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WEEKLY COMMENT: FRIDAY 26 JULY 2013

1. Two joint public binding rulings ("BR Pub") and a "Questions we've been asked' ("QWBA") were published in last month's *Tax Information Bulletin Vol 25 No 6 July 2013*. These were all issued in draft form earlier this year and, following submissions, have now been finalised. The publications are:

   (a) *BR Pub 13/01 and 13/02: Income tax – Treatment of a subdivision of shares under section CB 4*;

   (b) *BR Pub 13/03 and 13/04: Treatment of unclaimed amounts of $100 or less*; and

   (c) *QB 13/02: Income tax – Determining the "subscriptions" amount for an amalgamated company under the available subscribed capital rules.*

Treatment of a subdivision of shares

2. Section CB 4 of the *Income Tax Act 2007* states that an amount that a person derives from disposing of personal property is income of the person if they acquired the property for the purpose of disposing of it. Section 35 of the *Companies Act 1993* states that a share in a company is personal property.

3. Public ruling *BR Pub 13/01* states that a subdivision of shares will not result in a disposal of personal property for the purposes of s. CB 4 when a company subdivides all of its shares and the following factors apply:

   (a) The directors resolve that all of the shares will be subdivided so that each share splits into an equal number of shares.

   (b) The rights attaching to the shares will continue in existence throughout the subdivision process and will not be altered.

   (c) Each shareholder's proportionate shareholding in the company will remain the same relative to the other shareholders.

   (d) The subdivision will merely represent the reformatting of each shareholder's interest.

4. Public Ruling *BR Pub 13/02* also applies when a company subdivides its shares and the same 4 factors all apply. However, *BR Pub 13/02* deals with the situation where a shareholder who acquired the shares for the purpose of disposal subsequently disposes of some or all of their subdivided shares. In that case, the ruling states that:

(a) Section CB 4 applies to the disposal of the subdivided shares.

(b) The time of acquisition of a subdivided share held on revenue account is the time the original share (which was subdivided) was acquired.

(c) Under s. ED 1, the cost of each subdivided share can be determined by dividing the cost of an original share equally between the subdivided shares into which the original share was divided.

5. The rulings do not apply if the rights of the share are varied or if the general anti-avoidance rule in s. BG 1 applies to the arrangement involving the share subdivision.

6. The rulings also do not apply to any variation in the number of shares issued by a company other than by a share subdivision. In particular, cancellation of pre-existing shares followed by the issue of a greater number of new shares, and issues of additional shares, are not covered by the rulings.

7. The *Commentary* on the ruling is concerned mainly with the tax consequences when a shareholder who held the original (pre-subdivided) share on revenue account subsequently disposes of the subdivided shares. The Commissioner's view is that the subdivided shares are the same property as the original shares for the purposes of s. CB 4 because:

   (a) A share subdivision does not involve an issue of shares: nothing has left the company or been provided to the shareholder, and case law has established that an issue of shares involves something leaving the company and being provided to the shareholder – *Central Piggery Co Ltd v McNicholl* (1949) 78 CLR 594 and *National Westminster Bank plc v IR Commrs* (1994) 12 ACLC 3,215 (HL).

   (b) The original shares continue in existence: the shares are not cancelled and the shareholder's interest is never alienated, therefore, there is no "disposal" in the sense established by case law – *FCT v Wade* (1951) 84 CLR 105, *Lyttelton Port Co Ltd v CIR* (1996) 17 NZTC 12,556 (HC), and *Coles Myer Ltd v Commissioner of State Revenue* (VIC) (1998) ATC 4,537 (VICCA).

   (c) Shareholders' rights are unchanged because their proportionate interest in the company is unchanged: case law has established that a subdivision of shares does not give rise to new property – *Whittome v Whittome (No 1)* (1994) SLT 114 (OH) and *Greenhalgh v Arderne Cinemas Ltd* [1946] All ER 512 (CA); case law also suggests that a mere subdivision of land does not change the nature of the legal rights in the property and so there is identity of property before and after the subdivision – *Moruben Gardens Pty Ltd v FCT* 72 ATC 4,147.

   (d) The replaced definition of "bonus issue" in s. 98(6) & (7) of the Taxation (Livestock Valuation, Assets Expenditure, and Remedial Matters) Act 2013 specifically includes a "subdivision of shares" as a bonus issue and clarifies that a subdivision of shares is excluded from the dividend rules.

   (e) A share subdivision does not result in a disposal of the original pre-subdivided shares: a shareholder does not give up or lose their rights as a result of the subdivision - *Whittome v Whittome (No 1)* (1994) SLT 114 (OH).

8. The *Commentary* includes two examples. Perhaps the most important point is that Example 2 clarifies that a decision to sell shares at the time they are subdivided will not be taxable

under s. CB 4 because the original (pre-subdivision) shares were not acquired for the purpose of disposal.

Treatment of unclaimed amounts of $100 or less

9. Section CB 1 states that an amount that a person derives from a business is income of the person. The rulings BR Pub 13/03 & 13/04 deal with business receipts that are held as owing to another person and that are subject to the provisions of the *Unclaimed Money Act 1971* ("UMA 1971").

10. The UMA 1971 generally requires unclaimed money to be paid to the Commissioner of Inland Revenue. However, the proviso to s. 4(1) of the UMA 1971 contains an exception under which money ceases to be unclaimed money if:

    (a) In respect of any one owner it does not exceed $100; and

    (b) Without limiting the owner's claim, the unclaimed money is applied by the holder for its own purposes before the 1 June following the expiry of the relevant 6-year or 25-year period after which it became unclaimed money.

11. *BR Pub 13/03* states that unclaimed money that is applied by the holder in this way is business income under s. CB 1. However, *BR Pub 13/04* states that as long as amounts of otherwise unclaimed money are held in trust and cannot be applied for the holder's benefit, there will be no income that arises under s. CB 1.

12. The key issue addressed by the *Commentary* to the rulings is the timing of when the income is derived. *BR Pub 13/03* states that the amount will be income when:

    (a) It has been applied by the holder for its own purposes; and

    (b) It is probable that the amount will not have to be repaid.

13. The leading case of *Arthur Murray (NSW) Pty Ltd v FCT* [1965] HCA 58; (1965) 114 CLR 314 is discussed. This case is taken to provide authority for the view that amounts are not income while there is a possibility of having to pay them back. It is noted that *Arthur Murray* was cited with approval in *A Taxpayer v CIR* [1997] NZCA 135; (1997) 18 NZTC 13,350 (CA) and the same reasoning, that advances that have to be repaid do not have the quality of income earned and derived, was followed in *CIR v Molloy* (1990) 12 NZTC 7,146 (HC).

14. The UK decision that is closest to the facts relating to unclaimed money is *Pertemps Recruitment Partnership Ltd v HMRC* [2010] UKFTT 218 (TC) where the taxpayer, a recruitment agent, received overpayments from customers. The taxpayer did not know they were overpayments at the time they were received, and treated the amounts as its own money. The court held the payments were profits in the year that they were received. The arguments in the *Commentary* are that *Pertemps* is inconsistent with *Arthur Murray* and, while it provides support for the view that unclaimed money can be income, it is not good authority for when that income is derived.

15. The conclusion in the Commentary is that once it is probable that the unclaimed amount will not need to be repaid, it should be treated as income. The "probable" threshold is based on *Case N30* (1991) 13 NZTC 3,266 (TRA), where it was held that unredeemed pre-paid tickets should be included as income when the taxpayer could say as a matter of probability that a ticket would not be redeemed.

16. It is noted that when it is probable that an amount will not be repaid will depend on the particular business and will be a question of fact to be determined in each case:

    "Business records and accounting treatment are likely to be relevant to determining this. … It is not possible to provide more prescriptive factors."

17. In the example provided, business records over a 10-year period indicated that requests for repayment of unclaimed money were generally not received after 4 years. Therefore, in that case, the amounts became income at the time the 6-year holding period for the unclaimed money expired, and the money was applied for the business's own purposes.

"Subscriptions" amount for an amalgamated company

18. *QB 13/02* clarifies how section CD 43(15)(a)(iii), which deals with calculating available subscribed capital ("ASC") after an amalgamation, is meant to operate.

19. The general rule for calculating ASC in s. CD 43(2)(b) is that amounts subscribed for shares in a given class will form part of the ASC of shares in that class. The ASC of the continuing company after an amalgamation – the *amalgamated* company – will be calculated under this rule.

20. Section CD 43(15) serves to increase the amount that is treated as subscribed for shares in an amalgamated company. Under section CD 43(15)(a) the subscriptions amount for a class of share issued by the *amalgamated* company (the continuing company in an amalgamation) includes, as if it were consideration for the issue of the amalgamated company's shares of that class, the available subscribed capital ("ASC") of all shares of the *amalgamating* companies (the companies that have ceased to exist) that are:

    (a) In the same class of shares; and

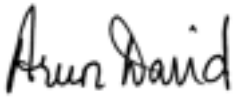
    (b) Not held directly or indirectly by an *amalgamating* company; and

    (c) Not shares in the *amalgamated* company.

21. Section CD 43(15) is seen as extending the ASC calculation so at include shares issued by amalgamating companies (that have ceased to exist). However, strictly speaking the term "amalgamating" refers to all the companies involved in the amalgamation, including the company that continues. Therefore, the shares in the continuing (or "amalgamated") company are carved out of the extension.

22. This ensures that the shares issued by the amalgamated company are not counted twice: once as part of the initial subscription calculation, and then a second time under the extension in s. CD 43(15) as part of the shares of all amalgamating companies (because the continuing amalgamated company is also one of the "amalgamating" companies).

23. An example is provided to demonstrate the point.



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