



Class Ruling

Income tax: Australia and New Zealand Banking Group Limited – allotment of convertible preference shares (CPS3)

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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;
- 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; and
- section 207-145 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 subscribers for Convertible Preference Shares (CPS3) in Australia and New Zealand Banking Group Limited (ANZ) who hold those CPS3 on capital account and are Australian residents (within the meaning of subsection 995-1(1)) (referred to in this Ruling as Holders).

4. The class of entities to which this Ruling applies does not extend to the holders of CPS3 who did not acquire their interest by initial subscription.

5. This Ruling does not apply to Holders for whom gains and losses from the CPS3 are subject to the taxation of financial arrangements rules in Division 230.

(Note – Division 230 will generally not apply to the financial arrangements of individuals, unless they have made an election for those rules to apply to them.)

6. This Ruling does not consider the tax implications of the Exchange of CPS3 by Conversion or Redemption in accordance with clauses 5 and 6 of the ANZ CPS3 Terms (Terms).

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

Qualifications

8. 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 12 to 52 of this Ruling.

9. 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

11. This Ruling applies from 28 September 2011 to 30 June 2020. The Ruling continues to apply after 30 June 2020 to all entities within the specified class who entered into the specified scheme at the time of the initial subscription for the CPS3. 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

12. The following description of the scheme is based on information provided by ANZ. 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 10 June 2011;
- Prospectus dated 31 August 2011 for the issue of CPS3 by ANZ (Prospectus);
- ANZ CPS3 Terms as contained in Appendix A of the Prospectus; and
- further correspondence provided by ANZ.

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

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

14. 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.

15. ANZ has applied for CPS3 to be quoted on the Australian Securities Exchange (ASX) and the CPS3 are expected to trade under ASX code 'ANZPC'.

16. In the Prospectus, ANZ announced its intention to undertake a capital raising by the issue of 12.5 million CPS3 to raise \$1.25 billion, with the ability to raise more or less (the Offer).

17. The capital raised from the issue of CPS3 will be used for ANZ's general corporate purposes and the offer of CPS3 is part of ANZ's continuing capital management strategy within the guidelines prescribed by the Australian Prudential Regulation Authority (APRA).

18. The classes of Applicants who can apply for CPS3, and the corresponding process for lodging applications, as described in the Prospectus, are:

- ANZ Securityholder Applicant – a holder of Ordinary Shares or a holder of CPS 1 or CPS 2, shown on the register at 7:00pm on 3 August 2011, with an address in Australia, applying through the ANZ Securityholder 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 invited to participate through the Broker Firm Offer; and
- Institutional Investor – an investor who was invited by ANZ Securities to bid for CPS3 in the Bookbuild and who is not a Broker Firm Applicant, ANZ Securityholder Applicant or General Applicant and who is applying through the Institutional Offer.

19. The Prospectus states that no action has been taken to register or qualify CPS3 or the Offer, or to otherwise permit a public offering of CPS3 outside Australia. However, CPS3 may be offered in a jurisdiction outside Australia under the Institutional Offer or Broker Firm Offer where such offer is made in accordance with the laws of that jurisdiction.

Main features of CPS3

20. A CPS3 is a fully paid mandatorily convertible preference share in the capital of ANZ.
21. The issue price of each CPS3 is \$100 (Issue Price), and on issue is fully paid.
22. A CPS3 holder does not have voting rights, except in the limited circumstances described in the Terms.

Dividend calculation

23. Subject to the conditions outlined at paragraph 26 of this Ruling, the holder of each CPS3 is entitled to receive on the relevant Dividend Payment Date, a dividend (Dividend) payable in arrears in respect of each CPS3 held, 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 180 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 180 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 180 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 (expressed as a percentage per annum) means the margin 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.

24. The Dividend Payment Dates are each 1 March and 1 September, commencing on 1 March 2012 until (but not including) the date on which Redemption or Conversion occurs. A Dividend will also be paid on the date on which a Conversion or Redemption occurs in accordance with the Terms.

25. 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 100%, as determined by the formula in clause 3.2 of the Terms.

Dividend payment conditions

26. Each 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 approves in writing;
- the payment of the Dividend not resulting in ANZ becoming, or being likely to become, insolvent for the purposes of the *Corporations Act 2001* (Corporations Act); and
- APRA not otherwise objecting to the payment of the Dividend.

27. A Dividend is only payable to those persons registered as the holders on the Record Date for that Dividend.

28. Dividends are non-cumulative and the holders of CPS3 will have no recourse in the event of non-payment arising because a resolution to pay a Dividend has not been made, an APRA Condition exists at the relevant Dividend Payment Date, or because of any applicable law. Non-payment of all, or part, of a Dividend does not constitute an event of default by ANZ, and the holders of CPS3 have no claim in respect of non-payment.

29. No interest accrues on any unpaid Dividends and the holders of CPS3 have no claim or entitlement in respect of interest on any unpaid Dividends.

Restrictions in the case of non-payment of Dividends

30. If for any reason a Dividend has not been paid in full on a Dividend Payment Date (the Relevant Dividend Payment Date), ANZ must not without approval of a Special Resolution, until and including the next Dividend Payment Date:

- declare or pay a dividend, or make any distribution on any Ordinary Shares; or
- buy-back or reduce capital on any Ordinary Shares,
- unless the Dividend is paid in full within 3 Business Days of the Relevant Dividend Payment Date.

Mandatory Conversion

31. Subject to a Common Equity Capital Trigger Event, ANZ must Convert all CPS3 on issue into Ordinary Shares on the Mandatory Conversion Date.

32. The Scheduled Mandatory Conversion Date is 1 September 2019, but Conversion will not occur unless conditions (Mandatory Conversion Conditions) are satisfied. If any of those conditions are not satisfied on 1 September 2019, the CPS3 will Convert on the first Dividend Payment Date after 1 September 2019 on which the Mandatory Conversion Conditions are satisfied.

33. The Mandatory Conversion Conditions for each Relevant Date (being the relevant Mandatory Conversion Date) 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 that Mandatory Conversion Date and including that Mandatory Conversion Date.

Common Equity Capital Conversion

34. 'Common Equity Capital Conversion' means the mandatory conversion of CPS3 to Ordinary Shares on the Common Equity Capital Conversion Date in accordance with clause 4.6 of the Terms on the occurrence of a Common Equity Capital Trigger Event.
35. A Common Equity Capital Trigger Event occurs when:
- (a) ANZ's Common Equity Capital Ratio, as reported in its most recent Relevant Disclosure, is equal to, or less than, 5.125%; or
 - (b) ANZ determines, or APRA has notified ANZ in writing that it believes, that ANZ's Common Equity Capital Ratio is equal to, or less than, 5.125%.

Optional Exchange

36. ANZ may elect to Exchange at their discretion (holders of CPS3 do not have a right to request an Exchange):
- (a) all, or some, CPS3 on an Exchange Date following the occurrence of a Tax Event or a Regulatory Event;
 - (b) all (but not some) CPS3 on the Exchange Date after the occurrence of an Acquisition Event; or
 - (c) all, or some, CPS3 on an Optional Exchange Date.
37. If ANZ elects to Exchange CPS3, it must elect which of the following (or which combination of the following) it intends to do in respect of CPS3:
- subject to APRA's prior written approval, Convert the CPS3 into Ordinary Shares in accordance with clause 7 of the Terms; or
 - subject to APRA's prior written approval, Redeem CPS3 in accordance with clause 8 of the Terms.
38. Redemption or Conversion of CPS3 on Optional Exchange is subject to, and in accordance with, the Terms.

Conversion

39. 'Conversion' is defined as the taking effect of the rights specified in clause 7 of the Terms.

40. Upon Conversion, each CPS3 converts into one Ordinary Share through a variation of the rights attaching to each CPS3 on the Mandatory Conversion Date, the Exchange Date, Common Equity Capital Conversion Date or the Change of Control Exchange Date (as the case may be).

41. Each holder of CPS3 will also be allotted, for no consideration, additional number of Ordinary Shares for each CPS3 that is Converted. The additional number of Ordinary Shares allotted to the holders of CPS3 will be equal to one less than the Conversion Number, where the Conversion Number (subject to the Conversion Number being no more than the Maximum Conversion Number) is a number calculated according to the formula provided in clause 7.1(b) of the Terms.

42. The Maximum Conversion Number is fixed and ascertainable from the date of issue of the CPS3 (although it may be adjusted for certain subsequent events).

43. The total market value of the Ordinary Shares held by a holder of CPS3 immediately after the Conversion of a CPS3 (and as a result of such Conversion) is expected to approximate the Issue Price. However, this may not be the case if Conversion occurs because of a Common Equity Capital Trigger Event and the Maximum Conversion Number applies.

44. Conversion does not constitute redemption, buy-back, cancellation or termination of CPS3, nor does it constitute an issue, allotment or creation of a new Ordinary Share (other than any additional Ordinary Shares allotted).

Redemption

45. ANZ may (subject to APRA giving its prior written approval) Redeem CPS3 in accordance with the Terms.

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

47. CPS3 will be Redeemed by payment on the Exchange Date or the Change of Control Exchange Date (as the case may be) of the Issue Price plus any amount payable under clause 8.3(a)(iii) of the Terms (Redemption Price) by way of the redemption, buy-back, reduction of capital or any combination thereof.

48. On the Exchange Date or the Change of Control Exchange Date, the only right the holders of CPS3 will have in respect of CPS3 will be to obtain the Redemption Price payable in accordance with the Terms and, upon the payment of the Redemption Price all other rights conferred or restrictions imposed by CPS3 will no longer have effect.

Interposition of Approved NOHC

49. Clause 12.1 of the Terms provides for an Approved non-operating holding company (NOHC) Event.

50. A 'NOHC Event' means an event which:

- (a) is initiated by the Directors, acting as a board; and
- (b) would otherwise be an Acquisition Event,

but the result of which would be that an ultimate holding company of ANZ would be a NOHC.

51. If an Approved NOHC Event occurs, ANZ may give notice to the holders of CPS3 specifying the amendments to the Terms to effect the substitution of the Approved NOHC as the issuer of ordinary shares to holders on Conversion.

Other matters

52. 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 CPS3;
- (c) CPS3 are equity interests in ANZ pursuant to Division 974;
- (d) Dividends on CPS3 will be frankable distributions pursuant to section 202-40;
- (e) ANZ will frank the Dividends paid on CPS3 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 the issue of CPS3 or the allotment of additional Ordinary Shares on Conversion of CPS3;
- (g) the additional Ordinary Shares issued in the event of Conversion of CPS3 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) CPS3 are expected to be treated as a liability for Australian International Financial Reporting Standards 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 CPS3) in relation to their CPS3 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 in receipt of Dividends on CPS3 will have held their CPS3 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 CPS3), within the period beginning on the day after the day on which the Holder acquired CPS3 and ending on the 90th day after the day on which CPS3 become ex-dividend;
- (l) Dividends on CPS3 will be paid out of the retained profits of ANZ;
- (m) 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 CPS3; and
- (n) on the date of Conversion of CPS3 into Ordinary Shares, the rights and obligations attached to those Ordinary Shares are the same as those contained in the Constitution of ANZ.

Ruling

Acquisition time of CPS3

53. Under item 2 in the table in section 109-10, the Holders will acquire CPS3 on 28 September 2011, being the date CPS3 are issued to the Holders.

CPS3 cost base and reduced cost base

54. Under subsections 110-25(2) and 110-55(2), the first element of the cost base and reduced cost base of each CPS3 is \$100.

Inclusion of Dividends in assessable income

55. The Holders must include in their assessable income all Dividends received in respect of their CPS3 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, unless the Holder is an entity whose ordinary or statutory income is exempt income.

Entitlement to a tax offset

56. 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 57 of this Ruling).

57. 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).

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).

Imputation benefits

59. 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 CPS3.

Section 177EA

60. 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 CPS3.

Gross-up and tax offset rules

61. 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.

Conversion of each CPS3 and allotment of additional Ordinary Shares – CGT implications

62. The Conversion of each CPS3 into Ordinary Shares and the allotment of additional Ordinary Shares will not result in a CGT event occurring.

63. CGT event H2 in section 104-155 will not happen on the Conversion of each CPS3 involving the allotment of additional Ordinary Shares as a cost base adjustment will be made to the Converted CPS3 because of the allotment of the additional Ordinary Shares. No other CGT event in Division 104 will happen on the Conversion of CPS3 involving the allotment of additional Ordinary Shares.

Cost base of the additional Ordinary Shares

64. 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 CPS3 over the Converted CPS3 and any additional Ordinary Shares allotted by ANZ.

Acquisition time of additional Ordinary Shares

65. Under subsection 130-20(3), the additional Ordinary Shares are taken to be acquired at the time CPS3 were originally acquired by the Holders, being 28 September 2011.

Allotment of additional Ordinary Shares – Dividend

66. The allotment of any additional Ordinary Shares on Conversion of CPS3 will not be assessable as dividend income in the hands of the Holders.

The value of additional Ordinary Shares – ordinary income

67. The value of any additional Ordinary Shares issued on Conversion of CPS3 will not be assessable as ordinary income in the hands of the Holders under subsection 6-5(1).

Conversion of each CPS3 and allotment of ordinary shares in an Approved NOHC – CGT implications

68. Where a NOHC is interposed as the ultimate holding company of ANZ, the Conversion of each CPS3 and the allotment of NOHC ordinary shares to Holders will result in CGT event C2 happening.

69. However, no Holder will make a capital gain or capital loss as the capital gain or capital loss is disregarded under subsection 130-60(3).

70. The amendment to the Terms to effect the substitution of an Approved NOHC as the issuer of ordinary shares to Holders on Conversion of the CPS3 will result in CGT event H2 happening.

71. However, no Holder will make a capital gain or capital loss as a result of CGT event H2 happening as there are no capital proceeds because of the amendments to the CPS3 Terms.

Section 45

72. Section 45 of the ITAA 1936 will not apply to treat the additional Ordinary Shares acquired on Conversion of CPS3 as an unfranked dividend paid by ANZ.

Section 45A

73. The Commissioner will not make a determination, under subsection 45A(2) of the ITAA 1936, that the additional Ordinary Shares acquired on Conversion of CPS3 will be an unfranked dividend in the hands of the Holders.

Section 45B

74. The Commissioner will not make a determination, under subsection 45B(3) of the ITAA 1936, that the additional Ordinary Shares acquired on Conversion of CPS3 will be an unfranked dividend in the hands of the Holders.

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 CPS3

75. 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).

76. CPS3 will be issued on 28 September 2011. Therefore, under item 2 in the table in section 109-10, CPS3 are acquired on 28 September 2011.

CPS3 cost base and reduced cost base

77. 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 the CGT asset (paragraph 110-25(2)(a) and subsection 110-55(2)).

78. The Issue Price of each CPS3 is \$100. Accordingly, when CPS3 are issued, the first element of the cost base and reduced cost base of each CPS3 is \$100.

Inclusion of dividends in assessable income

79. 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.

80. Dividends paid in respect of CPS3 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.

81. Dividends paid in respect of CPS3 are expected to be fully or substantially franked.

82. 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.

83. 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 that has been included in their assessable income.

Franking credit subject to the refundable tax offset rules

84. 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.

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

86. 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).

Exempt income or non-assessable non-exempt income

87. 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.

Imputation benefits – streaming of imputation benefits

88. 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.

89. 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)).

90. '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).

91. 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 CPS3.

92. The additional Ordinary Shares allotted on Conversion of CPS3 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.

93. 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.

Section 177EA

94. 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.

95. 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:
 - a frankable distribution has been paid, or is payable or expected to be payable, to a person in respect of the membership interests; or
 - 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.

96. The Commissioner considers that the conditions in paragraphs 177EA(3)(a) to 177EA(3)(d) of the ITAA 1936 are satisfied.

97. 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.

98. 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.

99. 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.

100. ANZ advised that it will issue CPS3 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 and relevant circumstances 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.

101. 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 other 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.

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

Gross-up and tax offset rules

103. 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.

104. 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));
- 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)).

105. 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).

106. The holding period rule applies where neither the taxpayer nor 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).

107. 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).

108. The Holders will be qualified persons, provided that:

- the Holders will have held their CPS3 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 CPS3 and ending on the 90th day after the day on which CPS3 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 CPS3 (former paragraph 160APHO(1)(a) and former section 160APHN of the ITAA 1936).

109. 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.

110. 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 59 and 60 of this Ruling).

111. 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.

112. The Transaction Documents provide no indication that the offering of CPS3 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.

Conversion of each CPS3 and allotment of additional Ordinary Shares – CGT implications

113. Under the transaction, each CPS3 will convert into one Ordinary Share through a variation of the rights attaching to each CPS3. The Holders will also receive an allotment of additional Ordinary Shares in ANZ.

114. 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).

115. 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)).

116. The mere variation of rights attaching to CPS3 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).

117. Further, the Conversion of CPS3 to Ordinary Shares by the variation of the rights attaching to CPS3 does not involve CPS3 being converted into equity interests under paragraph 104-25(1)(f).

118. The relinquishment by the Holders of some of the rights attaching to CPS3 is not a CGT event that happens to part of the CGT asset comprised by each CPS3 under section 112-30 (paragraph 40 of TR 94/30).

119. As CGT event C2 will not occur on Conversion of CPS3 into Ordinary Shares, Subdivision 130-C will have no application.

120. Although CGT event C2 does not happen because of the variation of the rights attaching to CPS3, 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).

121. 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.

122. The Conversion of CPS3 involving the allotment of additional Ordinary Shares will result in an adjustment to the cost base and reduced cost base of the Converted CPS3 under Subdivision 130-A of the ITAA 1997 or section 6BA of the ITAA 1936.

123. Accordingly, CGT event H2 does not happen on the Conversion of CPS3 involving the allotment of additional Ordinary Shares.

Cost base of the additional Ordinary Shares

124. 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 the CPS3 over the Converted CPS3 and any additional Ordinary Shares issued by ANZ.

125. 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.

126. 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 the CPS3 will be apportioned over the Converted CPS3 and any additional Ordinary Shares allotted.

127. 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.

128. 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.

129. 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 CPS3 are apportioned over both the Converted CPS3 and any additional Ordinary Shares issued to the Holders by ANZ.

Acquisition time of additional Ordinary Shares

130. The Holders are taken to have acquired the additional Ordinary Shares at the time when the CPS3 were originally acquired by the Holders, being 28 September 2011 (subsection 130-20(3)).

Allotment of additional Ordinary Shares – Dividend

131. 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.

132. Although the additional Ordinary Shares issued on Conversion of CPS3 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.

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

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

135. 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

136. The allotment of additional Ordinary Shares will be a bonus issue within the meaning of paragraph 254A(1)(a) of the Corporations Act, 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 CPS3 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).

Conversion of each CPS3 and allotment of ordinary shares in an Approved NOHC – CGT implications

137. Under section 104-25, CGT event C2 happens if, among other things, the ownership of an intangible asset that is a convertible interest ends by the conversion of the asset into another asset (paragraph 104-25(1)(f)).

138. However, Subdivision 130-C applies to the acquisition of shares by the conversion of a convertible interest. In order for this Subdivision to apply to the Conversion of the CPS3, the CPS3 must be a convertible interest. If the CPS3 is a convertible interest any capital gain or capital loss made under CGT event C2 happening in respect to the Conversion of the CPS3 is disregarded.

139. A convertible interest in a company is defined in section 995-1 as an interest of the kind referred to in item 4 of the table in subsection 974-75(1). Paragraph (b) of that item describes an interest that will or may convert into an equity interest in the company or a connected entity of the company.

140. The term 'an interest that will or may convert into another interest' is defined in section 974-165. It includes the circumstances where a first interest must be, or may be, satisfied by the issue of the second interest (subparagraph 974-165(b)(i)).

141. The Terms provide for the possibility of an Approved NOHC to be interposed as the ultimate owner of ANZ. If this occurs, ANZ may amend the Terms and provide notice to Holders that upon Conversion, shares in the Approved NOHC may be allotted to the Holders instead of ANZ Ordinary Shares.

142. The term 'connected entity' is defined in section 995-1 of the ITAA 1997 and includes an 'associate' of the entity being tested. 'Associate' is widely defined in section 995-1 of the ITAA 1997 and section 318 of the ITAA 1936. As the Approved NOHC will be the parent company of ANZ at the time of the Conversion the Approved NOHC will be an associate, and thus a connected entity of ANZ.

143. Accordingly, upon Conversion, Holders will disregard any capital gain or loss arising from that Conversion pursuant to subsection 130-60(3).

Cost base of the Approved NOHC Ordinary Shares

144. Pursuant to item 2 of the table in subsection 130-60(1), the first element of the cost base and the reduced cost base of each Approved NOHC Ordinary Share allocated to a Holder will be their cost base in the CPS3 at the time of Conversion divided by the number of Approved NOHC Ordinary Shares they receive for each CPS3.

Acquisition time of the Approved NOHC Ordinary Shares

145. Under subsection 130-60(2), the Approved NOHC Ordinary Shares are taken to be acquired at the time of the Conversion of the CPS3. This means that the 12 month holding period for the purposes of the CGT discount, as regards the Approved NOHC Ordinary Shares, will run from the acquisition date of the Approved NOHC Ordinary Shares and not from the acquisition of the CPS3.

Approved NOHC Interposition

146. The interposition of a NOHC between ANZ and its shareholders will not result in a CGT event for Holders for CGT purposes.

147. Subsection 104-155(1) provides that CGT event H2 happens if an act, transaction or event occurs in relation to a CGT asset that you own and the act, transaction or event does not result in an adjustment being made to the asset's cost base or reduced cost base.

148. The Terms provide that ANZ may amend the Terms where necessary and appropriate to effect the substitution of an Approved NOHC as the issuer of ordinary shares on Conversion.

149. The amendment to the Terms to effect the substitution of an Approved NOHC as the issuer of ordinary shares on Conversion results in a CGT event H2 happening for Holders. The amendment to the Terms is an act, transaction or event in relation to the CPS3 that does not result in an adjustment being made to the cost base or reduced cost base of the CPS3.

150. A capital gain is made if the capital proceeds from the CGT event H2 are more than the incidental costs incurred in relation to the event. A capital loss is made if the capital proceeds are less than the incidental costs (subsection 104-155(3)).

151. Subsection 116-20(2) provides that the capital proceeds from CGT event H2 happening is the money or other consideration received, or entitled to be received, because of the act, transaction or event.

152. Holders make no capital gain or capital loss from the happening of CGT event H2 as there are no capital proceeds because of the amendments to the Terms and no incidental costs are incurred by the Holders that relate to these amendments. No other CGT event will happen because of the amendments to the Terms.

Section 45

153. 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%.

154. 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 do not allow ANZ to issue Ordinary Shares to the Holders in satisfaction of their Dividend entitlements in relation to CPS3.

155. Therefore, section 45 of the ITAA 1936 will not apply to the additional Ordinary Shares acquired by the Holders on Conversion of CPS3.

Section 45A

156. 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).

157. 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.

158. 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 additional Ordinary Shares does not constitute the streaming of capital benefits.

159. 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 the CPS3 will be an unfranked dividend in the hands of the Holders.

Section 45B

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

161. The allotment of additional Ordinary Shares on Conversion of CPS3 is a scheme under which a capital benefit is provided to the Holders (paragraph 45B(5)(a) of the ITAA 1936).

162. 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.

163. The allotment of additional Ordinary Shares is not in satisfaction of the Holders' entitlement to Dividends, but rather a product of the Conversion of the CPS3 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.

164. 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.

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

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Previous draft:

Not previously issued as a draft

Related Rulings/Determinations:

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Subject references:

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

Legislative references:

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 Income Tax ~~ Capital Gains Tax ~~ cost base and reduced cost base
 Income Tax ~~ Capital Gains Tax ~~ CGT events C1 to C3 – end of a CGT asset
 Income Tax ~~ Capital Gains Tax ~~ CGT events H1 and H2 – special capital receipts
 Income Tax ~~ Tax offsets, credits and benefits ~~ franking tax offset
 Income Tax ~~ Tax integrity measures ~~ schemes