



Class Ruling

Income tax: proposed Special Dividend and Lion Nathan Limited Scheme of Arrangement

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This publication (excluding appendixes) is a public ruling for the purposes of the *Taxation Administration Act 1953*.

A public ruling is an expression of the Commissioner's opinion about the way in which a relevant provision applies, or would apply, to entities generally or to a class of entities in relation to a particular scheme or a class of schemes.

If you rely on this ruling, the Commissioner must apply the law to you in the way set out in the ruling (unless the Commissioner is satisfied that the ruling is incorrect and disadvantages you, in which case the law may be applied to you in a way that is more favourable for you – provided the Commissioner is not prevented from doing so by a time limit imposed by the law). You will be protected from having to pay any underpaid tax, penalty or interest in respect of the matters covered by this ruling if it turns out that it does not correctly state how the relevant provision applies to you.

What this Ruling is about

1. This Ruling sets out the Commissioner's opinion on the way in which the relevant provisions identified below apply to the defined class of entities, who take part in the scheme to which this Ruling relates.

Relevant provision(s)

2. The relevant provisions dealt with in this Ruling are:

- subsection 6(1) of the *Income Tax Assessment Act 1936* (ITAA 1936);
- section 44 of the ITAA 1936;
- section 128B of the ITAA 1936;
- section 128D of the ITAA 1936;
- section 177EA of the ITAA 1936;
- Division 1A of former Part IIIA of the ITAA 1936 (former Division 1A);
- section 104-10 of the *Income Tax Assessment Act 1997* (ITAA 1997);

- section 116-20 of the ITAA 1997;
- section 118-20 of the ITAA 1997;
- section 204-30 of the ITAA 1997;
- Division 208 of the ITAA 1997;
- section 855-10 of the ITAA 1997;
- section 855-15 of the ITAA 1997; and
- section 855-35 of the ITAA 1997.

Class of entities

3. The class of entities to which this Ruling applies are the shareholders of Lion Nathan Limited (LNL), excluding Kirin Holdings Company, Limited (Kirin Japan), who hold LNL ordinary shares on capital account and:

- receive the Special Dividend; or
- participate in the LNL Scheme of Arrangement (LNL Scheme) under which Kirin Japan or its nominee (referred to as Kirin) would acquire 100% of the shares in LNL (participating LNL shareholders) and who also receive the Special Dividend; or
- participate in the LNL Scheme under which Kirin would acquire 100% of the shares in LNL (participating LNL shareholders).

Qualifications

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

5. The class of entities defined in this Ruling may rely on its contents provided the scheme actually carried out is carried out in accordance with the scheme described in paragraphs 9 to 28 of this Ruling.

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

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

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Date of effect

8. This Ruling applies from 1 July 2008 to 30 June 2010. The Ruling continues to apply after 30 June 2010 to all entities within the specified class who entered into the specified scheme during the term of the Ruling. However, this Ruling will not apply to taxpayers to the extent that it conflicts with the terms of a settlement of a dispute agreed to before the date of issue of this Ruling (see paragraphs 75 and 76 of Taxation Ruling TR 2006/10).

Scheme

9. The following description of the scheme is based on information provided by the applicant. The following documents, or relevant parts of them form part of and are to be read with the description:

- application for Class Ruling dated 22 May 2009 with attachments;
- a copy of the Implementation Agreement dated 10 May 2009;
- a copy of the draft Scheme Booklet as at 16 July 2009; and
- correspondence from LNL dated 24 June 2009, 29 June 2009, 17 July 2009, 22 July 2009 and 10 August 2009.

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

10. LNL is a public company listed on the Australian Securities Exchange (ASX) and the New Zealand Stock Exchange.

11. LNL is the head company of the LNL tax consolidated group and is a resident of Australia under subsection 6(1) of the ITAA 1936.

12. LNL currently has total issued capital of 534,240,495 ordinary shares.
13. Kirin Japan is a company resident in Japan. Kirin holds 246,454,275 shares in LNL representing approximately 46.13% of the issued capital in LNL.
14. The remaining LNL shares are held by Australian resident and non-resident entities including individuals, companies and superannuation funds.
15. As at 12 May 2009, approximately 71% of LNL shares were held by non-resident entities (inclusive of Kirin).

The proposed LNL Scheme

16. On 27 April 2009 LNL announced that following discussions between the Independent Board of LNL and Kirin Japan, LNL had agreed key commercial terms under which Kirin would acquire all non Kirin owned ordinary shares in LNL.
17. On 10 May 2009 LNL and Kirin Japan executed an Implementation Agreement. The binding terms and conditions of the Implementation Agreement reflect the key commercial terms relating to Kirin's proposed offer.
18. At the request of Kirin, LNL intends to propose the LNL Scheme to non-Kirin LNL shareholders whereby, if implemented, LNL will become a wholly owned subsidiary of Kirin by means of a scheme of arrangement between LNL and its members in accordance with Part 5.1 of the *Corporations Act 2001*. LNL and Kirin have agreed to implement the proposed LNL Scheme on the terms and conditions of the Implementation Agreement.
19. Kirin Japan may acquire the non-Kirin LNL shares or nominate a wholly owned subsidiary to do so. Kirin Japan has nominated its wholly owned subsidiary Kirin Australia (Holdings) Pty Limited to acquire the LNL shares.
20. Implementation of the proposed LNL Scheme is subject to a number of conditions precedent. One of the conditions is that LNL obtain approval by the requisite majority of non-Kirin LNL shareholders at the LNL Members' Scheme Meeting (Scheme Meeting). The Scheme Meeting will be held on 17 September 2009.
21. Non-Kirin LNL shareholders who hold LNL shares on the Scheme Record Date will be entitled to participate. The Scheme Record Date will be 14 October 2009.
22. On the Implementation Date, LNL shares will be transferred to Kirin. The Implementation Date will be 21 October 2009.

23. The draft Scheme Booklet sets out the total cash payments that participating LNL shareholders will be entitled to receive if the LNL Scheme is approved and implemented. In consideration for the transfer of the LNL shares to Kirin, participating LNL shareholders will receive the Scheme Consideration of \$11.50 per LNL share. Where eligible, a participating LNL shareholder will also receive a Special Dividend of \$0.50 per LNL share.

The proposed Special Dividend

24. LNL shareholders, including Kirin, who are registered as holding LNL shares at 7.00 pm on the Special Dividend Record Date will be entitled to receive a Special Dividend of \$0.50 per LNL share. The Special Dividend Record Date will be 25 September 2009.

25. The Special Dividend will not be paid by LNL if the proposed LNL Scheme is not approved by the requisite majority of non-Kirin LNL shareholders at the Scheme Meeting on 17 September 2009. If approved, the Special Dividend will be paid on 6 October 2009.

26. Under the Implementation Agreement, LNL and Kirin acknowledged and agreed that matters, including but not limited to the form and manner of the Special Dividend, are subject to consultation and agreement between LNL and Kirin. LNL has undertaken and agreed not to pay the Special Dividend otherwise than in accordance with the agreement of Kirin.

27. The Special Dividend will be fully franked with Australian franking credits. Further, it will also be partly imputed with New Zealand imputation credits for New Zealand tax purposes.

28. The full amount of the Special Dividend will be debited to LNL's retained earnings and no amount of the Special Dividend will be debited to LNL's share capital account. The retained profits are profits derived by LNL from sources both in and outside of Australia.

Ruling

The Special Dividend

29. The Special Dividend of \$0.50 per share to be declared and paid to LNL shareholders will constitute a 'dividend' as defined in subsection 6(1) of the ITAA 1936.

30. The Special Dividend will not be a distribution made by an exempting entity, as LNL will not be an exempting entity pursuant to section 208-20 of the ITAA 1997 at the time the Special Dividend is paid.

Assessability of the Special Dividend

31. LNL shareholders who receive the fully franked Special Dividend and are residents of Australia as defined in subsection 6(1) of the ITAA 1936 are required to include the Special Dividend as assessable income under subparagraph 44(1)(a)(i) of the ITAA 1936.

32. LNL shareholders who receive the fully franked Special Dividend and are non-residents (other than those carrying on business in Australia at or through a permanent establishment in Australia) will not be required to include the dividend as assessable income under subparagraph 44(1)(b)(i) of the ITAA 1936 (section 128D of the ITAA 1936) and will not be liable for Australian withholding tax (paragraph 128B(3)(ga) of the ITAA 1936).

33. LNL shareholders who receive the fully franked Special Dividend and are non-residents carrying on business in Australia at or through a permanent establishment in Australia, where the Special Dividend is attributable to the permanent establishment, are required to include the Special Dividend as assessable income under subparagraphs 44(1)(b)(i) and 44(1)(c)(i) of the ITAA 1936.

Gross up and tax offset

34. LNL shareholders who receive the fully franked Special Dividend directly will:

- (a) include an amount equal to the franking credit attached to the Special Dividend as assessable income (gross up); and
- (b) be entitled to a tax offset equal to the franking credit (tax offset);

under section 207-20 of the ITAA 1997, subject to being a qualified person.

35. Where the fully franked Special Dividend is received by a LNL shareholder (not being an entity taxed as a corporate tax entity) who is a trustee of a trust (not being a complying superannuation fund) or a partnership, the trustee of the trust or the partnership will include an amount equal to the franking credit attached to the Special Dividend as assessable income under subsection 207-35(1) of the ITAA 1997, subject to the trustee or the partnership being a qualified person.

Qualified persons

36. The payment of the Special Dividend as part of the LNL Scheme will constitute a related payment for the purposes of former section 160APHN of the ITAA 1936.

37. Accordingly, each LNL shareholder will need to hold their LNL shares at risk for a continuous period of at least 45 days in the secondary qualification period in order to be a qualified person.

38. LNL shareholders will no longer be considered to hold their LNL shares 'at risk' for the purposes of former Division 1A as of 14 October 2009, which is the Scheme Record Date. Those LNL shareholders who have held their LNL shares 'at risk' for a continuous period of not less than 45 days during the period 12 August 2009 to 13 October 2009 will be qualified persons with respect to the fully franked Special Dividend.

Capital Gains Tax (CGT) consequences

CGT event A1 happens on the disposal of LNL shares

39. CGT event A1 will happen when a participating LNL shareholder disposes of each of their LNL shares pursuant to the LNL Scheme (subsections 104-10(1) and (2) of the ITAA 1997).

40. The time of the CGT event will be 21 October 2009, the Implementation Date (subsection 104-10(3) of the ITAA 1997).

41. A participating LNL shareholder will make a capital gain from CGT event A1 happening if the capital proceeds from the disposal of a LNL share exceed its cost base. A participating LNL shareholder will make a capital loss if those capital proceeds are less than the LNL share's reduced cost base (subsection 104-10(4) of the ITAA 1997).

Capital proceeds

42. The capital proceeds received by each participating LNL shareholder is the money received or entitled to be received in respect of the event happening (subsection 116-20(1) of the ITAA 1997).

43. The capital proceeds for each LNL share received by a participating LNL shareholder that is not entitled to be paid the Special Dividend will be the Scheme Consideration of \$11.50 per LNL share.

44. The capital proceeds for each LNL share received by a participating LNL shareholder that is entitled to be paid the Special Dividend will be \$12.00 per LNL share. This amount consists of the Scheme Consideration of \$11.50 to be paid by Kirin as consideration for acquiring each share held by the participating LNL shareholder and the Special Dividend of \$0.50 to be paid by LNL in respect of each LNL share held by the LNL shareholder.

Anti-overlap provisions

45. Any capital gain made by a participating LNL shareholder when CGT event A1 happens can be reduced by the amount of the Special Dividend that is included in the participating LNL shareholder's assessable income under subsection 44(1) of the ITAA 1936 (section 118-20 of the ITAA 1997).

Foreign resident participating LNL shareholders

46. A participating LNL shareholder that is a foreign resident, or the trustee of a foreign trust for CGT purposes, just before CGT event A1 happens under the LNL Scheme disregards under subsection 855-10(1) of the ITAA 1997 any capital gain or capital loss from CGT event A1 happening to the LNL shares if the shares are not taxable Australian property as defined in section 855-15 of the ITAA 1997.

47. Any capital gain or capital loss a foreign resident, or the trustee of a foreign trust for CGT purposes, makes from CGT event A1 in relation to taxable Australian property under item 3 of the table in section 855-15 of the ITAA 1997, is not reduced under section 855-35 of the ITAA 1997 if they used it in carrying on a business through a permanent establishment in Australia for the whole of the period from when they acquired it to when CGT event A1 happened.

Anti-avoidance provisions

48. The Commissioner will not make a determination under paragraph 204-30(3)(c) of the ITAA 1997 to deny the whole, or any part, of the imputation benefit received in relation to the Special Dividend.

49. The Commissioner will not make a determination under paragraph 177EA(5)(b) of the ITAA 1936 to deny the whole, or any part, of the imputation benefit received in relation to the Special Dividend.

Commissioner of Taxation

19 August 2009

Appendix 1 – Explanation

❶ *This Appendix is provided as information to help you understand how the Commissioner's view has been reached. It does not form part of the binding public ruling.*

The Special Dividend

Dividend as defined in subsection 6(1)

50. The term 'dividend' is defined in subsection 6(1) of the ITAA 1936 and includes any distribution made by a company to any of its shareholders. The Special Dividend will be a distribution in money made by LNL to its ordinary shareholders.

51. Paragraph (d) of the definition of 'dividend' in subsection 6(1) of the ITAA 1936 however excludes from the definition of 'dividend' any:

moneys paid or credited by a company to a shareholder or any other property distributed by a company to shareholders (not being moneys or other property to which this paragraph, by reason of subsection (4), does not apply or moneys paid or credited, or property distributed for the redemption or cancellation of a redeemable preference share), where the amount of the moneys paid or credited, or the amount of the value of the property, is debited against an amount standing to the credit of the share capital account of the company...

52. The Special Dividend will be sourced from LNL's retained earnings. LNL will not debit the Special Dividend to its share capital account. Therefore, the exclusion in paragraph (d) will not apply and the Special Dividend will constitute a 'dividend' for the purposes of subsection 6(1) of the ITAA 1936.

Section 208-20

53. Section 208-20 of the ITAA 1997 states that a corporate tax entity is an exempting entity at a particular time if it is effectively owned by prescribed persons at that time. Subsection 208-25(1) of the ITAA 1997 provides in broad terms that an entity is effectively owned by prescribed persons if not less than 95% of accountable membership interests or accountable partial interests (broadly direct and indirect ownership interests) are held by or on behalf of prescribed persons.

54. Section 208-40 of the ITAA 1997 provides the definition of a prescribed person in relation to another corporate tax entity. Generally, the definition includes companies, trustees, partnerships or individuals that are a foreign resident or if they were to receive a distribution by the corporate tax entity, the distribution would be exempt income or non-assessable non-exempt income of the company, trust estate, partnership or individual.

55. As at 12 May 2009 approximately 71% of the issued capital of LNL was held by non resident shareholders. As the percentage of non resident shareholder ownership in LNL does not amount to LNL being effectively controlled by prescribed persons, LNL will not be an exempting entity under Division 208 of the ITAA 1997.

Assessability of the Special Dividend

56. Subparagraph 44(1)(a)(i) of the ITAA 1936 includes in the assessable income of an Australian resident shareholder in a company:

dividends (other than non-share dividends) that are paid to the shareholder by the company out of profits derived by it from any source.

57. As the Special Dividend will be paid to LNL shareholders out of profits derived by LNL, LNL shareholders who are residents of Australia as defined in subsection 6(1) of the ITAA 1936 are required to include the Special Dividend as assessable income.

58. Subparagraph 44(1)(b)(i) of the ITAA 1936 includes in the assessable income of a non-resident shareholder in a company:

dividends (other than non-share dividends) paid to the shareholder by the company to the extent to which they are paid out of profits derived by it from sources in Australia.

59. Subsection 128B(1) of the ITAA 1936 imposes Australian withholding tax on income that:

- (a) is derived, on or after 1 January 1968, by a non resident; and
- (b) consists of a dividend paid by a company that is a resident.

60. However, subparagraph 128B(3)(ga)(i) of the ITAA 1936 excludes from subsection 128B(1) of the ITAA 1936 income derived by a non-resident that consists of the franked part of a dividend. As the Special Dividend will be fully franked, it will not be subject to Australian withholding tax when derived by non-resident LNL shareholders.

61. Additionally section 128D of the ITAA 1936 states that:

Income other than income to which section 128B applies by virtue of subsection (2A), (2C) or (9C) of that section upon which withholding tax is payable, or upon which withholding tax would, but for paragraph 128B(3)(ga) or (jb), section 128F, section 128FA or section 128GB, be payable, is not assessable income and is not exempt income of a person.

As the Special Dividend is income that is subject to withholding tax but for paragraph 128B(3)(ga) of the ITAA 1936 it will not be assessable income and will not be exempt income of non-resident LNL shareholders pursuant to section 128D.

62. Withholding tax will not apply under section 128B of the ITAA 1936 where:

- the Special Dividend is paid to a shareholder who is a non-resident carrying on business in Australia at or through a permanent establishment of the shareholder in Australia, and
- the dividend income is attributable to the permanent establishment – and the Special Dividend is not paid to the shareholder in the shareholder's capacity as trustee (pursuant to subsection 128B(3E)).

63. Subsection 128B(3E) of the ITAA 1936 also ensures that none of the Special Dividend will be non-assessable and non-exempt income under section 128D of the ITAA 1936.

64. Subparagraph 44(1)(c)(i) of the ITAA 1936 includes in the assessable income of a non-resident shareholder of a resident company who is carrying on business in Australia at or through a permanent establishment of the shareholder in Australia:

dividends (other than non-share dividends) that are paid to the shareholder by the company and are attributable to the permanent establishment, to the extent to which they are paid out of profits derived by the company from sources outside Australia.

65. As the Special Dividend will be paid out of profits derived by LNL from sources both in and outside of Australia, non-resident LNL shareholders carrying on business in Australia at or through a permanent establishment will include the Special Dividend in their assessable income to the extent they are attributable to the permanent establishment of the non-resident shareholder in Australia pursuant to subparagraphs 44(1)(b)(i) and 44(1)(c)(i) of the ITAA 1936.

Gross up and tax offset

66. Section 207-20 of the ITAA 1997 provides:

- (1) If an entity makes a *franked distribution to another entity, the assessable income of the receiving entity, for the income year in which the distribution is made, includes the amount of the *franking credit on the distribution. This is in addition to another amount included in the receiving entity's assessable income in relation to the distribution under any other provision of this Act.
- (2) The receiving entity is entitled to a *tax offset for the income year in which the distribution is made. The tax offset is equal to the *franking credit on the distribution.

67. Therefore, subject to satisfying the qualified person rule, where the fully franked Special Dividend is received directly by a LNL shareholder, the LNL shareholder will:

- (1) include the amount of the franking credit attached to the Special Dividend in their assessable income; and
- (2) be entitled to a tax offset equal to the amount of the franking credit.

68. Where the fully franked Special Dividend is received by a LNL shareholder (not being an entity taxed as a corporate tax entity) that is a trustee of a trust (not being a complying superannuation fund) or a partnership, subsection 207-35(1) of the ITAA 1997 applies, subject to the trustee or partnership being a qualified person. Subsection 207-35(1) provides:

If:

- (a) a *franked distribution is made in an income year to an entity that is a partnership or the trustee of a trust; and

- (b) the entity is not a *corporate tax entity when the distribution is made; and
- (c) if the entity is the trustee of a trust – the trust is not a *complying superannuation entity or *FHSA trust when the distribution is made;

the assessable income of the partnership or trust for that income year includes the amount of the *franking credit on the distribution.

69. Therefore, subject to satisfying the qualified person rule, the LNL shareholder will be required to include the amount of the franking credit attached to the Special Dividend in their assessable income under subsection 207-35(1) of the ITAA 1997.

Qualified persons

70. Former Division 1A contains the measures known as the holding period rule and the related payment rule. In broad terms, former Division 1A provides the statutory tests that must be satisfied for a taxpayer to be a 'qualified person' with respect to a franked distribution they have received and thus be entitled to a tax offset for the franking credit attached to the distribution.

71. The test of what constitutes a 'qualified person' is provided in former section 160APHO of the ITAA 1936 as follows:

A taxpayer who has held shares or an interest in shares on which a dividend has been paid is a ***qualified person*** in relation to the dividend if:

- (a) where neither the taxpayer nor an associate of the taxpayer has made, is under an obligation to make, or is likely to make, a related payment in respect of the dividend – the taxpayer has satisfied subsection (2) in relation to the primary qualification period in relation to the dividend; or
- (b) where the taxpayer or an associate of a taxpayer has made, is under an obligation to make, or is likely to make, a related payment in respect of the dividend – the taxpayer has satisfied subsection (2) in relation to the secondary qualification in relation to the dividend.

72. Former subsection 160APHO(2) of the ITAA 1936, referred to in the preceding paragraph, sets out the holding period requirement. Broadly, if a taxpayer is not under an obligation to make a related payment in relation to a dividend or distribution, the taxpayer will have to satisfy the holding period requirement within the primary qualification period. If a taxpayer is under an obligation to make a related payment in relation to a dividend or distribution, the taxpayer will have to satisfy the holding period requirement within the secondary qualification period.

Related payment rule

73. In order to determine which is the relevant qualification period, it is necessary to determine whether, under the present arrangement, the LNL shareholders are considered to be under an obligation to make a related payment.

74. Former section 160APHN of the ITAA 1936 provides non-definitive examples of what constitutes the making of a related payment for the purposes of former Division 1A. Former subsection 160APHN(2) provides:

The taxpayer or associate is taken, for the purposes of this Division, to have made, to be under an obligation to make, or to be likely to make, a related payment in respect of the dividend or distribution if, under an arrangement, the taxpayer or associate has done, is under an obligation to do, or may reasonably be expected to do, as the case may be, anything having the effect of passing the benefit of the dividend or distribution to one or more other persons.

75. Former subsection 160APHN(3) of the ITAA 1936 states:

Without limiting subsection (2), the doing of any of the following by the taxpayer or an associate of the taxpayer in the circumstances mentioned in subsection (4) may have the effect of passing the benefit of the dividend or distribution to one or more other person:

- (a) causing a payment or payments to be made to, or in accordance with the directions of, the other person or other persons; or
- (b) causing an amount or amounts to be credited to, or applied for the benefit of, the other person or the other persons; or
- (c) causing services to be provided to, or in accordance with the directions of, the other person or other persons; or
- (d) causing property to be transferred to, or in accordance with directions of, the other person or other persons; or
- (e) allowing any property or money to be used by the other person or other persons or by someone nominated by the other person or other persons; or
- (f) causing an amount or amounts to be set off against, or to be otherwise applied in reduction of, a debt or debts owed by the other person or other persons; or
- (g) agreeing to treat an amount or amounts owed to the other person or other persons by the taxpayer or associate as having been increased.

76. Former subsection 160APHN(4) of the ITAA 1936 states:

The circumstances referred to in subsection (3), are where:

- (a) the amount or the sum of the amounts paid, credited or applied; or
- (b) the value or the sum of the values of the services provided, of the property transferred or of the use of the property or money; or

- (c) the amount or the sum of the amounts of the set-offs, reductions or increases;

as the case may be:

- (d) is, or may reasonably be expected to be, equal to; or
- (e) approximates or may reasonably be expected to approximate; or
- (f) is calculated by reference to;
the amount of dividend or distribution.

77. In the current circumstances, it is considered that an integral part of the arrangement is the planned payment of the Special Dividend of \$0.50 per share. The payment of the Special Dividend is conditional upon LNL obtaining approval from the requisite majority of non-Kirin LNL shareholders at the Scheme Meeting for the LNL Scheme to be entered into. As such, the Special Dividend is conditional upon the scheme of arrangement being approved, tying the payment of the Special Dividend to the disposal of the LNL shares by participating LNL shareholders to Kirin.

78. The payment of the Special Dividend is an integral part of the total amount to be paid to LNL shareholders in relation to the disposal of the LNL shares to Kirin pursuant to the LNL Scheme. In these circumstances, in determining whether a LNL shareholder is taken to have made or be likely to make a related payment in respect of the Special Dividend, it is considered that the circumstances surrounding the payment of the Special Dividend would constitute an act that passes the benefit to another for the purposes of former subsection 160APHN(3) of the ITAA 1936. As such, it can be concluded that a LNL shareholder will be taken to have made or be likely to make a related payment in respect of the Special Dividend.

79. As the LNL shareholders are taken, for the purposes of former Division 1A, to have made or be likely to make a related payment in respect of the Special Dividend, the relevant holding period is thus the secondary qualification period pursuant to former paragraph 160APHO(1)(b) of the ITAA 1936.

80. The secondary qualification period is defined in former section 160APHD of the ITAA 1936 as follows:

In relation to a taxpayer in relation to shares or an interest in shares, means:

- (a) if the shares are not preference shares – the period beginning on the 45th day before, and ending on the 45th day after, the day on which the shares or interest becomes ex dividend...

81. The concept of 'ex-dividend' is defined by former subsection 160APHE(1) of the ITAA 1936 as follows:

a share in respect of which a dividend is to be paid, or an interest (other than an interest as a beneficiary of a widely held trust) in such a share, becomes ex dividend on the day after the last day on which the acquisition by a person of the share will entitle the person to receive the dividend.

82. LNL will determine eligibility for the Special Dividend on the Special Dividend Record Date of 25 September 2009. This is the last day on which acquisition by a person of a LNL share will entitle the person to receive the Special Dividend as per former section 160APHE of the ITAA 1936. Accordingly, the ex-dividend date for the purposes of former subsection 160APHE(1) is 26 September 2009.

83. The secondary qualification period thus runs from 45 days before the ex-dividend date of 26 September 2009 as determined above and ends 45 days after that day. In practical terms, this means that the secondary qualification period runs from 12 August 2009 to 10 November 2009. However, pursuant to former subsection 160APHO(3) of the ITAA 1936, any days on which a taxpayer has materially diminished risks of loss or opportunities for gain in respect of the LNL shares are to be excluded. This would mean that the secondary qualification period would run from 12 August 2009 until the date that LNL shareholders are no longer at risk for the purposes of former Division 1A.

84. In this context, entitlement to participate in the LNL Scheme will be determined on the Scheme Record Date on the basis of being a LNL shareholder who is registered in the register as the holder of the relevant Scheme Share on 14 October 2009. It is considered that once a LNL shareholder is identified as a participating LNL shareholder, that LNL shareholder would no longer be considered to hold their shares 'at risk' for the purposes of former Division 1A as at that time the LNL shareholder is committed to disposing of their LNL share and receiving the Scheme Consideration.

85. Accordingly, the secondary qualification period would run from 12 August 2009 until 13 October 2009 (inclusive). LNL shareholders who receive the Special Dividend would need to hold their shares at risk for a continuous period of not less than 45 days during this period in order to be a 'qualified person' for the purposes of former Division 1A. Further, pursuant to former paragraph 160APHO(2)(a) of the ITAA 1936, the date of acquisition or disposal are not included in the relevant 45 day period. This would have the effect in the present circumstances, for example, that the 45 day qualification period could not include 12 August 2009 if this was the date of acquisition of LNL shares.

CGT consequences

CGT event A1 happens on the disposal of LNL shares

86. CGT event A1 (section 104-10 of the ITAA 1997) happens if there is a change in the ownership of an asset from one entity to another. This event happens when a contract to dispose of the asset is entered into or, if there is no contract, when the change of ownership occurs (subsection 104-10(3)).

87. The Addendum to Taxation Determination TD 2002/4 indicates that a takeover or merger effected by a court approved scheme of arrangement does not involve a disposal of shares under a contract.

88. CGT event A1 therefore happens to participating LNL shareholders when the LNL shares are transferred to Kirin on the Implementation Date, being 21 October 2009.

89. The time when CGT event A1 happens determines the income year in which any capital gain or loss is made and whether the CGT discount applies to any capital gain (subsection 104-10(3) of the ITAA 1997).

90. A participating LNL shareholder will make a capital gain from CGT event A1 happening if the capital proceeds from the disposal of a LNL share exceed its cost base. A participating LNL shareholder will make a capital loss if those capital proceeds are less than the LNL share's reduced cost base (subsection 104-10(4) of the ITAA 1997).

Capital proceeds

91. The capital proceeds from the LNL Scheme taking place is the money received or entitled to be received in respect of the disposal of the interests in LNL (subsection 116-20(1) of the ITAA 1997).

92. A participating LNL shareholder will be entitled to receive Scheme Consideration of \$11.50 for each LNL share disposed of under the LNL Scheme. In addition, if the participating LNL shareholder holds the LNL share on the Special Dividend Record Date, the participating LNL shareholder will be entitled to the Special Dividend of \$0.50 per LNL share.

93. The term 'in respect of the event happening' in subsection 116-20(1) of the ITAA 1997 requires the relationship between the event and the receipt of the money, or entitlement to receive the money, must be more than coincidental. An amount is not 'capital proceeds' of an event merely because it is received in association with the event.

94. In this case, the payment of the Special Dividend will not occur independently of the LNL Scheme. The Special Dividend will be determined before the Scheme Meeting but will not be paid unless the requisite majority of non-Kirin LNL shareholders approve the LNL Scheme under which non-Kirin LNL shares are transferred to Kirin. Furthermore, pursuant to the Implementation Agreement, matters such as the manner and form of the Special Dividend are subject to consultation and agreement between LNL and Kirin. Indeed, the Special Dividend is integral to the entire transaction and cannot be paid otherwise than with the agreement of the acquirer, Kirin. Its non-payment may compromise the acquirer's obligations under the Implementation Agreement and, by extension, the LNL scheme. In these circumstances, it is considered that the Special Dividend forms part of the capital proceeds which a participating LNL shareholder will receive in respect of CGT event A1 happening.

95. However, as a LNL shareholder's entitlement to the Special Dividend is determined by the Special Dividend Record Date and entitlement to participate in the LNL Scheme is determined by the Scheme Record Date, it is possible for a participating LNL shareholder to receive only the Scheme Consideration. Therefore, the capital proceeds for each LNL share received by a participating LNL shareholder that is not entitled to be paid the Special Dividend will only be the Scheme Consideration of \$11.50 per LNL share.

96. The capital proceeds for each LNL share received by a participating LNL shareholder that is entitled to be paid the Special Dividend will be \$12.00 per LNL share. This amount consists of the Scheme Consideration of \$11.50 to be paid by Kirin as consideration for acquiring each LNL share held by the participating LNL shareholder and the Special Dividend of \$0.50 to be paid by LNL in respect of each share held by the LNL shareholder.

Anti-overlap provisions

97. Any capital gain made by a participating LNL shareholder from CGT event A1 can be reduced by the amount of the Special Dividend that is included in the participating LNL shareholder's assessable income under subsection 44(1) of the ITAA 1936 (section 118-20 of the ITAA 1997).

98. However, under paragraph 118-20(1B)(b) of the ITAA 1997, the capital gain made by the LNL shareholder will not be reduced by the amount of the franking credit that is included in their assessable income.

Foreign resident participating LNL shareholders

99. Under subsection 855-10(1) of the ITAA 1997, an entity disregards a capital gain or capital loss from a CGT event if they are a foreign resident, or the trustee of a foreign trust for CGT purposes, just before the CGT event happens and the CGT event happens in relation to a CGT asset that is not 'taxable Australian property'.

100. The term 'taxable Australian property' is defined in the table in section 855-15 of the ITAA 1997. The table sets out these five categories of CGT assets:

Item 1	taxable Australian real property;
Item 2	an indirect Australian real property interest not covered by item 5;
Item 3	a CGT asset used at any time in carrying on a business through a permanent establishment (within the meaning of section 23AH of the ITAA 1936) in Australia and which is not covered by item 1, 2 or 5;
Item 4	an option or right to acquire a CGT asset covered by item 1, 2 or 3.
Item 5	a CGT asset that is covered by subsection 104-165(3) of the ITAA 1997 (choosing to disregard a gain or loss on ceasing to be an Australian resident).

101. Therefore, a participating LNL shareholder who is a foreign resident, or the trustee of a foreign trust for CGT purposes, just before CGT event A1 happens under the LNL Scheme, can not disregard under subsection 855-10(1) of the ITAA 1997 a capital gain or capital loss from CGT event A1 if:

- their LNL share is an indirect Australian real property interest that is not covered by item 5 of the table in section 855-15 of the ITAA 1997 (item 2 of the table in section 855-15); or
- their LNL share has been used at any time by the foreign resident, or the trustee of a foreign resident trust for CGT purposes, in carrying on a business through a permanent establishment in Australia and is not covered by items 2 or 5 of the table in section 855-15 (item 3 of the table in section 855-15); or
- their LNL share is covered by subsection 104-165(3) of the ITAA 1997 (choosing to disregard a gain or loss on ceasing to be an Australian resident – item 5 of the table in section 855-15).

102. Section 855-35 of the ITAA 1997 applies to taxable Australian property under item 3 of the table in section 855-15 of the ITAA 1997. Under section 855-35, the capital gain or capital loss a foreign resident, or the trustee of a foreign trust for CGT purposes, makes from the CGT event in relation to the CGT asset is reduced if they used it in this way for only part of the period from when they acquired it to when the CGT event happened.

103. Therefore, any capital gain or capital loss a foreign resident, or the trustee of a foreign trust for CGT purposes, makes from CGT event A1 in relation to taxable Australian property under item 3 of the table in section 855-15 of the ITAA 1997, is not reduced under section 855-35 of the ITAA 1997 if they used it in carrying on a business through a permanent establishment in Australia for the whole of the period from when they acquired it to when CGT event A1 happened.

Anti-avoidance provisions

Section 204-30

104. Section 204-30 of the ITAA 1997 applies where a corporate tax entity streams the payment of dividends, or the payment of dividends and the giving of other benefits, to its members in such a way that:

- (a) an imputation benefit is, or apart from this section would be, received by a member of the entity as a result of the distribution or distributions (paragraph 204-30(1)(a));
- (b) the member would derive a greater benefit from franking credits than another member of the entity (paragraph 204-30(1)(b)); and
- (c) the other member of the entity will receive lesser imputation benefits, or will not receive any imputation benefits, whether or not the other member receives other benefits (paragraph 204-30(1)(c)).

105. Relevantly, if section 204-30 of the ITAA 1997 applies the Commissioner is vested with a discretion under subsection 204-30(3) to make a determination in writing either:

- (a) that a specified franking debit arises in the franking account of the entity, for a specified distribution or other benefit to a disadvantaged member (paragraph 204-30(3)(a)); or
- (b) that no imputation benefit is to arise in respect of any distributions made to a favoured member and specified in the determination (paragraph 204-30(3)(c)).

106. For section 204-30 of the ITAA 1997 to apply, members to whom distributions are streamed must derive a greater benefit from franking credits than the members who consequently do not receive franking credits, or do not receive the same amount of franking credits as they would have had streaming not occurred.

107. Under the current proposal for the payment of the Special Dividend, all LNL shareholders will receive an imputation benefit as a result of the Special Dividend; the resident shareholders in the form of a tax offset (paragraph 204-30(6)(a) of the ITAA 1997) and the non-resident shareholders in the form of an exemption from dividend withholding tax (paragraph 204-30(6)(e) of the ITAA 1997). The resident shareholders will derive a greater benefit from franking credits than the non-resident shareholders (subsection 204-30(8) of the ITAA 1997).

108. However, the Special Dividend will be paid to all LNL shareholders, including Kirin and will be fully franked with Australian franking credits. Accordingly, it cannot be argued that LNL will direct the flow of distributions in such a manner as to stream the imputation benefits such that one class of members will derive a greater benefit from the franking credits attached to the Special Dividend, while the other members will receive lesser or no imputation benefits.

109. As the conditions in subsection 204-30(1) of the ITAA 1997 for the provision to apply will not be met, the Commissioner will not make a determination under paragraph 204-30(3)(c) of the ITAA 1997 to deny the whole, or any part, of the imputation benefit received in relation to the Special Dividend.

Section 177EA

110. Section 177EA of the ITAA 1936 is a general anti-avoidance provision that applies to a wide range of schemes seeking to obtain a tax advantage in relation to imputation benefits. Subsection 177EA(3) provides that section 177EA applies if:

- (a) there is a scheme for a disposition of membership interests, or an interest in membership interests, in a corporate tax entity; and
- (b) either:
 - (i) a frankable distribution has been paid, or is payable or expected to be payable, to a person in respect of the membership interests; or
 - (ii) a frankable distribution has flowed indirectly, or flows indirectly or is expected to flow indirectly, to a person in respect of membership interests, as the case may be;
- (c) the distribution was, or is expected to be, a franked distribution or a distribution franked with an exempting credit;
- (d) except for this section, a person (the 'relevant taxpayer') would receive, or could reasonably be expected to receive, imputation benefits as a result of the distribution; and
- (e) having regard to the relevant circumstances of the scheme, it would be concluded that the person, or one of the persons, who entered into or carried out the scheme or any part of the scheme did so for a purpose (whether or not the dominant purpose, but not including an incidental purpose) of enabling the relevant taxpayer to obtain an imputation benefit.

111. If section 177EA of the ITAA 1936 applies, the Commissioner may make a determination under subsection 177EA(5) that either a franking debit arises to the company in respect of each dividend paid to the relevant taxpayer or, in the alternative, that no franking credit benefit arises in respect of a dividend paid to the relevant taxpayer.

112. LNL is a corporate tax entity. The disposal of the ordinary shares in LNL pursuant to the LNL Scheme is a scheme for the disposition of membership interests. The fully franked Special Dividend is a frankable distribution that will be paid to LNL shareholders as a part of this scheme.

113. In the present case the conditions of paragraphs 177EA(3)(a) to (d) of the ITAA 1936 are satisfied. Accordingly, the issue is whether having regard to the relevant circumstances of the scheme, it would be concluded that, on the part of LNL or its shareholders, there is a purpose, more than merely an incidental purpose, of conferring an imputation benefit under the scheme.

114. In arriving at a conclusion the Commissioner must have regard to the relevant circumstances of the scheme which include, but are not limited to, the circumstances set out in subsection 177EA(17) of the ITAA 1936. The relevant circumstances listed there encompass a range of circumstances which taken individually or collectively could indicate the requisite purpose. Due to the diverse nature of these circumstances, some may not be present at any one time in any one scheme.

115. The relevant circumstances of LNL indicate that there is no requisite purpose. The Special Dividend will be fully franked, which is a continuation of LNL's dividend policy to fully frank dividends distributed. LNL only has ordinary shares on issue and the Special Dividend will be paid to all LNL shareholders on a pro-rata basis in proportion to the number of shares that the LNL shareholder holds on the Special Dividend Record Date. The amount of the dividend is largely consistent with dividends previously paid out by LNL and allows LNL shareholders to share in the current profits of LNL which would otherwise not be available once the LNL Scheme is implemented.

116. In considering the manner, form and substance of the payment of the Special Dividend and the LNL Scheme it is considered that the scheme is not being entered into for the purpose of enabling participating members to obtain an imputation benefit. Having regard to the relevant circumstances of the scheme, the Commissioner has come to the view that the requisite purpose is not present and accordingly the Commissioner will not make a determination under paragraph 177EA(5)(b) of the ITAA 1936 to deny the whole, or any part, of the imputation benefit received in relation to the Special Dividend.

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References

Previous draft:

Not previously issued as a draft

Related Rulings/Determinations:

TR 2006/10; TD 2002/4

Subject references:

- CGT asset
- CGT capital proceeds
- CGT cost base
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- CGT event A1
- dividend income
- dividend streaming arrangements
- frankable dividends
- imputation system
- franking credits
- qualified persons
- related payments rule
- foreign residents

Legislative references:

- ITAA 1936 6(1)
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royalty income
Income Tax – Capital gains tax – capital proceeds
Income Tax – CGT event A1 – disposal of a CGT asset
Income Tax – Tax integrity measures – dividend
streaming and demerger benefits
Income Tax – Tax integrity measures – qualified persons
– franking credits