



CR 2005/10 - Income tax: scrip for scrip roll-over: proposed takeover of National Foods Ltd by Fonterra Co-operative Group Ltd

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Class Ruling

Income tax: scrip for scrip roll-over: proposed takeover of National Foods Ltd by Fonterra Co-operative Group Ltd

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Preamble

*The number, subject heading, **What this Class Ruling is about** (including **Tax law(s)**, **Class of persons** and **Qualifications** sections), **Date of effect**, **Arrangement** and **Ruling** parts of this document are a 'public ruling' in terms of Part IVAAA of the **Taxation Administration Act 1953**. CR 2001/1 explains Class Rulings and Taxation Rulings TR 92/1 and TR 97/16 together explain when a Ruling is a 'public ruling' and how it is binding on the Commissioner.*

What this Class Ruling is about

1. This Ruling sets out the Commissioner's opinion on the way in which the 'tax law(s)' identified below apply to the defined class of persons who take part in the arrangement to which this Ruling relates.

Tax law(s)

2. The tax laws dealt with in this Ruling are:
- section 104-55 of the *Income Tax Assessment Act 1997* (ITAA 1997); and
 - Subdivision 124-M of the ITAA 1997.

Class of persons

3. The class of persons to whom this Ruling applies is the shareholders in National Foods Ltd (NFL) who:
- (a) are residents of Australia within the meaning of that expression in subsection 6(1) of the *Income Tax Assessment Act 1936*;
 - (b) are not 'significant stakeholders' or 'common stakeholders' within the meaning of those expressions in Subdivision 124-M; and
 - (c) accept the takeover offer from Fonterra Foods Pty Ltd (FFPL) to exchange some or all of their shares in NFL for redeemable preference shares in Fonterra Co-operative Group Ltd (FCGL).

Qualifications

4. The Commissioner makes this Ruling based on the precise arrangement identified in this Ruling.
5. The class of persons defined in this Ruling may rely on its contents provided the arrangement actually carried out is carried out in accordance with the arrangement described in paragraphs 9 to 17.
6. If the arrangement actually carried out is materially different from the arrangement that is described in this Ruling, then:
 - this Ruling has no binding effect on the Commissioner because the arrangement entered into is not the arrangement on which the Commissioner has ruled; and
 - this Ruling may be withdrawn or modified.
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Date of effect

8. This Class Ruling applies to the year ended 30 June 2005 and later income years.

Arrangement

9. The arrangement that is the subject of this Ruling is described below. This description is based on the documents listed below. These documents, or relevant parts of them, as the case may be, form part of and are to be read with this description. The relevant documents or parts of documents incorporated into this description of the arrangement are:
 - (a) Class Ruling Application dated 10 January 2005 from KPMG requesting the Australian Taxation Office (the Tax Office) make a Class Ruling;

- (b) letters from KPMG dated 20 January 2005, 27 January 2005, 22 February 2005, 25 February 2005 and 2 March 2005 providing further clarification and information to the Tax Office; and
- (c) final drafts of the following documentation:
 - Indicative Terms Sheet – Redeemable Preference Shares – draft dated 21 February 2005;
 - Terms and Conditions of the A\$ Redeemable Preference Shares – draft dated 24 February 2005; and
 - Shareholding Deed Poll – draft dated 24 February 2005.

10. The arrangement that is the subject of this Ruling involves the proposed takeover of NFL by FFPL, which is a member of a wholly-owned group of which FCGL, a New Zealand registered co-operative company, is the ultimate holding company.

11. The arrangement allows for Australian resident and New Zealand resident NFL shareholders to dispose of their NFL shares to FFPL for either:

- a cash payment per NFL share; or
- a number of redeemable preference shares in FCGL per NFL share.

12. The amount of the payment and the number of redeemable preference shares is dependent on the level of acceptance of the offer.

13. Other foreign resident NFL shareholders will only be entitled to receive the cash payment for their NFL shares.

14. The key terms in regard to the redeemable preference shares in FCGL include:

- the redeemable preference shares will not be listed on any stock exchange;
- the redeemable preference shares will be redeemable on a set maturity date (15 March 2010) unless redeemed earlier;
- FCGL will have the right to redeem the redeemable preference shares prior to the maturity date upon the happening of certain events; and
- the redeemable preference shares will initially carry voting rights.

15. NFL shareholders who elect to receive redeemable preference shares in FCGL will be required to provide an irrevocable direction that the redeemable preference shares be issued to a Custodian on trust for their benefit. This ensures that FCGL will not breach its constitution which requires that at least 60% of the voting rights be held by 'transacting shareholders'.

16. The Custodian would hold the redeemable preference shares upon the terms of a Shareholding Deed Poll. The key terms of the Deed Poll include:

- a separate trust will be established for each NFL shareholder who accepts the share offer;
- the Custodian will hold the legal title to the redeemable preference shares;
- as holder of the beneficial interest in the redeemable preference share, each participating NFL shareholder will be able to transfer its beneficial interest to another person;
- a participating NFL shareholder will be able to exit the trust and be registered as the legal holder by notice to the Custodian;
- the Custodian will be able to exercise voting rights that are attached to the redeemable preference shares and is required to solicit instructions where practicable; and
- dividends and capital distributions paid on the redeemable preference shares will pass through to the NFL shareholders.

17. Where the NFL shareholders hold their NFL shares jointly, the redeemable preference shares will be issued to the Custodian to be held under the terms of separate trusts for each of the former joint shareholders.

Ruling

18. Subject to the qualifications in paragraphs 4 to 6 of this Ruling and subject to FFPL and other members of the FCGL wholly-owned group becoming owners of 80% or more of the voting shares in NFL as a result of the arrangement, NFL shareholders who are within the class of persons to which this Ruling applies can choose roll-over under Subdivision 124-M of the ITAA 1997 in relation to a NFL share they acquired on or after 20 September 1985 if:

- (a) apart from the roll-over for which Subdivision 124-M provides, they would make a capital gain in relation to the disposal of their NFL share; and

- (b) any capital gain that could be made upon a future CGT event happening in relation to the redeemable preference share in FCGL would not be disregarded (except because of a roll-over).

19. Where a NFL shareholder has exchanged some, but not all, of their shares in NFL for redeemable preference shares in FCGL, the shareholder cannot choose roll-over in respect of a NFL share for which they have received a cash payment.

20. Where a shareholder chooses roll-over in respect of a NFL share, the capital gain arising from the exchange of that share is disregarded.

21. CGT event E1 in section 104-55 of the ITAA 1997 will not happen to the NFL shareholders upon the issuing of the redeemable preference shares to the Custodian because each former NFL shareholder will be absolutely entitled to their redeemable preference shares as against the Custodian.

Explanation

Availability of scrip for scrip roll-over

22. Scrip for scrip roll-over enables a shareholder to disregard a capital gain they make from a share that is disposed of as part of a corporate takeover or merger if the shareholder receives in exchange a replacement share. The capital gain is disregarded completely if the only capital proceeds the shareholder receives is a replacement share. The roll-over also provides that the cost base and reduced cost base of the replacement shares is based on the cost base and reduced cost base of the original shares at the time of the roll-over.

23. Subdivision 124-M of the ITAA 1997 contains a number of conditions for, and exceptions to, the eligibility of a shareholder to choose scrip for scrip roll-over. Below is an outline of the main conditions and exceptions which are relevant to the circumstances of the arrangement that is the subject of this Ruling.

Subparagraph 124-780(1)(a)(i) of the ITAA 1997 requires an entity to exchange a share in a company for a share in another company

24. This requirement will be satisfied by each NFL shareholder electing the share offer as under the terms of the arrangement NFL shares are exchanged for redeemable preference shares in FCGL.

25. The requirement that each NFL shareholder give an irrevocable direction that the legal title to the redeemable preference shares be issued to and held by the Custodian on their behalf does not mean that the NFL shareholders have not exchanged a share for a share. A contract between FFPL and each NFL shareholder will be formed upon acceptance of the share offer under which the

consideration for the transfer of NFL shares will be clearly expressed to be the redeemable preference shares in FCGL.

Paragraphs 124-780(1)(b) and 124-780(2)(a) of the ITAA 1997 require that shares in an original entity (NFL) be exchanged in consequence of a single arrangement that results in the acquiring entity (FFPL), and members of the wholly-owned group of which FFPL is a member, becoming the owner of 80% or more of the voting shares in the original entity

26. The acquisition of NFL shares by FFPL in consideration for the issue of redeemable preference shares in FCGL will occur as a consequence of a single arrangement.

27. Members of the FCGL wholly-owned group currently hold 19.03% of the issued shares of NFL. Whether or not the arrangement results in the FCGL wholly-owned group becoming the owner of 80% or more of the voting shares in NFL is a question of fact that can only be satisfied if the FCGL wholly-owned group becomes the owner of 80% or more of the voting shares in NFL as a result of the arrangement. Paragraph 18 limits this Ruling in this regard.

Paragraphs 124-780(1)(b) and 124-780(2)(b) of the ITAA 1997 require that the exchange of shares is in consequence of a single arrangement in which at least all owners of voting shares in the original entity (NFL) could participate

28. This requirement will be satisfied as all shareholders in NFL are able to participate in the arrangement.

Paragraphs 124-780(1)(b) and 124-780(2)(c) of the ITAA 1997 require that the exchange of shares is in consequence of a single arrangement in which participation was available on substantially the same terms for all of the owners of interests of a particular type in the original entity (NFL)

29. Australian resident and New Zealand resident NFL shareholders will have the choice of taking up either the share or cash offer. Whilst other foreign resident NFL shareholders will only have access to the cash offer, it is considered that this does not prevent participation being available on substantially the same terms for all owners of NFL shares. This is because the value of the cash offer and the share offer is the same.

30. Accordingly, the requirement that participation be available on substantially the same terms for all owners of NFL shares is satisfied.

Paragraphs 124-780(1)(c) and 124-780(3)(a) require the original interest holder (a NFL shareholder) to have acquired their original interest (a NFL share) on or after 20 September 1985

31. Roll-over will only be available for those NFL shares that were acquired on or after 20 September 1985. Paragraph 18 limits this Ruling in this regard.

Paragraphs 124-780(1)(c) and 124-780(3)(b) of the ITAA 1997 require that, apart from the roll-over, the original interest holder (a NFL shareholder) would make a capital gain from a CGT event happening in relation to the original interest (a NFL share)

32. Whether a NFL shareholder would, apart from the roll-over, make a capital gain from the disposal of any of its shares to FFPL is a question of fact that is dependent on the specific circumstances of each shareholder - in particular on the cost base of each NFL share and the value of the capital proceeds received. Paragraph 18(a) limits this Ruling in this regard.

Paragraphs 124-780(1)(c) and 124-780(3)(c) of the ITAA 1997 require that the replacement interest be in the ultimate holding company of the wholly-owned group (FCGL) which includes the acquiring entity (FFPL)

33. This requirement is satisfied as the replacement interest received by NFL shareholders will be in FCGL which is the ultimate holding company of a wholly-owned group of companies of which FFPL is a member.

Paragraphs 124-780(1)(c) and 124-780(3)(d) of the ITAA 1997 require that the original interest holder (a NFL shareholder) choose to obtain the roll-over

34. Whether a NFL shareholder has chosen roll-over in relation to the disposal of a NFL share is a question of fact.

Additional requirements in subsection 124-780(5) of the ITAA 1997 must be satisfied if the original interest holder (a NFL shareholder) and the acquiring entity (FFPL) did not deal with each other at arm's length and:

- a. neither the original entity (NFL) nor the replacement entity (FCGL) had at least 300 members just before the arrangement started: paragraph 124-780(4)(a) of the ITAA 1997; or***
- b. the original interest holder (a NFL shareholder), the original entity (NFL) and the acquiring entity (FFPL) were all members of the same linked group just before the arrangement started: paragraph 124-780(4)(b) of the ITAA 1997***

35. Paragraph 124-780(4)(a) of the ITAA 1997 will not apply because both NFL and FCGL will have at least 300 members just before the arrangement started. Section 124-810 of the ITAA 1997 will not apply to either NFL or FCGL as their ownership is not concentrated in the manner contemplated by that section.

36. Paragraph 124-780(4)(b) of the ITAA 1997 will not apply because NFL and FFPL were not members of the same linked group (within the meaning of section 170-260 of the ITAA 1997) just before the arrangement started.

Exceptions to obtaining scrip for scrip roll-over

Paragraph 124-795(2)(a) of the ITAA 1997 provides that the roll-over is not available if any capital gain the original interest holder (a NFL shareholder) might make from their replacement interest (a FCGL share) would be disregarded

37. This exception may apply if, for example, the FCGL redeemable preference shares are held as trading stock. Paragraph 18(b) limits this Ruling in this regard.

Paragraph 124-795(2)(b) of the ITAA 1997 provides that the roll-over is not available if the original interest holder (a NFL shareholder) and the acquiring entity (FFPL) are members of the same wholly-owned group just before the original interest holder stops owning their original interest (a NFL share), and the acquiring entity is a foreign resident

38. This exception does not apply as FFPL is not a foreign resident.

CGT event E1

39. CGT event E1 in section 104-55 of the ITAA 1997 happens if a taxpayer creates a trust over a CGT asset by declaration or settlement. In this case, a trust is created over the redeemable preference shares upon their issue to the Custodian.

40. An exception to CGT event E1 applies under paragraph 104-55(5)(a) if the taxpayer who created the trust over the asset is a beneficiary of the trust and is absolutely entitled to the asset as against the trustee. Below is an outline of the main conditions for that exception to CGT event E1 which are relevant to the circumstances of the arrangement that is the subject of this Ruling.

The NFL shareholder must be the sole beneficiary of the trust

41. Under the terms of the Shareholding Deed Poll, a separate trust will be established for each NFL shareholder who accepts the share offer. In cases where the NFL shareholders hold their NFL shares jointly, the redeemable preference shares will be issued to the Custodian to be held under the terms of separate trusts for each of the former joint shareholders.

42. As a result, the requirement that the NFL shareholder be the sole beneficiary of the trust will be satisfied.

Each NFL shareholder must be absolutely entitled to their redeemable preference shares as against the Custodian (disregarding any legal disability)

43. It is considered that each NFL shareholder will be absolutely entitled to their redeemable preference shares as against the Custodian as they will have a vested and indefeasible interest in their redeemable preference shares and will have the ability to call for the shares to be transferred to them or to be transferred at their direction.

44. Whilst FCGL will have the right to redeem the redeemable preference shares prior to the maturity date upon the happening of certain events, this does not affect the beneficiary's relationship with the Custodian.

45. Accordingly, each NFL shareholder will be absolutely entitled to their redeemable preference shares as against the Custodian.

The trust must not be a unit trust

46. The interest in each trust upon which the Custodian will hold the legal title to the redeemable preference shares for each NFL shareholder will not be divided into units.

Detailed contents list

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Previous draft:

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Related Rulings/Determinations:

CR 2001/1; TR 92/1; TR 97/16

Legislative references:

- ITAA 1936 6(1)

- ITAA 1997 104-55

- ITAA 1997 104-55(5)(a)

- ITAA 1997 Subdiv 124-M

- ITAA 1997 124-795(2)(a)

- ITAA 1997 124-795(2)(b)

- ITAA 1997 124-780(1)(a)(i)

- ITAA 1997 124-780(1)(b)

- ITAA 1997 124-780(1)(c)

- ITAA 1997 124-780(2)(a)

- ITAA 1997 124-780(2)(b)

- ITAA 1997 124-780(2)(c)

- ITAA 1997 124-780(3)(a)

- ITAA 1997 124-780(3)(b)

- ITAA 1997 124-780(3)(c)

- ITAA 1997 124-780(3)(d)

- ITAA 1997 124-780(4)(a)

- ITAA 1997 124-780(4)(b)

- ITAA 1997 124-780(5)

- ITAA 1997 124-810

- ITAA 1997 170-260

- TAA 1953 Pt IVA

- Copyright Act 1968

ATO references

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