



Class Ruling

Income tax: Australia and New Zealand Banking Group Limited – allotment of convertible preference shares (CPS 2)

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① This publication provides you with the following level of protection:

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 provision(s) 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:

- section 6BA of the *Income Tax Assessment Act 1936* (ITAA 1936);
- subsection 44(1) of the ITAA 1936;
- section 45 of the ITAA 1936;
- section 45A of the ITAA 1936;
- section 45B of the ITAA 1936;
- subsection 177EA(5) of the ITAA 1936;
- former Division 1A of Part IIIAA of the ITAA 1936;
- subsection 6-5(1) of the *Income Tax Assessment Act 1997* (ITAA 1997);

- Division 67 of the ITAA 1997;
- Division 104 of the ITAA 1997;
- section 109-10 of the ITAA 1997;
- subsection 110-25(2) of the ITAA 1997;
- subsection 110-55(2) of the ITAA 1997;
- Subdivision 130-A of the ITAA 1997;
- subsection 204-30(3) of the ITAA 1997;
- Division 207 of the ITAA 1997;
- section 207-145 of the ITAA 1997; and
- subsection 995-1(1) of the ITAA 1997.

All legislative references are to the ITAA 1997 unless otherwise indicated.

Class of entities

3. The class of entities to which this Ruling applies are Australian resident (within the meaning of subsection 6(1) of the ITAA 1936) subscribers (Holders) of Convertible Preference Shares (CPS 2) in Australia and New Zealand Banking Group Limited (ANZ) who hold those CPS 2 on capital account.

4. The class of entities to which this Ruling applies does not extend to Holders of CPS 2 who did not acquire their interest by initial subscription.

5. This Ruling does not deal with how the taxation law applies to Holders who hold their CPS 2 as trading stock or revenue assets.

6. This Ruling does not consider the tax implications of the Exchange of CPS 2 by Conversion, Redemption or Resale in accordance with clauses 5 and 6 of the Terms.

7. This Ruling does not consider how the taxation law applies to a Nominated Purchaser who acquires CPS 2 under the Resale facility.

8. This Ruling does not consider how the gross-up and tax offset rules in Division 207 apply to partnership or trustee Holders, or to indirect distributions to partners in a partnership, or beneficiaries or trustees of a trust.

9. This Ruling does not deal with how the taxation law applies to ANZ in relation to the issue of CPS 2.

Qualifications

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

11. 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 15 to 50 of this Ruling.

12. 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

14. This Ruling applies from 17 December 2009 to 30 June 2017. The Ruling continues to apply after 30 June 2017 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

15. The following description of the scheme is based on information provided by the Applicant. The following documents (Transaction Documents), or relevant parts of them form part of and are to be read with the description:

- Application for Class Ruling from ANZ dated 25 September 2009;

- Prospectus dated 18 November 2009 for the issue of CPS 2 by ANZ (Prospectus); and
- CPS 2 Terms contained in Appendix A of the Prospectus (Terms).

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

16. In this Ruling, unless otherwise defined, capitalised terms take on the same meaning as in the Prospectus.

17. During the term of the Transaction, ANZ will be a resident of Australia under the income tax laws of Australia and of no other jurisdiction.

18. ANZ will apply for CPS 2 to be quoted on the Australian Securities Exchange (ASX) and are expected to trade under ASX code 'ANZPA'.

19. In the Prospectus, ANZ announced its intention to undertake a capital raising by means of the issue of CPS 2.

20. ANZ intends to issue 17 million CPS 2 to raise \$1.7 billion with the ability to raise more or less.

21. The capital raised from the issue of CPS 2 will be used for ANZ's general corporate purposes and as part of its continuing capital management strategy within the guidelines prescribed by the Australian Prudential Regulation Authority (APRA).

22. The classes of Applicants for CPS 2 and the process for lodging are described in the Prospectus as follows:

- ANZ Security holder Applicant – a holder of Ordinary Shares or a holder of 2008 CPS, shown on the register at 7:00pm on 30 October 2009, with an address in Australia – applying through the ANZ Security holder Offer;
- General Applicant – a member of the general public who is an Australian resident – applying through the General Offer;
- Broker Firm Applicant – a retail client of a Syndicate Broker (whether an Australian resident or not) – applying through the Broker Firm Offer; and
- Institutional Investors – an Investor (whether an Australian resident or not) who has been invited by the Joint Lead Managers to bid for CPS 2 in the Bookbuild and who is not a Broker Firm Applicant, ANZ Security holder Applicant or General Applicant – applying through the Institutional Offer.

23. The Prospectus states that no action has been taken to register or qualify CPS 2 or the Offer, or to otherwise permit a public offering of CPS 2 outside Australia. It further states that the Joint Lead Managers and Syndicate Brokers may offer CPS 2 outside Australia under the Institutional Offer or Broker Firm Offer where such offer is made in accordance with the laws of that jurisdiction. ANZ have confirmed that CPS 2 was offered to a limited number of non-resident Investors.

Main features of CPS 2

24. CPS 2 are fully paid mandatorily convertible preference shares in the capital of ANZ.

25. The issue price of each CPS 2 (Issue Price) is \$100. CPS 2 are fully paid up to \$100 face value on issue.

26. CPS 2 generally do not have voting rights, except in the limited circumstances described in the Terms.

Dividend calculation

27. Subject to the conditions outlined at paragraph 30 of this Ruling, the Holder of each CPS 2 is entitled to receive on the relevant Dividend Payment Date, a dividend (Dividend) payable in arrears (starting 15 March 2010) calculated using the formula:

$$\text{Dividend} = \frac{\text{Dividend Rate} \times \text{Issue Price} \times N}{365}$$

where:

Dividend Rate (expressed as a percentage per annum) is calculated using the following formula:

$$\text{Dividend Rate} = (\text{Bank Bill Rate} + \text{Margin}) \times (1 - \text{Tax Rate})$$

where:

Bank Bill Rate (expressed as a percentage per annum) means, for a Dividend Period, the average mid-rate for bills of a term of 90 days which average mid-rate is displayed on Reuters page BBSW (or any page which replaces that page) on the first Business Day of the Dividend Period or if there is a manifest error in the calculation of that average mid-rate or that average mid-rate is not displayed by 10.30am (Melbourne time) on that date, the rate specified in good faith by ANZ at or around that time on that date having regard, to the extent possible, to:

- (a) the rates otherwise bid and offered for bills of a term of 90 days or for funds of that tenor displayed on Reuters page BBSW (or any page which replaces that page) at that time on that date; or

- (b) if bid and offer rates for bills of a term of 90 days are not otherwise available, the rates otherwise bid and offered for funds of that tenor at or around that time on that date.

Margin is 3.10% per annum as determined under the Bookbuild; and

Tax Rate (expressed as a decimal) means the Australian corporate tax rate applicable to the franking account of ANZ at the relevant Dividend Payment Date; and

N means in respect of:

- (a) the first Dividend Payment Date, the number of days from (and including) the Issue Date until (but not including) the first Dividend Payment Date; and
- (b) each subsequent Dividend Payment Date, the number of days from (and including) the preceding Dividend Payment Date until (but not including) the relevant Dividend Payment Date.

28. The Dividend Payment Dates are each 15 March, 15 June, 15 September and 15 December, commencing on 15 March 2010 until (but not including) the date on which Redemption or Conversion occurs. A Dividend will also be paid on the date of which a Conversion, Resale or Redemption occurs in accordance with CPS 2 Terms.

29. The Dividends are expected to be fully or substantially franked. However, if any Dividend is not franked or only partially franked, the Dividend will be grossed-up to the extent that the franking percentage of the Dividend is less than or equal to 100%, as determined by the calculation in clause 3.2 of the Terms.

Dividend payment conditions

30. Each Dividend (including an Optional Dividend) is subject to:

- the Directors, at their absolute discretion, resolving to pay the Dividend;
- such payment of the Dividend not resulting in the Prudential Capital Ratio or the Tier 1 Capital Ratio of ANZ (on a Level 1 basis) or of the ANZ group (on a Level 2 basis or, if applicable, Level 3 basis) not complying with APRA's then current capital adequacy guidelines as they are applied to ANZ or the ANZ group (as the case may be) at the time, unless APRA otherwise approves in writing;
- the amount of the Dividend not exceeding Distributable Profits, unless APRA otherwise agrees;
- payment of the Dividend not resulting in ANZ becoming, or being likely to become, insolvent for the purposes of the *Corporations Act 2001*; and
- APRA not otherwise objecting to the payment of the Dividend.

31. The Directors, in their absolute discretion but with the prior written approval of APRA, may determine an Optional Dividend to be payable on any date, subject to the above conditions.

32. A Dividend or an Optional Dividend is only payable to those persons registered as the Holders on the Record Date for that Dividend or Optional Dividend respectively.

33. The Dividends are non-cumulative and the Holders will have no recourse in the event of non-payment. Accordingly, non-payment of all or part of a declared Dividend does not constitute an event of default by ANZ, and the Holders have no claim against ANZ in respect of non-payment.

34. No interest accrues on any unpaid Dividends or Optional Dividends and the Holders have no claim or entitlement in respect of interest on any unpaid Dividends or Optional Dividends.

Restrictions in the case of non-payment of Dividends

35. If a Dividend has not been paid in full within 21 Business Days after the relevant Dividend Payment Date, ANZ must not (without approval of a Special Resolution) declare or pay a Dividend, or make any distribution on any capital instruments (which rank equally with or junior to CPS 2 for distributions) of ANZ, or redeem, buy-back or reduce capital on any capital instruments (which rank equally with or junior to CPS 2 for a return of capital in a winding up) of ANZ unless:

- consecutive Dividends scheduled to be payable on CPS 2 on the Dividend Payment Dates falling during the 12 months after the Dividend Payment Date of the Dividend that has not been paid, have been paid in full;
- with the prior written approval of APRA, an Optional Dividend has been paid to the Holders equal to the aggregate unpaid amount of any unpaid Dividends which were scheduled to be paid in the 12 months prior to the date of payment of the Optional Dividend; or
- all CPS 2 have been Redeemed or Converted.

Mandatory Conversion

36. Subject to paragraph 45 of this Ruling (ANZ electing to Resell all CPS 2 on the Relevant Dates), ANZ must Convert all CPS 2 on issue into Ordinary Shares on the Mandatory Conversion Date.

37. The Mandatory Conversion Date is 15 December 2016 provided all the Mandatory Conversion Conditions are satisfied. If any of the Mandatory Conversion Conditions are not satisfied on 15 December 2016, the Mandatory Conversion Date will be deferred until the next Dividend Payment Date on which the Mandatory Conversion Conditions are satisfied.

38. The Mandatory Conversion Conditions are:

- the average of the daily volume weighted average sale prices (VWAP) of Ordinary Shares on the 25th Business Day on which trading in Ordinary Shares took place immediately preceding (but not including) the Relevant Date (the First Test Date) is greater than 56.00% of the Issue Date VWAP;
- the VWAP during the period of 20 Business Days on which trading in Ordinary Shares took place immediately preceding (but not including) the Relevant Date (the Second Test Date) is greater than 50.51% of the Issue Date VWAP;
- and either:
 - the Ordinary Shares remain listed and admitted to trading on the ASX; or
 - trading of Ordinary Shares on the ASX has not been suspended for at least five consecutive Business Days prior to a possible Mandatory Conversion Date and that Mandatory Conversion Date.

39. On Conversion, each CPS 2 will Convert into one Ordinary Share through a variation of the rights attaching to each CPS 2 on the Mandatory Conversion Date, the Exchange Date or the Change of Control Exchange Date (as the case may be). Each Holder will be allotted, for no consideration, an additional number of Ordinary Shares for each CPS 2 that is Converted.

40. The total market value of the Ordinary Shares held by a Holder immediately after the Conversion of CPS 2 (and as a result of such Conversion) will approximate the Issue Price of CPS 2 (\$100).

41. Conversion does not constitute redemption, buy-back or cancellation of CPS 2, nor does it constitute an issue, allotment or creation of a new Ordinary Share (other than any additional Ordinary Shares allotted).

Redemption

42. If any of the Mandatory Conversion Conditions are not satisfied, ANZ may (subject to APRA giving its prior written approval) Redeem all CPS 2. Otherwise, Conversion is deferred until the next Dividend Payment Date on which all the Mandatory Conversion Conditions are satisfied.

43. 'Redeem' means redeem, buy-back (other than an on-market buy-back within the meaning of the *Corporations Act 2001*) or reduce capital, or any combination of such activities.

44. CPS 2 will be redeemed by payment of the Issue Price. However, where the Redemption involves a buy-back of CPS 2, the Directors may determine that the consideration payable for each CPS 2 that is bought back will include an amount equal to a Dividend for that Dividend Period as well as the Issue Price.

Resale

45. Whether or not the Mandatory Conversion Conditions are satisfied in relation to a Relevant Date, ANZ may elect to Resell all (but not some) CPS 2 on the Relevant Date. If ANZ elects to Resell, ANZ must appoint one or more Nominated Purchasers for the Resale upon such terms as may be agreed between ANZ and the Nominated Purchaser. The Nominated Purchaser must undertake to acquire CPS 2 from the Holders for the Issue Price.

46. Each Holder is taken irrevocably to offer to sell CPS 2 to the Nominated Purchaser for the cash equivalent to the Issue Price. Subject to payment by the Nominated Purchaser of the Issue Price to the Holders, all rights, title and interest in such CPS 2 (excluding the right to any Dividend payable on that date) will be transferred to the Nominated Purchaser on the Relevant Date or the Exchange Date (as the case may be).

Exchange

47. ANZ may elect to Exchange all or some of CPS 2 on an Exchange Date following the occurrence of a Tax Event or a Regulatory Event; or may choose to Exchange all (but not some) CPS 2 on issue after the occurrence of an Acquisition Event.

48. If ANZ elects to Exchange CPS 2, it must elect which of the following (or which combination of the following) it intends to do in respect of CPS 2 :

- subject to APRA's prior written approval and the satisfaction of either of the Optional Conversion Restrictions, Convert the CPS 2 into Ordinary Shares;
- subject to APRA's prior written approval, Redeem CPS 2; or
- Resell the CPS 2.

49. ANZ may make an election to Exchange all (but not some) CPS 2 following an Acquisition Event. The right to Exchange is at the discretion of ANZ. Holders do not have a right to request an Exchange.

Other matters

50. The Ruling is made on the basis that:

- (a) the Transaction Documents represent a complete and accurate description of the Transaction, are intended by parties to have their legal effect and will be implemented according to their terms;
- (b) all parties to the Transaction are dealing with each other on arm's length terms and fair value consideration will be provided by the Holders to acquire CPS 2;
- (c) CPS 2 are equity interests in ANZ pursuant to Division 974;
- (d) Dividends on CPS 2 will be frankable distributions pursuant to section 202-40;
- (e) ANZ will frank the distributions on CPS 2 at the same franking percentage as the benchmark for the franking period in which the payments are made;
- (f) the share capital of ANZ will not become tainted within the meaning of Subdivision 197-A by an issue of CPS 2 or the allotment of additional Ordinary Shares on Conversion of CPS 2;
- (g) the additional Ordinary Shares issued in the event of Conversion of CPS 2 will be equity interests in ANZ pursuant to Division 974;
- (h) the majority of the Holders are expected to be residents of Australia for tax purposes, although some may be non-residents;
- (i) CPS 2 are expected to be treated as a liability for Australian International Financial Reporting Standards (AIFRS) purposes;
- (j) for the purposes of determining whether a Holder is a 'qualified person' under the former definition of 'qualified person' in subsection 995-1(1), a Holder has taken no positions (apart from the holding of CPS 2) in relation to their CPS 2 and has not made, is not under an obligation to make, or is not likely to make, a related payment in relation to the Dividends;
- (k) the Holders, or their associates, will not make any related payments (within the meaning of former section 160APHN of the ITAA 1936) in relation to the Dividends on CPS 2;

- (l) the Holders in receipt of Dividends on CPS 2 will have held their CPS 2 for a period of at least 90 days (excluding the day of acquisition and the day of disposal, and any days on which the Holder has materially diminished risks of loss or opportunities for gain in respect of the CPS 2), within the period beginning on the day after the day on which the Holder acquired CPS 2 and ending on the 90th day after the day on which CPS 2 become ex-dividend;
- (m) Dividends on CPS 2 will be paid out of the retained profits of ANZ;
- (n) the dividend payout ratios or the franking credits in relation to the ordinary share capital or other preference share capital of ANZ are not expected to materially change as a result of the issue of CPS 2; and
- (o) on the date of Conversion of CPS 2 into Ordinary Shares, the rights and obligations attached to the Ordinary Shares are the same as those contained in the Constitution of ANZ.

Ruling

Acquisition time of CPS 2

51. Under item 2 in the table in section 109-10, the Holders acquired CPS 2 on 17 December 2009, being the date CPS 2 were issued to them.

CPS 2 cost base and reduced cost base

52. Under subsections 110-25(2) and 110-55(2), the first element of the cost base and reduced cost base of each CPS 2 is \$100.

Inclusion of Dividends in assessable income

53. The Holders must include in their assessable income all Dividends received in respect of their CPS 2 under subparagraph 44(1)(a)(i) of the ITAA 1936, and an amount equal to the franking credit received on those Dividends under Division 207 of the ITAA 1997.

Entitlement to a tax offset

54. The Holders will be entitled to a tax offset equal to the franking credit received on the Dividends under subsection 207-20(2), unless Subdivision 207-D applies (refer to paragraph 58 of this Ruling).

55. The Holders who are entitled to a tax offset under Division 207, in respect of franking credits received, will also be subject to the refundable tax offset rules in Division 67. This is unless the Holders are specifically excluded from the refundable tax offset rules under section 67-25. Excluded entities include certain trustees and corporate tax entities under subsections 67-25(1A) to 67-25(1D).

Imputation benefits

56. The Commissioner will not make a determination under paragraph 204-30(3)(c) to deny the whole, or any part, of the imputation benefits received by Holders in relation to the Dividends payable in respect of CPS 2.

Determination under paragraph 177EA(5)(b)

57. 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 benefits received by Holders in relation to the Dividends payable in respect of CPS 2.

Exempt income or non-assessable non-exempt income

58. If the Dividend (or a part of it) is either exempt income or non-assessable non-exempt income in the hands of the relevant Holder, then the amount of any franking credit on the Dividend is not included in the assessable income of the Holder and the Holder is not entitled to a tax offset under Division 207 (Subdivision 207-D).

Gross up

59. Section 207-145 will not apply to the whole, or any part, of the Dividends received by the Holders. Accordingly, section 207-145 will not adjust the gross up of the Holders' assessable income to exclude the franking credit, nor will it deny the tax offset to which the Holders would have been entitled.

Qualified person and the Resale facility

60. Under the former definition of 'qualified person', within subsection 995-1(1) of the ITAA 1997, the Resale facility contained in clause 9 of the Terms will not affect a Holder's risks of loss or opportunities for gain in respect of CPS 2 on the basis that it does not constitute a separate position for the purposes of former Division 1A of Part IIIAA of the ITAA 1936.

Conversion of each CPS 2 and allotment of additional Ordinary Shares – CGT implications

61. The Conversion of each CPS 2 into Ordinary Shares and the allotment of additional Ordinary Shares will not result in a CGT event occurring.

62. CGT event H2 in section 104-155 will not happen on the Conversion of each CPS 2 involving the allotment of additional Ordinary Shares, as a cost base adjustment will be made to CPS 2 because of the allotment of the additional Ordinary Shares. No other CGT event in Division 104 will happen on the Conversion of each CPS 2 involving the allotment of additional Ordinary Shares.

Allotment of additional Ordinary Shares – Dividend

63. The allotment of additional Ordinary Shares on Conversion of CPS 2 will not be assessable as dividend income in the hands of the Holders.

The value of additional Ordinary Shares – ordinary income

64. The value of any additional Ordinary Shares issued on Conversion of CPS 2 will not be assessable as ordinary income in the hands of the Holders under subsection 6-5(1).

Section 45

65. Section 45 of the ITAA 1936 will not apply to treat the additional Ordinary Shares acquired on Conversion of CPS 2 as an unfranked dividend paid by ANZ.

Section 45A

66. The Commissioner will not make a determination, under subsection 45A(2) of the ITAA 1936, that the additional Ordinary Shares acquired on Conversion of CPS 2 will be an unfranked dividend in the hands of the Holders.

Section 45B

67. The Commissioner will not make a determination, under subsection 45B(3) of the ITAA 1936, that the additional Ordinary Shares acquired on Conversion of CPS 2 will be an unfranked dividend in the hands of the Holders.

Cost base of the additional Ordinary Shares

68. Either section 6BA of the ITAA 1936 or Subdivision 130-A of the ITAA 1997 will apply to apportion the first element of the cost base and reduced cost base of each CPS 2 over the Converted CPS 2 and any additional Ordinary Shares allotted by ANZ.

Acquisition time of additional Ordinary Shares

69. Under subsection 130-20(3), the additional Ordinary Shares are taken to be acquired at the time CPS 2 were originally acquired by the Holders, being 17 December 2009.

Commissioner of Taxation

2 December 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.*

Acquisition time of CPS 2

70. An equity interest that is issued or allotted by a company is acquired when the contract is entered into or, if no contract exists, when the equity interest is issued or allotted (item 2 in the table in section 109-10).

71. CPS 2 were issued on 17 December 2009. Therefore, under item 2 in the table contained in section 109-10, CPS 2 were acquired on 17 December 2009.

CPS 2 cost base and reduced cost base

72. The first element of the cost base and reduced cost base of a CGT asset includes the money paid, or required to be paid, in respect of acquiring a CGT asset (paragraph 110-25(2)(a) and subsection 110-55(2)).

73. The Issue Price of each CPS 2 is \$100. Accordingly, when CPS 2 are issued, the first element of the cost base and reduced cost base of each CPS 2 is \$100.

Inclusion of dividends in assessable income

74. Paragraph 44(1)(a) of the ITAA 1936 provides that the assessable income of a resident shareholder in a company includes dividends that are paid to the shareholder by the company out of profits derived by it from any source.

75. Dividends paid in respect of CPS 2 will be paid out of ANZ's retained profits. Accordingly, the Holders must include the amount of the Dividends received by them in their assessable income.

76. Dividends paid in respect of CPS 2 are expected to be fully or substantially franked.

77. Under the Australian imputation system, where a franked distribution is paid by an Australian resident company to a shareholder, the assessable income of the shareholder must also include the franking credit attached to the dividend under Division 207. The inclusion of both the dividend and the associated franking credit in a shareholder's assessable income is termed 'grossing up' the dividend receipt.

78. Accordingly, the franking credits attached to the Dividends received by the Holders must be included in their assessable income.

79. In accordance with subsection 207-20(2), and with respect to the 'grossing up' of the Dividend receipt, the Holders are entitled to receive a tax offset equal to the value of the franking credit, which has been included in their assessable income.

Franking credit subject to the refundable tax offset rules

80. The Holders who are entitled to a tax offset under subsection 207-20(2) in respect of the franking credit received, will also be subject to the refundable tax offset rules contained in Division 67, unless specifically excluded under section 67-25.

81. The refundable tax offset rules ensure that certain taxpayers are entitled to a refund, once their available tax offsets have been utilised to reduce any income tax liability to nil.

82. Accordingly, the Holders will be subject to the refundable tax offset rules unless they are listed as specifically excluded entities under section 67-25.

83. Entities excluded by Division 67 include corporate tax entities (such as companies, corporate limited partnerships, corporate unit trusts and public trading trusts), unless they satisfy the requisite conditions as set out in subsections 67-25(1C) or 67-25(1D).

Imputation benefits – streaming of imputation benefits

84. Subdivision 204-D broadly enables the Commissioner to make a determination where distributions with attached imputation benefits are streamed to a member of a corporate tax entity in preference to another member.

85. Section 204-30 prescribes the circumstances that are required to exist before the Commissioner may make such a determination. Section 204-30 applies where an entity 'streams' the payment of distributions in such a way that:

- an 'imputation benefit' is, or apart from section 204-30 would be, received by a member of the entity as a result of the distribution or distributions (paragraph 204-30(1)(a));
- the member (favoured member) would derive a greater benefit from franking credits than another member of the entity (paragraph 204-30(1)(b)); and
- the other member (disadvantaged 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)).

86. 'Streaming' is not defined for the purposes of Subdivision 204-D. However, the Commissioner has understood it to refer to a company 'selectively directing the flow of franked distributions to those members who can most benefit from the imputation credits' (refer to paragraph 3.28 of the Explanatory Memorandum to the New Business Tax System (Imputation) Bill 2002).

87. ANZ has indicated that all Holders will receive fully or substantially franked Dividends regardless of their tax attributes or their individual tax position. The dividend payout ratios or franking credits, in relation to the Ordinary Shares or other preference shares, will not be materially affected by the issue of CPS 2. CPS 2 were offered to non-resident Investors.

88. The additional Ordinary Shares allotted on Conversion of CPS 2 will not attract the application of section 204-30. This is because the issue of the additional Ordinary Shares does not constitute a distribution and the allotment of additional Ordinary Shares will not materially affect ANZ's fully franked dividend policy on its share capital.

89. Based on the information provided, the Commissioner has concluded that the requisite element of streaming does not exist in relation to the franked distributions to be paid by ANZ to the Holders. Accordingly, based on the information provided, the Commissioner will not make a determination under paragraph 204-30(3)(c) to deny imputation benefits to the Holders.

Determination under paragraph 177EA(5)(b)

90. Section 177EA of the ITAA 1936 is a general anti-avoidance provision that applies where one of the purposes (other than an incidental purpose) of the scheme is to obtain an imputation benefit. In these circumstances, subsection 177EA(5) of the ITAA 1936 enables the Commissioner to make a determination with the effect of either:

- imposing franking debits or exempting debits on the distributing entity's franking account; or
- denying the imputation benefit on the distribution that flowed directly or indirectly to the relevant taxpayer.

91. Pursuant to subsection 177EA(3) of the ITAA 1936, the provision applies if the following conditions are satisfied:

- (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 the interest in membership interests, as the case may be; and
- (c) the distribution was, or is expected to be, a franked distribution or a distribution franked with an exempting credit; and
- (d) except for this section, the 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.

92. The Commissioner has considered that the conditions in paragraphs 177EA(3)(a) to 177EA(3)(d) of the ITAA 1936 are satisfied because:

- (a) the issue of CPS 2 constitutes a scheme for the disposition of a membership interest (paragraph 177EA(3)(a) of the ITAA 1936).

Pursuant to paragraph 177EA(14)(a) of the ITAA 1936, a 'scheme for a disposition of membership interests or an interest in membership interests' includes a scheme that involves the issuing of membership interests.

The issuance of CPS 2 on the terms set out in the Prospectus is a scheme that involves the issuing of membership interests because, once CPS 2 are issued, the Holders are members of ANZ and CPS 2 are not debt interests (sections 960-130 and 960-135);
- (b) frankable distributions are expected to be payable to the Holders (paragraph 177EA(3)(b) of the ITAA 1936). The Commissioner accepts that Dividends payable on CPS 2 will be frankable distributions to the extent that the Dividends on CPS 2 do not fall within the list in section 202-45 of the ITAA 1997;

- (c) franked distributions are expected to be paid to the Holders (paragraph 177EA(3)(c) of the ITAA 1936). It is expected that these distributions will be made on a quarterly basis. Furthermore, ANZ has advised that it will continue its policy of fully franking all frankable distributions made by it, to the extent of the franking credits available in its franking account; and
- (d) it is reasonable to expect that an imputation benefit will be received by the relevant taxpayers as a result of distributions made to the Holders, given that ANZ expects to frank the distributions on CPS 2 (paragraph 177EA(3)(d) of ITAA 1936).

93. Accordingly, the issue is whether having regard to the relevant circumstances of the scheme, it would be concluded that a person, or one of the persons, who entered into or carried out 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.

94. Circumstances which are relevant in determining whether any person has the requisite purpose include, but are not limited to, the factors listed in subsection 177EA(17) of the ITAA 1936.

95. The relevant circumstances listed 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 or may not be present at any one time in any one scheme.

96. ANZ advised that it will issue CPS 2 as part of its ongoing capital management strategy and to provide ANZ with Tier 1 capital as required by APRA for capital adequacy purposes. A consideration of all the terms does not lead to the conclusion that the scheme was entered into for the purpose (which is not merely an incidental purpose) of enabling the relevant taxpayer to obtain an imputation benefit under the scheme.

97. Based on the information provided, and having regard to the factors listed in subsection 177EA(17) of the ITAA 1936, the qualifications set out in this Ruling and the relevant circumstances of the scheme, it would not be reasonable to conclude that in entering into the scheme, ANZ and/or the Holders demonstrate the objective purpose of securing imputation benefits for the Holders. To the extent that any imputation benefits are secured, those benefits are considered to be incidental to the more significant objective purposes of the raising of Tier 1 Capital by ANZ to meet its capital adequacy requirements.

98. Accordingly, the Commissioner will not make a determination under paragraph 177EA(5)(b) of the ITAA 1936 that would deny the imputation benefits to the Holders.

Exempt income or non-assessable non-exempt income

99. Subdivision 207-D creates the appropriate adjustment to cancel the effect of the gross-up and tax offset rules where the Holder receives a franked distribution, and the franked distribution (or share of it) is or would be exempt income or non-assessable non-exempt income in the hands of the relevant Holder.

Gross up

100. Subdivision 207-F creates the appropriate adjustment to cancel the effect of the gross up and tax offset rules where the entity concerned has manipulated the imputation system in a manner that is not permitted under the income tax law.

101. Section 207-145 provides the circumstances that must exist before this adjustment can occur. Pursuant to subsection 207-145(1) a 'manipulation of the imputation system' may occur where:

- the entity is not a 'qualified person' in relation to the distribution (paragraph 207-145(1)(a));
- the Commissioner has made a determination under paragraph 177EA(5)(b) of the ITAA 1936 that no imputation benefit is to arise in relation to the dividend (paragraph 207-145(1)(b) of the ITAA 1997);
- the Commissioner has made a determination under paragraph 204-30(3)(c) that no imputation benefit is to arise in relation to the distribution (paragraph 207-145(1)(c)); or
- the dividend is made as part of a dividend stripping operation (paragraph 207-145(1)(d)).

102. A person is generally a 'qualified person' for the purposes of Division 1A of former Part IIIA of the ITAA 1936 if, generally speaking, they satisfy the holding period rule and the related payments rule (former section 160APHO of the ITAA 1936).

103. The holding period rule applies where neither the taxpayer or an associate has made, is under an obligation to make, or is likely to make, a related payment in respect of the dividend, and requires the shares to have been continuously held at risk throughout the primary qualification period (former paragraph 160APHO(1)(a) of the ITAA 1936).

104. The related payments rule applies where the taxpayer or an associate, has made, is under an obligation to make, or is likely to make, a related payment in respect of the dividend and requires the shares to have been continuously held at risk throughout the secondary qualification period (former subsection 160APHO(1) and former section 160APHN of the ITAA 1936).

105. The Commissioner has concluded that the Holders will be qualified persons, provided that:

- the Holders, in receipt of Dividends on CPS 2 will have held their CPS 2 at risk for a period of at least 90 days, (excluding the day of acquisition and the day of disposal, and any days on which the Holder has materially diminished risks of loss or opportunities for gain in respect of the shares or interest), in the period beginning on the day after the day on which the Holders acquired CPS 2 and ending on the 90th day after the day on which CPS 2 become ex-dividend (former subsections 160APHO(2) and 160APHO(3) and former sections 160APHM and 160APHJ of the ITAA 1936); and
- neither the Holders, nor associates of the Holders, have made, are under an obligation to make, or are likely to make a related payment in relation to the Dividends on CPS 2 (former paragraph 160APHO(1)(a) and former section 160APHN of the ITAA 1936).

106. If either or both of the above two considerations are not met, the Holders will not be a 'qualified person' for the purposes of Division 1A of former Part IIIA of the ITAA 1936. Subdivision 207-F of the ITAA 1997 will create the appropriate adjustment to cancel the effect of the gross-up and tax offset rules for the Holders.

107. The Commissioner has confirmed that he will not make a determination under paragraph 177EA(5)(b) of the ITAA 1936 or paragraph 204-30(3)(c) of the ITAA 1997 to deny the imputation benefits attached to Dividends paid by ANZ to the Holders (see paragraphs 56 and 57 of this Ruling).

108. A distribution will be taken to be made as part of a dividend stripping operation, pursuant to section 207-155, where the distribution arose out of, or was made in the course of, a scheme or substantially similar arrangement that was in the nature of dividend stripping.

109. The Transaction Documents provide no indication that the offering of CPS 2 and the associated payment of franked Dividends to the Holders in any way constitute a dividend stripping arrangement. As such, the dividend stripping provision will have no application to the Holders.

Qualified person and the Resale facility

110. In determining whether a shareholder is a 'qualified person' in relation to dividends paid on their shares, all 'positions' in respect of the shares are taken into account in identifying a 'net position' to ensure that there is no material diminution in the risks of loss or opportunities for gain.

111. In accordance with former subsection 160APHJ(2) of the ITAA 1936, a position in relation to a share is anything that has a 'delta' in relation to that share. Although 'delta' is not a defined term, paragraph 4.56 of the Explanatory Memorandum to the Taxation Laws Amendment Bill (No. 2) 1999 states that it 'is a well-recognised financial concept that measures the relative change in the price of an option or other derivative for a given small change in the price of an underlying asset. An option with a positive delta indicates that its price is expected to rise and fall with the underlying asset, while a negative delta indicates an inverse price relationship.'

112. An embedded share option is a position in relation to a share if it is exercisable by or against a party other than the issuer of the share (Taxation Determination TD 2007/29).

113. Under the Resale facility, ANZ can elect to require all Holders to sell their CPS 2 to a Nominated Purchaser. Accordingly, a Nominated Purchaser, until nominated by ANZ, has no right or ability to trigger Redemption or call for CPS 2 from the Holders.

114. ANZ is also not required to exercise the Resale facility and has not appointed any Nominated Purchaser. It follows that the Resale facility is an option that is held by ANZ, as the issuer of the share, and not by a third party. The Resale facility therefore does not represent a separate position in relation to CPS 2 for the purposes of former Division 1A of Part IIIA of the ITAA 1936.

115. Therefore, the Commissioner has concluded that the Resale facility does not affect a Holder's risks of loss or opportunities for gain in respect of CPS 2.

Conversion of each CPS 2 and allotment of additional Ordinary Shares – CGT implications

116. Under the Transaction, each CPS 2 will Convert into one Ordinary Share through a variation of the rights attaching to each CPS 2. The Holders will also receive an allotment of additional Ordinary Shares in ANZ.

117. Subject to satisfaction of the Mandatory Conversion Conditions and ANZ not electing to Resell all CPS 2 on a Relevant Date, CPS 2 will Convert into Ordinary Shares on 15 December 2016. If the Mandatory Conversion Conditions are not satisfied on that date, the Mandatory Conversion Date moves to the next Dividend Payment Date on which the conditions are satisfied. CPS 2 may Convert earlier, if ANZ elects to Convert CPS 2 into Ordinary Shares following the occurrence of certain events defined in the Terms.

118. Shares are comprised of a bundle of rights; however, those rights are not separate pieces of property capable of being divided out and held separately. Accordingly, the rights attaching to shares do not constitute individual assets as defined by section 108-5, but rather combine to make up the relevant CGT asset, being the share (Taxation Ruling TR 94/30).

119. Under section 104-25, CGT event C2 happens if, among other things, the ownership of an intangible asset, such as a preference share, ends by the share:

- being redeemed or cancelled (paragraph 104-25(1)(a)); or
- if the share is a convertible interest – being converted (paragraph 104-25(1)(f)).

120. The mere variation of rights attaching to CPS 2 and allotment of an additional number of Ordinary Shares for no consideration is not a 'redemption' or 'cancellation' of the share under paragraph 104-25(1)(a). Further, the Conversion of CPS 2 does not involve CPS 2 being converted into equity interests under paragraph 104-25(1)(f), but rather Conversion according to the Terms.

121. Furthermore, the relinquishment by the Holders of some of the rights attaching to CPS 2 is not a CGT event that happens to part of the CGT asset comprised by each CPS 2 under section 112-30 (paragraph 40 of TR 94/30).

122. As CGT event C2 will not occur on Conversion of CPS 2 into Ordinary Shares, Subdivision 130-C will have no application.

123. Although CGT event C2 does not happen because of the variation of the rights attaching to CPS 2, the receipt of money or other consideration in respect of such a variation may attract the operation of CGT event H2 (paragraphs 9 and 46 to 48 of TR 94/30).

124. Subsection 104-155(1) provides that CGT event H2 happens if:

- (a) an act, transaction or event occurs in relation to a CGT asset that you own; and
- (b) the act, transaction or event does not result in an adjustment being made to the asset's cost base or reduced cost base.

125. The Conversion of CPS 2 involving the allotment of additional Ordinary Shares will result in an adjustment to the cost base and reduced cost base of CPS 2 under Subdivision 130-A of the ITAA 1997 or section 6BA of the ITAA 1936.

126. Accordingly, CGT event H2 does not happen on the Conversion of CPS 2 involving the allotment of additional Ordinary Shares.

Allotment of additional Ordinary Shares – Dividend

127. Subsection 6(1) of the ITAA 1936 defines a 'dividend' to include any distribution made by a company to any of its shareholders, whether in money or other property, and any amount credited by a company to any of its shareholders as shareholders.

128. Although the additional Ordinary Shares issued on Conversion of CPS 2 will constitute 'property' in the hands of the Holders, the allotment is not a disposition of property in the ordinary meaning of that expression (*Ord Forrest Pty Ltd v. FC of T* (1974) 130 CLR 124; 74 ATC 4034; (1974) 4 ATR 230, per Barwick CJ and McTiernan J). As there is no disposition there cannot be a distribution of property by ANZ.

129. The allotment of additional Ordinary Shares does not constitute a dividend under subsection 6BA(5) of the ITAA 1936 as the Terms of CPS 2 do not provide Holders with a choice of being paid a dividend or being issued shares.

130. Furthermore, no amount is credited to the Holders, nor is an amount paid out of profits.

131. Accordingly, the allotment of additional Ordinary Shares does not constitute a dividend within the meaning of subsection 6(1) of the ITAA 1936.

The value of additional Ordinary Shares – ordinary income

132. The allotment of additional Ordinary Shares will be a bonus issue within the meaning of paragraph 254A(1)(a) of the *Corporations Act 2001*, that is, an issue of shares for which consideration is not payable to ANZ. The issue of additional Ordinary Shares will result in a re-expression of the Holder's interest in the share capital of ANZ. Accordingly, the value of any additional Ordinary Shares issued on Conversion of CPS 2 will not be assessable as ordinary income under subsection 6-5(1) of the ITAA 1997 (*Commissioner of Taxation v. McNeil* (2007) 229 CLR 656; 2007 ATC 4223; (2007) 64 ATR 431).

Section 45

133. Section 45 of the ITAA 1936 applies where a company streams the provision of shares and the payment of minimally franked dividends to its shareholders in such a way that the shares are received by some shareholders and minimally franked dividends are received by other shareholders. Minimally franked dividends are dividends which are not franked or are franked to less than 10%.

134. ANZ has consistently paid fully franked dividends and has stated it will pay fully or substantially franked dividends to all its shareholders, including the Holders, to the extent of the franking credits available in its franking account. Furthermore, the Terms of CPS 2 do not allow ANZ to issue Ordinary Shares to all or some of the Holders in satisfaction of their Dividend entitlements in relation to CPS 2.

135. Therefore, section 45 of the ITAA 1936 will not apply to the additional Ordinary Shares acquired by the Holders on Conversion of CPS 2.

Section 45A

136. Section 45A of the ITAA 1936 applies in circumstances where capital benefits are streamed to certain shareholders who derive a greater benefit from the receipt of capital (the advantaged shareholders) and it is reasonable to assume that the other shareholders have received or will receive dividends (the disadvantaged shareholders).

137. The allotment of additional Ordinary Shares to the Holders is a provision of capital benefits pursuant to paragraph 45A(3)(a) of the ITAA 1936.

138. The allotment of additional Ordinary Shares is in effect a restatement of the Holders' interest in the capital of ANZ. In the absence of any other additional factors that would contribute to an alternative conclusion, the allotment of Ordinary Shares does not constitute the streaming of capital benefits.

139. Accordingly, it cannot be said that the Holders derive a greater benefit from capital benefits than other ANZ shareholders. Therefore, the allotment of additional Ordinary Shares does not trigger the application of section 45A of the ITAA 1936, and the Commissioner will not make a determination under subsection 45A(2) of the ITAA 1936 that the additional Ordinary Shares acquired on Conversion of CPS 2 will be an unfranked dividend in the hands of the Holders.

Section 45B

140. Section 45B of the ITAA 1936 applies where certain capital benefits are provided to shareholders in substitution for dividends.

141. The allotment of additional Ordinary Shares on Conversion of CPS 2 is a scheme under which a capital benefit is provided to the Holders (paragraph 45B(5)(a) of the ITAA 1936).

142. For the provision to apply paragraph 45B(2)(c) of the ITAA 1936 requires that, having regard to the relevant circumstances of the scheme, it would be concluded that the person, or one of the persons, entered into the scheme or carried out the scheme or any part of the scheme for a purpose, other than an incidental purpose, of enabling a taxpayer to obtain a tax benefit. The relevant circumstances of the scheme are listed in subsection 45B(8) of the ITAA 1936.

143. The allotment of additional Ordinary Shares is not in satisfaction of the Holders' entitlement to Dividends, but rather a product of the Conversion of CPS 2 held by the Holders according to the Terms. Consequently, each Holder's interest in the share capital of ANZ will not change when the capital benefit is provided. Furthermore, ANZ has paid, and has stated it will continue to pay, franked dividends to all its shareholders to the extent of the franking credits available.

144. Having regard to these relevant circumstances of the scheme as required by subsection 45B(8) of the ITAA 1936, it would not be concluded that any of the parties to the scheme entered into or carried out the scheme for a more than incidental purpose of enabling the Holders to obtain a tax benefit. Therefore, section 45B of the ITAA 1936 will not apply to treat the additional Ordinary Shares acquired on Conversion as an unfranked dividend in the hands of the Holders.

145. Accordingly the Commissioner will not make a determination under subsection 45B(3) of the ITAA 1936.

Cost base of the additional Ordinary Shares

146. Either section 6BA of the ITAA 1936 or Subdivision 130-A of the ITAA 1997 will apply to apportion the first element of the cost base and reduced cost base of CPS 2 over the Converted CPS 2 and any additional Ordinary Shares issued by ANZ.

147. Section 6BA of the ITAA 1936 applies if a shareholder holds shares in a company (the original shares) and the company issues other shares (the bonus shares) in respect of the original shares.

148. Pursuant to subsection 6BA(3) of the ITAA 1936, as the additional Ordinary Shares are issued to Holders for no consideration and are not a dividend or taken to be a dividend, the issue price of CPS 2 (being \$100 per CPS 2) will be apportioned over the Converted CPS 2 and any additional Ordinary Shares allotted.

149. Subdivision 130-A applies in a similar manner. It provides special rules relating to the time of acquisition and the cost base of bonus equities for CGT purposes.

150. Section 130-20 sets out what happens if an entity owns shares in a company (the original equities) and the company issues other shares (the bonus equities) in relation to the original equities.

151. Under item 1 of the table in subsection 130-20(3), as the additional Ordinary Shares are not a dividend nor taken to be a dividend, the first element of the cost base and reduced cost base of each CPS 2 are apportioned over both the Converted CPS 2 and any additional Ordinary Shares issued to the Holders by ANZ.

Acquisition time of additional Ordinary Shares

152. The Holders are taken to have acquired the additional Ordinary Shares at the time when the CPS 2 were originally acquired by the Holders, being 17 December 2009 (subsection 130-20(3)).

Appendix 2 – Detailed contents list

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Previous draft:

Not previously issued as a draft

Related Rulings/Determinations:

TR 94/30; TR 2006/10;
TD 2007/29

Subject references:

- acquisition dates
- capital gains tax
- CGT cost base
- conversion of securities
- dividend imputation
- dividend income
- dividend streaming arrangements
- franking tax offset
- preference shares
- qualified person

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Income Tax ~~ Capital Gains Tax ~~ CGT events H1 and H2 - special capital receipts
Income Tax ~~ Tax offsets, credits and benefits ~~ franking tax offset