

# ***CR 2005/28 - Income tax: AMP Limited: proposed capital return***

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⚠ This document has changed over time. This is a consolidated version of the ruling which was published on *1 July 2004*



## Class Ruling

### Income tax: AMP Limited: proposed capital return

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#### **Preamble**

*The number, subject heading, **What this Class Ruling is about** (including **Tax laws, Class of persons and Qualifications** sections), **Date of effect, Withdrawal, Arrangement and Ruling** parts of this document are a 'public ruling' in terms of Part IVAAA of the **Taxation Administration Act 1953**. CR 2001/1 explains Class Rulings and Taxation Rulings TR 92/1 and TR 97/16 together explain when a Ruling is a 'public ruling' and how it is binding on the Commissioner.*

#### **What this Class Ruling is about**

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1. This Ruling sets out the Commissioner's opinion on the way in which the 'tax laws' identified below apply to the defined class of persons, who take part in the arrangement to which this Ruling relates.

#### **Tax law(s)**

2. The tax laws dealt with in this Ruling:
- subsection 6(1) of the *Income Tax Assessment Act 1936* (ITAA 1936);
  - section 45A of the ITAA 1936;
  - section 45B of the ITAA 1936;
  - section 45C of the ITAA 1936; and
  - section 104-135 of the *Income Tax Assessment Act 1997* (ITAA 1997).

#### **Class of persons**

3. The class of persons to which this Ruling applies is persons who hold ordinary shares in AMP Limited (AMPL) and who are registered on the AMP Share Register on the Record Date, being the date for determining entitlements to the proposed capital return.

#### **Qualifications**

4. The Commissioner makes this Ruling based on the precise arrangement identified in this Ruling.

5. The class of persons defined in this Ruling may rely on its contents provided the arrangement actually carried out is carried out in accordance with the arrangement described in paragraphs 10 to 16.

6. If the arrangement actually carried out is materially different from the arrangement that is described in this Ruling, then:

- this Ruling has no binding effect on the Commissioner because the arrangement entered into is not the arrangement on which the Commissioner has ruled; and
- this Ruling may be withdrawn or modified.

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## Date of effect

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8. This Ruling applies to the income year ended 30 June 2005. The Ruling only applies to the extent that:

- it is not later withdrawn by *Gazette*;
- it is not taken to be withdrawn by an inconsistent later public ruling; or
- the relevant tax laws are not amended.

## Withdrawal

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9. This Ruling is withdrawn and ceases to have effect after 30 June 2005. However, the Ruling continues to apply after its withdrawal in respect of the tax laws ruled upon, to all persons within the specified class who entered into the specified arrangement during the term of the Ruling, subject to there being no change in the arrangement or in the person's involvement in the arrangement.

## Arrangement

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10. The arrangement that is the subject of this Ruling is described below. This description is based on a number of documents. These documents, or relevant parts of them, as the case may be, form part of and are to be read with this description. The relevant documents or parts of documents incorporated into this description of the arrangement are:

- a) class ruling request from Mallesons Stephen Jaques (MSJ) dated 4 February 2005;
- b) correspondence dated 3 November 2004 to 18 March 2005 from MSJ and AMPL providing further particulars;
- c) Explanatory Memorandum and Notice of General Meeting entitled 'Proposal to Demutualise' which was provided to Australian Mutual Provident Society (AMP Society) members in respect of a general meeting which was held on 20 November 1997; and
- d) AMP Australian Stock Exchange (ASX) Announcement of 17 February 2005 'AMP proposes A\$1 billion capital return and debt repayment'.

**Note:** Certain information has been provided on a commercial-in-confidence basis and will not be disclosed or released under the Freedom of Information legislation.

11. AMPL is an Australian resident public company listed on the ASX and is the ultimate parent of the AMP group. The company became the ultimate parent of the AMP group as part of the demutualisation of the AMP Society in 1998. The AMP Society upon demutualisation became AMP Life Limited (AMP Life), a subsidiary member of the AMP group. At the time of demutualisation Division 9AA of the ITAA 1936 applied to base the cost of the shares in AMPL for CGT purposes on the embedded value of the AMP Society.

12. On 17 February 2005 AMPL announced, amongst other things, that it intended to return capital of \$750 million (the capital return) to shareholders of AMPL (AMPL shareholders), which equates to 40 cents per ordinary share.

13. Prior to the announcement the AMP group determined, following a review of the capital requirements of the group subsequent to the demerger of its UK operations in December 2003, that it had capital surplus to requirements.

14. The capital return of \$750 million is subject to shareholder approval at AMPL's Annual General Meeting to be held on 19 May 2005. All AMPL shareholders registered on the Record Date will be entitled to the return of capital. The Record Date and date of payment of the capital return are expected to be 26 May and 20 June 2005, respectively.

15. AMPL proposes to debit the capital return against the share capital of AMPL. The source of funds for the distribution is an amount recognised as shareholders' capital (in terms of section 61 of *Life Insurance Act 1995*) in the statutory funds of AMP Life. The amount involved formed part of the embedded value of the AMP Society before demutualisation. AMPL confirms that its share capital account, as defined in section 6D of the ITAA 1936, is not tainted as there have been no transfers to the share capital account from other accounts.

16. The proposed capital return will be made in addition to the payment of interim and final dividends anticipated by AMPL in respect of the year ended 31 December 2005.

## Ruling

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### **Is the capital return a dividend as defined in subsection 6(1) of the ITAA 1936?**

17. The proposed capital return will not be a dividend as defined in subsection 6(1) of the ITAA 1936.

### **Sections 45A, 45B and 45C of the ITAA 1936**

18. Subject to the qualifications in paragraphs 4 to 6 of this ruling, the Commissioner will not make a determination (under sections 45A or 45B of the ITAA 1936) that section 45C of the ITAA 1936 applies to the capital return. Accordingly, no part of the capital return will be taken to be a dividend for income tax purposes under section 45C.

### **CGT Event G1 – section 104-135 of the ITAA 1997**

19. CGT event G1 in section 104-135 of the ITAA 1997 will happen when AMPL makes the capital return of 40 cents per share to an AMPL shareholder.

20. Pursuant to subsections 104-135(3) and (4), the cost base and reduced cost base of each AMPL share will be reduced (not below nil) by the amount of the capital return. A shareholder will make a capital gain from CGT event G1 occurring to each share to the extent (if any) that the payment exceeds the share's cost base in accordance with subsection 104-135(3) of the ITAA 1997.

21. If the shareholder is not an Australian resident for income tax purposes, a CGT event G1 capital gain will not be made unless the shares have the necessary connection with Australia in terms of section 136-25 of ITAA 1997.

## **Explanation**

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### **Is the capital return a dividend as defined in subsection 6(1) of the ITAA 1936?**

22. Subject to certain exceptions, the subsection 6(1) definition includes:

- (a) any distribution made by a company to any of its shareholders, whether in money or other property ...

The capital return will be a distribution made by AMPL to all of its shareholders.

23. However, the exception in paragraph (d) of the definition excludes a distribution if the amount is debited against an amount standing to the credit of the share capital account of a company.

24. The capital return will be debited against AMPL's untainted share capital account. Therefore, paragraph (d) of the definition of 'dividend' applies.

25. Paragraph (d) is qualified by subsection 6(4) which, broadly, applies to certain arrangements where amounts provided by a person to a company and recorded as share capital are distributed to another person. In the present case, the return of capital will be made to all shareholders indifferently and subsection 6(4) does not apply.

26. Therefore, the capital return will not be a dividend as defined in subsection 6(1).

### **Sections 45A and 45B of the ITAA 1936**

27. Sections 45A and 45B of the ITAA 1936 are two anti-avoidance provisions which, if they apply, allow the Commissioner to determine that all or part of a distribution is treated as an unfrankable dividend that is paid by the company out of profits to the shareholder.

#### ***Section 45A – streaming of dividends and capital benefits***

28. By making the distribution, AMP will provide a 'capital benefit' in terms of paragraph 45A(3)(b) to all its shareholders and all shareholders will receive the same amount of return of capital per share. In these circumstances, there is no streaming of capital benefits to some shareholders and dividends to other shareholders. Accordingly section 45A of the ITAA 1936 does not apply to the proposed return of capital.

***Section 45B – schemes to provide capital benefits in substitution for dividends***

29. Section 45B of the ITAA 1936 applies where certain amounts of a capital nature are provided to shareholders in substitution for dividends.

30. Subsection 45B(2) sets out the conditions under which the Commissioner will make a determination under subsection 45B(3) of the ITAA 1936 that section 45C of the ITAA 1936 applies. These conditions are that:

- there is a scheme under which a person is provided with a capital benefit by a company;
- 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; 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 the relevant taxpayer to obtain a tax benefit.

Each of the conditions are considered below.

31. The return of capital is a 'scheme' for the purposes of section 45B.

32. The phrase 'provided with a capital benefit' is defined in subsection 45B(5) of the ITAA 1936. Relevantly, it includes a distribution to a person of share capital. As AMP proposes to debit the return of capital against its untainted share capital account, its shareholders will be provided with a capital benefit.

33. A taxpayer 'obtains a tax benefit', as defined in subsection 45B(9) of the ITAA 1936, where:

- the amount of tax payable; or
- any other amount payable under the ITAA 1936 or the ITAA 1997;

by the taxpayer would, apart from the operation of section 45B:

- be less than the amount that would have been payable; or
- be payable at a later time than it would have been payable,

if the capital benefit had instead been a dividend.

34. A return of capital, ordinarily, would be subject to the CGT provisions of the income tax law. Unless the amount of the distribution exceeds the cost base of the shares there will only be a cost base reduction under CGT event G1 (section 104-135 of the ITAA 1997). It is only to the extent (if any) that the distribution exceeds the cost base of the shares that a capital gain arises. A capital gain may not arise at all for certain non-resident shareholders: see paragraph 46. By contrast a dividend would generally be included in the assessable income of a resident shareholder or in the case of a non-resident, subject to dividend withholding tax. Therefore, the shareholders will obtain tax benefits from the capital return.

35. The Commissioner is required to consider the circumstances set out under subsection 45B(8) of the ITAA 1936 to determine whether any part of the arrangement would be entered into for a purpose, other than an incidental purpose, of enabling a relevant taxpayer to obtain a tax benefit.

36. The test of purpose is an objective one. The question is whether, objectively, it would be concluded that a person who entered into or carried out the scheme, did so for the purpose of obtaining a tax benefit for the relevant taxpayer in respect of the capital benefit. The purpose does not have to be the most influential or prevailing purpose but it must be more than an incidental purpose.

37. The relevant circumstances under subsection 45B(8) cover the circumstances of the company and the tax profile of the shareholders. In this instance, as the capital return is made to all shareholders regardless of individual circumstances, paragraphs 45B(8)(c) to (h) do not incline for or against a conclusion as to purpose. The circumstances covered by paragraph 45B(8)(i) and (j) pertaining to the provision of ownership interests and demerger are not relevant. So, in this case the relevant matters are those covered by the circumstances described in paragraphs 45B(8)(a), (b) and (k).

38. Paragraph 45B(8)(a) refers to the extent to which the capital benefit is attributable to capital and profits (realised and unrealised) of the company or an associate (within the meaning of section 318 of the ITAA 1936) of the company. In this case, the return of capital is referable to pre-demutualisation capital in the statutory funds of AMP Life which was integral to the business structure of the AMP group at demutualisation. This was reflected in the cost base of the AMPL shares as a result of the operation of Division 9AA. Since demutualisation, AMPL has maintained a policy of paying annual dividends but the AMP group has incurred significant losses resulting in a large reduction in retained earnings, whereas the share capital of AMPL has increased markedly through various capital raisings. In these circumstances, the capital benefit is attributable to capital not profits, realised or unrealised.

39. Paragraph 45B(8)(b) refers to the pattern of distributions made by a company or an associate (within the meaning of section 318) of the company. Since demutualisation AMPL has paid dividends each year. The capital return will be made in addition to the payment of interim and final dividends anticipated by AMPL in respect of the year ended 31 December 2005. In regard to its share capital, AMPL has not made capital distributions to its shareholders except in the context of demerging 85% of its UK operations. The company's pattern of distributions does not suggest that the capital distribution is made in substitution for a dividend.

40. Paragraph 45B(8)(k) refers to the matters in subparagraphs 177D(b)(i) to (viii) of the ITAA 1936. These are matters by reference to which a scheme is able to be examined from a practical perspective in order to identify and compare its tax and non-tax objectives. The matters include the manner in which the scheme is carried out, its form and substance, and its financial and other implications for the parties involved. In this case, the practical implications of the scheme for AMPL and its shareholders are consistent with its being, in form and substance, a distribution of share capital.

41. Therefore, having regard to the relevant circumstances of the scheme to return capital to the shareholders of AMPL, as discussed in paragraphs 37 to 40, it would not be concluded that the parties who enter into or carry out the scheme do so for a more than incidental purpose of enabling the shareholders to obtain a tax benefit. Accordingly, the Commissioner will not make a determination under subsection 45B(3) that section 45C applies to the capital return.

#### **Section 45C of the ITAA 1936 – deeming dividends to be paid where determinations under section 45A or 45B are made**

42. As the Commissioner will not make a determination under subsection 45A(2) or subsection 45B(3) of the ITAA 1936 in relation to the arrangement as described, section 45C will not apply.

#### **CGT Event G1 – section 104-135 of the ITAA 1997**

43. CGT event G1 (section 104-135 of the ITAA 1997) occurs if a company makes a payment to a shareholder in respect of a share they own in a company and some or all of the payment is not a dividend as defined in subsection 995-1(1) of the ITAA 1997, or an amount that is taken to be a dividend under section 47 of the ITAA 1936.

44. AMPL proposes to make a payment to its shareholders out of its share capital account. This payment will not be a dividend as the term is defined in subsection 995-1(1). The provisions referred to in that definition are not applicable. Furthermore, the capital return will not be taken to be a dividend under section 47 which applies to distributions made by liquidators. Accordingly, CGT event G1 will occur.

45. Pursuant to subsections 104-135(3) and (4), the cost base and reduced cost base of each AMPL share will be reduced (not below nil) by the amount of the capital return. Capital gains can also arise from CGT event G1 but only to the extent (if any) that the payment exceeds the share's cost base: subsection 104-135(3).

46. If the shareholder is not an Australian resident for income tax purposes, a CGT event G1 capital gain cannot be made unless the shares have the necessary connection with Australia in terms of section 136-25 of ITAA 1997. Broadly, shares in public companies will not have the necessary connection with Australia, and a capital gain will not be made, where the non-resident shareholder and their associates beneficially own less than 10% by value of the shares in the company during the 5 years before the CGT event.

## **Detailed contents list**

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**Commissioner of Taxation**

4 May 2005

<i>Previous draft:</i>	- ITAA 1936 45B(8)(e)
Not previously issued as a draft	- ITAA 1936 45B(8)(f)
	- ITAA 1936 45B(8)(g)
	- ITAA 1936 45B(8)(h)
<i>Related Rulings/Determinations:</i>	- ITAA 1936 45B(8)(i)
CR 2001/1; TR 92/1; TR 97/16	- ITAA 1936 45B(8)(j)
	- ITAA 1936 45B(8)(k)
	- ITAA 1936 45B(9)
<i>Subject references:</i>	- ITAA 1936 45C
- capital benefit	- ITAA 1936 47
- capital reductions	- ITAA 1936 Pt III Div 9AA
- dividend substitution	- ITAA 1936 177D(b)(i)
- return on capital shares	- ITAA 1936 177D(b)(ii)
- share capital	- ITAA 1936 177D(b)(iii)
<i>Legislative references:</i>	- ITAA 1936 177D(b)(iv)
- ITAA 1936 6(1)	- ITAA 1936 177D(b)(v)
- ITAA 1936 6(4)	- ITAA 1936 177D(b)(vi)
- ITAA 1936 6D	- ITAA 1936 177D(b)(vii)
- ITAA 1936 45A	- ITAA 1936 177D(b)(viii)
- ITAA 1936 45A(2)	- ITAA 1936 318
- ITAA 1936 45A(3)(b)	- ITAA 1997 104-135
- ITAA 1936 45B	- ITAA 1997 104-135(3)
- ITAA 1936 45B(2)	- ITAA 1997 104-135(4)
- ITAA 1936 45B(3)	- ITAA 1997 136-25
- ITAA 1936 45B(5)	- ITAA 1997 995-1(1)
- ITAA 1936 45B(8)	- TAA 1953 Pt IVAAA
- ITAA 1936 45B(8)(a)	- Copyright Act 1968
- ITAA 1936 45B(8)(b)	- Life Insurance Act 1995
- ITAA 1936 45B(8)(c)	
- ITAA 1936 45B(8)(d)	

## ATO references

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