



TECHNICAL DECISION SUMMARY > PRIVATE RULING

WHAKARĀPOPOTO WHAKATAU HANGARAU > WHAKATAUNGA
TŪMATAITI

Off-market share cancellation

Decision date | Rā o te Whakatau: 19 December 2025

Issue date | Rā Tuku: 22 May 2026

TDS 26/05

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Subjects | Kaupapa

This item summarises a private ruling that considered an off-market share cancellation.

Taxation laws | Ture tāke

All legislative references are to the Income Tax Act 2007.

Summary of facts | Whakarāpopoto o Meka

1. The Applicant is an incorporated company. It has a single class of Ordinary Shares on issue, all of which carry equal voting and distribution rights.
2. The Applicant proposes an off-market cancellation of its Ordinary Shares as part of a broader capital management strategy. The share cancellation will be offered to all shareholders and funded through a combination of existing cash reserves and new external debt.
3. The Applicant had intended to return capital to shareholders following the sale of a significant capital asset but deferred that return of capital due to weaker trading performance and limited refinancing capacity at the time. The Applicant intends to use the proposed share cancellation to recapitalise the business by moving its debt-to-equity ratio to market levels and to return the capital now that its financial position has improved.
4. The Applicant does not intend to issue new shares, pay dividends or repay the new external debts from retained earnings following the return of capital.

Issues | Take

5. The main issues considered in this ruling were:
 - whether the shares in the Applicant are all “shares of the same class” for the purposes of s CD 23;
 - whether the Applicant’s available subscribed capital (ASC) under s CD 43, for the purposes of s CD 23, was at least enough to cover the amount to be paid to shareholders because of the proposed share cancellation;

- for the purposes of s CD 22(3)(a), whether the proposed off-market share cancellation is a pro rata cancellation that results in a 15% reduction for the Applicant; and
- whether the amount the Applicant pays to a shareholder because of the proposed off-market share cancellation is “in lieu of the payment of a dividend” for the purposes of s CD 22(6).

Decisions | Whakatau

6. The Tax Counsel Office (TCO) concluded that:
 - the shares in the Applicant are all “shares of the same class” for the purposes of s CD 23;
 - the Applicant’s ASC under s CD 43 is at least enough to cover the amount to be paid to shareholders because of the proposed share cancellation;
 - the proposed off-market share cancellation is a pro rata cancellation that results in a 15% reduction for the Applicant, for the purposes of s CD 22(3)(a); and
 - the amount the Applicant pays to a shareholder because of the proposed off-market share cancellation is not “in lieu of the payment of a dividend” for the purposes of s CD 22(6).

Reasons for decisions | Pūnga o ngā whakatau

Issue 1 | Take tuatahi: Shares of the same class

7. Section CD 4(1) provides that a transfer of value from a company to a person is a dividend if the cause of the transfer is a shareholding in the company.
8. However, under s CD 22(2), if an off-market share cancellation meets certain criteria, the amount the shareholders receive on the cancellation is not a dividend for tax purposes. Under s CD 22, the amount will not be a dividend to the extent it is less than or equal to the ASC per share calculated under the ordering rule as set out in s CD 23, provided that:
 - the transaction is an off-market share cancellation;
 - the transaction satisfies one of the “bright line tests” in s CD 22(3);
 - the company is not an unlisted trust that has chosen the slice rule for the share; and

- the anti-avoidance rule in s CD 22(6) and (7) does not apply – that is, no part of the payment is in lieu of the payment of a dividend.
9. Issue 1 was concerned with a requirement that arises from the ordering rule in s CD 23, which refers to the shares being cancelled as “shares of the same class”.
 10. Relevantly, to be shares of the same class, the Ordinary Shares in the Applicant must carry the same shareholder decision-making rights and carry the same distribution rights (definition of “shares of the same class” in s YA 1).
 11. “Shareholder decision-making right” means a right carried by company shares that allows the shareholder to vote or participate in decisions on company dividends or distributions, the company’s constitution, changes to the company’s capital, or the appointment of directors.
 12. TCO considered that all Ordinary Shares in the Applicant carry the same shareholder decision-making rights and the same distribution rights because the rights attached to the shares are identical.
 13. Under the Applicant’s constitution, each Ordinary Share confers one vote per share on shareholder resolutions, together with equal rights to distributions and surplus assets. These rights are not differentiated between Ordinary Shares.
 14. Although the shareholders’ agreement allocates director appointment rights differently between certain shareholders, those arrangements operate by reference to the identity of the shareholder and, in some cases, the shareholder’s level of shareholding. They do not alter the rights attached to the shares themselves.
 15. Therefore, the shares in the Applicant are all “shares of the same class” for the purposes of s CD 23.

Issue 2 | Take tuarua: ASC calculation

16. If the requirements of s CD 22 are met, an amount paid to shareholders because of the off-market cancellation of a share (other than on liquidation of the company) is not a dividend to the extent the amount is less than or equal to the ASC per share calculated under the ordering rule.
17. In considering this issue, TCO was asked to confirm that the amount of ASC for the purpose of the ordering rule in s CD 23 was at least enough to cover the amount to be paid to shareholders because of the proposed share cancellation.
18. The formula for calculating ASC is set out in s CD 43 as follows:
$$1 \text{ July 1994 balance} + \text{subscriptions} - \text{returns} - \text{look-through company returns}$$

19. It was possible to ascertain that there was at least enough ASC to cover the amount to be paid to shareholders because of the proposed share cancellation by reference to shares that particular identified shareholders held. TCO therefore applied the ASC formula in s CD 43 to those particular shares only. For each item in the formula, TCO considered the following:
- “1 July 1994 balance” is the amount calculated under s CD 43(3) if the company existed before 1 July 1994, and zero in any other case. As the Applicant did not exist before 1 July 1994, the “1 July 1994 balance” in the formula is zero.
 - “Subscriptions” is relevantly defined in s CD 43(2)(b) as the total amount of consideration that the company received, after 30 June 1994 and before the calculation time, for the issue of shares of the same class as the share. This definition is subject to subss (6) to (21), which TCO considered were not relevant to Ordinary Shares held by the particular shareholders. According to the shareholding information for the Applicant, the “subscriptions” amount is at least the total amount of consideration that the Applicant has received to date for the issue of those particular Ordinary Shares.
 - “Returns” is relevantly defined in s CD 43(2)(c) as the total amount of consideration that the company paid, after 30 June 1994 and before the calculation time, on the cancellation of shares in the relevant class and that was not a dividend because of s CD 22. According to the shareholding information for the Applicant, there have been no previous share cancellations in relation to Ordinary Shares held by the particular shareholders. Therefore, the item “returns” in the ASC formula is zero.
 - “Look-through company returns” is defined as the total amount of consideration that the company paid, before the calculation time, on the cancellation or buyback of shares while the company was a look-through company. As the Applicant has never been a look-through company, this item in the formula is not relevant and the item is therefore zero.
20. Based on the above, TCO calculated the ASC was at least equal to the amount to be paid to shareholders because of the proposed share cancellation.

Issue 3 | Take tuatoru: Pro rata cancellation

21. As noted at [8], one of the criteria in s CD 22 is that the transaction satisfies one of the “bright line tests” in s CD 22(3). The relevant bright line test is s CD 22(3)(a), which requires that the off-market share cancellation is part of a pro rata cancellation that results in a 15% capital reduction for the company.

22. The definition of “pro rata cancellation” in s YA 1 includes a partial cancellation resulting from an offer to all shareholders that would not alter any person’s voting interest if each shareholder who received the offer accepted it in full (para (c) of the definition).
23. A person’s voting interest equals the percentage of the total decision-making rights carried by their shares (s YC 2).
24. TCO considered that a shareholder’s proportionate interest in a company is measured by reference to the number of shares they hold, rather than to their actual ability to vote. The same approach should be applied in determining whether a person’s voting interest is altered in a share cancellation. This recognises the underlying purpose of the share cancellation rules: that voting interests are assessed by reference to shareholding proportions, rather than a shareholder’s ability to exercise control.
25. For the Applicant, even if some shareholders declined the offer, the cancellation would still be a pro rata cancellation where the offer is made to all shareholders of the Ordinary Shares. Further, if all of the Ordinary Share shareholders were to accept the offer, the percentage of the total shareholder decision-making rights for the company carried by shares that each person holds would not change. On this basis, the cancellation would not alter any person’s voting interest.
26. Therefore, the proposed off-market share cancellation meets the definition of “pro rata cancellation”.
27. To determine whether the share cancellation results in a 15% capital reduction, s CD 22(9) provides that there is a 15% capital reduction where the total amount paid by the company on account of the cancellation is at least 15% of the market value of all participating shares in the company at the time the company first notifies shareholders of the cancellation.
28. Based on the market value of the company and the information provided on the proposed share cancellation, TCO calculated the capital reduction to be at least 15%.
29. Therefore, TCO concluded that the proposed off-market share cancellation meets the bright line test in s CD 22(3)(a).

Issue 4 | Take tuawhā: Payment will not be in lieu of the payment of a dividend

30. Section CD 22(6) provides that s CD 22(2) does not exclude an amount paid by a company on an off-market cancellation of a share from being a dividend if any part of the payment is in lieu of the payment of a dividend.

31. Section CD 22(7) sets out the factors that must be considered when applying the anti-avoidance rule in s CD 22(6). These factors are:
- the nature and amount of dividends paid by the company before or after the cancellation;
 - the issue of shares in the company after the cancellation;
 - the expressed purpose or purposes of the cancellation; and
 - any other relevant factor.
32. TCO considered each of these factors, as follows.¹

Nature and amount of dividends before or after the cancellation

33. This factor focuses on the company's dividend policy or practice both before and after the share cancellation. Its purpose is to detect any changes or variations in the company's dividend policy or practice that indicate the share cancellation is replacing a dividend the company would normally pay. However, where it is clear that earnings are retained for sound business reasons, the absence of dividend payments alone does not indicate that the share cancellation is in lieu of the payment of a dividend.
34. The Applicant has no formal dividend policy and has paid only one dividend since its incorporation. TCO considered that commercial factors and a series of external events explain the lack of regular dividends, and that the nature and timing of the Applicant's dividend payments do not indicate the cancellation is intended to distribute retained earnings in lieu of the payment of dividends.

Issue of shares after the cancellation

35. If new shares are issued soon after a cancellation, factors such as the timing, reasons for the issue, amounts of capital returned and raised, and the company's financial position are likely to be relevant in determining whether the cancellation is in lieu of the payment of a dividend.
36. The Applicant has stated that it does not intend to issue any new shares following the return of capital. Therefore, this factor is not relevant.

¹ TCO considered and applied the factors in accordance with IS 25/19: Income Tax – Whether an off-market share cancellation is made in lieu of the payment of a dividend *Tax Information Bulletin* Vol 37, No 9 (September 2025): 9.

Expressed purpose of the cancellation

37. A share is less likely to be a substitute for a dividend if strong objective evidence shows the cancellation is undertaken to achieve a commercial outcome, such as returning excess capital from selling major assets.
38. The Applicant's stated purpose for the cancellation is to return capital from the sale of the capital asset and recapitalise the business with a market level of debt financing, altering its debt-to-equity ratio to a more appropriate and sustainable level, now that it is in a position to do so. The original intention was to return capital at the time of the sale but, due to a series of external events, it is only now that the Applicant is in a financial position to proceed. The funding of the return through a mix of excess cash and external borrowing, along with the rebalancing of the Applicant's debt-to-equity ratio to market levels, reinforces that the transaction is directed at capital structure management rather than profit distribution.
39. Further, the Applicant does not intend to repay the external borrowings using its retained earnings. This suggests the cancellation was not aimed at returning retained earnings in lieu of the payment of a dividend.

Other relevant factors

40. Other factors that may be relevant to determining whether a share cancellation is in lieu of the payment of a dividend include whether amounts payable on cancellation are left outstanding and whether the capital return is an unusual one-off event.
41. The Applicant's sale of the capital asset was a significant one-off event, and the share cancellation does not involve any shareholder loans. These factors indicate that the amount paid on the cancellation is not in lieu of the payment of a dividend.

Overall conclusion

42. Considering all of the above factors as required by s CD 22(7), TCO concluded that the amount paid on the share cancellation will not be in lieu of the payment of a dividend, for the purposes of s CD 22(6).