked dividend made by an entity only a 'qualified person' in relation to the distribution for the purposes of former Division 1A of Part IIIAA of the ITAA 1936 is required to include the franking credit in its assessable income or is entitled to claim the franking credit as a tax offset. Broadly speaking, to be a qualified person in relation to the Dividend Component paid under the Buy-Back, a Participating Shareholder must satisfy both the 'holding period rule' and the 'related payments rule'.

89. Broadly, a Participating Shareholder will not satisfy the related payments rule if the Participating Shareholder, or an associate of the Participating Shareholder, is under an obligation to make, or makes, a payment in respect of the dividend, which effectively passes on the economic benefit of the dividend to another person.

90. The holding period rule requires a shareholder to hold the shares on which the dividend is paid 'at risk' for a continuous period of at least 45 days during the relevant qualification period. In the absence of a related payment, the relevant qualification period is the primary qualification period, which commences on the day after the shares are acquired and ends on the 45th day after the day on which they became ex-dividend. In determining whether a shareholder has satisfied the holding period rule, any days during which there is a materially diminished risk of loss or opportunity for gain in respect of the relevant shares are not counted. The day of acquisition and the day of disposal of the relevant shares are also not counted.

91. Under former subsection 160APHM(2) of the ITAA 1936, a shareholder is taken to have materially diminished the risks of loss and opportunities for gain with respect to shares if the 'net position' in respect of the risks of loss and opportunity for gain of the shareholder results in the shareholder having less than 30% of the risks and opportunities relating to the shares.

92. The Commissioner does not regard the announcement of the Buy-Back as affecting whether CIC Shares were held at risk or not.

93. There are 45 clear days between 10 April 2015 and 26 May 2015 (the date the Buy-Back was implemented under the SOA). As a result, a Participating Shareholder who acquired shares on or before 10 April 2015 satisfies the holding period rule as long as those shares were held at risk for at least 45 continuous days. A Participating Shareholder who acquired shares after 10 April 2015 that were subsequently bought back under the Buy-Back may not be a qualified person in relation to the dividend paid under the Buy-Back for the purposes of former Division 1A of Part IIIAA of the ITAA 1936 except in certain circumstances.

94. Generally, under the holding period rule a shareholder will be deemed to have disposed of his or her most recently acquired shares first (former subsection 160APHI(4) of the ITAA 1936). The 45 day rule operates on a 'last-in first-out' basis, so that shareholders will be deemed to have disposed of their most recently acquired shares first for the purposes of applying the 45 day rule. Accordingly, Participating Shareholders who, after 10 April 2015, acquired any additional CIC Shares, which conferred an entitlement to participate in the Buy-Back, may not qualify for the franking credits attached to the dividends paid on some or all of the shares sold into the Buy-Back.

The anti-avoidance provisions

Section 45A

95. Section 45A of the ITAA 1936 is an anti-avoidance rule that applies where a company streams 'capital benefits' to shareholders who derive a greater benefit from the receipt of share capital (advantaged shareholders), and it is reasonable to assume that other shareholders (disadvantaged shareholders) have received or will receive dividends.

96. Although a 'capital benefit' (as defined paragraph 45A(3)(b) of the ITAA 1936) will be provided to Participating Shareholders under the Buy-Back, the circumstances of the Buy-Back indicate that there is no streaming of capital benefits to some shareholders and dividends to other shareholders.

97. Accordingly, the Commissioner will not make a determination under subsection 45A(2) of the ITAA 1996 that section 45C of the ITAA 1936 applies to the Capital Component of the Buy-Back.

Section 45B

98. 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 (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).

99. While the conditions of paragraphs 45B(2)(a) and (b) of the ITAA 1936 were met in respect of the Buy-Back, having regard to the 'relevant circumstances' (as set out in subsection 45B(8) of the ITAA 1936), the requisite purpose of enabling a person to obtain a tax benefit as a result of the capital distribution was not present, in particular:

- the distribution of share capital of \$0.49 per share accords with an average capital per share method and could not be said to be attributable to the profits of CIC
- the pattern of distribution of CIC does not indicate that the distribution of share capital of \$0.49 per share reflects amounts in substitution for a dividend
- the Buy-Back is not expected to alter CIC's dividend policy, and
- as a consequence of the Buy-Back, the distribution of share capital resulted in the cancellation of shares in CIC held by Participating Shareholders and a corresponding loss of dividend, voting and other rights.

100. Therefore, the Commissioner will not make a determination under subsection 45B(3) of the ITAA 1936 that section 45C of the ITAA 1936 applies to treat all or any part of the distribution of share capital of \$0.49 per share as an unfranked dividend paid by CIC.

Section 177EA

101. Section 177EA of the ITAA 1936 is a general anti-avoidance provision that applies to a wide range of schemes designed to obtain 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 buy-back with a franked dividend component.

102. Specifically, subsection 177EA(3) of the ITAA 1936 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.

103. The conditions of paragraphs 177EA(3)(a) to 177EA(3)(d) of the ITAA 1936 are satisfied in respect of the Buy-Back. Accordingly, the issue is whether, having regard to the relevant circumstances of the scheme, it would be concluded that on the part of CIC, its shareholders or any other relevant party, there is more than a merely incidental purpose of conferring an imputation benefit under the scheme. In respect of the Buy-Back, the relevant taxpayer is the Participating Shareholder and the scheme comprises the circumstances surrounding the Buy-Back.

104. 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) of the ITAA 1936. The relevant circumstances listed in subsection 177EA(17) of the ITAA 1936 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.

105. The Commissioner has come to the view that section 177EA of the ITAA 1936 applies to the Buy-Back. In coming to this conclusion the Commissioner had regard to all the relevant circumstances of the arrangement, as outlined in subsection 177EA(17) of the ITAA 1936. Among the circumstances of the Buy-Back reflected in those paragraphs is the greater attraction of the Buy-Back to resident shareholders of the franking credits than for non-resident shareholders.

106. Where section 177EA of the ITAA 1936 applies, the Commissioner has a discretion pursuant to subsection 177EA(5) of the ITAA 1936 to make a determination to debit CIC's franking account pursuant to paragraph 177EA(5)(a) of the ITAA 1936, or deny the imputation benefit to each Participating Shareholder pursuant to paragraph 177EA(5)(b) of the ITAA 1936. The Commissioner will exercise his discretion in such a way that he will not make a determination that the imputation benefit obtained by the Participating Shareholders will be denied under paragraph 177EA(5)(b) of the ITAA 1936.

Section 204-30

107. Section 204-30 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:

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

108. If section 204-30 applies, the Commissioner is vested with a discretion under subsection 204-30(3) to make a determination in writing either:

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

109. For section 204-30 to apply, a member of an entity must derive a greater benefit from franking credits. Some of the cases in which a member of an entity 'derives a greater benefit from franking credits' are listed in subsection 204-30(8) by reference to the ability of a member to fully utilise franking credits.

110. A small portion of CIC's ordinary shares are held by non-resident shareholders who do not benefit from franking credits to the same extent as resident shareholders. As a result, the conditions in subsection 204-30(1) for section 204-30 to apply are met. However, the Commissioner will not make a determination under subsection 204-30(3).

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Related Rulings/Determinations:

TR 2006/10

Subject references:

- frankable dividends
- qualified person
- schemes
- share buy-backs
- share capital

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