


CR 2007/9 - Income tax: capital gains: demerger of Tower Australia Group Limited by Tower Limited

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Class Ruling

Income tax: capital gains: demerger of Tower Australia Group Limited by Tower 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 (unless we are satisfied that the ruling is incorrect and disadvantages you, in which case we may apply the law in a way that is more favourable for you – provided 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 44 of the *Income Tax Assessment Act 1936* (ITAA 1936);
- section 45B of the ITAA 1936;
- section 45BA of the ITAA 1936;
- section 45C of the ITAA 1936;
- section 104-25 of the *Income Tax Assessment Act 1997* (ITAA 1997); and
- Division 125 of the ITAA 1997.

Class of entities

3. The class of entities to which this Ruling applies is the shareholders of Tower Limited (Tower) who:
- (a) participated in the scheme that is the subject of this Ruling;
 - (b) owned ordinary shares in Tower and held those shares on capital account at the time of the demerger; and
 - (c) were residents of Australia (as that term is defined in subsection 6(1) of the ITAA 1936) at the time of the demerger.
4. In this Ruling this class of entities is referred to as the 'participating shareholders'.

Qualifications

5. The Commissioner makes this Ruling based on the precise scheme identified in this Ruling.
6. 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 14 to 33 of this Ruling.
7. 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

9. This Ruling applies from 1 July 2006 to 30 June 2007. However, the Ruling continues to apply after this date 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 entities involved in the scheme.

10. The Ruling does 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 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.

11. If this 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)).

12. If this Ruling is inconsistent with an earlier private ruling, the private ruling is taken not to have been made if, when this 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.

13. 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).

Scheme

14. The following description of the scheme is based on information provided by the applicant.

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

Background

15. The scheme that is the subject of this Ruling involved the demerger of the Australian businesses that were operated by the Tower group of companies. The businesses located in New Zealand remained in Tower.

The Tower group

16. Tower is a company incorporated in New Zealand that was demutualised and listed on the New Zealand Stock Exchange (NZSE) and the Australian Stock Exchange (ASX) in September 1999 following a NZ\$350 million initial public offer. It is also the head company of the Tower group of companies (the Tower group). The demerged entity, Tower Australia Group Limited (TAL), was a wholly-owned subsidiary of the Tower group.

17. At the time of the demerger, Tower had approximately 359.8 million ordinary shares on issue. Australian residents owned approximately 36% of the shares on issue. The largest foreign resident shareholder held 19.8% of the shares on issue.

18. All Tower shares on issue were acquired by shareholders on or after 20 September 1985.

19. Tower also had a total of 13,515,757 options on issue (the executive options) at the time of the demerger. These options were issued to a number of key executives of Tower, and gave the holder the right to acquire ordinary Tower shares. Prior to the demerger, the options represented approximately 3.75% of the total number and approximately 1.5% of the total market value of ownership interests in Tower.

Pre-demerger transactions

20. Prior to the demerger, the Tower group undertook a number of transactions (including the transfer of shares) that resulted in TAL and its subsidiaries owning the Australian business.

The demerger

21. Tower then undertook a restructure to demerge TAL to its shareholders. As a result of the demerger, Tower shareholders acquired ordinary shares in TAL.

22. The demerger was undertaken pursuant to a New Zealand Court approved scheme of arrangement. Tower shareholders voted at a special meeting to approve (by way of special resolution) the scheme of arrangement under which:

- Tower cancelled 0.4760 Tower shares for every Tower share held at record date by a Tower shareholder; and
- as consideration for the cancellation, Tower transferred 0.6511 TAL shares (subject to rounding) for every Tower share held by a Tower shareholder at the record date (17 November 2006).

23. Under this scheme of arrangement, Tower cancelled a total of approximately 171.3 million shares in Tower, and transferred a total of approximately 234.3 million shares in TAL to its shareholders. This happened on 20 November 2006.

24. Tower accounted for the cancellation of the Tower shares by:

- debiting its share capital account in the amount of NZ\$454 (A\$393) million in total (or approximately NZ\$2.65 (A\$2.29) per ordinary share cancelled) (the capital reduction amount); and

- debiting its demerger reserve account in the amount of NZ\$113 (A\$97.8) million in total (or approximately NZ\$0.66 (A\$0.57) per ordinary share cancelled).¹
25. Tower shareholders did not receive any distribution in cash as a result of this transaction.
26. Following the demerger:
- TAL was listed on the ASX; and
 - Tower continues to be listed on the NZSE and the ASX.
27. Tower shareholders that were not residents of Australia or New Zealand (foreign shareholders) had a proportion of their Tower shares cancelled on the same basis as other Tower shareholders. However, the TAL shares provided as consideration for the cancellation were transferred to a nominee on behalf of each of those foreign shareholders. The nominee has or will sell these TAL shares and has or will remit the net proceeds to each of the foreign shareholders.
28. The holders of executive options did not receive TAL shares under the scheme of arrangement. As part of the scheme, the terms of these executive options were reconstructed in a manner that took into account the effect of the demerger on these options, adjusting them in a manner that preserved the intrinsic value of these options for the holders.

Reasons for the demerger

29. The demerger resulted in the separation of TAL and Tower into two independent listed companies. TAL will focus on its life insurance and investment business and will operate in Australia. Tower will focus on its insurance and investment businesses operating in New Zealand.
30. Tower's Board of Directors believes that the separation will:
- allow each company to better pursue independently focused strategies that are consistent with its strengths and capabilities;
 - enable management of each entity to adopt a stronger focus on operational issues as they specifically relate to the individual businesses;

¹ Most participating shareholders are required to translate the capital reduction amount into Australian currency applying the rule in Item 5 in the table in subsection 960-50(6) of the ITAA 1997. This requires that the money expressed in foreign currency be translated into Australian currency at the time of the relevant CGT event using an appropriate exchange rate. In the present case, the Commissioner accepts the exchange rate of 1.1551 New Zealand dollars to 1 Australian dollar as appropriate (being the daily exchange rate published by the Reserve Bank of Australia on 20 November 2006 (the date of the demerger)).

- achieve a commercial separation of the businesses of the Tower group in a way that is consistent with the geographic separation of the markets in which they operate;
- allow the operations of each company to be funded more efficiently as they will each have direct access to the equity and debt capital markets by virtue of their separate listings;
- improve investment choices available to investors; and
- allow each company to have simpler and more transparent corporate structures with no cross ownership or funding arrangements.

Other matters

31. Tower confirms that there have been no transfers to its share capital account, as defined in section 975-300 of the ITAA 1997, from any of its other accounts.

32. Just after the demerger, at least 50% of the market value of the CGT assets owned by TAL and its demerger subsidiaries were used in the carrying on of a business by those entities.

33. Tower did not elect under subsection 44(2) of the ITAA 1936 that subsections 44(3) and (4) of the ITAA 1936 not apply to the scheme of arrangement.

Ruling

CGT event C2

34. CGT event C2 happened for each participating shareholder on the cancellation of their Tower shares (section 104-25 of the ITAA 1997).

35. Participating shareholders received A\$2.81 as the capital proceeds in respect of the cancellation of each of their Tower shares (the relevant market value on 20 November 2006 of each cancelled Tower share for the purposes of subsection 116-30(2) of the ITAA 1997).

36. To the extent that the capital proceeds received by each shareholder in respect of the cancellation of their share exceed its cost base, a capital gain will result. This capital gain will be reduced by the amount of the demerger dividend received (subsection 118-20(4) of the ITAA 1997).

37. To the extent that the reduced cost base of each cancelled share exceeds the capital proceeds amount, a capital loss will arise (subsection 104-25(3) of the ITAA 1997).

Demerger rollover

38. Tower and its subsidiary, TAL, were part of a demerger group under subsection 125-65(1) of the ITAA 1997.

39. A demerger, as described under section 125-70 of the ITAA 1997, happened to this demerger group under the scheme.

40. Participating shareholders are eligible to choose demerger rollover relief under subsection 125-55(1) of the ITAA 1997 for each of their Tower shares cancelled.

Participating shareholders who choose demerger rollover

41. Participating shareholders who choose demerger rollover for their cancelled Tower shares can disregard any capital gain or capital loss made in respect of CGT event C2 happening to those Tower shares (subsection 125-80(1) of the ITAA 1997).

42. If a participating shareholder chooses demerger rollover for their cancelled Tower shares, the first element of the cost base of each remaining Tower share and corresponding TAL share they received under the demerger is worked out by taking the sum of the cost bases of their Tower shares (just before the demerger) and apportioning it over their remaining Tower shares and new TAL shares. The apportionment of this sum is done on a basis that is reasonable having regard to the market values (just after the demerger) of the Tower shares and TAL shares, or a reasonable approximation of those market values (subsections 125-80(2) and (3) of the ITAA 1997).

Participating shareholders who do not choose demerger rollover

43. For participating shareholders who do not choose demerger rollover:

- they are not entitled to disregard any capital gain or capital loss made in respect of CGT event C2 that happened to their Tower shares that were cancelled under the demerger; and
- the first element of the cost base and reduced cost base of each Tower share and the corresponding TAL shares is calculated in the manner described in paragraph 42 of this Ruling (subsections 125-85(1) and (2) of the ITAA 1997).

Acquisition date of the TAL shares for the purposes of the CGT discount

44. For the purpose of accessing the CGT discount, the TAL shares received by the participating shareholders are taken to have been acquired on the date that the shareholder acquired the corresponding Tower shares that were cancelled (subsection 115-30(1) of the ITAA 1997 (item 2)).

Demerger dividend

45. Any dividend arising under the demerger is a demerger dividend (subsection 6(1) of the ITAA 1936).

46. The demerger dividend is neither assessable income nor exempt income of the participating shareholders (subsections 44(3) and (4) of the ITAA 1936).

47. As the capital reduction amount was debited to Tower's share capital account it is not a dividend, as defined in subsection 6(1) of the ITAA 1936.

Application of sections 45B and 45C

48. The Commissioner will not make a determination under paragraph 45B(3)(a) of the ITAA 1936 that section 45BA of the ITAA 1936 applies to the whole or any part of any demerger benefit provided to participating shareholders under the demerger.

49. The Commissioner will not make a determination under paragraph 45B(3)(b) of the ITAA 1936 that section 45C of the ITAA 1936 applies to the whole or any part of the capital benefit provided to participating shareholders under the demerger.

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.*

CGT event C2

50. CGT event C2 happens if ownership of an intangible CGT asset ends by the asset being redeemed or cancelled (paragraph 104-25(1)(a) of the ITAA 1997). Under the scheme of arrangement, CGT event C2 therefore happened in relation to the Tower shares that were cancelled.

51. A capital gain will arise under CGT event C2 if the capital proceeds received in relation to the ending of the asset exceeds the cost base of that asset (subsection 104-25(3) of the ITAA 1997). If an amount from the CGT event happening is treated as non-assessable non-exempt income (NANE income), the capital gain will be reduced by that amount of NANE income (subsection 118-20(4) of the ITAA 1997).

52. A capital loss will arise under CGT event C2 if those capital proceeds are less than the asset's reduced cost base (subsection 104-25(3) of the ITAA 1997).

Capital proceeds

53. For the purposes of determining the capital proceeds from the cancellation of each Tower share, sections 116-20 and 116-30 of the ITAA 1997 require that the amount paid to the shareholder in respect of the cancellation of each Tower share be compared with the market value of each Tower share on the date of cancellation. If these amounts differ, the capital proceeds will be the market value of the Tower share (section 116-30 of the ITAA 1997).

54. The amount paid in respect of the cancelled Tower share was 1.3677758 of the market value of a TAL share (subsections 116-20(1) and 116-40(1) of the ITAA 1997). For the purposes of determining the market value of a TAL share, the Commissioner accepts that the market value may be calculated using the volume weighted average price of TAL shares over the first five ASX trading days after TAL was listed (this was A\$2.32). A Tower shareholder therefore received A\$3.17 in capital proceeds for each Tower share cancelled.

55. In comparison, for the purposes of section 116-30 of the ITAA 1997, the Commissioner accepts that the market value of a cancelled Tower share on the date of cancellation may be calculated by reference to the volume weighted average price of a Tower share on the last day the shares traded with entitlement to participate in the demerger. This price was A\$2.81.

56. Since these amounts differ, the capital proceeds are the market value of the cancelled Tower share (A\$2.81) (section 116-30 of the ITAA 1997).

Capital gain or loss amount

57. Participating shareholders will therefore make a capital gain on the cancellation of their Tower share to the extent that the capital proceeds (A\$2.81) exceed the cost base of the cancelled Tower share. This amount is then reduced by the amount of the demerger dividend for the cancelled Tower share, since it constitutes NANE income (paragraph 80 of this Ruling explains that the demerger dividend is \$A0.88 per cancelled Tower share).

58. Participating shareholders will make a capital loss to the extent that the capital proceeds (A\$2.81) are less than the reduced cost base of the cancelled Tower share.

Demerger rollover

59. Demerger rollover enables a shareholder to disregard a capital gain or capital loss as a result of CGT event C2 happening when a share is cancelled under a demerger.

60. In order for the demerger rollover to apply the following conditions must be met.

Requirements for a demerger – Division 125

61. Subsection 125-55(1) of the ITAA 1997 provides that rollover may be chosen if, at the time of the scheme:

- a shareholder owns a share in a company – this requirement is satisfied as participating shareholders owned shares in Tower;
- the company is the head entity of a demerger group – this requirement is satisfied as Tower was the head company of a demerger group (refer to paragraphs 64 and 65 of this Ruling);
- a demerger happens to the demerger group – this requirement is satisfied as a demerger happened to the Tower demerger group (refer to paragraph 67 of this Ruling); and
- under the demerger a CGT event happens to the original interest and a new or replacement interest is acquired in the demerged entity – this requirement is satisfied because CGT event C2 happened to the Tower shares (refer to paragraph 50 of this Ruling) and participating shareholders received TAL shares under the demerger.

62. Since the participating shareholders to whom this Ruling applies is limited to Australian residents, the condition in subsection 125-55(2) of the ITAA 1997 is not relevant.

63. Therefore, participating shareholders may choose rollover for the demerger.

Was Tower the head entity of a demerger group?

64. A demerger group comprises one head entity and at least one demerger subsidiary (subsection 125-65(1) of the ITAA 1997). The demerger group in this case included Tower as head entity and TAL as a demerger subsidiary (Tower demerger group).

65. Tower was the head entity because:

- TAL had no ownership interests in Tower (subsection 125-65(3) of the ITAA 1997); and
- there was no other company or trust that was capable of being a head entity of a demerger group of which Tower could have been a demerger subsidiary (subsection 125-65(4) of the ITAA 1997).

66. TAL was a demerger subsidiary of Tower because Tower, together with other members of the Tower group, owned ownership interests that carried the right to:

- receive 100% of any distribution of income or capital of TAL; and
- exercise 100% of the voting power in TAL (subsection 125-65(6) of the ITAA 1997).

Did a demerger happen to a demerger group?

67. A demerger happened (subsections 125-70(1), (2) and (3) of the ITAA 1997) to the Tower demerger group because:

- there was a restructuring (paragraph 125-70(1)(a) of the ITAA 1997) under which the Tower group disposed of 100% of its existing shares in TAL to the Tower shareholders (subparagraph 125-70(1)(b)(i) of the ITAA 1997);
- CGT event C2 happened to Tower shares, and Tower shareholders acquired new shares in TAL and nothing else (subparagraph 125-70(1)(c)(i) of the ITAA 1997);
- under the restructure, TAL shares were acquired by Tower shareholders on the basis of their ownership of shares in Tower (paragraph 125-70(1)(d) and subparagraph 125-70(1)(e)(i) of the ITAA 1997);

- it was reasonable to assume that more than 50% of the original ownership interests in Tower were owned by Australian residents or foreign residents whose TAL shares had the necessary connection with Australia (paragraph 125-70(1)(f) of the ITAA 1997);
- paragraph 125-70(1)(g) of the ITAA 1997 was satisfied since neither Tower or TAL was a trust that was a superannuation fund;
- each Tower shareholder acquired TAL shares in the same proportion as they owned Tower shares just before the demerger (paragraph 125-70(2)(a) of the ITAA 1997);
- each Tower shareholder owned, just after the demerger, the same proportionate total market value of Tower and TAL shares as they owned in Tower just before the demerger (paragraph 125-70(2)(b) of the ITAA 1997); and
- subsections 125-70(4) and (5) of the ITAA 1997 had no application.

68. The executive options are ownership interests for the purposes of subsection 125-60(1) of the ITAA 1997 since they give the owner the entitlement to acquire a share in Tower. However, they are also adjusting instruments for the purposes of subsection 125-75(4) of the ITAA 1997. Since the executive options accounted for approximately 3.75% of the total ownership interests in Tower at the time of the demerger, these options were disregarded in working out whether the requirements in subsection 125-70(2) of the ITAA 1997 were met (subsection 125-75(4) of the ITAA 1997).

Participating shareholders who choose demerger rollover

69. For participating shareholders who choose demerger rollover, a capital gain or capital loss made from CGT event C2 happening to their cancelled Tower shares under the demerger is disregarded (subsection 125-80(1) of the ITAA 1997).

70. Each participating shareholder was required to calculate the first element of the cost base and reduced cost base of their remaining Tower shares and their corresponding new TAL shares just after the demerger (subsections 125-80(2) and (3) of the ITAA 1997).

71. Section 125-80 of the ITAA 1997 requires participating shareholders to have apportioned the total cost bases of their pre-demerger Tower shares over their remaining Tower shares and the new TAL shares. The apportionment must have had regard to the relative market values of the Tower and TAL shares (or anticipated reasonable approximations of those market values) just after the demerger. Tower has advised shareholders of these proportions following the demerger; they are as follows:

- 39.25% of the total cost base of the pre-demerger Tower shares to be apportioned over the remaining Tower shares; and
- 60.75% of the total cost base of the pre-demerger Tower shares to be apportioned over the new TAL shares

These proportions are based on the volume weighted average price of the Tower and TAL shares in the first five ASX trading days after TAL was listed.

Participating shareholders who do not choose demerger rollover

72. For participating shareholders who do not choose demerger rollover, any capital gain or capital loss made from CGT event C2 happening to their cancelled Tower shares under the demerger is not disregarded. Any capital gain made by a participating shareholder under CGT event C2 is reduced by the amount of the demerger dividend received under the demerger (subsection 118-20(4) of the ITAA 1997).

73. The method of calculating the first element of the cost base and reduced cost base for a participating shareholder's remaining Tower shares and the new TAL shares is the same whether or not rollover is chosen (see paragraph 71 of this Ruling, subsection 125-85(2) of the ITAA 1997 and Note 1 to subsection 125-80(2) of the ITAA 1997).

Acquisition date of the TAL shares for the purposes of the CGT discount

74. Before a capital gain can be reduced by the CGT discount, one of the conditions that must be satisfied is that the capital gain relates to an asset that was owned for at least 12 months (subsection 115-25(1) of the ITAA 1997).

75. For the purposes of this 12 month ownership condition, participating shareholders are taken to have acquired the TAL shares received under the demerger on the date they acquired the corresponding cancelled Tower shares (item 2 in the table in subsection 115-30(1) of the ITAA 1997).

Note: for general CGT purposes, shareholders acquired their TAL shares when those shares were received under the demerger (section 109-10 of the ITAA 1997). This means, for example, that when calculating a capital gain on the subsequent disposal of these TAL shares, indexation will not be included in the cost base of those shares.

Demerger dividend

76. Subsection 44(1) of the ITAA 1936 operates to include in a shareholder's assessable income any dividends, within the meaning of that term in subsection 6(1) of the ITAA 1936, paid to a shareholder out of company profits.

77. Paragraph (d) of the definition of dividend in subsection 6(1) of the ITAA 1936 provides that a dividend excludes amounts debited against an amount standing to the credit of the share capital account of the company.

78. In the circumstances of this demerger, Tower debited an amount of NZ\$454 million (or approximately NZ\$2.65 (A\$2.29)) per cancelled share) to its 'share capital account' as that term is defined in subsection 6(1) of the ITAA 1936 and section 975-300 of the ITAA 1997. This amount is therefore not a dividend for the purposes of subsection 6(1) of the ITAA 1936 and is not assessable as a subsection 6(1) dividend under subsection 44(1) of the ITAA 1936.

79. However, participating shareholders did receive a dividend to the extent that the market value of the TAL shares distributed under the demerger exceeded the amount debited against the share capital account (see Taxation Ruling TR 2003/8).

80. The market value of the 1.3677758 TAL shares received under the demerger as consideration for the cancellation of each Tower share was A\$3.17. The dividend received by Tower shareholders for each Tower share that was cancelled was therefore A\$0.88 (A\$3.17 – A\$2.29).

81. This dividend is neither an assessable income nor an exempt income amount (subsections 44(3) and (4) of the ITAA 1936) if:

- the dividend is a demerger dividend (as defined in subsection 6(1) of the ITAA 1936);
- the head entity did not elect that subsections 44(3) and (4) of the ITAA 1936 do not apply to the demerger dividend (subsection 44(2) of the ITAA 1936); and
- subsection 44(5) of the ITAA 1936 is satisfied.

82. In the present circumstances, each of the conditions in paragraph 81 of this Ruling are satisfied. Therefore, the dividend received by participating shareholders under the demerger is neither assessable income nor exempt income by operation of subsections 44(3) and (4) of the ITAA 1936.

Application of sections 45B, 45BA and 45C

83. Section 45B of the ITAA 1936 applies to ensure that relevant amounts are treated as dividends for taxation purposes if:

- (a) components of a demerger allocation as between capital and profit do not reflect the circumstances of the demerger; or
- (b) certain payments, allocations and distributions are made in substitution for dividends.

84. Specifically, the provision applies where:

- there is a scheme under which a person is provided with a demerger benefit or capital benefit by a company (paragraph 45B(2)(a) of the ITAA 1936);
- under the scheme a taxpayer, who may or may not be the person provided with the demerger benefit or the capital benefit, obtains a tax benefit (paragraph 45B(2)(b) of the ITAA 1936); and
- having regard to the relevant circumstances of the scheme, it would be concluded that the person, or one of the persons, who entered into the scheme or carried out the scheme or any part of the scheme did so for a purpose, other than an incidental purpose, of enabling a taxpayer to obtain a tax benefit (paragraph 45B(2)(c) of the ITAA 1936).

85. Where the requirements of subsection 45B(2) of the ITAA 1936 are met, subsection 45B(3) of the ITAA 1936 empowers the Commissioner to make a determination under either section 45BA of the ITAA 1936 in relation to a demerger benefit or section 45C of the ITAA 1936 in relation to a capital benefit.

Scheme, demerger and capital benefit

86. The restructure that is the subject of this Ruling constitutes a 'scheme' within the broad meaning of that term (subsection 45B(10) of the ITAA 1936).

87. The provision of ownership interests to a shareholder under a demerger constitutes the shareholder being provided with a demerger benefit (subsection 45B(4) of the ITAA 1936) and a capital benefit (subsection 45B(5) of the ITAA 1936) to the extent that the demerger benefit is not a demerger dividend (subsection 45B(6) of the ITAA 1936).

88. In the present scheme, therefore, the provision of the TAL shares constitutes the participating shareholders receiving a demerger benefit and a capital benefit.

Tax benefit

89. For most shareholders, the tax payable on the demerger benefit and the capital benefit is less than it would be if they had been an assessable dividend or a dividend, respectively. This arises because the CGT and dividend concessions ensure that the demerger is largely free of tax for shareholders. As such, the provision of those benefits constitutes the participating shareholders obtaining a tax benefit (subsection 45B(9) of the ITAA 1936).

Purpose

90. In this case, while the conditions of paragraphs 45B(2)(a) and 45B(2)(b) of the ITAA 1936 are met, the requisite purpose of enabling the participating shareholders to obtain a tax benefit (by way of a demerger benefit or a capital benefit) is not present. In other words, having regard to the relevant circumstances of the scheme set out in subsection 45B(8) of the ITAA 1936, it would not be concluded that any of the parties to the demerger entered into or carried out the scheme to obtain a tax benefit in the form of a demerger benefit or a capital benefit.

91. Those circumstances, particularly those enumerated in paragraph 177D(b) of the ITAA 1936 and incorporated by operation of paragraph 45B(8)(k) of the ITAA 1936, are concerned with the commercial or business effects of the demerger. Under the scheme, it is apparent that a substantial purpose of the demerger was to achieve the geographic separation of two distinct businesses which, following their separation, will apply independent business strategies tailored to their own specific commercial objectives. This is consistent with the underlying object of the demerger measures.

92. It is also apparent from the circumstances of the demerger that the capital and profit components of the demerger allocation are consistent with the commercial circumstances of the transaction. The share capital distributed under this demerger was determined by reference to the market value of TAL relative to the market value of the Tower group.

93. In addition, there is nothing in the other relevant circumstances of the demerger, including Tower's distribution history or the known circumstances of the shareholders, to suggest that the favourable tax outcome under the demerger for the participating shareholders is anything more than a natural incident of the business restructure.

94. Therefore, the Commissioner will not make a determination under either paragraph 45B(3)(a) or (b) of the ITAA 1936 that sections 45BA or 45C of the ITAA 1936 apply to the scheme.

Appendix 2 – Detailed contents list

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

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Previous draft:

Not previously issued as a draft

Related Rulings/Determinations:

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Subject references:

- capital benefit
- capital gains
- cost base adjustments
- demerger
- demerger allocation
- demerger benefit
- demerger dividend
- demerger group
- demerger subsidiary
- return of capital rollover
- schemes to provide certain benefits

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