



Class Ruling

Income tax: off-market takeover of Adelhill Ltd and Permitted Special Dividend

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

When it issues, the class ruling will have the following preamble:

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:

- subsection 6(1) of the *Income Tax Assessment Act 1936* (ITAA 1936);
- subsection 44(1) of the ITAA 1936;
- section 128B of the ITAA 1936;
- section 128D of the ITAA 1936;
- former section 160APHM of the ITAA 1936;
- former section 160APHN of the ITAA 1936;
- subsection 177EA(5) of the ITAA 1936;

- Division 1A of former Part IIIAA of the ITAA 1936 (former Division 1A);
- Division 67 of the *Income Tax Assessment Act 1997* (ITAA 1997);
- section 67-25 of the ITAA 1997;
- section 104-10 of the ITAA 1997;
- Division 115 of the ITAA 1997;
- section 116-20 of the ITAA 1997;
- section 118-20 of the ITAA 1997;
- section 204-30 of the ITAA 1997;
- section 207-20 of the ITAA 1997;
- subsection 855-10(1) of the ITAA 1997;
- section 855-15 of the ITAA 1997;

Class of entities

3. The class of entities to which this Ruling applies is the ordinary shareholders of Adelhill Ltd (Adelhill), who:

- held their Adelhill ordinary shares on capital account;
- accepted the offer made by Gange Corporation Australia Ltd (Gange) to acquire their Adelhill ordinary shares or had their Adelhill ordinary shares compulsorily acquired by Gange pursuant to the terms of the Bid Implementation Agreement between Adelhill and Gange;
- received a Permitted Special Dividend of \$0.39 cash per ordinary share pursuant to the Scheme described in paragraphs 9 to 26 of this Ruling; and
- are not subject to the taxation of financial arrangements (TOFA) rules in Division 230 of the ITAA 1997 in relation to gains and losses on their Adelhill ordinary shares.

(Note – Division 230 of the ITAA 1997 will generally not apply to individuals, unless they have made an election for it to apply to them.)

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 26 of this Ruling.

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

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- this Ruling may be withdrawn or modified.

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Date of effect

8. This Ruling applies from 1 July 2012 to 30 June 2013. The Ruling continues to apply after 30 June 2013 to all entities within the specified class who entered into the specified scheme during the term of the Ruling. However, this Ruling will not apply to taxpayers to the extent that it conflicts with the terms of a settlement of a dispute agreed to before the date of issue of this Ruling (see paragraphs 75 and 76 of Taxation Ruling TR 2006/10).

Scheme

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

- Class Ruling application from Irish and Saunders on behalf of Adelhill dated 12 October 2012;
- Bid Implementation Agreement dated 12 October 2012;
- Deed of variation to Bid Implementation Agreement dated 28 November 2012;

- Deed of variation to Bid Implementation Agreement dated 24 December 2012;
- Loan Agreement dated 12 October 2012;
- Bidder's Statement dated 8 January 2013;
- First Supplementary Bidder's Statement dated 30 January 2013;
- Second Supplementary Bidder's Statement dated 5th March 2013.
- Target's Statement dated 8 January 2013;
- Supplementary Target's Statement dated 23 January 2013;
- Independent Expert Report dated 8 January 2013; and
- Other correspondence from the applicant dated between 25 October 2012 and 8 April 2013 inclusive.

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

Adelhill Ltd

10. Adelhill is an Australian resident unlisted public company. Adelhill is the holding company of a group that operates a taxi services business in Sydney.

11. As at 14 December 2012 Adelhill's issued capital comprised 36,733,740 ordinary shares.

Gange Corporation Australia Ltd

12. Gange is an Australian resident unlisted public company.

13. As at 14 December 2012 Gange owned 7,296,060 ordinary shares in Adelhill (19.86%).

The Offer

14. On 12 October 2012 Adelhill entered into a Bid Implementation Agreement (BIA) with Gange. The BIA provided for Gange to make an offer for all of the issued capital of Adelhill that it did not currently own.

15. The Gange bid offer consideration under the BIA was \$0.47 cash for each Adelhill ordinary share.

16. The takeover offer by Gange for the ordinary shares in Adelhill was conditional upon Gange achieving a relevant interest in at least 90% of the Adelhill shares on issue.

17. The offer period commenced on 9 January 2013 and ended on 8 March 2013. The Scheme Record Date was 13 March 2013.

The Permitted Special Dividend

18. The BIA provided that the board of Adelhill could at its discretion, pay a special dividend of up to \$0.39 cash per ordinary Adelhill share (Permitted Special Dividend) prior to the Gange offer becoming unconditional. The offer became unconditional on the Scheme Record Date of 13 March 2013.

19. Under a separate Loan Agreement dated 12 October 2012, Gange provided a loan to Adelhill in the amount of \$10,000,000. The Loan Agreement stated that the loan was to be used by Adelhill, solely for the purpose of paying part of the Permitted Special Dividend to its shareholders in accordance with the terms of the BIA.

20. The total loan amount of \$10,000,000 together with any accrued but unpaid interest was to be repaid by Adelhill to Gange on the date 24 months after the date of the agreement. The interest rate payable under the Loan Agreement was the Reserve Bank base rate on the day the advance was provided to Adelhill plus 2% per annum.

21. The loan from Gange to Adelhill was subject to a Financial Assistance Resolution being passed at the Adelhill annual general meeting held on 31 January 2013 by the requisite majority of shareholders. The financial assistance resolution was approved by the shareholders on 31 January 2013.

22. The provision of the loan amount by Gange to Adelhill was also subject to a number of conditions precedent under the Loan Agreement, including Gange giving notice to Adelhill that its voting power in Adelhill equalled or exceeded 75% (excluding any Adelhill shares in which Adelhill director Peter Hyer has a relevant interest).

23. The bid offer consideration payable by Gange to an Adelhill shareholder for their Adelhill ordinary shares was not reduced by the amount of the Permitted Special Dividend.

24. On 27 February 2013 the board of Adelhill declared that the Permitted Special Dividend of \$0.39 cash per Adelhill ordinary share would be paid. The Permitted Special Dividend Record Date was 27 February 2013 and Payment Date was 28 February 2013.

25. The Permitted Special Dividend was debited against Adelhill's retained earnings account. Adelhill has franking credits available to fully frank the Permitted Special Dividend.

Compulsory acquisition

26. By 1 March 2013, Gange had acquired more than 90% of Adelhill ordinary shares. On 5 March 2013, Gange served notice to Adelhill shareholders that it intended to proceed with a compulsory acquisition of the remaining Adelhill ordinary shares, on the same terms as the BIA as provided for under the *Corporations Act 2001*. The compulsory acquisition of the remaining Adelhill ordinary shares occurred on 8 April 2013.

Ruling

The Permitted Special Dividend

27. The Permitted Special Dividend of \$0.39 cash for each ordinary Adelhill share paid to an Adelhill shareholder will constitute a 'dividend' as defined in subsection 6(1) of the ITAA 1936.

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

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

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

Gross up and tax offset

31. Resident Adelhill shareholders who receive the fully franked Permitted Special Dividend:

- must include the amount of the franking credit attached to the Permitted Special Dividend in their assessable income; and

- will be entitled to a tax offset equal to the amount of the franking credit (tax offset);

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

32. The franking credit allocated to the Permitted Special Dividend is subject to the refundable tax offset rules in Division 67 of the ITAA 1997, provided the Adelhill shareholder is not excluded by the operation of section 67-25 of the ITAA 1997.

Qualified persons

33. The payment of the Permitted Special Dividend of \$0.39 per share as part of the Scheme, constitutes a related payment for the purposes of former section 160APHN of the ITAA 1936.

34. Adelhill shareholders who accepted the takeover offer will no longer be considered to hold their Adelhill shares 'at risk', for the purposes of former Division 1A of Part IIIA of the ITAA 1936 as of the Scheme Record date of 13 March 2013 (which is the date the takeover offer was declared unconditional). Accordingly, for those Adelhill shareholders who accepted the offer, the second qualification period would run from 14 January 2013 to 12 March 2013.

35. Adelhill shareholders who did not accept the takeover offer, but had their shares compulsorily acquired pursuant to the *Corporations Act 2001*, will no longer be considered to hold their Adelhill shares 'at risk' when the shares were acquired by Gange on 8 April 2013. For Adelhill shareholders who had their shares compulsorily acquired, the secondary qualification period would run from 14 January 2013 to the date the shares were compulsorily acquired (8 April 2013).

36. Accordingly, during the second qualification period that is applicable to them, an Adelhill shareholder who received the Permitted Special Dividend must hold their shares 'at risk' for at least 45 days (not counting the day on which the share was acquired or the day of disposal of the share) in order to be a qualified person in relation to the Permitted Special Dividend (former section 160APHO).

Capital gains tax

CGT Event A1

37. CGT event A1 happened when an Adelhill shareholder disposed of their Adelhill ordinary share to Gange (subsections 104-10(1) and 104-10(2) of the ITAA 1997).

38. Where an Adelhill shareholder accepted the Gange offer, CGT event A1 happened on the day that the Adelhill shareholder entered into the contract to dispose of their Adelhill ordinary shares to Gange (paragraph 104-10(3)(a) of the ITAA 1997).

39. Where an Adelhill shareholder did not accept the Gange offer and had their shares compulsorily acquired by Gange, CGT event A1 happened when Gange became the owner of the relevant ordinary shares (paragraph 104-10(6)(b) of the ITAA 1997).

Capital gain or capital loss

40. An Adelhill shareholder will make a capital gain if the capital proceeds from the disposal of their Adelhill ordinary share exceeds its cost base. The capital gain is the amount of the excess (subsection 104-10(4) of the ITAA 1997).

41. An Adelhill shareholder will make a capital loss if the capital proceeds from the disposal of their Adelhill ordinary share were less than its reduced cost base. The capital loss is the amount of the difference (subsection 104-10(4) of the ITAA 1997).

Capital proceeds

42. The capital proceeds received by an Adelhill shareholder for their Adelhill shares is the money received or entitled to be received in respect of the event happening (subsection 116-20(1) of the ITAA 1997).

43. The capital proceeds for each Adelhill ordinary share received by an Adelhill shareholder who disposed of their Adelhill ordinary share under the Scheme is \$0.86. This amount includes the Permitted Special Dividend of \$0.39.

Anti-overlap provisions

44. Any capital gain made by an Adelhill shareholder from CGT event A1 happening to their Adelhill shares can be reduced (but not below zero) by the amount of the Permitted Special Dividend that is included in the Adelhill shareholder's assessable income under subsection 44(1) of the ITAA 1936 (section 118-20 of the ITAA 1997). The amount of any capital loss made by an Adelhill shareholder will not be adjusted under section 118-20 of the ITAA 1997 by the amount of the Permitted Special Dividend that is included in the Adelhill shareholder's assessable income.

Discount capital gain

45. Any capital gain made by an Adelhill shareholder when they dispose of their Adelhill ordinary shares under the Scheme is a discount capital gain if they acquired the shares at least 12 months before the date of disposal and the other conditions in Division 115 of the ITAA 1997 are satisfied.

Foreign resident shareholders

46. An Adelhill shareholder who is a foreign resident, or the trustee of a foreign trust for CGT purposes, disregards any capital gain made when CGT event A1 happens to their Adelhill ordinary share if their Adelhill ordinary share is not 'taxable Australian property' (sections 855-10(1) and 855-15 of the ITAA 1997).

Anti-avoidance provisions

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

48. The Commissioner will not make a determination under paragraph 177EA(5)(b) of the ITAA 1936 to deny the whole, or any part, of the imputation benefit received in relation to the Permitted Special Dividend paid in respect of an Adelhill ordinary share.

Commissioner of Taxation**1 May 2013**

Appendix 1 – Explanation

① *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 Permitted Special Dividend

49. The term 'dividend' is defined in subsection 6(1) of the ITAA 1936 as a distribution made by a company to shareholders, whether in money or other property.

50. The payment of the Permitted Special Dividend is a distribution of money by Adelhill to its shareholders.

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

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

52. The payment of the Permitted Special Dividend is from Adelhill's existing cash reserves and/or existing loan facilities, including any funds to be provided by Gange under the Loan Agreement dated 12 October 2012. The payment amounts will be debited against Adelhill's retained earnings account and not the share capital account. Therefore, the exclusion in paragraph (d) will not apply. The Permitted Special Dividend will constitute a 'dividend' for the purposes of subsection 6(1) of the ITAA 1936.

Assessability of the Permitted Special Dividend

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

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

54. As the Permitted Special Dividend is paid to Adelhill shareholders out of profits derived by Adelhill, Adelhill shareholders who are residents of Australia as defined in subsection 6(1) of the ITAA 1936 are required to include the Permitted Special Dividend in their assessable income under paragraph 44(1)(a)(i) of the ITAA 1936.

Gross up and tax offset

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

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

56. Therefore, subject to satisfying the qualified person rule, where the fully franked Permitted Special Dividend was received directly by an Adelhill shareholder, the Adelhill shareholder will:

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

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

If:

- (a) a *franked distribution is made in an income year to an entity that is a partnership or the trustee of a trust; and
- (b) the entity is not a *corporate tax entity when the distribution is made; and
- (c) if the entity is the trustee of a trust – the trust is not a *complying superannuation entity or *FHSA trust when the distribution is made;

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

58. Therefore, subject to satisfying the qualified person rule, an Adelhill shareholder that is a trust or a partnership will be required to include the amount of the franking credit attached to the Permitted Special Dividend in their assessable income under subsection 207-35(1) of the ITAA 1997.

Qualified persons

59. Pursuant to paragraph 207-145(1)(a), an entity must be a 'qualified person' in relation to a dividend in order to be entitled to a tax offset in respect of the franking credit allocated to the dividend.

60. Division 1A of former Part IIIAA of the ITAA 1936 (former Division 1A) contains the measures known as the holding period rule and the related payments rule. In broad terms, former Division 1A provides the statutory tests that must be satisfied for a taxpayer to be a 'qualified person' with respect to a franked distribution they have received and thus be entitled to a tax offset for the franking credit attached to the distribution.

61. The test of what constitutes a 'qualified person' is provided in former subsection 160APHO(1) of the ITAA 1936 as follows:

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

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

62. Former subsection 160APHO(2) of the ITAA 1936, referred to in paragraph 61 of this Ruling, sets out the holding period requirement. Broadly, if a taxpayer is not under an obligation to make a related payment in relation to a dividend or distribution, the taxpayer will have to satisfy the holding period requirement within the primary qualification period. If a taxpayer is under an obligation to make a related payment in relation to a dividend or distribution, the taxpayer will have to satisfy the holding period requirement within the secondary qualification period.

Related payment rule

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

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

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

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

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

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

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

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

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

as the case may be:

- (d) is, or may reasonably be expected to be, equal to; or
- (e) approximates or may reasonably be expected to approximate; or
- (f) is calculated by reference to;

the amount of dividend or distribution.

67. In the current circumstances, it is considered that the payment of the Permitted Special Dividend of \$0.39 cash per ordinary share is an integral part of the Scheme. The payment of the Permitted Special Dividend was conditional upon Gange obtaining the requisite majority interest in Adelhill. Also, Gange provided a loan of \$10,000,000 to Adelhill, subject to the condition that:

- the loan amount was to be used solely by Adelhill, to pay the Permitted Special Dividend in accordance with the BIA; and
- Gange had given notice to Adelhill that its voting power in Adelhill equalled or exceeded 75%, excluding any Adelhill shares in which Adelhill director, Peter Hyer, had an interest.

68. The circumstances described in paragraph 67 indicate that the Permitted Special Dividend was not declared or paid independently of the contract for the sale of Adelhill ordinary shares under the BIA, as Gange has participated in arrangements in respect of the dividend. Accordingly, the payment of the Permitted Special Dividend is part of the total payment of \$0.86 cash per ordinary share that was paid to an Adelhill shareholder for the disposal of their Adelhill ordinary shares to Gange.

69. In these circumstances, it is considered the payment of the Permitted Special Dividend would constitute an act that passes a benefit to another for the purposes of former subsection 160APHN(3) of the ITAA 1936. Therefore an Adelhill shareholder is taken to have made or be likely to make a related payment in respect of the Permitted Special Dividend.

Holding period rule

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

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

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

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

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

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

73. The eligibility for the Permitted Special Dividend was determined on the Permitted Special Dividend Record Date of 27 February 2013. This was the last day on which acquisition by a person of an Adelhill share entitled the person to receive the Permitted Special Dividend as per former section 160APHE of the ITAA 1936. Accordingly the ex-dividend date for the purposes of former subsection 160APHE(1) of the ITAA 1936 was 28 February 2013.

74. The secondary qualification period thus runs from 45 days before the ex-dividend date of 28 February 2013 and ends 45 days after that date. In practical terms, this means that the secondary qualification period runs from 14 January 2013 to 13 April 2013. However, pursuant to former subsection 160APHO(3) of the ITAA 1936, any days on which a taxpayer has materially diminished risks of loss or opportunities for gain in respect of the Adelhill shares are to be excluded. This would mean that the secondary qualification period would run from 14 January 2013 until the date that Adelhill shareholders are no longer at risk for the purposes of former Division 1A.

75. Adelhill shareholders who accepted the takeover offer will no longer be considered to hold their Adelhill shares 'at risk' for the purposes of former Division 1A, as of the Scheme Record date of 13 March 2013, which was the date the takeover offer was declared unconditional. Accordingly, for those Adelhill shareholders who accepted the offer, the second qualification period would run from 14 January 2013 to 12 March 2013.

76. For Adelhill shareholders who had their shares compulsorily acquired, the secondary qualification period would run from 14 January 2013 to the date the shares were compulsorily acquired (8 April 2013).

77. Accordingly, during the second qualification period that is applicable to them, an Adelhill shareholder who received the Permitted Special Dividend must hold their shares 'at risk' for at least 45 days, in order to be a qualified person. In determining whether they hold the shares for at least 45 days in the secondary qualification period, an entity does not count the day of acquisition of the shares or the day on which the shares were disposed of. An entity must exclude any days on which the entity has materially diminished risks of loss or opportunities for gain in respect of the shares (within the meaning of former sections 160APHO, 160APHM and 160APHJ of the ITAA 1936).

Refundable tax offset

78. Adelhill shareholders who are entitled to a tax offset under subsection 207-20(2) of the ITAA 1997, in respect of the franking credit received, are also subject to the refundable tax offset rules in Division 67 of the ITAA 1997, unless specifically excluded under section 67-25 of the ITAA 1997.

79. Pursuant to section 67-25 of the ITAA 1997, certain taxpayers are specifically excluded from the operation of the refundable tax offset rules. The identified entities include:

- non-complying superannuation funds or non-complying approved deposit funds (subsection 67-25(1A) of the ITAA 1997);
- a trustee of a trust who is liable to be assessed under section 98 or 99A of the ITAA 1936 (subsection 67-25(1B) of the ITAA 1997);
- corporate tax entities, unless the entity is an exempt institution that is eligible for a refund, or a life insurance company that has received distributions on membership interests which were not held by the company on behalf of its shareholders (subsections 67-25(1C) and 67-25(1D) of the ITAA 1997); and
- foreign resident entities carrying on business in Australia at or through a permanent establishment (subsection 67-25(1DA) of the ITAA 1997).

80. Accordingly, a holder of Adelhill ordinary shares is subject to the refundable tax offset rules unless they are specifically excluded pursuant to section 67-25 of the ITAA 1997. Generally, corporate tax entities (including companies, corporate limited partnerships, corporate unit trusts, and public trading trusts) will be excluded from the operation of the refundable tax offset rules.

Non-resident shareholders

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

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

82. However, subsection 44(1) of the ITAA 1936 does not apply to a dividend to the extent to which another provision of the ITAA 1936 that expressly deals with dividends excludes some or all of the dividend from assessable income.

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

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

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

85. In addition, section 128D of the ITAA 1936 states that:

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

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

87. Accordingly, an Adelhill shareholder who received the fully franked Permitted Special Dividend and is a non-resident (other than those carrying on business in Australia at or through a permanent establishment in Australia) is not required to include the dividend as assessable income under subparagraph 44(1)(b)(i) of the ITAA 1936 (section 128D of the ITAA 1936) and will not be liable for Australian withholding tax (paragraph 128B(3)(ga) of the ITAA 1936).

88. Subsection 128B(1) of the ITAA 1936 is subject to subsection 128B(3E) of the ITAA 1936. Subsection 128B(3E) of the ITAA 1936 states that section 128B of the ITAA 1936 does not apply to dividend income that:

- (a) is paid to a person who is a non-resident carrying on business in Australia at or through a permanent establishment of the person in Australia; and

- (b) is attributable to the permanent establishment; and
- (c) is not paid to the person in the person's capacity as a trustee.

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

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

90. Accordingly, non-resident Adelhill shareholders carrying on business in Australia at or through a permanent establishment who received the fully franked Permitted Special Dividend (to the extent to which the dividend is attributable to the permanent establishment) are required to include the Permitted Special Dividend in assessable income under subparagraph 44(1)(c)(i) of the ITAA 1936; and will not be liable for Australian withholding tax in respect of the Permitted Special Dividend.

CGT Consequences

CGT event A1

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

92. For an Adelhill shareholder who accepted the Gange offer CGT event A1 happened when the Adelhill shareholder entered into the contract to dispose of their Adelhill ordinary shares to Gange pursuant to the Scheme (subsections 104-10(1) and 104-10(2) of the ITAA 1997).

93. Where an Adelhill shareholder did not accept the Gange Offer, but had their ordinary shares compulsorily acquired by Gange, CGT event A1 happened when Gange became the owner of those Adelhill ordinary shares (subsection 104-10(6) of the ITAA 1997).

94. The time when CGT event A1 happens determines the income year in which any capital gain or capital loss is made and whether the CGT discount applies to any capital gain.

95. An Adelhill shareholder made a capital gain from CGT event A1 happening if the capital proceeds from the disposal of their Adelhill ordinary share exceeded its cost base. An Adelhill shareholder made a capital loss if those capital proceeds were less than the Adelhill ordinary share's reduced cost base (subsection 104-10(4) of the ITAA 1997).

Capital proceeds

96. The capital proceeds received by an Adelhill shareholder is the money received or entitled to be received in respect of the event happening to their shares (subsection 116-20(1) of the ITAA 1997).

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

98. A dividend declared by a company that is subject to a takeover can form part of the vendor shareholders' capital proceeds from the disposal of the shares. Taxation Ruling TR 2010/4¹ states in paragraph 9 that:

A dividend declared or paid by the target company to the vendor shareholder will be money or property that the vendor shareholder has received, or is entitled to receive, under the contract or the scheme of arrangement, in respect of the transfer of the shares, if the vendor shareholder has bargained for the receipt of the dividend (whether or not in addition to other consideration) in return for giving up the shares. That is to say, if the dividend forms the whole or part of that sum of money or property in return for which the vendor shareholder is willing, and under the contract has promised or under the scheme of arrangement is bound, to transfer the shares in the target company, it will be capital proceeds in respect of the CGT event A1 happening.

99. In this case, it is considered that the payment of the Permitted Special Dividend did not occur independently of the Scheme. This is primarily reflected in the following scheme attributes:

- the Permitted Special Dividend was only payable if the Scheme became effective;
- Gange loaned Adelhill part of the amount required to pay Adelhill shareholders the Permitted Special Dividend on the condition that it be used solely by Adelhill to pay the Permitted Special Dividend in accordance with the BIA; and
- The declaration, payment or distribution of the Permitted Special Dividend was subject to Gange having acquired 75% of the Adelhill ordinary shares (excluding any Adelhill shares in which director Peter Hyer has a relevant interest).

¹ Taxation Ruling TR 2010/4: Income tax: capital gains: when a dividend will be included in the capital proceeds from a disposal of shares that happens under a contract or a scheme of arrangement.

100. These scheme attributes support a conclusion that the Permitted Special Dividend was received in respect of the disposal of Adelhills ordinary shares under the Scheme. Accordingly, the Permitted Special Dividend forms part of the capital proceeds which an Adelhills shareholder received in respect of CGT event A1 happening.

101. Therefore, the capital proceeds received by an Adelhills shareholder for each Adelhills ordinary share disposed of under the Scheme is \$0.86.

Anti-overlap provisions

102. A capital gain made from a CGT event is reduced if the capital gain includes an amount that is included in assessable income under another provision of the ITAA 1936 or the ITAA 1997 (section 118-20 of the ITAA 1997). This has the effect of reducing (but not below zero) the capital gain by the amount that is assessable under the other provision. A capital loss made from a CGT event will not be increased by the operation of section 118-20 of the ITAA 1997.

103. Where a dividend forms part of the capital proceeds from the disposal of shares and is assessable income under subsection 44(1) of the ITAA 1936, section 118-20 of the ITAA 1997 will reduce any capital gain by the amount of the dividend.

104. The Permitted Special Dividend is included in the assessable income of Adelhills shareholders who are either Australian residents, or non-residents carrying on a business in Australia at or through a permanent establishment under subsection 44(1) of the ITAA 1936. Therefore, section 118-20 of the ITAA 1997 will operate to reduce (but not below zero) any capital gain made by an Adelhills shareholder from CGT event A1 happening to their Adelhills shares by the amount of the Permitted Special Dividend that is included in the Adelhills shareholder's assessable income under subsection 44(1) of the ITAA 1936.

105. However, under paragraph 118-20(1B)(b) of the ITAA 1997, the capital gain made by an Adelhills shareholder is not reduced by the amount of the franking credit referable to the Permitted Special Dividend that is included in their assessable income.

106. The amount of a capital loss made by an Adelhills shareholder is not adjusted by the amount of the Permitted Special Dividend under section 118-20 of the ITAA 1997.

Discount capital gain

107. If an Adelhills shareholder made a capital gain from the disposal of their Adelhills ordinary shares, the Adelhills shareholder may be eligible to treat the capital gain as a discount capital gain provided that all relevant requirements of Division 115 of the ITAA 1997 are met.

108. One of those requirements is that the capital gain must result from a CGT event happening to a CGT asset that was acquired by the entity making the capital gain at least 12 months before the CGT event (subsection 115-25(1) of the ITAA 1997).

109. This means that a capital gain made by an Adelhill shareholder when they disposed of their Adelhill ordinary shares can be treated as a discount capital gain if the shareholder acquired the Adelhill ordinary share at least 12 months before the date of disposal, subject to the other requirements in Division 115 of the ITAA 1997 being satisfied.

Foreign resident shareholders

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

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

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

112. An Adelhill shareholder that is a foreign resident, or the trustee of a foreign trust for CGT purposes, just before CGT event A1 happens under the Scheme, cannot disregard under subsection 855-10(1) of the ITAA 1997 a capital gain or capital loss from CGT event A1 happening if:

- their Adelhill ordinary share was an indirect Australian real property interest (item 2 of the table in section 855-15 of the ITAA 1997); or
- their Adelhill ordinary share had been used at any time by the foreign resident, or the trustee of a foreign trust for CGT purposes, in carrying on a business through a permanent establishment in Australia (item 3 of the table in section 855-15 of the ITAA 1997); or

- their Adelhill ordinary share was covered by subsection 104-165(3) of the ITAA 1997 (item 5 of the table in section 855-15 of the ITAA 1997).

The anti-avoidance provisions

Section 204-30

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

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

114. If section 204-30 of the ITAA 1997 applies, the Commissioner may make a determination in writing:

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

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

116. Pursuant to the payment of the Permitted Special Dividend, all Adelhill shareholders received an imputation benefit as a result of the Permitted Special Dividend. Subject to being 'qualified persons', Australian resident Adelhill shareholders received an imputation benefit in the form of a tax offset (paragraph 204-30(6)(a) of the ITAA 1997). Non-resident Adelhill shareholders received an imputation benefit in the form of an exemption from dividend withholding tax (paragraph 204-30(6)(e) of the ITAA 1997). Resident Adelhill shareholders derived a greater benefit from franking credits than the non-resident shareholders.

117. However, the Permitted Special Dividend was paid to all Adelhill shareholders identified at the Permitted Special Dividend Record Date and was fully franked. Accordingly, it cannot be concluded that Adelhill intended to direct the flow of distributions in such a manner as to stream the imputation benefits to members that derive a greater benefit from the franking credits attached to the Permitted Special Dividend, while other members received lesser or no imputation benefits.

118. As the conditions in subsection 204-30(1) of the ITAA 1997 are not met in respect of the Permitted Special Dividend, the Commissioner will not make a determination under paragraph 204-30(3)(c) to deny the whole, or any part, of the imputation benefit received in respect of the Permitted Special Dividend.

Section 177EA

119. Section 177EA of the ITAA 1936 is a general anti-avoidance provision that applies to a wide range of schemes seeking to obtain a tax advantage in relation to imputation benefits. In essence, it applies to schemes for the disposition of shares or an interest in shares, where a franked distribution is paid or payable in respect of the shares or an interest in shares.

120. Subsection 177EA(3) of the ITAA 1936 provides that section 177EA of the ITAA 1936 applies if:

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

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

122. Adelhill is a corporate tax entity. The disposal of the ordinary shares in Adelhill pursuant to the Scheme is a scheme for the disposition of membership interests. The fully franked Permitted Special Dividend is a frankable distribution that was paid to Adelhill shareholders (the relevant taxpayers) as a part of this Scheme and who could, therefore, reasonably be expected to receive imputation benefits.

123. In the present case, the conditions of paragraphs 177EA(3)(a) to 177EA(3)(d) of the ITAA 1936 are satisfied. Accordingly, the issue is whether, having regard to the relevant circumstances of the scheme (as provided for in subsection 177EA(17) of the ITAA 1936), it would be concluded that, on the part of Adelhill, its shareholders or any other relevant party, there is a purpose, more than merely an incidental purpose, of conferring an imputation benefit under the Scheme.

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

125. The relevant circumstances of the Scheme include the fact that the passing of the Financial Assistance Resolution, voted upon by Adelhill's existing shareholders was a condition of the Takeover.

126. The Permitted Special Dividend was fully franked and was paid to the existing shareholders of Adelhill in proportion to their shareholding, and irrespective of their ability to utilise the relevant franking credits. The Permitted Special Dividend allowed Adelhill shareholders to share in the accumulated profits of Adelhill.

127. In considering the manner, form and substance of the Scheme, it is considered that the Scheme was not entered into by Adelhill or the Adelhill shareholders for more than an incidental purpose of enabling participating shareholders to obtain imputation benefits. The goal of providing imputation benefits to Adelhill shareholders remained incidental, in the sense of being subservient to, the purpose of transferring their shares to Gange.

128. Having regard to the relevant circumstances of the Scheme, the Commissioner has come to the view that the requisite purpose is not present and accordingly the Commissioner will not make a determination under paragraph 177EA(5)(b) of the ITAA 1936 to deny the whole, or any part, of the imputation benefit received in relation to the Permitted Special Dividend.

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References

Previous draft:

Not previously issued as a draft

Related Rulings/Determinations:

TD 2002/4; TR 2006/10;
TR 2010/4

Subject references:

- arrangement
- CGT asset
- CGT capital proceeds
- CGT event A1 – disposal of a CGT asset
- distributions
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Legislative references:

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NO: 1-4B9AMRC

ISSN: 1445-2014

ATOlaw topic: Income Tax ~~ Assessable income ~~ dividend, interest
and royalty income
Income Tax ~~ Capital Gains Tax ~~ capital proceeds
Income Tax ~~ Capital Gains Tax ~~ CGT event A1 –
disposal of a CGT asset
Income Tax ~~ Tax integrity measures ~~ qualified
persons – franking credits