CR 2006/60 - Income tax: scrip for scrip roll-over: acquisition of Patrick Corporation Limited by Toll Holdings Limited

Class Ruling

Income tax: scrip for scrip roll-over: acquisition of Patrick Corporation Limited by Toll Holdings Limited

Contents Para

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 Class Ruling are:

- section 104-10 of the *Income Tax Assessment Act 1997* (ITAA 1997);
- section 109-10 of the ITAA 1997;
- Division 110 of the ITAA 1997;
- section 115-25 of the ITAA 1997;
- section 116-20 of the ITAA 1997; and
- Subdivision 124-M of the ITAA 1997.

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

Class of entities

3. The class of entities to which this Ruling applies are the holders of ordinary shares in Patrick Corporation Limited (Patrick) who:

(a) accepted the offer made by Toll Holdings Limited (Toll) to acquire their Patrick shares or whose Patrick shares are compulsorily acquired under the compulsory acquisition process set out in Chapter 6A of the *Corporations Act 2001*;

(b) held their Patrick shares on capital account;

(c) are 'residents of Australia' within the meaning of that expression in subsection 6(1) of the *Income Tax Assessment Act 1936* (ITAA 1936); and

(d) are not 'significant stakeholders' or 'common stakeholders' within the meaning of those expressions in Subdivision 124-M of the ITAA 1997.

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 13 to 15 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- this Ruling may be withdrawn or modified.

Date of effect

8. This Ruling applies from 15 September 2005. However, the Ruling does not apply to taxpayers to the extent that it conflicts with the terms of settlement of a dispute agreed to before the date of issue of the Ruling. Furthermore, the Ruling only applies to the extent that:

- it is not later withdrawn by notice in the *Gazette*; or
- the relevant provisions are not amended.

9. If this Class Ruling is inconsistent with a later public or private ruling, the relevant class of entities may rely on either ruling which applies to them (item 1 of subsection 357-75(1) of Schedule 1 to the *Taxation Administration Act 1953* (TAA)).

10. If this Class Ruling is inconsistent with an earlier private ruling, the private ruling is taken not to have been made if, when the Class Ruling is made, the following two conditions are met:

- the income year or other period to which the rulings relate has not begun; and
- the scheme to which the rulings relate has not begun to be carried out.

11. If the above two conditions do not apply, the relevant class of entities may rely on either ruling which applies to them (item 3 of subsection 357-75(1) of Schedule 1 to the TAA).

Withdrawal

12. This Ruling is withdrawn immediately after 30 June 2007. The Ruling continues to apply, in respect of the relevant provision(s) relied upon, to all persons within the specified class who enter into the arrangement during the term of the Ruling.

Scheme

13. The scheme that is the subject of this Ruling is described below. The description is based on, and includes reference to, the following documents:

(a) Class Ruling application dated 30 September 2005 and amended Class Ruling application dated 30 March 2006 from KPMG requesting the Commissioner make a Class Ruling in relation to the proposed acquisition of Patrick by Toll;

(b) Toll's Bidder's Statement of 15 September 2005;

(c) Toll's Seventh Supplementary Bidder's Statement of 22 March 2006;

(d) Toll's Ninth Supplementary Bidder's Statement of 21 April 2006;

(e) Toll's Tenth Supplementary Bidder's Statement of 12 May 2006; and

(f) Correspondence from KPMG from 30 September 2005 to 19 June 2006.

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

14. Toll has made an off-market takeover offer (the Offer) to acquire all of the shares in Patrick. The terms of the Offer, contained in section 16 of Toll's Bidder's Statement of 15 September 2005 as amended by the Ninth Supplementary Bidder's Statement, provide that a Patrick shareholder will receive 0.4 of a Toll share and $3.00 for each Patrick share.

15. On 25 May 2006 Toll owned 95.16% of Patrick shares and proceeded to compulsorily acquire the remaining ordinary shares in Patrick in accordance with Chapter 6A of the *Corporations Act 2001*.

Ruling

Disposal of Patrick shares to Toll

16. CGT event A1 happens when a Patrick shareholder accepted the Offer to dispose of their Patrick shares to Toll or when their Patrick shares are compulsorily acquired by Toll under the Offer (subsections 104-10(1), 104-10(2), 104-10(3) and 104-10(6)).

17. The capital proceeds for each Patrick share are $3.00 plus the market value of 0.4 of a Toll share at the time the shareholder accepted the Offer to dispose of their Patrick shares or when their Patrick share are compulsory acquired by Toll under the Offer (section 116-20).

18. A Patrick shareholder will make a capital gain from CGT event A1 happening if the capital proceeds for a Patrick share exceeded its cost base. The shareholder will make a capital loss if those capital proceeds are less than the share's reduced cost base (subsection 104-10(4)).

Availability of scrip for scrip roll-over

19. Patrick shareholders will be eligible to choose scrip for scrip roll-over to the extent that they receive Toll shares in exchange for their Patrick shares under the Offer if:

(a) they acquired their Patrick shares on or after 20 September 1985 (paragraph 124-780(3)(a));

(b) apart from the roll-over under Subdivision 124-M, they would make a capital gain from the CGT event A1 (section 104-10) that happens to their Patrick shares (paragraph 124-780(3)(b)); and

(c) they could not disregard (except because of a roll-over) any capital gain they might make from a replacement Toll share (subsection 124-795(2)).

20. If a Patrick shareholder chooses roll-over, a capital gain from a Patrick share is disregarded to the extent that the shareholder received a Toll share. The capital gain is not disregarded to the extent that the shareholder received cash for the disposal of their Patrick share (section 124-790).

21. If a Patrick shareholder chooses roll-over, the cost base of a replacement Toll share is worked out by reasonably attributing to it the cost base of any Patrick share for which it was exchanged and for which a partial roll-over was obtained. However, the cost base of the Patrick share must first be reduced by so much of it that is taken into account in working out the shareholder's capital gain relating to the cash proceeds (subsections 124-785(2) and (3)).

Discount capital gain

22. A Patrick shareholder who makes a capital gain will be eligible to treat the gain as a discount capital gain providing they held the share for at least 12 months before the disposal and the other requirements of Subdivision 115-A are satisfied (section 115-25).

The acquisition of Toll shares

23. A Patrick shareholder who acquires new Toll shares under the Offer acquires them for CGT purposes on the day when the contract is entered into (section 109-10).

24. A Patrick shareholder who acquires Toll shares as the result of the compulsory acquisition of their Patrick shares acquires the Toll shares for CGT purposes on the day when the Toll shares are issued or allotted to them (section 109-10).

Example

25. The following example provides guidance for Patrick shareholders to work out their capital gains consequences if they choose roll-over in respect of their disposal of their shares to Toll under the Offer.

26. The example, including the figures used, is only to illustrate the application of the relevant taxation provisions and does not refer to any particular Patrick shareholder nor to any particular share price. The market value to be used will vary depending upon the day the Patrick shareholder accepts the Offer or has their Patrick shares compulsory acquired.

27. The example shows how to work out:

- a capital gain attributable to the cash they received for their Patrick shares; and
- the first element of the cost base of their replacement Toll shares.

28. Where a Patrick shareholder works out the first element of the cost base of their Toll shares in accordance with the approach adopted in the example, the Tax Office will accept that this represents a reasonable attribution of the cost base of each Patrick share. However, it is recognised that this approach may not be the only reasonable method.

29. Andrew acquired 500 shares in Patrick for $2,500 in July 2004. On 11 May 2006 he accepted the Offer from Toll, and Andrew received $1,500 cash ($3.00 × 500) and 200 Toll shares. The closing price of a Toll share on 11 May 2006 (the date Andrew accepted the Offer) was $15.41. In the circumstances, the Commissioner accepts that the closing price of a Toll share on 11 May 2006 is the market value of a Toll share on that day.

Capital gain attributable to ineligible proceeds

30. Andrew chooses for roll-over to apply to the extent that he is able. Andrew works out the capital gain from the ineligible proceeds using the following formula:

Ineligible proceeds = $1,500

Total proceeds = $1,500 + 200 × $15.41

= $ 4,582

Capital gain = Ineligible proceeds less cost base of ineligible part

Cost base of ineligible part = Cost base of Patrick shares × (ineligible proceeds/Total proceeds)

= $2,500 × $1,500/$4,582

= $818.42

Capital Gain = $1,500 - $818.42

= $681.58

Cost base of Toll shares

31. The first element of the cost base of each of Andrew's 200 Toll shares is determined by reference to the cost base of each of his Patrick shares that was not taken into account in working out the capital gain Andrew made in respect of the ineligible proceeds. The cost base of Andrew's shares will therefore be:

Cost base of Patrick shares = $2,500

Cost base attributable to ineligible proceeds = $818.42 (taken into account above)

First element of cost base of each Toll share = $1,681.58/200

(ie. $2,500 – $818.42)/200)

= $8.41

32. The first element of the reduced cost base of Andrew's shares will be calculated in a similar manner.

Commissioner of Taxation
28 June 2006

Appendix 1 – Explanation

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.

Disposal of Patrick shares to Toll

33. CGT event A1 happens if there is a change in the ownership of an asset from one entity to another. The 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. CGT event A1 will happen if a Patrick shareholder disposes of a Patrick share to Toll under the Offer (section 104-10).

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

35. CGT event A1 happened on the day the Patrick shareholder entered into the contract to dispose of the share to Toll under the Offer. The time of entering into the contract was the day the Patrick shareholder accepted the Offer.

36. Certain Patrick shareholders did not accept the Offer but will have their Patrick shares compulsorily acquired in accordance with the *Corporations Act 2001*. Those shareholders will be taken to have disposed of their shares when the compulsory acquisition occurs. CGT event A1 will happen when the change of ownership of the Patrick share occurs (paragraph 104-10(3)(b) and subsection 104-10(6)).

37. A Patrick shareholder will make a capital gain from CGT event A1 happening if the capital proceeds in respect of the disposal of their Patrick share exceeded its cost base. A Patrick shareholder will make a capital loss if the capital proceeds in respect of the disposal of a Patrick share were less than the Patrick share's reduced cost base (subsection 104-10(4)).

38. The time of CGT event A1 happening is also relevant to determining the capital proceeds received for each Patrick share. Subsection 116-20(1) provides that the capital proceeds from a CGT event are the money and market value of any property received or entitled to be received (worked out at the time of the event happening).

Market value of the Toll shares

39. Patrick shareholders must therefore determine the market value of the Toll shares at the date of the disposal of their Patrick shares. The Commissioner will accept as the market value of those shares the closing price of a Toll share on the Australian Stock Exchange (ASX) on the day that the shareholder disposed of their Patrick shares provided that the closing price does not vary by more than 5% from either the minimum or maximum traded price over the course of the day. If the closing price does vary by more than 5% the Commissioner will accept the volume-weighted average price

(VWAP) for the shares over the day as representing the market value of the share for that day.

Availability of scrip for scrip roll-over

40. Where scrip for scrip roll-over is chosen in respect of the capital gain arising on the disposal of a Patrick share, the capital gain from the disposal will be disregarded to the extent that the shareholder receives a Toll share. Roll-over may be chosen whether the disposal is because a Patrick shareholder accepts the Offer or because the Patrick share is compulsorily acquired.

41. If the Patrick shareholder chooses roll-over, the cost base of each Toll share is worked out by reasonably attributing to it a proportion of the cost base of the Patrick share for which it was exchanged and for which roll-over was obtained. The cost base of the Patrick share must first be reduced by so much of it that is taken into account in working out the shareholder's capital gain relating to the ineligible proceeds (cash of $3.00 per Patrick share).

42. A Patrick shareholder who derives a capital gain from the ineligible proceeds may be eligible to treat the gain as a discount capital gain in respect of those Patrick shares that are held for at least 12 months and provided the other requirements of Subdivision 115-A are satisfied (section 115-25).

43. Subdivision 124-M contains a number of conditions regarding the eligibility of a shareholder to choose scrip for scrip roll-over. The main conditions and exceptions that are relevant to this scheme are outlined below.

Subparagraph 124-780(1)(a)(i) requires an entity (a Patrick shareholder) to exchange a share in a company for a share in another company

44. This requirement will be satisfied by a Patrick shareholder who receives the Toll share and cash as consideration for the disposal of their Patrick share under the Offer because at least some of the consideration they receive for the disposal of their Patrick share will consist of a Toll share. Roll-over will be available to the extent that the Patrick shareholder received Toll shares for their Patrick shares.

Paragraphs 124-780(1)(b) and 124-780(2)(a) require that shares in an entity (Patrick – the original entity) be exchanged in consequence of a single arrangement that results in another entity (Toll – the acquiring entity) becoming the owner of 80% or more of the voting shares in the original entity (Patrick)

45. The only issued shares in Patrick are ordinary shares. These shares satisfy the definition of 'voting share' in section 995-1.

46. In the context of the scrip for scrip roll-over provisions, the offer to Patrick shareholders is a 'single arrangement'. As Toll has acquired more than 80% of the ordinary shares in Patrick in consequence of this arrangement this condition has been satisfied.

47. The compulsory acquisition of shares can be in consequence of an arrangement. The Explanatory Memorandum to the New Business Tax System (Capital Gains Tax) Bill 1999 that introduced section 124-780 states that this test will be satisfied if the share acquisition has a causal connection with the arrangement. It indicates further that this connection will exist if, after a takeover offer expires, shares are acquired under powers of compulsory acquisition under the Corporations Law.

Paragraphs 124-780(1)(b) and 124-780(2)(b) requires 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 (Patrick) (apart from the acquiring entity or members of the acquiring entity's wholly-owned group) could participate

48. This requirement will be met as the Offer was made to all Patrick shareholders.

Paragraphs 124-780(1)(b) and 124-780(2)(c) requires that the exchange 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 (Patrick)

49. This requirement will be satisfied as all of the ordinary shareholders in Patrick are entitled to participate in the Offer on substantially the same terms.

50. All foreign Patrick shareholders are eligible to participate in the Offer. Some foreign Patrick shareholders who accept the Offer will receive the cash component of the capital proceeds and the cash proceeds of a nominee sale of the shareholder's entitlement to Patrick shares. Accordingly, a foreign Patrick shareholder is entitled to participate on substantially the same terms as any other Patrick shareholder.

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

51. As all of the issued shares in Patrick were acquired on or after 20 September 1985, roll-over will be available for those Patrick shares.

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

52. Whether a Patrick shareholder would, apart from the roll-over, make a capital gain from the disposal of any of their shares to Toll is a question of fact that is dependent on the specific circumstances of each shareholder – in particular, on the cost base of each Patrick share and the value of the capital proceeds received.

Paragraphs 124-780(1)(c) and 124-780(3)(c) require that the replacement interest is in the acquiring entity (Toll), or the ultimate holding company of the wholly owned group which includes the acquiring entity

53. This requirement will be satisfied as the Patrick shareholders will receive shares in Toll, the acquiring entity.

Paragraphs 124-780(1)(c) and 124-780(3)(d) require that the original interest holder (a Patrick shareholder) chooses the roll-over, or if section 124-782 applies to it for the arrangement, it and the replacement entity jointly choose to obtain the roll-over

54. Whether a Patrick shareholder chooses to obtain roll-over in relation to the disposal of a Patrick share is a question of fact.

Subsection 124-780(4) provides that the additional requirements in subsection 124-780(5) must be satisfied if the original interest holder (a Patrick shareholder) and the acquiring entity (Toll) did not deal with each other at arm's length and:

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

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

56. Paragraph 124-780(4)(b) does not apply as Patrick and Toll will not be members of the same linked group just before the arrangement commences.

Exceptions to obtaining scrip for scrip roll-over

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

57. Whether the capital gain arising because of the disposal of a Patrick share is disregarded under another provision of the ITAA 1997 (for example, the shareholder holds their Patrick shares as trading stock) is a question of fact.

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

58. This exception will not apply as Toll is not a foreign resident.

Consequences of roll-over

59. Scrip for scrip roll-over enables a shareholder to disregard all or part of a capital gain from a share that is disposed of as part of a corporate takeover or merger if the shareholder receives a replacement share in exchange.

60. If the only capital proceeds the shareholder receives are replacement shares, the capital gain is disregarded completely (subsection 124-785(1)). All of the cost base of the original shares can be allocated to the replacement shares (subsection 124-785(2)).

61. If the shareholder receives other capital proceeds as well as the replacement shares, the capital gain is disregarded in part (subsection 124-790(1)). Only a portion of the cost base of the original shares can be allocated to the replacement shares (subsections 124-785(2) and 124-785(3)).

Consequences of roll-over where Toll shares and cash are received as capital proceeds

62. Because the capital proceeds paid to Patrick shareholders in respect of their Patrick shares consist of Toll shares and cash, a Patrick shareholder can choose only partial roll-over. Roll-over will not be available to the extent that any capital gain is attributable to the cash of $3.00 per Patrick share (subsection 124-790(1)).

63. In calculating the capital gain attributable to their ineligible proceeds, a Patrick shareholder should deduct from the total proceeds a reasonable portion of the cost base of their Patrick shares (just before their disposal to Toll) (subsection 124-790(2)).

64. In making a reasonable apportionment of the cost base of a Patrick share, it would be appropriate for a shareholder to consider the value of the ineligible proceeds, fixed at $3.00, and the value of the Toll shares on the date that CGT event A1 happens to their Patrick share.

65. The cost base and reduced cost base of the Patrick shares, reduced by that portion that is taken into account in working out any capital gain in respect of the ineligible proceeds, will form the first element of the cost base of Toll shares (subsections 124-785(2), 124-785(3) and 124-785(4)).

The acquisition of Toll shares

66. Under the Offer, Toll will give 0.4 of a Toll share as part of the consideration for the acquisition of each Patrick share from a Patrick shareholder.

67. The Patrick shareholder may acquire the Toll shares under the Offer or as a result of the compulsory acquisition of Patrick shares.

68. The Toll shares are acquired by each Patrick shareholder when they accept the Offer (item 2 of the table in section 109-10). Where the Patrick shares are compulsorily acquired, the Toll shares are acquired at the time of the compulsory acquisition (section 109-5).

Appendix 2 – Detailed contents list

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

References

Previous draft:

Not previously issued as a draft

Subject references:

- arrangement
- capital proceeds
- CGT event
- company
- cost base
- interests
- ordinary share
- original interest
- replacement interest
- resident
- roll-over
- scrip for scrip roll-over
- share
- shareholder
- takeover

Legislative references:

- ITAA 1936 6(1)
- ITAA 1997 104-10
- ITAA 1997 104-10(1)
- ITAA 1997 104-10(2)
- ITAA 1997 104-10(3)
- ITAA 1997 104-10(3)(b)
- ITAA 1997 104-10(4)
- ITAA 1997 104-10(6)
- ITAA 1997 109-5
- ITAA 1997 109-10
- ITAA 1997 Div 110
- ITAA 1997 Subdiv 115-A
- ITAA 1997 115-25
- ITAA 1997 116-20
- ITAA 1997 116-20(1)
- ITAA 1997 Subdiv 124-M
- ITAA 1997 124-780
- 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)
- ITAA 1997 124-780(4)(a)
- ITAA 1997 124-780(4)(b)
- ITAA 1997 124-780(5)
- ITAA 1997 124-782
- ITAA 1997 124-785(1)
- ITAA 1997 124-785(2)
- ITAA 1997 124-785(3)
- ITAA 1997 124-785(4)
- ITAA 1997 124-790
- ITAA 1997 124-790(1)
- ITAA 1997 124-790(2)
- ITAA 1997 124-795(2)
- ITAA 1997 124-795(2)(a)
- ITAA 1997 124-795(2)(b)
- ITAA 1997 124-810
- ITAA 1997 995-1
- TAA 1953
- TAA 1953 Sch 1 357-75(1)
- Copyright Act 1968
- Corporations Act 2001

Other references:

- Explanatory Memorandum to the New Business Tax System (Capital Gains Tax) Bill 1999

ATO references

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