Inland Revenue
Te Tari Taake

TECHNICAL DECISION SUMMARY > PRIVATE RULING

WHAKARĀPOPOTO WHAKATAU HANGARAU > WHAKATAUNGA TŪMATAITI

Amalgamation and liquidation

Decision date | Rā o te Whakatau: 15 February 2023

Issue date | Rā Tuku: 12 September 2023

TDS 23/12

Subjects | Kaupapa

The wind-up of a holding structure used by the Taxpayer for investments. The wind-up was to be done in two steps: amalgamation and liquidation.

Taxation laws | Ture tāke

All legislative references are to the Income Tax Act 2007 (ITA 2007) unless otherwise stated.

Facts | Meka

1. The Taxpayer is a company.
2. The Taxpayer had a number of subsidiaries. The arrangement in the ruling application was the wind-up of a group of the Taxpayer's subsidiaries.
3. The wind-up of the group of subsidiaries was to be done in two steps:

   - **Amalgamation**

     The group of subsidiaries would be amalgamated by way of a short-form amalgamation under s 222 of the Companies Act 1993 (Companies Act), with one of the subsidiaries continuing as the amalgamated company. The shares of each group company, other than the amalgamated company, would be cancelled without payment or other consideration. By operation of s 225 of the Companies Act, the amalgamated company would succeed to all property, rights, powers and privileges, as well as to all the liabilities and obligations, of each of the amalgamating companies. After the amalgamation, the amalgamated company would be left with surplus assets.

   - **Liquidation**

     Following the amalgamation, the amalgamated company would distribute its surplus assets to the Taxpayer and be removed from the Companies Register pursuant to s 318(1)(d) of the Companies Act. Section 318(1)(d) of the Companies Act allows for the removal of a company from the register on the grounds that it had ceased to carry on business, has discharged in full its liabilities to all its known creditors, and has distributed its surplus assets in accordance with its constitution and the Companies Act.

Issues | Take

4. The issues considered in the ruling application were:

- Whether the amalgamation of the group of subsidiaries would be a "resident's restricted amalgamation" (as defined in section FO 3).
- How s FO 6 applies in relation to the shares in each amalgamating company.
- The effect of the amalgamation on financial arrangements (eg, intercompany loans) between the group of amalgamating subsidiaries.
- The effect of the amalgamation on an intercompany loan from another of the Taxpayer's subsidiaries (not in the group).
- Whether taxable dividends arose on the amalgamation under s CD 35.
- Whether the amalgamated company would inherit capital gain amounts of the other subsidiaries under s CD 44(8).
- Whether the distribution of the amalgamated company's surplus assets would occur "on the liquidation" of the company for the purposes of s CD 26.
- Whether the amount the amalgamated company distributes to the Taxpayer, to the extent it is not a dividend, produces a capital gain amount for the Taxpayer under s CD 44(7)(c).
- Whether the amount derived by the Taxpayer from the disposal of its shares in the amalgamated company as a result of the liquidation would be income under any of ss CA 1(2), CB 1, CB 3, CB 4, CB 5 or CV 1.
- Whether s BG 1 would apply to negate or vary any of the above.

Decisions | Whakatau

5. The Tax Counsel Office (TCO) concluded that it could rule as follows:

- The amalgamation of the group of subsidiaries was a "resident's restricted amalgamation" (as defined in s FO 3), provided that:
  - at the time of the amalgamation, none of the group of subsidiaries was to be treated under, and for the purposes of, a double tax agreement as resident in another country; and
  - the group of subsidiaries did not opt out of this treatment in accordance with s FO 3(5).

- Under s FO 6, the shares in each group company, other than the amalgamated company, were to be treated as having been disposed of immediately before the amalgamation by their respective shareholders for an amount equal to the cost of those shares to the respective shareholder.
- In respect of the intercompany loans between the subsidiaries in the group that were eliminated as a result of the amalgamation:
    - Those loans were to be treated as repaid in full on the date of the amalgamation in accordance with s FO 21.
    - Each debtor would have a nil base price adjustment (BPA) calculated under s EW 31(5) and therefore no income under s EW 31(1) or expenditure under s EW 31(4).
    - One of the subsidiaries in the group was a creditor of some of the other subsidiaries in the group. The creditor subsidiary would not be required to calculate a base price adjustment under s EW 31 because the loans are excepted financial arrangements for that subsidiary under s EW 5(10).
    - The creditor subsidiary would not derive any income under s CA 1(2) or s CB 1.
- In respect of intercompany lending from one of the subsidiaries in the group to another of the Taxpayer's subsidiaries (not in the group) and as a consequence of the amalgamation:
    - The lending subsidiary would not be required to calculate a base price adjustment under s EW 31 because the loan is an excepted financial arrangement for that subsidiary under s EW 5(10).
    - That subsidiary would not derive any income under s CA 1(2) or s CB 1.
- Any amounts derived by the amalgamated company on the amalgamation from acquiring property of the other subsidiaries in the group, or being relieved of obligations owed to the other subsidiaries in the group, were not dividends under s CD 35.
- When the amalgamated company calculated its "available capital distribution amount" (ACDA) in accordance with s CD 44(1), that company would be treated under s CD 44(8) as deriving a capital gain amount on amalgamation equal to the net "capital gain amount" of the creditor subsidiary (determined in accordance with s CD 44) to the extent that the amount was available for distribution at the time of the amalgamation.
- The distribution of the amalgamated company's surplus assets to the Taxpayer would occur on "liquidation" (as defined in s YA 1) so that under s CD 26 the

amount paid in relation to shares in the amalgamated company would only be a dividend to the extent to which it is more than the amalgamated company's:

- "available subscribed capital" (ASC) per share calculated under the ordering rule in accordance with ss CD 23 and CD 43; and
- ACDA calculated under s CD 44.

- The amount the amalgamated company distributes to the Taxpayer under the liquidation, to the extent it is excluded from being a dividend under ss CD 26(2)(b) and CD 44, will be treated as a capital gain amount for the Taxpayer under s CD 44(7)(c) when the Taxpayer calculates its ACDA in accordance with s CD 44(1).
- The amount the Taxpayer derived from the disposal of its shares in the amalgamated company as a result of the liquidation would not be income under any of ss CA 1(2), CB 1, CB 3, CB 4, CB 5 or CV 1.
- Section BG 1 does not apply to negate or vary the above ruling points.

Reasons for decisions | Pūnga o ngā whakatau

Issue 1 | Take tuatahi: Resident's restricted amalgamation (s FO 3)

6. The Taxpayer requested the Commissioner to rule that the amalgamation of the group of companies will be a "resident's restricted amalgamation" (as defined in s FO 3).

7. TCO considered the requirements of s FO 3 as follows:

- Resident in New Zealand – s FO 3(1)(a) and (b): It was clear that each of the group companies would be New Zealand resident under s YD 2(1)(a), and therefore "resident in New Zealand" as per the definition in s YA 1. A proviso to the ruling was included to ensure none of the group companies would be treated under, and for the purposes of, a double tax agreement as resident in another country.
- Not derive only exempt income – s FO 3(1)(c): While the group companies were not currently deriving any income, if they did derive income, it would not only be exempt income (excluding exempt income under ss CW 9 and CW 10).
- Not a qualifying company – s FO 3(1)(d) and s FO 3(2): TCO was satisfied that none of the group companies could be qualifying companies as they did not meet the criteria for a qualifying company.

- Not opt out – s FO 3(5): For completeness, TCO made it a proviso of the ruling that the group companies do not opt out of this treatment in accordance with s FO 3(5).

Conclusion

8. TCO concluded the Commissioner could rule that the amalgamation of the group companies would be a "resident's restricted amalgamation" (as defined in s FO 3), provided that:

   - at the time of the amalgamation, none of the group companies will be treated under, and for the purposes of, a double tax agreement as resident in another country; and
   - the group companies do not opt out of this treatment in accordance with s FO 3(5).

Issue 2 | Take tuarua: Shares in amalgamating companies (s FO 6)

9. The Taxpayer requested the Commissioner to rule that, as a consequence of the amalgamation, the shares in the amalgamating companies be treated as disposed of immediately prior to the amalgamation for an amount equal to their cost per s FO 6.

10. Section FO 6 states:

> **FO 6 Cancellation of shares**
>
> If an amalgamating company (company A) holds shares in another amalgamating company (company B), and the shares are cancelled on the amalgamation, company A is treated as having disposed of the shares in company B immediately before the amalgamation for an amount equal to the cost of the shares to company A.

11. For company law purposes, the shares of each group company (other than the amalgamated company) would be cancelled without payment or other consideration as a consequence of amalgamating under s 222 of the Companies Act.

12. TCO was satisfied that, prior to the proposed amalgamation, all the shares in each amalgamating company that were to be cancelled on the amalgamation were held by another amalgamating company. Accordingly, under s FO 6 the direct holding company would be treated as having disposed of those shares immediately before the amalgamation for an amount equal to the cost of the shares to it.

Conclusion

13. TCO concluded the Commissioner could rule that the shares in the amalgamating companies would be treated as having been disposed of immediately before the amalgamation by their respective shareholders for an amount equal to the cost of those shares to the respective shareholder under s FO 6.

Issue 3 | Take tuatoru: Financial arrangements between amalgamating companies (s FO 21)

14. The Taxpayer requested the Commissioner to rule that financial arrangements (eg, intercompany loans) between the amalgamating companies that are eliminated as a result of the amalgamation will be treated as repaid in full with the result that no taxable income or expenditure arose.

15. TCO structured its analysis as follows:

- Application of s FO 21 to the intercompany loans.
- Whether income arises for the debtors under the financial arrangements rules.
- Whether a BPA is required for the lender.
- Whether income arises for the creditor under s CA 1(2) or s CB 1.

Application of s FO 21 to the intercompany loans

16. Where s FO 21 applies, the debtor is treating as having paid (s FO 21(2)) and the creditor is treated as having been paid (s FO 21(3)) the amount of the financial arrangement on the date of the amalgamation (ie, it is treated as having been repaid in full). TCO considered the three requirements of s FO 21(1) as set out below.

Section FO 21(1)(a)

17. For s FO 21 to apply, the "amalgamating companies" must be "parties to a financial arrangement that exists on the date of the amalgamation".

18. A loan is a financial arrangement under the general definition in s EW 3(2). However, s EW 4(3) provides that an excepted financial arrangement is not a financial arrangement.

19. Section EW 5 sets out what arrangements constitute excepted financial arrangements. In the context of the intercompany loans, only s EW 5(10) is relevant and provides that

a loan to which all the following apply is an excepted financial arrangement for the lender:

- the loan is in New Zealand currency, and
- the loan is interest-free, and
- the loan is repayable on demand.

20. The above requirements were included as facts in the description of the arrangement, meaning the intercompany loans between the group companies would be excepted financial arrangements under s EW 5(10) for the lenders.

21. Accordingly, the intercompany loans were:

- excepted financial arrangements under s EW 5(10), and therefore not financial arrangements under s EW 4(3), for the lenders; and
- financial arrangements for the borrowers.

22. TCO then considered the following question: What does this mean in terms of the application of s FO 21, which proceeds on the basis that "amalgamating companies are parties to a financial arrangement" (ie, on either side of it such that it is eliminated on amalgamation)?

23. A "financial arrangement" exists for each of the amalgamating company debtors that are party to the intercompany advances. Logically (and legally), the amalgamating company lenders are also party to those intercompany advances, being that the principal was lent by them and is owed to them. TCO concluded that s FO 21(1)(a) was technically met.

24. TCO also considered whether the fact that the intercompany loans were not financial arrangements for the creditor due to the application of s EW 5(10) meant that s FO 21(1)(a) should be treated as not being met.

25. In TCO's view, the text of the legislative requirement that "amalgamating companies are parties to a financial arrangement that exists on the date of the amalgamation" indicates a purpose that the provision is limited to financial arrangements that will be eliminated upon amalgamation due to the obligor/obligee interests merging. This entry requirement in s FO 21 is also in s FO 18, which may have application where the other requirements of s FO 21 are not met.

26. Both ss FO 18 and FO 21 treat the financial arrangement as discharged (because it ceases to exist). This can be compared with the other provisions in subpart FO concerning financial arrangements (s FO 12 to s FO 15) that provide for a disposal and

acquisition of the financial arrangement (because it remains on foot and is not eliminated).

27. As the intercompany loans that are financial arrangements for the debtors are eliminated as a result of the amalgamation (ie, due to the creditor and debtor being amalgamated such that the obligor/obligee interests merge), s FO 21(1)(a) being met appears consistent with its purpose.

28. TCO concluded that the s FO 21(1)(a) requirement was met.

Section FO 21(1)(b)

29. For s FO 21 to apply, the next requirement is that s EW 46C(1)(a) or (b) (Consideration when debt remitted within economic group) applies to the amalgamating companies as creditor and debtor for the financial arrangement.

30. Relevantly, s EW 46C(1)(a) applies to the extent to which an amount of debt is remitted and the creditor is a member of the same wholly-owned group of companies as the debtor and the debtor is a New Zealand resident company.

31. In respect of the intercompany loans, each of the group companies are incorporated in New Zealand and therefore resident in New Zealand for tax purposes. Accordingly, provided the creditor is a member of the same wholly-owned group of companies as the debtors, s EW 46C(1)(a)(i) will apply to the amalgamating companies as creditor and debtor for the relevant intercompany loan.

32. As the amalgamating companies were a wholly-owned group of companies, the requirement in s FO 21(1)(b) was met.

Section FO 21(1)(c)

33. For s FO 21 to apply, the final requirement is that s EW 46C(3) does not apply. Section EW 46C(3) states that it does not apply in certain circumstances where the creditor is a non-resident.

34. As the lender in respect of each of the intercompany loans between the amalgamating companies is incorporated in New Zealand and therefore resident in New Zealand, s EW 46C(3) will not apply.

Section FO 21: conclusion

35. TCO concluded above that the requirements of s FO 21(1) were met and therefore s FO 21 applies to the intercompany loans. Accordingly, under s FO 21(2) the debtor is

treated as having paid, and under s FO 21(3) the creditor is treated as having been paid, the amount of the financial arrangement on the date of the amalgamation. In other words, the intercompany loans will be treated as having been repaid in full.

Whether income arises for the debtors under the financial arrangements rules

36. As the intercompany loans were financial arrangements for the borrowers (and not excepted financial arrangements), the borrowers would be required to calculate and allocate income and expenditure from the loans in accordance with the financial arrangements rules: s EW 9(1).

37. Section EW 29 requires that a BPA is calculated when a person effectively ceases to be party to the financial arrangement (ie, on maturity of the financial arrangement when the last payment contingent on the financial arrangement is treated as having been paid).

38. The last payment contingent on the financial arrangement is treated as having been paid on the date of the amalgamation under s FO 21. Accordingly, the financial arrangement will have matured and a BPA will be required.

39. The BPA formula is (s EW 31(5)):

consideration – income + expenditure + amount remitted.

40. As set out in s FO 21, each debtor is treated as having paid the amount of the financial arrangement on the date of the amalgamation.

41. The item "consideration" in the BPA is all consideration that has been paid or is or will be payable to the person, less all consideration that has been paid or is or will be payable by the person, under the financial arrangement (s EW 31(7)). In respect of the intercompany loans, as the loans were in NZD and interest-free, the only consideration payable under the loans was the initial principal advanced, less the principal that is treated as having been repaid by the debtor under s FO 21(2). Accordingly, the item "consideration" will net out to zero in the BPA formula.

42. The items "income" and "expenditure" refer to amounts derived and incurred by the person under the financial arrangement in earlier income years. As the only consideration payable under the loans was in respect of principal and nets out, no income or expenditure would have been incurred under the financial arrangements rules in respect of the intercompany loans in previous years.

43. The item "remitted amount" only ever gives rise to an amount in a creditor's BPA, and therefore there will be no "remitted amount" for the borrowers under the intercompany loans.

44. Accordingly, the result of the BPA calculation in s EW 31 for the borrower is nil. TCO therefore concluded that the Commissioner could rule that each debtor will have a nil BPA calculated under s EW 31(5) and therefore no income under s EW 31(1) or expenditure under s EW 31(4).

Whether a BPA is required for the lender

45. As set out above at [18]-[21], the intercompany loans were excepted financial arrangements and not financial arrangements for the lender. Therefore, the lender did not need to apply the financial arrangements rules to the loans that were excepted financial arrangements under s EW 5(10) (unless they chose to treat them as financial arrangements under s EW 8(1)(b)).

46. In light of the above, TCO concluded that the lender was not required to calculate a BPA under s EW 31.

Whether income arises for the creditor under s CA 1(2) or s CB 1

47. An amount will be income of a person if it is their income under ordinary concepts (s CA 1(2)).

48. Under s FO 21(3), the lender would be treated as having been paid the amount of each of the intercompany advances on the date of the amalgamation – in other words, will be treated as having been repaid the principal that was advanced. Given this is simply a repayment of the amount advanced, rather than any gain on top of that amount, TCO considered:

    - It was difficult to see how this could be considered "income" in accordance with ordinary concepts.
    - An amount of principal is more in the nature of a return of contributed capital rather than any kind of gain or income stream (such as interest).

49. For the same reason, repayment of the amount advanced would not constitute business income under s CB 1. TCO considered that, as the repayment of loan principal is of a capital nature, it would not give rise to income under s CB 1.

50. Accordingly, TCO concluded that the Commissioner could rule that the creditor would not derive any income under s CA 1(2) or s CB 1.

Conclusion

51. TCO concluded the Commissioner could rule in respect of the intercompany loans between the amalgamating companies that are eliminated as a result of the amalgamation:

    - Those loans would be treated as repaid in full on the date of the amalgamation in accordance with s FO 21.
    - Each debtor would have a nil BPA calculated under s EW 31(5) and therefore no income under s EW 31(1) or expenditure under s EW 31(4).
    - The creditor would not be required to calculate a BPA under s EW 31 because the loans were excepted financial arrangements for the creditor under s EW 5(10).
    - The creditor would not derive any income under s CA 1(2) or s CB 1.

Issue 4 | Take tuawhā: Financial arrangements between amalgamating company and other group company

52. There were intragroup loans between one of the amalgamating companies and another group company that is not being amalgamated (ie, the loans would continue on foot but pass to the amalgamated company after the amalgamation).

53. The Taxpayer requested the Commissioner to rule that the lender would not be required to calculate a BPA as a consequence of the loans passing to the amalgamated company because the loans were an excepted financial arrangement.

Financial arrangements rules

54. A loan is a financial arrangement under the general definition in s EW 3(2). Accordingly, the intragroup loans will each be a "financial arrangement" in accordance with s EW 3. However, s EW 4(3) provides that an excepted financial arrangement is not a financial arrangement.

55. The description of the Arrangement includes as facts that the intragroup loans are in NZ currency, interest-free and repayable on demand.

56. This means that the loans were an excepted financial arrangement for the lender under s EW 5(10), and therefore not a financial arrangement for the lender in accordance with s EW 4(3).

57. Accordingly, the amalgamating company did not need to apply the financial arrangements rules to the loans that were an excepted financial arrangement under

s EW 5(10) (unless they chose to treat it as a financial arrangement under s EW 8(1)(b)). As the amalgamating company did not need to apply the financial arrangements rules to the receivable, it was not required to perform a BPA under s EW 31 in accordance with those rules when the amalgamated company succeeds to that loan on amalgamation.

Section FO 10

58. When the amalgamation occurs (and in accordance with s 225 of the Companies Act 1993) the amalgamated company succeeds to the amalgamating company's receivable. Accordingly, as a result of the amalgamation, the amalgamating company would no longer be party to the receivable.

59. Subpart FO sets out the rules that provide for some tax consequences when companies amalgamate. As the receivable is not a financial arrangement for the amalgamating company (it is an excepted financial arrangement), the amalgamation provisions addressing financial arrangements (ss FO 12 to FO 15 and ss FO 18 to FO 21) would not apply. Nor would ss FO 16 and FO 17 apply as the receivable was not amortising property or land.

60. TCO considered this left s FO 10 as the default provision when "property" belonging to an amalgamating company becomes the property of the amalgamated company on a resident's restricted amalgamation.

61. The term "property" is not defined for the purposes of the amalgamation rules. TCO considered that "property" was something that was capable of being owned and being transferred. As the receivable was an enforceable right of the amalgamating company that could be transferred, it therefore constituted "property" of the amalgamating company.

62. TCO concluded the result of s FO 10 applying is that the amalgamating company will be treated as having disposed of the receivable immediately before the amalgamation, and the amalgamated company will be treated as having acquired the receivable, under s FO 10(3).

63. Accordingly, under s FO 10(4) the amalgamated company would be treated as having acquired the property on the date on which the amalgamating company acquired it for an amount that is the sum of-

- the price paid for the property; and
- any expenditure incurred in acquiring or improving the property; and

- any expenditure incurred in securing or improving the amalgamating company's legal rights to the property.

64. The only amount paid by the amalgamating company, or expenditure incurred by the amalgamating company, in respect of the receivable is the principal advanced. The amalgamated company would therefore be treated as having acquired the receivable for that amount.

65. In summary, the amalgamating company would be treated as having disposed of the receivable to the amalgamated company immediately before the amalgamation, for an amount equal to the principal outstanding.

Sections CA 1(2) and CB 1

66. Similar to the analysis in respect of the disposal of the intercompany loans in Issue 3 of this Technical Decision Summary (TDS), the disposal should not give rise to income under ordinary concepts or business income under s CA 1(2) or s CB 1. The loan itself, being interest free, was solely of a capital nature and no gain would be made on its disposal or repayment.

67. Accordingly, TCO considered that the amalgamating company would not derive any income under s CA 1(2) or s CB 1 in respect of the disposal of the receivable on amalgamation.

Conclusion

68. TCO concluded the Commissioner could rule that, in respect of the intercompany lending as a consequence of the amalgamation:

- The amalgamating company would not be required to calculate a BPA under s EW 31 because the loan was an excepted financial arrangement under s EW 5(10).
- The amalgamating company would not derive any income under s CA 1(2) or s CB 1.

Issue 5 | Take tuarima: No dividend arises on amalgamation (s CD 35)

69. The Taxpayer requested the Commissioner to rule that no taxable dividends arise on the amalgamation because amounts derived by the amalgamated company from

acquiring property of the amalgamating companies, or being relieved of obligations owed to the amalgamating companies, are not dividends under s CD 35.

70. As summarised above under previous issues in this TDS, when the amalgamation occurs the amalgamated company:

- will succeed to a number of receivables, and
- a number of loans between amalgamating companies will be eliminated due to the merging of the obligor/obligee interests when the amalgamated company succeeds to the other parties' rights and obligations under those agreements.

71. Section CD 3 states that ss CD 4 to CD 20 define what is a dividend.

72. The amalgamated company acquiring property of, or being relieved of obligations owed to, the other amalgamating companies on amalgamation will give rise to a dividend in accordance with s CD 4 if:

- there is a "transfer of company value" from a "company" to a person (as defined in s CD 5); and
- the cause of the transfer is a "shareholding in the company" (as described in s CD 6); and
- none of the exclusions in ss CD 22 to CD 37 apply to the transfer.

To the extent that a transfer of company value arises as a result of this, s CD 35 will be directly relevant.

73. Section CD 35 states that an amount derived by an amalgamated company on a resident's restricted amalgamation from an amalgamating company that ends its existence on the amalgamation is not a dividend if it arises from-

- the amalgamated company acquiring property of the amalgamating company; or
- the amalgamated company being relieved of an obligation owed to the amalgamating company.

74. As concluded by TCO above at [8], the Commissioner could rule that the proposed amalgamation would be a "resident's restricted amalgamation" as defined in s FO 3.

75. In light of this, any amount that the amalgamated company derived from any of the amalgamating companies in respect of acquiring property of those companies, or being relieved of an obligation owed to those companies, was not a dividend in accordance with s CD 35. TCO considered that this meant it would not constitute a dividend as defined in s CD 4.

Conclusion

76. TCO concluded the Commissioner could rule that any amounts derived by the amalgamated company on the amalgamation from acquiring property of the amalgamating companies, or being relieved of obligations owed to the amalgamating companies, are not dividends under s CD 35.

Issue 6 | Take tuaono: Amalgamated company inherits amalgamating companies' capital gain amounts (s CD 44(8))

77. The Taxpayer requested the Commissioner to rule that, for the purposes of the ACDA calculation in s CD 44, the amalgamated company would inherit capital gain amounts of one of the amalgamating companies to the extent these amounts were available for distribution at the time of the amalgamation under s CD 44(8).

78. Section CD 44(1) and (2) provide for the ACDA calculation. In summary, the ACDA is the amount of any distribution made on the liquidation of a company that represents capital property or previously derived net capital gains. A "capital gain amount" is taken into account in the item "capital gains" in the ACDA formula in s CD 44(1).

79. Section CD 44(8) provides that the amalgamated company inherits any "capital gain amount" from a non-surviving amalgamating company to the extent to which the amalgamating company's capital gain amount was available for distribution at the time of the amalgamation and was not distributed to anyone other than the amalgamated company.

80. Accordingly, to the extent the amalgamating company has a "capital gain amount" at the time of the amalgamation that is available for distribution and not distributed to anyone other than the amalgamated company, s CD 44(8) provides that the amalgamated company would be treated as deriving a capital gain amount equal to that amount.

81. The facts as described by the Taxpayer did not detail any distributions being made to any person as a result of the amalgamation (and TCO considered that if this was to occur, it would be a material difference for the purposes of s 91EB(2) of the Tax Administration Act 1994 (TAA)). Accordingly, the amalgamating company's capital gain amounts were not distributed to anyone other than the amalgamated company.

82. TCO considered this was sufficient to rule favourably, as the ruling paragraph requested largely mirrored s CD 44(8).

83. For completeness, TCO noted that the Taxpayer's calculations in their submissions demonstrate their expectation that the amalgamated company inherited the net capital gain amounts, not the gross amounts, under s CD 44(8).

Conclusion

84. TCO concluded the Commissioner could rule that, when the amalgamated company calculated its ACDA in accordance with s CD 44(1), the amalgamated company would be treated as deriving a capital gain amount on amalgamation equal to the net "capital gain amount" of the amalgamating company to the extent that amount was available for distribution at the time of the amalgamation under s CD 44(8).

Issue 7 | Take tuawhitu: Distribution on liquidation of the amalgamated company (s CD 26)

85. The Taxpayer requested the Commissioner to rule that the distribution of the amalgamated company's surplus assets will occur "on liquidation" for tax purposes so that s CD 26 will apply.

86. Relevantly, s CD 26 applies when a shareholder is paid an amount in relation to a share on the liquidation of the company, and specifies that the amount paid is a dividend only to the extent to which it is more than:

- The ASC per share calculated under the ordering rule; and
- the ACDA calculated under section CD 44.

TCO noted that the amalgamated company is not a statutory producer board and therefore ss CD 26(3) and (4) were not relevant.

87. As stated above in the facts at [3], the wind-up of the group of subsidiaries was to be done in two steps and the second step states that the liquidation will occur by the amalgamated company being removed from the register of companies under s 318(1)(d) of the Companies Act.

88. Removal from the register of companies under s 318(1)(d) of the Companies Act will constitute liquidation under para (a)(i) of the definition of "liquidation" in s YA 1. For the purposes of s CD 26, the question is then whether the distribution of surplus assets (required to facilitate the removal under s 318(1)(d)) occurs "on the liquidation" of the amalgamated company. This is informed by para (b) of the definition of "liquidation" in s YA 1, which states that this includes the period that starts with a step that is legally

necessary to achieve liquidation, including a request of the kind referred to in s 318(1)(d) of the Companies Act.

89. The Commissioner has previously considered this matter in BR Pub 14/09 (issued for an indefinite period beginning on 1 January 2015). BR Pub 14/09 is directly relevant and confirms the following:

> **The Arrangement to which this Ruling applies**
>
> The Arrangement is the liquidation of a company when a request is made under s 318(1)(d) of the Companies Act 1993 that the company be removed from the New Zealand register of companies.
>
> **How the Taxation Laws apply to the Arrangement**
>
> The Taxation Laws apply to the Arrangement as follows:
>
> When a request is made to the Registrar of Companies to remove a company from the New Zealand register of companies under s 318(1)(d) of the Companies Act 1993, the first step legally necessary to achieve liquidation is a resolution by the shareholders or board of directors or, where applicable, another overt decision-making act provided for in a company's constitution to adopt a course of action that will end in removal from the register.
>
> That first step starts the period specified in para (b)(i) of the definition of "liquidation" in s YA 1. Anything done after that first step to enable liquidation occurs "on liquidation" for the purposes of the Income Tax Act 2007.

90. TCO was satisfied, based on the facts provided, that the Taxpayer would commence the liquidation of the amalgamated company by resolving to undertake the required activities to seek, and then seeking, removal from the register of companies. This would be the first step starting the period specified in para (b)(i) of the definition of "liquidation" in s YA 1. The subsequent distribution of surplus assets to the Taxpayer would then occur in order to enable removal under s 318(1)(d) of the Companies Act (it is a requirement of that section that surplus assets are distributed). Accordingly, the distribution of surplus assets by the amalgamated company to the Taxpayer would occur on the "liquidation" of the amalgamated company, as per the definition of "liquidation" in s YA 1 and BR PUB 14/09.

Conclusion

91. TCO concluded the Commissioner could rule that the distribution of the amalgamated company's surplus assets to the Taxpayer would occur on "liquidation" (as defined in

s YA 1) so that under s CD 26 the amount paid in relation to shares in the amalgamated company will only be a dividend to the extent to which it is more than the amalgamated company's:

- ASC per share calculated under the ordering rule; and
- ACDA calculated under s CD 44.

Issue 8 | Take tuawaru: Capital gain amount for the Taxpayer on liquidation of the amalgamated company (s CD 44(7)(c))

92. The Taxpayer requested the Commissioner to rule that the amount the amalgamated company distributed to the Taxpayer, to the extent it represents the distribution of a capital gain amount and is excluded from being a dividend under ss CD 26(2)(b) and CD 44, will produce a capital gain amount for the Taxpayer under s CD 44(7)(c).

93. Section CD 44(1) and (2) provide for the ACDA calculation. In summary, the ACDA is the amount of any distribution made on the liquidation of a company that represents capital property or previously derived net capital gains.

94. Relevant to the ruling requested by the Taxpayer, s CD 44(7)(c) states:

> For the purposes of this section, a company derives a capital gain amount if,-
>
> …
>
> (c) an amount is derived by the company [the Taxpayer] from another company [the amalgamated company] on liquidation of the other company [the amalgamated company] that is excluded from being a dividend as a result of section CD 26(2)(b) and this section;
>
> …

95. As set out under Issue 7 in this TDS, removal from the register of companies under s 318(1)(d) of the Companies Act constitutes a "liquidation" for tax purposes and a distribution will occur "on liquidation" following the directors' resolution to undertake the steps necessary to action the removal. Accordingly, as stated above at [91], any distribution will only be a dividend to the extent to which it is more than the amalgamated company's:

- ASC per share calculated under the ordering rule; and
- ACDA calculated under s CD 44.

96. Where the amount is excluded from being a dividend under ss CD 26(2)(b) and CD 44, the Taxpayer will have a capital gain amount under s CD 44(7)(c) when calculating its ACDA on liquidation in accordance with s CD 44(1).

97. The ruling paragraph requested by the Taxpayer reflects the statutory language of s CD 44(7)(c), and therefore TCO considered that it could rule favourably.

Conclusion

98. TCO concluded the Commissioner could rule that the amount the amalgamated company distributes to the Taxpayer, to the extent it is excluded from being a dividend under ss CD 26(2)(b) and CD 44, will produce a capital gain amount for the Taxpayer under s CD 44(7)(c) when the Taxpayer calculates its ACDA in accordance with s CD 44(1).

Issue 9 | Take tuaiwa: Whether the receipt was capital or revenue in nature

99. The Taxpayer requested the Commissioner to rule that the amount derived by the Taxpayer from the liquidation of the amalgamated company was not a business profit within the meaning of s CB 1 and that the following related provisions did not apply:

- Section CB 3 (the amount is not income of the Taxpayer from a profit-making undertaking or scheme).
- Section CB 4 (the Taxpayer did not acquire the shares in the amalgamated company with the purpose of disposal).
- Section CB 5 (the Taxpayer did not carry on a business of dealing in shares).
- Section CA 1(2) (the amount is not otherwise income of the Taxpayer under ordinary concepts).
- Section CV 1 (no taxable income arises because treating the Taxpayer and its wholly-owned group members as a notional single company, the amount was not income for the Taxpayer).

100. In summary, TCO considered that:

- The amount the Taxpayer derived from the liquidation of the amalgamated company would not be caught by s CB 1, s CB 3, s CB 4, s CB 5 or s CA 1(2) if that receipt was a capital gain.
- In order to determine whether the amalgamated company's profit would be income under any of those provisions, it was necessary to determine whether the receipt was capital or revenue in nature.

- The purpose of s CV 1 was to prevent undue advantage being gained through some profits being regarded as capital gains when received by a single company when in reality they were revenue profits in the context of the overall business activities of a group of commonly owned companies.

101. In TCO's view, based on the information provided by the Taxpayer (including the reasons for the Taxpayer's investment and divestment decisions as set out in the ruling application, and the large number of documents provided) there was nothing to suggest the Taxpayer made investments for the purpose of disposal. Accordingly, TCO considered that the Taxpayer held its investments on capital account.

102. Further, TCO considered that even if some of the Taxpayer's investments were held on revenue account, that would not change the outcome. This was because TCO considered it unlikely in light of the decisions in the *Rangatira* line of cases and *Renouf* that the tax status of the Taxpayer's shares held in the amalgamated company would be tainted by a wholly owned subsidiary holding an investment on revenue account.[1] In disposing of its shares in the amalgamated company, the Taxpayer was not manufacturing a capital receipt out of what would otherwise have been a taxable receipt.

103. In addition, for the same reasons, TCO considered the mischief contemplated by s CV 1 did not exist in this case and that section did not apply.

Conclusion

104. TCO concluded the Commissioner could rule that:

- The amount derived by the Taxpayer on the liquidation of the amalgamated company was not business profits under s CB 1.
- The Taxpayer did not acquire its shares in the amalgamated company with the purpose of disposal for the purposes of s CB 4.
- The amount derived by the Taxpayer on the liquidation of the amalgamated company was not income from a profit-making undertaking or scheme under s CB 3.
- The Taxpayer did not carry on a business of dealing in shares, for the purposes of s CB 5.

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[1] *Rangatira Ltd v CIR* (1994) 16 NZTC 11,197 (HC), *CIR v Rangatira Ltd* (1995) 17 NZTC 12,182 (CA), *Rangatira Ltd v CIR* (1996) 17 NZTC 12,727 (PC), *CIR v Renouf Corporation & Ors* (1998) 18 NZTC 13,914 (CA).

- The amount derived by the Taxpayer on the liquidation of the amalgamated company was not otherwise income of the Taxpayer under ordinary concepts, for the purposes of s CA 1(2).
- The amount the Taxpayer derived from the disposal of its shares in the amalgamated company as a result of liquidating the amalgamated company was not income under s CV 1.

Issue 10 | Take tekau: Tax avoidance?

105. The Taxpayer requested the Commissioner to rule that s BG 1 did not apply to the arrangement summarised in the facts above at [1]-[3].

106. Section BG 1(1) provides that a "tax avoidance arrangement" is void as against the Commissioner. The approach to s BG 1 was settled by the Supreme Court in *Ben Nevis Forestry Ventures Ltd v CIR* [2008] NZSC 115, [2009] 2 NZLR 289, which has been followed in subsequent judicial decisions.

107. TCO's approach in making this decision is consistent with Interpretation Statement: IS 23/01 Tax avoidance and the interpretation of the general anti-avoidance provisions sections BG 1 and GA 1 of the Income Tax Act 2007 (3 February 2023) (IS 23/01).[2] IS 23/01 will not be replicated in this TDS but in summary the steps are as follows:

- Understanding the legal form of the arrangement. This involves identifying and understanding the steps and transactions that make up the arrangement, the commercial or private purposes of the arrangement and the arrangement's tax effects.
- Determining whether the arrangement has a tax avoidance purpose or effect. This involves:
  - Identifying and understanding Parliament's purpose for the specific provisions that are used or circumvented by the arrangement.
  - Understanding the commercial and economic reality of the arrangement as a whole by using the factors identified by the courts.
  - Considering the implications of the preceding two steps and answering the ultimate question under the Parliamentary contemplation test: Does the arrangement, when viewed in a commercially and economically realistic

[2] Please note the Tax Counsel Office decision was made before the previous interpretation statement (IS 13/01) was updated and replaced by IS 23/01.

way, make use of or circumvent the specific provisions in a manner consistent with Parliament's purpose?

- If the arrangement does have a tax avoidance purpose or effect, consider the merely incidental test.

108. Taking into account all of the relevant facts and circumstances (noting that as this is a summary it may not contain all the facts or assumptions relevant to the decision and, therefore, cannot be relied on) TCO concluded as follows.

The "arrangement"

109. An arrangement is defined widely and includes enforceable contracts, unenforceable understandings, and all steps and transactions carrying the arrangement into effect.[3] TCO considered it important to:

- fully understand the arrangement and to take into account all pertinent facts and information relating to it, and
- identify the provisions at issue and relevant tax effects.

110. For the purposes of the ruling application, the Taxpayer provided the facts and information relating to them. In particular, this involved the wind-up of the group of subsidiaries through a process of amalgamation and liquidation.[4]

111. The previous issues in this TDS summarise TCO's consideration of the provisions at issue and outline the relevant tax effects.

Does the arrangement involve "tax avoidance"?

112. For s BG 1 to apply, the arrangement must be a "tax avoidance arrangement".

113. TCO considered the test to identify whether an arrangement involved tax avoidance was to ask whether, viewed in a commercially and economically realistic way, the arrangement makes use of the Act (or circumvents provisions) in a manner that was consistent with Parliament's purpose (*Ben Nevis* at [109]). This involved identifying:

- Parliament's purpose for the relevant provisions; and
- the commercial reality and economic effects of the arrangement.

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3 Section YA 1 of the Act.

4 See above at [1]-[3].

Parliament's purpose for the specific provisions

114. Deciding whether provisions apply (or do not apply) as Parliament contemplated involves identifying Parliament's purpose for those provisions. Parliament's purpose is the result Parliament intended to achieve, or the end in mind Parliament had, for the provisions. Sometimes Parliament's purpose will be readily ascertainable from the words used. Other times it will be less obvious and a more in depth analysis will be required. It may also be relevant to consider Parliament's purpose for combinations of provisions.

115. IS 13/01 explains that it is logical to first ascertain Parliament's purpose to see whether the arrangement makes use of the Act in a way that is consistent with its purpose. Knowledge of Parliament's purpose provides a principled basis for the inquiry into the facts (ie, the commercial and economic reality of the arrangement). This order is consistent with comments in *Ben Nevis* at [102] and [104] that the test is one of "statutory construction" and is "firmly grounded in the statutory language".

Amalgamation provisions

116. Section FO 6 clearly prescribes that where shares held by an amalgamating company (A) in another amalgamating company (B) are cancelled on an amalgamation, company A is treated as disposing of those shares at cost.

117. Under s CD 35 an amount derived by an amalgamated company on a resident's restricted amalgamation is not a dividend if it arises from the amalgamated company acquiring property of an amalgamating company, or being relieved of an obligation owed to the amalgamating company.

118. Further, s CD 44(8) provides for amalgamated companies inheriting capital gains of amalgamating companies which cease to exist. Capital gain amounts are not lost on amalgamation (or liquidation of subsidiary companies), although they are still prevented from distribution tax free to ultimate shareholders until liquidation.

119. Section FO 21 applies when amalgamating companies are parties to financial arrangements that are to be eliminated as a result of an amalgamation. The loans are treated as being repaid in full on the amalgamation.

120. Both ss FO 21 and EW 46C were inserted by the Taxation (Annual Rates for 2016-17, Closely Held Companies, and Remedial Matters) Act 2017. Under s EW 46C a debt is treated as fully repaid so no debt remission income arises where the parties are part of the same wholly-owned group and there is no change in the net wealth of the economic group or dilution of ownership interest. This is because the creditor is

denied a bad debt deduction and the treatment would be otherwise asymmetrical. Section FO 21 replicates this effect for amalgamating companies.

121. Section EW 5(10) removes lenders of NZD, interest free, repayable on demand loans from the financial arrangements regime because such loans do not have any accrual implications for the lenders as they do not give rise to income or expenditure. Only lenders were provided this treatment, as borrowers could have income arising from debt remission.

122. For s FO 21 to apply the "amalgamating companies" must be "parties to a financial arrangement that exists on the date of the amalgamation". TCO considered that s FO 21 applies even though the intercompany loans that will be eliminated are excepted financial arrangements for the lenders.

123. TCO considered the purpose of s EW 5(10) and s EW 46C (which resulted in the introduction of s FO 21 to replicate the effect for amalgamating companies), and found that this purpose aided the interpretation of s FO 21. Section EW 46C only refers to a "debt", the "debtor" and the "creditor". There is no requirement that the debtor and creditor are parties to a financial arrangement. However, in the context of a wholly owned group of companies, one might expect that the debt could well be an excepted financial arrangement for a creditor under s EW 5(10). This does not prevent s EW 46C from applying to treat the debtor as fully repaying the debt.

On liquidation

Capital gain amounts

124. In general, under s CD 44(7) a company derives a "capital gain amount" (and a "capital gain" for the purposes of the formula in s CD 44(1)) if it disposes of "capital property" (to a person, subject to restrictions for related parties) for an amount that is more than the "cost of the property to the company". A "capital gain amount" also includes an "available capital distribution amount" derived from another company that was excluded from being a dividend on liquidation of that company under s CD 26(2)(b).

125. If a distribution of surplus assets occurs on liquidation s CD 26 provides that the amount paid is a dividend only to the extent to which it is more than:

- the "available subscribed capital" per share calculated under the ordering rule; and
- the "available capital distribution amount" calculated under s CD 44.

126. Where a receipt is excluded from being a dividend under s CD 26(2)(b), the recipient company will have a capital gain amount under s CD 44(7)(c) when calculating its "available capital distribution amount" under s CD 44(1).

127. Parliament's purpose is that a capital profit should retain its character when passed on to shareholders on liquidation. Further, Parliament intended to exclude from dividends any returns of available subscribed capital and approved capital gains distributed by a company in liquidation.

Sections CA 1(2), CB 1 - CB 5, CV 1

128. Taxpayers are taxed on income but not on capital receipts. This is set out most clearly in s CB 1 which states that an amount that a person derives from a business is income of the person, but this does not apply to an amount that is of a capital nature. The purpose of s CB 1 and the other identified provisions is to ensure that income is captured for tax purposes and capital receipts are not. This is a fundamental cornerstone of our tax system.

Identifying the facts, features, and attributes Parliament expected to be present or absent

129. TCO considered, from the above analysis on Parliament's purposes for the specific provisions at issue, that Parliament would expect the following facts, features and attributes to be present in, or absent from such an arrangement:

- For the concessionary amalgamation rules to apply, Parliament would expect that two or more companies have amalgamated and continued as one company as part of a genuine corporate restructuring.
- For a capital profit to be distributed tax free on liquidation and retain its character when passed on to shareholders, Parliament would expect that the company has ceased to exist on liquidation, the amount to be a bona fide capital amount, and that the distribution is made in a true economic sense.
- For the consideration on a share disposal to constitute capital and not income Parliament would expect the shares to be held long term in the nature of an investment to support the underlying business structure and to derive dividend income, rather than to realise a gain on disposal.

The commercial reality and economic effects of the arrangement

130. According to *Ben Nevis*, to consider whether an arrangement accords with Parliament's purpose for the relevant provisions, the arrangement is to be considered from the

perspective of its commercial reality and economic effects. The arrangement needs to be examined to see whether, and to what degree, the facts, features and attributes identified above are present (or absent). This is not a matter of simply identifying the commercial features or purposes of an arrangement. The focus is on what the arrangement, viewed as a whole, actually achieves.

131. Any steps in the arrangement that disguise the actual consequences for the parties, are artificial in a relevant way, or involve any pretence or circularity, may be ignored for these purposes. Only the true commercial and economic outcomes of an arrangement are tested against Parliament's purpose for the relevant provisions. For example, the court in *Ben Nevis* said that a "classic indicator" of a use that is outside Parliament's contemplation is an arrangement structured so the taxpayer gains the benefit of the relevant provision in an artificial or contrived way.

132. The court in *Ben Nevis* set out some of the factors that may be taken into account as part of an inquiry into the commercial reality and economic effects of an arrangement. These include the following:

- the manner in which the arrangement is carried out
- the role of all relevant parties and their relationships
- the economic and commercial effect of documents and transactions
- the duration of the arrangement, and
- the nature and extent of the financial consequences.

Application of the Parliamentary contemplation test

133. To assess whether the arrangement was in accordance with Parliament's purpose for the relevant provisions, TCO conducted a detailed analysis of the arrangement provided by the Taxpayer from the perspective of its commercial reality and economic effects (which was too detailed and specific to the Taxpayer's circumstances to be summarised in this TDS). Overall, TCO considered that the tax effects were uncontroversial, the use of the various provisions were within Parliament's purpose for those provisions. The facts, features and attributes that Parliament expected to be present (or absent) were present.

Conclusion

134. Accordingly, TCO concluded that the arrangement entered into by the Taxpayer did not have a tax avoidance purpose or effect. Given this conclusion it was not necessary for TCO to go on to consider the "merely incidental" test.