Inland Revenue
Te Tari Taake

TECHNICAL DECISION SUMMARY > PRIVATE RULING

WHAKARĀPOPOTO WHAKATAU HANGARAU > WHAKATAUNGA TŪMATAITI

Disposal of shares following amalgamation

Decision date | Rā o te Whakatau: 20 December 2024

Issue date | Rā Tuku: 14 April 2025

TDS 25/08

Subjects | Kaupapa

Amalgamation of companies; disposal of shares held on capital account; whether taxable

Taxation laws | Ture tāke

All legislative references are to the Income Tax Act 2007

Summary of facts | Whakarāpopoto o Meka

1. The Arrangement was the amalgamation of several related companies (the Applicants) which collectively held shares in E Ltd and the sale of those shares after amalgamation. A Ltd continued as the amalgamated company.

2. The shares in E Ltd had been acquired over a number of years and as long-term, open-ended investments and were held on capital account by the Applicants. The Applicants entered into an agreement to sell those shares to P Ltd prior to amalgamating.

Issues | Take

3. The main issues considered in this ruling were:

   - Whether the amalgamation of the Applicants was a "resident's restricted amalgamation" as defined in s FO 3;
   - Whether A Ltd (as the amalgamated company) was treated as having acquired the shares in E Ltd on the same date as they were acquired by the amalgamating company, for the same amount, and with the same intention and purpose;
   - Whether the amount that A Ltd (as the amalgamated company) derived from the disposal of the shares in E Ltd was taxable income under any of ss CA 1(2), CB 1, CB 3, CB 4 or CB 5.

Decisions | Whakatau

4. TCO concluded:

   - The amalgamation of the Applicants (with A Ltd continuing as the amalgamated company) was a "resident's restricted amalgamation" as defined in s YA 1 and s FO 3.

- Pursuant to s FO 10, A Ltd (as the amalgamated company) is treated as having acquired the shares in E Ltd which were held by other applicants on the same date those other applicants acquired them and for the sum of the amounts paid or incurred by them (relating to the shares in E Ltd) referred in s FO 10(4)(a), (b) and (c).
- The amount that A Ltd derived from the disposal of the shares in E Ltd after amalgamation was not taxable income under any of ss CA 1(2), CB 1, CB 3, CB 4 or CB 5.

5. The conclusion was subject to conditions that the administrative requirements of the Inland Revenue Acts were met by the Applicants.

Reasons for decisions | Pūnga o ngā whakatau

Issue 1 | Take tuatahi: Resident's restricted amalgamation

6. This issue concerned the requirements of a "resident's restricted amalgamation" as defined in FO 3.

7. TCO concluded that the proposed amalgamation met the requirements to qualify as a "resident's restricted amalgamation" as defined in s FO 3 because:

- The amalgamation met the definition of "amalgamation" in s YA 1.
- A resident's restricted amalgamation is an amalgamation between New Zealand resident companies that do not solely derive exempt income, except income under ss CW 9 and CW 10. The Applicants met these requirements, and this was stated in the description of Arrangement.
- Special rules which apply to qualifying companies were irrelevant as the relevant companies were not qualifying companies.

8. This conclusion was subject to the conditions that the administrative requirements of the Inland Revenue Acts were met by the Applicants.

Issue 2 | Take tuarua: Purpose of deemed acquisition under s FO 10

9. This issue concerned the interaction between s CB 4 and s FO 10. In particular, whether undertaking the amalgamation would cause s CB 4 to apply to the subsequent sale of

the shares in E Ltd to P Ltd. This is because at the time of the amalgamation, A Ltd had already entered into an agreement to dispose of the shares in E Ltd.

10. Section CB 4 provides 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.

11. Section FO 10 sets out the tax consequences where property passes on a resident's restricted amalgamation from an amalgamating company to an amalgamated company. Generally, it treats the amalgamated company as having acquired the property on the date the amalgamating company originally acquired the property, for the same cost. While s FO 10 deems an amalgamating company to acquire certain property, it does not specify the purpose of that deemed acquisition.

12. TCO considered that there was some ambiguity on the plain words as to how s CB 4 should apply in the context of the acquisition deemed to occur by s FO 10. TCO considered that the following interpretations were possible:

- the amalgamated company had no purpose for the acquisition,
- the amalgamated company's purpose should be treated as being the same purpose as that of the amalgamating company (at the time of the original acquisition),
- the acquisition is deemed to occur for the purposes of s FO 10, but not for the purposes of s CB 4, or
- the amalgamated company's purpose should be based on its state of mind at the time of the amalgamation.

13. TCO was of the view that the purposes of ss CB 4 and FO 10 did not support that the amalgamated company's purpose for the acquisition was based on the state of mind of the amalgamated company at the time of the amalgamation as:

- Section CB 4 refers to the person's intention as at the date of acquisition. The date of acquisition under s FO 10(3) and (4) is on the same date the amalgamating company originally acquired the property and is not the date of amalgamation.
- It is arguable that as the acquisition effected by s FO 10(3) is a deemed acquisition, it may not have been entered into for any purpose.
- The principle of continuance is more consistent with the amalgamated company adopting the purpose of the amalgamating companies with respect to property.

- The provisions relating to land that passes on amalgamation (s FO 17) directly address the treatment of land that is held on capital account by an amalgamating company and revenue account by an amalgamated company.
- However, the provisions relating to personal property (s FO 10) in the same circumstances do not directly address this even though similar policy concerns would arise.
- The background to the amalgamation rules shows that where property passes on amalgamation it was intended that the outcome should be the same as property that passes between members of a consolidated group.

14. Considering the above, TCO concluded that s FO 10(3) would not cause the disposal of the shares in E Ltd by A Ltd (as the amalgamated company) to be treated differently under s CB 4 than the same disposal would have been treated if the disposal occurred pre-amalgamation.

Issue 3 | Take tuatoru: ss CA 1(2), CB 1, CB 3, CB 4 and CB 5

15. This issue concerned the application of ss CA 1(2), CB 1, CB 3, CB 4 and CB 5.

16. Sections CA 1(2), CB 1, CB 3, CB 4 and CB 5 address:

- Income under ordinary concepts.
- Amounts derived from business.
- Amounts derived from a profit-making undertaking or scheme.
- Amounts derived from the disposal of personal property which was acquired for the purpose of disposal.
- Amounts derived from a business of dealing in personal property.

17. In summary, TCO considered that:

- The relevant case law[1] concerning s CA 1(2), s CB 1, s CB 3, s CB 4 and s CB 5 and the capital revenue test suggested that, if the amount A Ltd (as the amalgamated company) received from the sale of the shares in E Ltd was capital in nature, it would not be caught by s CA 1(2), s CB 1, s CB 3, s CB 4 or s CB 5.
- As the application of s FO 10 did not mean A Ltd (as the amalgamated company) was treated as having acquired shares in E Ltd for the purpose of disposal, s CB 4 did not apply.

[1] Including *Reid v CIR* (1985) 7 NZTC 5,176 and *Grieve v CIR* (1984) 6 NZTC 61,682 (CA).

- The Applicants had acquired the shares in E Ltd over a number of years as long-term, open-ended investments and held these shares on capital account.
- Therefore, the amount derived from disposal of these shares by A Ltd (as the amalgamated company) was not caught by s CA 1(2), s CB 1, s CB 3, s CB 4 or s CB 5.

Section CA 1(2) – Income under ordinary concepts

18. Section CA 1(2) provides that "an amount is also income of a person if it is their income under ordinary concepts".

19. The phrase "under ordinary concepts" is not defined. However, the courts have considered the meaning of what is income "under ordinary concepts" in several cases.[2]

20. It is implicit in the wording of s CA 1(2) and Richardson J's judgment in *Reid* that an amount that is capital in nature will not constitute income under ordinary concepts for the purposes of s CA 1(2).[3]

Whether the amount is capital or revenue in nature

21. The factors to consider when determining where an amount is capital or revenue in nature include (but are not limited to):
    - The scope of the recipient's business.
    - Periodicity, recurrence, or regularity.
    - The consideration provided for the receipt.
    - The purpose or reason for which the money is received.
    - The accounting treatment.

22. It was the view of TCO that the factors indicated that the shares in E Ltd which were held by amalgamating companies would be capital property of A Ltd (as the amalgamated company) after amalgamation. This was because:
    - Each of the amalgamating companies and A Ltd were holding companies established for the purpose of holding the parent company's investments.
    - By the very nature of the transaction it could not be recurring.
    - The shares in E Ltd were acquired over a prolonged period of time.

[2] *Reid v CIR* (1985) 7 NZTC 5,176.

[3] *Case S86* (1996) 17 NZTC 7,538.

23. Therefore, TCO concluded that the amount derived on disposal of the shares in E Ltd by A Ltd (as the amalgamated company) would not be income under s CA 1(2).

Section CB 1 – Amount derived from a business

24. Section CB 1 provides that an amount that a person derives from a business is income of the person unless the amount is of a capital nature (s CB 1(2)).

25. As TCO concluded the disposal was capital in nature, s CB 1(2) applied and the amount derived on disposal of the shares in E Ltd by A Ltd (as the amalgamated company) would not be income under s CB 1.

Section CB 3 – Profit-making undertaking or scheme

26. Section CB 3 includes in a taxpayer's assessable income amounts derived from the carrying on or carrying out of an undertaking or scheme entered into for the purpose of making a profit.

27. A number of cases have considered what constitutes an "undertaking or scheme". The key points are that:

- An undertaking or scheme is some plan or purpose which is coherent and has some unity of conception. It does not need to be precise. The assessment of any profit-making purpose is made at the time the scheme is entered into and property which is already held can become part of a later formulated scheme. There must be a nexus between the undertaking or scheme and any gain derived.
- For s CB 3 to apply, the scheme must produce assessable income. The mere realisation of a capital asset to the best advantage is not an undertaking or scheme.
- The courts have also held that any purpose of making a profit (under s CB 3) must be the dominant purpose. In this regard, "purpose" is construed in the same manner as it is construed in relation to s CB 4 (Personal property acquired for purpose of disposal), which is discussed further below. A taxpayer's subjective purpose needs to be established, but this is objectively assessed. The time at which the dominant purpose is applied is when an undertaking or scheme is entered into.

28. While it was clear A Ltd had a "purpose", at the time of the amalgamation which involved disposing of the shares in E Ltd for a profit; this involved the realisation of a capital asset. Therefore, it was not an undertaking or scheme to which s CB 3 is concerned.

Section CB 4 – Personal property acquired for purpose of disposal

29. TCO concluded in issue 2 that A Ltd (as the amalgamated company) either had no purpose of acquisition in relation to the shares in E Ltd deemed to be acquired on amalgamation or the same purpose of acquisition as the other Applicants had at the time of original acquisition. In either case, no income arises under s CB 4 on disposal of the shares in E Ltd.

Section CB 5 – Business of dealing in personal property

30. Section CB 5 states that an amount derived by a person from disposing of personal property is income to that person if it was their business to deal in property of that kind.

31. TCO concluded that amounts derived from the disposal of the shares in E Ltd by A Ltd subsequent to amalgamation (as the amalgamated company) was not income under s CB 5. This is because the shares in E Ltd were held on capital account.