

CR 2006/74 - Income tax: SFE Corporation Limited - Executive Equity Plan - merger with Australian Stock Exchange Limited

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Class Ruling

Income tax: SFE Corporation Limited – Executive Equity Plan – merger with Australian Stock Exchange Limited

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① This publication provides you with the following level of protection:

This publication (excluding appendixes) is a public ruling for the purposes of the *Taxation Administration Act 1953*.

A public ruling is an expression of the Commissioner's opinion about the way in which a relevant provision applies, or would apply, to entities generally or to a class of entities in relation to a particular scheme or a class of schemes.

If you rely on this ruling, we must apply the law to you in the way set out in the ruling (or in a way that is more favourable for you if we are satisfied that the ruling is incorrect and disadvantages you, and we are not prevented from doing so by a time limit imposed by the law). You will be protected from having to pay any underpaid tax, penalty or interest in respect of the matters covered by this ruling if it turns out that it does not correctly state how the relevant provision applies to you.

What this Ruling is about

1. This Ruling sets out the Commissioner's opinion on the way in which the relevant provision(s) identified below apply to the defined class of entities, who take part in the scheme to which this Ruling relates.

Relevant provision(s)

2. The relevant provisions dealt with in this Ruling are:

- section 139B of the *Income Tax Assessment Act 1936* (ITAA 1936);
- section 139CA of the ITAA 1936;
- section 139CB of the ITAA 1936;
- section 139CD of the ITAA 1936
- section 139DQ of the ITAA 1936;
- section 139DR of the ITAA 1936;
- section 139E of the ITAA 1936;
- section 139G of the ITAA 1936; and
- section 139GCB of the ITAA 1936.

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

Class of entities

3. The class of entities to which this Ruling applies is all persons who acquired a beneficial interest in shares under the SFE Corporation Limited (SFE) Executive Equity Plan (the Plan) as employees of SFE. They are persons who immediately prior to the merger between SFE and Australian Stock Exchange Limited (ASX), as described in paragraphs 20 to 21 of this Ruling:

- had legal title to those shares;
- had not made an election under section 139E in relation to those shares;
- had not had a cessation time happen, within the meaning of section 139CA, in relation to those shares; and
- under the terms of the merger, received 0.51 new ASX shares for each SFE share held on the record date.

In this Ruling, a person belonging to this class of entities is referred to as a 'participating employee'.

Qualifications

4. 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 22 of this Ruling.

5. This Ruling does not apply to SFE employees who, immediately before the merger, held shares acquired under the Plan, but after the merger were no longer employed by SFE or by a company within the group of which SFE is a member.

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 to the income years ended 30 June 2006 and 30 June 2007. 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 and ceases to have effect after 30 June 2007. However, the Ruling continues to apply after its withdrawal, in respect of the relevant provisions ruled upon, to all entities within the specified class who entered into the specified scheme during the term of the Ruling, subject to there being no change in the scheme or in the entity's involvement in the scheme.

Scheme

13. The scheme that is the subject of the Ruling is described below. This description is based on the following documents. 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 scheme are:

- the request for a class ruling from Ernst & Young (the applicant) dated 17 May 2006;
- SFE Corporation Limited Equity Plan Trust Deed;
- SFE Corporation Limited Executive Equity Plan Rules (the Rules);
- Invitation and Offer Booklet for the SFE Corporation Limited Executive Equity Plan 2005 awards granted in December 2005;
- Explanatory Memorandum dated 29 May 2006, Proposed Merger of SFE Corporation Limited and the Australian Stock Exchange Limited; and
- correspondence providing further particulars dated 15 June and 3 July 2006 from Ernst and Young.

14. The Plan was established on 25 October 2005.

15. In accordance with the Rules, selected SFE employees were invited to participate in the Plan and were offered an allocation of fully paid ordinary shares in SFE for no consideration.

16. Where an SFE employee accepted the invitation to participate, shares were acquired and allocated by the trustee (the Trustee) of the SFE Corporation Limited Equity Plan Trust for the benefit of the employee in accordance with the Rules.

17. SFE shares allocated under the Plan were subject to disposal restrictions and were at risk of forfeiture until certain vesting conditions were satisfied. These conditions were partly performance based and partly time based. The disposal restrictions prevented employees from disposing or dealing with the shares and normally applied for approximately 3 years from grant, unless specified events occurred during that period.

18. The merger process is one of the specific events provided for in the Rules which resulted in the lifting of the disposal restrictions and forfeiture conditions and hence, the early vesting of the SFE shares. The Trustee was required, as soon as practicable, to transfer those shares to the employees. Once transferred, employees could choose to sell their SFE shares (subject to the normal share trading restrictions that might apply to an employee), but must have done so at a time prior to the merger when dealings in SFE shares were no longer permitted.

19. The applicant has advised that SFE shares acquired by participating employees under the Plan were qualifying shares within the meaning of section 139CD.

Merger of SFE and ASX

20. On 27 March 2006, SFE and ASX jointly announced a proposal to merge their businesses. This was followed on 29 May 2006 by a Court order that SFE convene a meeting of shareholders to approve the scheme of arrangement to effect the merger. A meeting of shareholders was held on 5 July 2006 which approved the scheme of arrangement.

21. On implementation of the merger on 25 July 2006 all shareholders, including participating employees, received either:

- 0.51 new ASX ordinary shares for each SFE share held at the record date (share alternative);

or, if they so elected:

- \$2.58 cash per SFE share plus a variable ratio of new ASX ordinary shares per SFE share held at the record date such that the value of the cash and the new ASX shares was equivalent to the share alternative immediately prior to the scheme meeting (cash and share alternative).

22. The applicant advised that:

- the Court order to convene the meeting of SFE shareholders to vote on the merger had the effect that, under the Rules, the shares were no longer the subject of the disposal restrictions or forfeiture conditions;
- in accordance with the Rules, the Trustee then transferred the SFE shares to the employees;
- the merger was intended to result in SFE becoming a 100% subsidiary of ASX;
- the participating employees retained their employment with SFE; and
- at the time the participating employees acquired their ASX shares, no participating employee held a legal or beneficial interest in more than 5% of the shares in ASX and no participating employee was in a position to cast, or control the casting of, more than 5% of the maximum number of votes that may be cast at a general meeting of ASX.

Ruling

23. Where under the Plan, the Trustee acquired a share and held it for the benefit of a participating employee, the participating employee acquired a qualifying share for the purposes of Division 13A of Part III (Division 13A).

24. The discount given in relation to the share is included in the assessable income of the participating employee in the year that the cessation time happens in relation to the SFE share.

25. When the participating employee accepted the share alternative offer, the ASX shares received as a replacement for the SFE shares acquired under the Plan, are treated as if they are a continuation of the SFE shares for the purposes of Division 13A. Thus, this event did not trigger a cessation time.

Commissioner of Taxation

9 August 2006

Appendix 1 – Explanation

❶ *This Appendix is provided as information to help you understand how the Commissioner's view has been reached. It does not form part of the binding public ruling.*

26. Section 139G provides that a person will acquire a share in several circumstances, including by acquiring a beneficial interest in the share.

27. For the purposes of this Ruling, the Commissioner accepts the statement by the applicant that SFE shares acquired under the Plan are qualifying shares within the meaning of section 139CD. Thus, a participating employee will have acquired a qualifying share when the Trustee acquired and allocated the share to the participating employee under the Plan and the participating employee acquired a beneficial interest in the share.

28. However, where an employee acquires a share under an employee share scheme the discount given in relation to the share is included in the assessable income of the employee, pursuant to subsection 139B(1).

29. Where an employee acquires a qualifying share and does not make an election under section 139E, the discount given in relation to the share is included in assessable income in the year of income in which the cessation time occurs, in accordance with subsection 139B(3).

30. As this Ruling applies to participating employees who have not made an election under section 139E, the cessation time will be determined in accordance with subsection 139CA(2) and will be the earliest of:

- the time when the participating employee disposes of the share;
- the time when any restriction preventing the disposal of the share by the participating employee and any forfeiture conditions cease to have effect;
- the time when the participating employee ceases to be employed by either their employer (being their employer at the time they acquired the share) or a group company, pursuant to subsection 139CA(3); or
- the end of the ten year period starting when the participating employee acquired the share.

31. As the SFE shares acquired under the Plan were subject to disposal restrictions and forfeiture conditions, the lifting of such would ordinarily give rise to a cessation time under subsection 139CA(2). However, where the lifting of disposal restrictions and removal of forfeiture conditions is part of a process that leads to a takeover or restructure, Subdivision DA of Division 13A may apply.

Rollover provisions

32. Subdivision DA of Division 13A, which came into effect from 1 April 2005, was implemented to provide relief from the possible early application of sections 139CA or 139CB (determination of a cessation time) in the event of a corporate takeover or restructure occurring on or after 1 July 2004.

33. Where these provisions apply, shares acquired in the new company are treated as if they are a continuation of the shares in the old company.

The effect of a takeover or restructure on an employee share scheme

34. The rollover provisions are intended to apply to 100% takeovers and restructures of companies that have employee share schemes.

35. Relevantly, a 100% takeover is defined in section 139GCB as an arrangement that is intended to result in the company becoming a 100% subsidiary of the other company, or of a holding company or subsidiary of the other company'.

36. It is accepted that as the proposed merger was intended to result in SFE becoming a 100% subsidiary of ASX, it satisfies this definition and is a 100% takeover within the meaning of section 139GCB.

37. Section 139DQ sets out in the first instant the circumstances that the rollover provisions will apply to. In this case the relevant requirements are that:

- (a) an employee acquires a share in a new company;
- (b) that share can reasonably be regarded as matching a share in another company (the old company);
- (c) the share in the old company was acquired under an employee share scheme;
- (d) the acquisition of the share in the new company occurs in connection with a 100% takeover of the old company; and
- (e) as a result of the restructure the employee ceased to hold shares in the old company.

38. For the purposes of paragraph 37(a) above, a participating employee who held an SFE share prior to the merger and who received the share alternative, acquired a share in a new company, being ASX.

39. For the purposes of paragraph 37(b) above, the note to subsection 139DQ(1) provides a guide as to a factor that is relevant in determining to what extent something can reasonably be regarded as matching a share in the old company. That is, the respective market values of the old shares and the new shares. The Explanatory Memorandum to the Tax Laws Amendment (2004 Measures No. 7) Bill that introduced the rollover provisions provides further guidance on this issue when it states at paragraph 3.14:

Matching shares or rights should be no more than that which is required to place the employee in the same position financially as if the restructure had not occurred.

40. The applicant has advised that the terms of the scheme of arrangement sought to ensure an outcome where the market value of the SFE shares before the merger will be the same or equivalent to the market value of the replacement ASX shares acquired as a result of the merger.

41. Further, the applicant has advised that the shares (being qualifying shares) were acquired under an employee share scheme as defined, satisfying paragraph 37(c).

42. The acquisition of the shares in the ASX occurred as a result of the merger which was intended to result in a 100% takeover as defined in section 139GCB.

43. As a result of the merger, participating employees ceased to hold shares in SFE (the old company).

Conditions for continuation of shares

44. Section 139DQ also provides that the treatment of matching shares as a continuation of shares in the old company is subject to the conditions in section 139DR.

45. Section 139DR sets out the following conditions that must be met before matching shares will be treated (for the purposes of Division 13A) as being a continuation of shares in the old company:

- the employee must have held shares in the old company under an employee share scheme immediately before the takeover;
- where the employee has not made an election under section 139E in relation to shares in the old company, the employee, at or about the time they acquire the matching shares, must be employed by the new company, a holding company of the new company or a subsidiary of either the new company or a holding company of the new company;
- the matching shares must be ordinary shares; and

- at the time of acquiring the matching shares the employee:
 - i) must not hold a legal or beneficial interest in more than 5% of the shares of the new company; and
 - ii) must not be in a position to cast or control more than 5% of the votes at a general meeting of the new company.

46. As to the first condition, the class of entities (as described in paragraph 3 of this Ruling) being participating employees, have acquired SFE shares under the Plan and held those shares immediately prior to the proposed merger.

47. For the purposes of the second condition, the applicant has advised that SFE has become a subsidiary of the ASX and that the participating employees retained their employment with SFE after the merger. Therefore, as participating employees have not made elections under section 139E in relation to their SFE (the old company) shares at the time of the proposed merger, it is accepted that the second condition is satisfied.

48. As to the third condition, the shares in ASX (the matching shares) are ordinary shares.

49. In relation to the fourth condition, the applicant has advised that at the time participating employees acquired their matching shares no participating employees held a legal or beneficial interest in more than 5% of the shares of ASX or were in a position to cast or control more than 5% of the votes at a general meeting of ASX.

50. Lastly, it is accepted that as a consequence of the operation of the Rules:

- the lifting of disposal restrictions and removal of forfeiture conditions prior to the proposed merger; and
- the transfer by the Trustee of legal title in SFE shares to employees prior to the proposed merger,

are necessary parts of the merger process. Therefore, where the provisions of Subdivision DA of Division 13A apply, the above events do not give rise to an early cessation time under section 139CA.

51. In summary, it is accepted that the circumstances described in section 139DQ are present and the conditions set out in section 139DR are met. Therefore, the acquisition by a participating employee of matching shares in ASX as a consequence of the merger are treated as if they are a continuation of the SFE shares for the purposes of Division 13A.

Appendix 2 – Detailed contents list

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

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References

Previous draft:

Not previously issued as a draft

Subject references:

- cessation time
- disposal
- employee share scheme
- restructures

Legislative references:

- TAA 1953
- TAA 1953 Sch 1 357-75(1)
- Copyright Act 1968
- ITAA 1936 Pt III Div 13A
- ITAA 1936 139B
- ITAA 1936 139B(1)
- ITAA 1936 139B(3)
- ITAA 1936 139CA

- ITAA 1936 139CA(2)
- ITAA 1936 139CA(3)
- ITAA 1936 139CB
- ITAA 1936 139CD
- ITAA 1936 Pt III Div 13A Subdiv DA
- ITAA 1936 139DQ
- ITAA 1936 139DQ(1)
- ITAA 1936 139DR
- ITAA 1936 139E
- ITAA 1936 139G
- ITAA 1936 139GCB

Other references:

- Explanatory Memorandum to the
Tax Laws Amendment (2004
Measures No. 7) Bill

ATO references

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