



Class Ruling

Income tax: demerger of Members Equity Bank Pty Limited by Industry Super Holdings Pty Limited

Contents	Para
LEGALLY BINDING SECTION:	
What this Ruling is about	1
Date of effect	8
Scheme	9
Ruling	37
NOT LEGALLY BINDING SECTION:	
Appendix 1:	
Explanation	56
Appendix 2:	
Detailed contents list	71

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 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 45A of the ITAA 1936;
- section 45B of the ITAA 1936;
- section 45C of the ITAA 1936;
- section 104-135 of the *Income Tax Assessment Act 1997* (ITAA 1997);
- section 115-30 of the ITAA 1997; and
- Division 125 of the ITAA 1997.

All subsequent legislative references in this Ruling are to the ITAA 1936 unless otherwise indicated.

Class of entities

3. The class of entities to which this Ruling applies consists of all ordinary shareholders of Industry Super Holdings Pty Limited (ISH) who:

- (a) were listed on the share register of ISH as at 7pm (EST) on 30 June 2011 (Record Date);
- (b) were residents of Australia as defined in subsection 6(1) on the Record Date;
- (c) held their ISH shares on capital account on that date; and
- (d) were not subject to taxation of financial arrangement rules in Division 230 of the ITAA 1997 in relation to gains and losses on their ISH shares.

In this Ruling, a person belonging to this class of entities is referred to as an ISH shareholder.

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 36 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.

7. This work is copyright. Apart from any use as permitted under the *Copyright Act 1968*, no part may be reproduced by any process without prior written permission from the Commonwealth. Requests and inquiries concerning reproduction and rights should be addressed to:

Commonwealth Copyright Administration
Copyright and Classification Policy Branch
Attorney-General's Department
3-5 National Circuit
Barton ACT 2600

or posted at: <http://www.ag.gov.au/cca>

Date of effect

8. This Ruling applies from 1 July 2011 to 30 June 2012. The Ruling continues to apply after 30 June 2012 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.

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

Background

10. At a General Meeting on 8 April 2011, the ISH shareholders passed a resolution approving a reduction in ISH's share capital through an *in specie* distribution of the Members Equity Bank Pty Limited (MEB) shares to the ISH shareholders.

ISH shareholders

11. The shareholders of ISH are 33 industry complying superannuation funds who are all residents of Australia within the meaning of that term in subsection 6(1).

ISH

12. ISH is an Australian resident company and is the head company of a tax consolidated group of companies (ISH Group) for the purposes of Part 3-90 of the ITAA 1997.

13. On 1 January 2007, the ISH group was formed when the assets of the Industry Funds Banking Trust (IFBT) (a subsidiary MEB) was rolled into ISH and the unit holders in IFBT acquired shares in ISH. Roll-over relief was elected under Subdivision 124-N of the ITAA 1997.

14. ISH is a financial services institution. Before the demerger it had operations in:

- (a) banking via MEB and its subsidiaries;

- (b) funds management via IFM Holdings Pty Ltd (IFM) and its subsidiaries; and
- (c) funds services via Industry Funds Services Pty Ltd (IFS) and its subsidiaries.

15. Immediately before the demerger, the total issued share capital of ISH was \$831,284,433 as follows:

- \$160,002 of share capital representing the value of ISH prior to the acquisition of MEB;
- \$536,000,000 of share capital issued on 1 January 2007 (in relation to the acquisition of MEB);
- \$57,000,000 of share capital issued on 2 January 2007 (in relation to the acquisition of IFS); and
- \$238,124,431 of share capital issued after 2 January 2007 to date.

16. All of the capital raised after 2 January 2007 was contributed to MEB.

17. There were no employee shares on issue just before the demerger.

18. There were no other ownership interests in ISH just before the demerger.

MEB

19. MEB is an Australian resident company and immediately prior to the demerger was a wholly-owned subsidiary of ISH and a member of the ISH group.

20. MEB is an authorised deposit-taking institution (ADI) for the purposes of the *Banking Act 1959*. As a result of its ADI status, MEB is subject to regulatory compliance requirements as administered by the Australian Prudential Regulation Authority (APRA).

21. Immediately before the demerger, the issued share capital of MEB was \$430,098,616.

22. There were no other ownership interests in MEB just before the demerger.

The demerger of MEB

23. ISH consolidated all of its partly paid shares on a 2 for 1 basis, with the holding of partly paid shares of any individual member rounded up to the nearest whole number of shares on 29 June 2011.

24. On the Demerger Date, 1 July 2011, ISH distributed 100% of the shares it owned in MEB to the ISH shareholders such that for every 128.1467 ISH shares held, each ISH shareholder received 1 share in MEB.

25. As a result of the demerger, the ISH shareholders hold separate ownership interests in ISH and MEB.

26. The market value of the MEB shares was \$636,800,000, based on the independent market valuation of MEB as at 30 June 2011.

Accounting for the demerger

27. ISH accounted for the demerger as follows:

DR Share capital – fair value at 30 June 2011	\$636,800,000
CR Investment in MEB	\$636,800,000
DR Share capital	\$137,324,431
CR Equity reserve	\$137,324,431

28. The capital reduction amount reflects the share capital of ISH that was applied to the MEB investment.

Reasons for the demerger

29. ISH expected that a number of advantages would accrue to its shareholders as a result of the demerger of MEB, including:

- (a) the separation of businesses with fundamentally different characteristics, allowing ISH and MEB to focus on their respective core competencies, growth objectives and strategies;
- (b) giving legal effect to the separation of the business units within ISH. Each of the three business units within ISH had different management teams and individual Boards of Directors for a number of years prior to the demerger;
- (c) achieving compliance cost savings in terms of audit, statutory reporting etc;
- (d) improving the investment choice for ISH shareholders who have the choice to hold either or both ISH and MEB shares;
- (e) greater strategic freedom for MEB, including the ability to pursue growth opportunities without competing for capital with other ISH businesses;
- (f) releasing ISH from regulatory obligations imposed by APRA, subject to APRA approving revocation of its status as a non-operating holding company; and
- (g) allowing ISH to pursue alternative capital structures, including greater flexibility with debt and equity funding.

Other matters

30. None of the ISH shareholders acquired their shares in ISH before 20 September 1985.
31. ISH confirmed that capital gains tax (CGT) assets representing more than 50% of the market value of all CGT assets of MEB and its subsidiaries would be used directly or indirectly in a business carried on by MEB or its subsidiaries just after the demerger.
32. ISH confirmed that its share capital account was not tainted within the meaning of Division 197 of the ITAA 1997 as at the Record Date.
33. No transactions in relation to the shares in MEB were contemplated to occur after the demerger.
34. No other consideration (other than the MEB shares) was paid to ISH shareholders on the demerger of MEB.
35. ISH has never paid a dividend to its shareholders.
36. ISH confirmed it did not make an election under subsection 44(2).

Ruling

The demerger of MEB

CGT event G1

37. CGT event G1 happened in relation to each of the ISH ordinary shares owned by ISH shareholders at the time ISH made the payment of the capital reduction amount in the form of the MEB shares (section 104-135 of the ITAA 1997).

Capital gain

38. An ISH shareholder made a capital gain when CGT event G1 happened if the market value of the proportion of the capital reduction amount received for each ISH share exceeded the cost base of that share. The amount of the capital gain is equal to this excess (subsection 104-135(3) of the ITAA 1997). No capital loss can be made when CGT event G1 happens.
39. If an ISH shareholder acquired their shares at least 12 months before the payment of the capital reduction amount, any capital gain made when CGT event G1 happened may qualify as a discount capital gain under subsection 115-25(1) of the ITAA 1997 (provided the other conditions in Subdivision 115-A of the ITAA 1997 are satisfied).

Demerger roll-over

40. ISH and MEB were part of a demerger group as described in subsection 125-65(1) of the ITAA 1997.

41. A demerger, as described under section 125-70 of the ITAA 1997 happened to this demerger group under the scheme.

42. ISH shareholders are eligible to choose demerger roll-over relief under subsection 125-55(1) of the ITAA 1997.

CGT consequences of choosing demerger roll-over

43. ISH shareholders who choose demerger roll-over relief can disregard any capital gains made when CGT event G1 happened to their ISH shares under the demerger (subsection 125-80(1) of the ITAA 1997).

Other CGT consequences of choosing demerger roll-over

44. An ISH shareholder who chooses demerger roll-over relief must recalculate the cost base and reduced cost base of their ISH and MEB shares.

45. The first element of the cost base and reduced cost base of each ISH share and corresponding MEB share received under the demerger is worked out as follows:

- total the cost bases of the ISH shares (just before the demerger); and
- apportion that sum over the ISH shares and corresponding new MEB shares received under the demerger.

46. The apportionment of this sum is done on a reasonable basis having regard to the market values (just before the demerger) of the ISH shares and MEB shares, or a reasonable approximation of those market values (subsections 125-80(2) and 125-80(3) of the ITAA 1997).

ISH shareholders who do not choose demerger roll-over

47. ISH shareholders who do not choose demerger roll-over relief:

- are not entitled to disregard any capital gain made when CGT event G1 happened to their ISH shares; and
- the first element of the cost base and reduced cost base of each ISH share and the corresponding MEB share is calculated in the same manner as if they had chosen demerger roll-over relief (see paragraph 45 of this Ruling) (subsections 125-85(1) and 125-85(2) of the ITAA 1997).

Acquisition date of the MEB shares

48. For the purpose of determining eligibility for a discount capital gain, a MEB share received by an ISH shareholder will be taken to have been acquired on the date the shareholder acquired, for CGT purposes, the corresponding ISH share (item 2 in the table in subsection 115-30(1) of the ITAA 1997). This will be the case whether or not the shareholder chooses demerger roll-over relief.

49. For the ISH shares that were subject to roll-over under Subdivision 124-N of the ITAA 1997 at the time the ISH group was formed, the acquisition date should be the date of acquisition of the ISH shareholders' original units in the Industry Funds Banking Trust.

50. For all other ISH shares, the acquisition date should be the date on which each respective ISH share was acquired by an ISH shareholder.

Dividend consequences

51. As the share capital reduction amount was debited to ISH's share capital account, it is not a dividend as defined in subsection 6(1).

52. No demerger dividend arose under the demerger.

Application of sections 45A, 45BA, 45B and 45C

53. The Commissioner will not make a determination under subsection 45A(2) in respect of the demerger.

54. The Commissioner will not make a determination under paragraph 45B(3)(a) that section 45BA applies to the whole or any part of the demerger benefit provided to an ISH shareholder under the demerger.

55. The Commissioner will not make a determination under paragraph 45B(3)(b) that section 45C applies to the whole or any part of the capital benefit provided to an ISH shareholder under the demerger.

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 demerger of MEB

56. A significant tax consequence of the scheme is the availability of demerger roll-over under Division 125 of the ITAA 1997. Broadly, ISH shareholders can choose roll-over relief to disregard a capital gain made under the demerger. There are special rules for calculating the cost base and reduced cost base of the ISH and MEB shares for ISH shareholders, whether or not they choose roll-over.

57. Subsection 125-55(1) of the ITAA 1997 provides that roll-over can be chosen if, at the time of the scheme:

- (a) a person owns a share in a company;
- (b) the company is the head entity of a demerger group;
- (c) a demerger happens to the demerger group; and
- (d) under the demerger, a CGT event happens to the original interest and a new or replacement interest is acquired in the demerged entity and nothing else.

58. Under the scheme, the conditions for choosing demerger roll-over under Division 125 of the ITAA 1997 were satisfied in respect of the demerger of MEB. Consequently, demerger roll-over relief in Division 125 is available to the ISH shareholders in respect of the demerger of MEB. The Ruling section provides a detailed explanation of the Commissioner's decision. Therefore, no further explanation is warranted.

Demerger dividend

59. Subsection 44(1) includes in a shareholder's assessable income any dividends, as defined in subsection 6(1), paid to shareholders out of profits derived by the company from any source if the shareholder is a resident of Australia.

60. Paragraph (d) of the definition of dividend in subsection 6(1) provides that a dividend excludes amounts debited against an amount standing to the credit of the share capital account of the company.

61. The term 'share capital account' is defined in section 975-300 of the ITAA 1997 as an account which the company keeps of its share capital, or any other account created on or after 1 July 1998, where the first amount credited to the account was an amount of share capital.

62. Subsection 975-300(3) of the ITAA 1997 states that an account is not a share capital account if it is tainted.

63. The *in specie* distribution of the MEB shares to ISH shareholders was recorded as a debit to ISH's share capital account. As the share capital account of ISH was not tainted within the meaning of Division 197 of the ITAA 1997, paragraph (d) of the definition of dividend in subsection 6(1) of the ITAA 1936 applies. Accordingly, the *in specie* distribution to ISH shareholders of MEB shares is not a dividend as defined in subsection 6(1) of the ITAA 1936.

The application of sections 45A, 45BA, 45B and 45C

Section 45A

64. Section 45A is an anti-avoidance provision that applies 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 (the disadvantaged shareholders) have received or will receive dividends.

65. Where the Commissioner makes a written determination under subsection 45A(2) that section 45C applies in relation to the whole or part of the capital benefits, the capital benefits will be treated as unfranked dividends paid out of the company's profits.

66. Although ISH provided its shareholders with a 'capital benefit' as defined in paragraph 45A(3)(b) in the form of MEB shares, the capital benefit was provided to all ISH shareholders in the same proportion as their shareholdings in ISH. Consequently, there are no advantaged or disadvantaged shareholders as contemplated by subsection 45A(1).

Section 45B

67. Section 45B is an anti-avoidance provision that applies to ensure that relevant amounts are treated as dividends for taxation purposes if:

- components of a demerger allocation as between capital and profit do not reflect the circumstances of the demerger; or
- certain payments, allocations and distributions are made in substitution for dividends (subsection 45B(1)).

68. Where the requirements of subsection 45B(2) are met, subsection 45B(3) empowers the Commissioner to make a determination that either section 45BA applies in relation to a demerger benefit or section 45C applies in relation to a capital benefit.

69. While the conditions of paragraphs 45B(2)(a) and 45B(2)(b) are met, the requisite purpose of enabling the ISH shareholders to obtain a tax benefit (by way of a demerger benefit or a capital benefit) is not present.

70. Accordingly, the Commissioner will not make a determination under paragraphs 45B(3)(a) or (b) that either sections 45BA or 45C apply to the scheme to which this Ruling relates.

Appendix 2 – Detailed contents list

71. The following is a detailed contents list for this Ruling:

	Paragraph
What this Ruling is about	1
Relevant provision(s)	2
Class of entities	3
Qualifications	4
Date of effect	8
Scheme	9
Background	10
<i>ISH shareholders</i>	11
<i>ISH</i>	12
<i>MEB</i>	19
The demerger of MEB	23
Accounting for the demerger	27
Reasons for the demerger	29
Other matters	30
Ruling	37
The demerger of MEB	37
<i>CGT event G1</i>	37
<i>Capital gain</i>	38
<i>Demerger roll-over</i>	40
<i>CGT consequences of choosing demerger roll-over</i>	43
<i>Other consequences of choosing demerger roll-over</i>	44
ISH shareholders who do not choose demerger roll-over	47
Acquisition date of MEB shares	48
Dividend consequences	51
Application of sections 45A, 45BA, 45B, 45C	53
Appendix 1 – Explanation	56
The demerger of MEB	56
Demerger dividend	59
The application of sections 45A, 45BA, 45B, 45C	64
<i>Section 45A</i>	64
<i>Section 45B</i>	67
Appendix 2 – Detailed contents list	71

References

Previous draft:

Not previously issued as a draft

Related Rulings/Determinations:

TR 2006/10

Subject references:

- capital gains tax
- capital benefit
- capital gains
- capital reductions
- CGT capital proceeds
- CGT events G1-G3 - shares
- cost base adjustments
- demerger
- demerger roll-over
- return of capital on shares

Legislative references:

- ITAA 1936
 - ITAA 1936 6(1)
 - ITAA 1936 44
 - ITAA 1936 44(1)
 - ITAA 1936 44(2)
 - ITAA 1936 45A
 - ITAA 1936 45A(1)
 - ITAA 1936 45A(2)
 - ITAA 1936 45A(3)(b)
 - ITAA 1936 45B
 - ITAA 1936 45B(1)
 - ITAA 1936 45B(2)
 - ITAA 1936 45B(2)(a)
 - ITAA 1936 45B(2)(b)
 - ITAA 1936 45B(3)
 - ITAA 1936 45B(3)(a)
 - ITAA 1936 45B(3)(b)
 - ITAA 1936 45BA
 - ITAA 1936 45C
 - ITAA 1997
 - ITAA 1997 104-135
 - ITAA 1997 104-135(3)
 - ITAA 1997 Subdiv 115-A
 - ITAA 1997 115-25(1)
 - ITAA 1997 115-30
 - ITAA 1997 115-30(1)
 - ITAA 1997 Subdiv 124-N
 - ITAA 1997 Div 125
 - ITAA 1997 125-55(1)
 - ITAA 1997 125-65(1)
 - ITAA 1997 125-70
 - ITAA 1997 125-80(1)
 - ITAA 1997 125-80(2)
 - ITAA 1997 125-80(3)
 - ITAA 1997 125-85(1)
 - ITAA 1997 125-85(2)
 - ITAA 1997 Div 197
 - ITAA 1997 Div 230
 - ITAA 1997 Pt 3-90
 - ITAA 1997 975-300
 - ITAA 1997 975-300(3)
 - TAA 1953
 - Banking Act 1959
 - Copyright Act 1968
-

ATO references:

NO: 1-2X65S1V

ISSN: 1445-2014

ATOlaw topic: Income Tax ~~ Capital Gains Tax ~~ demerger relief
 Income Tax ~~ Capital Gains Tax ~~ CGT event G1
 Income Tax ~~ Capital Gains Tax ~~ roll-overs – other