


CR 2008/63 - Income tax: scrip for scrip: merger of St George Bank Limited and Westpac Banking Corporation

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Class Ruling

Income tax: scrip for scrip: merger of St George Bank Limited and Westpac Banking Corporation

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

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

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

What this Ruling is about

1. This Ruling sets out the Commissioner's opinion on the way in which the relevant provisions 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);
- Division 1A of the former Part IIIA of the ITAA 1936;
- section 177EA of the ITAA 1936;
- section 104-10 of the *Income Tax Assessment Act 1997* (ITAA 1997);
- section 109-10 of the ITAA 1997;
- section 110-25 of the ITAA 1997;
- section 112-30 of the ITAA 1997;
- Subdivision 115-A of the ITAA 1997;

- section 116-20 of the ITAA 1997;
- section 116-40 of the ITAA 1997;
- Subdivision 124-M of the ITAA 1997;
- section 204-30 of the ITAA 1997;
- Division 207 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 whom this Ruling applies consists of entities who were ordinary shareholders of St George Bank Limited (St George) at the time of the scheme, and who:

- (a) held their St George ordinary shares (St George Shares) on capital account at that time;
- (b) exchanged their St George Shares for ordinary shares in Westpac Banking Corporation (Westpac) under the scheme; and
- (c) were 'residents of Australia' within the meaning of that expression in subsection 6(1) of the ITAA 1936 at that time.

In this Ruling an entity belonging to this class of entities is referred to as a 'St George shareholder'.

4. The equities and options referred to in paragraph 26 to 28 are not covered by this Ruling.

5. This ruling does not consider how the gross-up and tax offset rules in Division 207 apply to partnerships or trustee holders in receipt of the Final Dividend and Special Dividend, or to indirect distributions of these dividends to partners in a partnership, or beneficiaries or trustees of a trust.

Qualifications

6. The Commissioner makes this Ruling based on the proposed scheme precisely identified in this Ruling.

7. 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 15 to 32 of this Ruling.

8. 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

10. This Ruling applies from 1 July 2008 to 30 June 2009. However, the Ruling continues to apply after 30 June 2009 to all entities within the specified class who entered into the specified scheme during the term of the Ruling.

11. 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.

12. 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)).

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

14. 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

15. The following description of the scheme is based on documents and information provided by Greenwoods & Freehills Pty Limited, the applicant for this Ruling (the Applicant). These documents include the following:

- Merger Implementation Agreement dated 26 May 2008 between Westpac and St George;
- Amended and restated Merger Implementation Agreement dated 8 September 2008 between Westpac and St George;
- Applications for a Class Ruling dated 25 July and 31 July 2008 lodged by the Applicant on behalf of St George; and
- St George Bank Limited Scheme Booklet dated 29 September 2008.

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

Overview

16. The scheme that is the subject of this Ruling involves the merger of St George and Westpac.

St George

17. As at 29 September 2008 St George had the following shares on issue which were listed on the Australian Securities Exchange (ASX):

- fully paid ordinary shares;
- subordinated adjustable income non-refundable Tier 1 securities (SAINTS) which are non-cumulative, redeemable, convertible preference shares;
- non-cumulative unsecured preference shares (SPS);
- non-cumulative, unsecured, converting preference shares (CPS); and
- non-cumulative, unsecured, converting preference shares (CPS II).

18. All shares were acquired by St George shareholders on or after 20 September 1985.

19. At the same date, St George also had on issue the following rights and shares which were not listed on the ASX:

- options to acquire St George Shares under St George employee share schemes (employee options);
- redeemable preference depositor shares (depositor shares); and
- redeemable preference borrower shares (borrower shares).

Disposal of St George Shares

20. On 26 May 2008, St George and Westpac jointly announced that they had signed a Merger Implementation Agreement for a proposed merger of the two companies. An amended and restated Merger Implementation Agreement was signed by the parties on 8 September 2008.

21. The proposed merger is to be implemented by way of a scheme of arrangement under Part 5.1 of the *Corporations Act 2001* (Corporations Act) between St George and St George Shareholders (Scheme of Arrangement). The Scheme of Arrangement is subject to the approval of St George shareholders, the Federal Court of Australia and various regulatory bodies.

22. Under the Scheme of Arrangement, on the Implementation Date of 1 December 2008, all ordinary shares in St George will be transferred to Westpac in exchange for Westpac issuing new shares to the ordinary shareholders of St George.

23. St George ordinary shareholders will receive 1.31 fully paid ordinary shares in Westpac for each ordinary share they held on 24 November 2008 (the Scheme Record Date).

24. As a result, all St George ordinary shares will be owned by Westpac.

Foreign shareholders

25. Westpac shares will not be issued to certain ordinary shareholders of St George whose address is in a place outside Australia, New Zealand, the UK, US, Hong Kong and Singapore (foreign shareholders). The relevant Westpac shares will instead be issued to a nominee agent who will sell them on the ASX and will pay the net proceeds to each foreign shareholder.

SAINTS, SPS, CPS, CPS II, depositor shares, borrower shares and employee options

26. The SAINTS, SPS, CPS, CPS II, depositor shares and borrower shares are not voting shares as defined by section 9 of the Corporations Act.

27. The SAINTS and employee options granted under the Executive Performance Share Plan (Award Options) are the subject of separate schemes of arrangement under Part 5.1 of the Corporations Act.

28. The SAINTS, SPS, CPS, CPS II, depositor shares, borrower shares and Award options will not be acquired by Westpac under the scheme of arrangement to which this Ruling applies.

Dividends

29. St George will declare a Final Dividend on St George Shares for the 2008 Financial Year and a Special Dividend on St George Shares on 29 October 2008. The amount of the Final Dividend and Special Dividend will be announced when declared on 29 October 2008. The aggregate amount of the Final Dividend and Special Dividend will not exceed \$1.25 per ordinary share. St George will pay its Final Dividend, and the Special Dividend on 18 December 2008. Shareholders entitled to the Final Dividend and Special Dividend are those St George shareholders registered on 24 November 2008, the Record Date.

30. St George will pay the Final Dividend and the Special Dividend regardless of whether shareholders vote in favour of the Scheme of Arrangement or whether the Scheme of Arrangement will come into effect under subsection 411(10) of the Corporations Act.

31. Both the Final Dividend and the Special Dividend will be fully franked and will be debited against St George's retained profits account.

Other matters

32. There are no 'significant stakeholders' or 'common stakeholders' in relation to the scheme within the meaning of those expressions in section 124-783.

Ruling

Capital Gains Tax

CGT event A1 happens on the disposal of St George Shares

33. CGT event A1 will happen as a result of the disposal by a St George shareholder of each of their St George Shares to Westpac on 1 December 2008, the Implementation Date (subsections 104-10(1) and 104-10(2)).

34. The time of the event will be 1 December 2008, (paragraph 104-10(3)(b)).

Capital gain or capital loss

35. A St George shareholder will make a capital gain from CGT event A1 happening if the capital proceeds from the disposal of a St George Share exceed its cost base. A St George shareholder will make a capital loss if those capital proceeds are less than the St George Share's reduced cost base (subsection 104-10(4)).

Capital proceeds

36. The capital proceeds for each St George Share will be the market value of the 1.31 Westpac shares received in respect of the event happening, worked out as at the time of the event (subsections 116-20(1) and 116-40(1)).

37. The Commissioner accepts that the market value of Westpac shares on 1 December 2008 may be determined by reference to the volume weighted average price (VWAP) of Westpac shares traded on the ASX on that day.

38. The Final Dividend and the Special Dividend will not form part of the capital proceeds received by a St George shareholder from the disposal of a St George Share.

If a capital loss is made

39. If a St George shareholder makes a capital loss from the disposal of their St George Shares, they cannot choose scrip for scrip roll-over under Subdivision 124-M (subsection 124-780(3)).

If a capital gain is made

40. Subject to the qualification in paragraph 41 of this Ruling, a St George shareholder who makes a capital gain from the disposal of a St George Share may choose scrip for scrip roll-over under Subdivision 124-M (section 124-780).

41. Scrip for scrip roll-over cannot be chosen if any capital gain the St George shareholder might make from the replacement Westpac share would be disregarded, except because of a roll-over (subsection 124-795(2)).

If scrip for scrip roll-over is chosen

42. If a St George shareholder chooses scrip for scrip roll-over, the capital gain made from the disposal of a St George Share is disregarded (subsection 124-785(1)).

If scrip for scrip roll-over is not chosen

43. If a St George shareholder does not choose scrip for scrip roll-over, the capital gain made from the disposal of a St George Share is not disregarded.

44. St George shareholders who dispose of a St George Share and make a capital gain that is not disregarded are eligible to treat the capital gain as a 'discount capital gain' provided that they satisfy the requirements of Subdivision 115-A.

Cost base of Westpac shares

If scrip for scrip roll-over is chosen

45. Where scrip for scrip roll-over is chosen, the first element of the St George shareholder's cost base and reduced cost base of each Westpac share is worked out by reasonably attributing to it part of the cost base of the St George Share exchanged for the relevant Westpac share (subsections 124-785(2) and 124-785(4)).

If scrip for scrip roll-over is not, or cannot be chosen

46. Where scrip for scrip roll-over is not, or cannot, be chosen, the first element of the St George shareholder's cost base and reduced cost base of each Westpac share is equal to the market value of part of the St George Share exchanged for the relevant Westpac share (subsection 110-25(2) and subsection 112-30(1)).

47. The Commissioner will accept the market value of the 1.31 Westpac shares received by the St George shareholder on 1 December 2008 as the market value of the St George Share exchanged. The market value of Westpac shares on 1 December 2008 may be determined by reference to the VWAP of Westpac shares traded on the ASX on that day.

Acquisition date of Westpac shares

48. St George shareholders will acquire their Westpac shares on the date those shares are issued to each St George shareholder, that is, 1 December 2008 (item 2 in the table in section 109-10).

49. For the purposes of determining if a capital gain made on any later disposal of their Westpac shares is a discount capital gain, St George shareholders who choose scrip for scrip roll-over are taken to have acquired their Westpac shares when they acquire the corresponding St George Share(s) (item 2 in the table in subsection 115-30(1)).

Dividends received**Inclusion of Dividends in assessable income**

50. St George shareholders must include in their assessable income the Dividends received under subparagraph 44(1)(a)(i) of the ITAA 1936.

51. Subject to the St George shareholder being a qualified person, the St George shareholder must include in their assessable income an amount equal to the franking credit received on those Dividends under subsection 207-20(1).

Entitlement to a tax offset

52. St George shareholders who are required to include an amount equal to the franking credit in their assessable income will be entitled to a tax offset equal to the franking credit under subsection 207-20(2), provided the requirements of Division 207 are satisfied.

Qualified persons

53. Having regard to the relevant circumstances of the scheme, nothing in the offer documents indicates that the St George shareholder has made, is under an obligation to make, or is likely to make a related payment in respect of the Dividends.

54. As the St George shareholders are not taken, for the purposes of Division 1A of the former Part IIIA of the ITAA 1936, to be under an obligation to make a related payment in respect of the Dividends as a result of the scheme, the relevant holding period is therefore the primary qualification period pursuant to former paragraph 160APHO(1)(a) of the ITAA 1936.

55. For those St George shareholders that have not previously satisfied the primary qualification period for the purposes of Division 1A of former Part IIIA of the ITAA 1936, they will be considered to have satisfied the holding period rule under former section 160APHO of the ITAA 1936 and therefore be a qualified persons in relation to the dividends if:

- (a) the St George shareholder acquired the St George Share or interest in the share on or before 9 October 2008; and
- (b) during the period when the share or interest in the share was held, the St George shareholder did not have 'materially diminished risks of loss or opportunities for gain' (as defined under former section 160APHM of the ITAA 1936) for a continuous period of at least 45 days.

Anti-avoidance provisions-imputation benefits

56. The Commissioner will not make a determination pursuant to paragraph 204-30(3)(c) in respect of the payment of the Dividends.

57. The Commissioner will not make a determination pursuant to paragraph 177EA(5)(b) of the ITAA 1936 in respect of the Dividends.

Commissioner of Taxation

22 October 2008

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.*

Capital Gains Tax

58. The tax consequences and relevant legislative provisions that arise concerning the scheme that is the subject of this Ruling are outlined in the Ruling part of this document.

59. The significant tax consequence is the availability of scrip for scrip roll-over under Subdivision 124-M. It enables a shareholder to disregard 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. It also provides special rules for calculating the cost base and reduced cost base of the replacement share.

60. Subdivision 124-M contains a number of conditions that determine whether scrip for scrip roll-over is available under an arrangement. The main conditions and exceptions that are relevant to the circumstances of the merger of St George and Westpac are:

- (a) shares are exchanged for shares in another company;
- (b) the exchange occurs as part of a single arrangement;
- (c) conditions for roll-over are satisfied;
- (d) further conditions are not applicable or are satisfied;
and
- (e) exceptions to obtaining scrip for scrip roll-over are not applicable.

61. Under the scheme the conditions for roll-over under Subdivision 124-M are satisfied.

Capital proceeds

62. The capital proceeds for each St George Share will be the market value of the Westpac ordinary shares received as consideration for the disposal of each St George Share (subsection 116-20(1)).

63. The Scheme Consideration is not calculated by reference to, or connected in any way, with the amount of the Final Dividend or the Special Dividend, and the declaration and payment of these dividends is not a term of the merger. Further, the declaration and payment of the dividends is not contingent upon the merger going ahead. Accordingly, the Final Dividend and the Special Dividend will not form part of the capital proceeds for the disposal of the St George Shares.

Dividends received

Inclusion of dividends in assessable income

64. Subsection 44(1) of the ITAA 1936 requires that the assessable income of a resident shareholder in a company include dividends that are paid to the shareholder by the company out of profits derived by it from any source.

Inclusion of franking credits in assessable income

65. Subject to the St George shareholder being a qualified person, the St George shareholder must include in their assessable income an amount equal to the franking credit received on those Dividends under subsection 207-20.

Qualified Persons

66. Unless otherwise stated, the law applies in the same way to both the Final Dividend and the Special Dividend and therefore a reference to 'the Dividend' in paragraphs 66 to 74 is taken to be a reference to the Final Dividend or the Special Dividend, as the case may be.

67. Pursuant to paragraph 207-145(1)(a), a St George shareholder must be a 'qualified person' in relation to the Dividend in order to be entitled to the franking credit on the Dividend.

68. Broadly, to be a 'qualified person' in relation to the Dividend, the shareholder must hold the shares 'at risk' during the relevant holding period. Where the related payment rule does not apply, the primary qualification period will be the relevant holding period. Where the related payment rule does apply, the secondary qualification period will be the relevant holding period.

Related payment rule

69. The related payment rule applies where a St George shareholder or an associate has made, is under an obligation to make, or is likely to make, a related payment in respect of the Dividend.

70. A St George shareholder is taken to have made, to be under an obligation to make, or to be likely to make, a related payment in respect of the Dividend if, under an arrangement, the St George shareholder or associate has done, is under an obligation to do, or may reasonably be expected to do, as the case may be, anything having the effect of passing the benefit of the Dividend to one or more other persons.

71. Having regard to the relevant circumstances of the scheme, it cannot be said that the offer documents indicate that a St George shareholder, or an associate of a St George shareholder, does anything that has the effect of passing the benefit of the Dividend to another person. The Dividend is to be paid regardless of whether or not the scheme is implemented, and therefore it has no effect on the total consideration paid by Westpac under the scheme. As the eligible shareholders are not taken, for the purposes of Division 1A of the former Part IIIAA of the ITAA 1936, to be under an obligation to make a related payment in respect of the Dividend as a result of the scheme, the relevant holding period is therefore the primary qualification period pursuant to former paragraph 160APHO(1)(a) of the ITAA 1936.

72. Accordingly, the holding period rule requires St George shareholders to hold the St George Shares, or the interest in the shares, on which the Dividend is paid at risk for a continuous period of at least 45 days during the period beginning from the day after the date of acquisition and ending on the 45th day after the day on which the shares became ex-dividend. In determining whether a shareholder has satisfied the holding period rule, any days during which there is a materially diminished risk in relation to the relevant shares are not counted.

73. Under former subsection 160APHM(2) of the ITAA 1936, a shareholder is taken to have materially diminished the risks of loss and opportunities for gain with respect to shares or interests in shares if the 'net position' of the shareholder results in the shareholder having less than 30% of the risks and opportunities relating to the shares or interest in shares.

74. It is considered that until the record date for the scheme, St George shareholders will not, by reason of the scheme, have done anything to materially diminish their risks of loss or opportunities for gain in respect of their St George Shares. There are 45 clear days between 9 October 2008 and 24 November 2008 (it should be noted that as the ex-dividend date for the Dividends is 25 November 2008, no days after the scheme record date will be capable of being counted to satisfy the at risk requirements, nor will the shares be considered at risk on the record date of 24 November 2008). Therefore, a St George shareholder who acquired shares on or after 10 October 2008 will not satisfy the holding period rule. Shares purchased on or before 9 October 2008 will satisfy the holding period rule as long as those shares are held at risk for at least 45 continuous days.

Anti-avoidance provisions - imputation benefits**Section 204-30**

75. Section 204-30 is a general anti-streaming measure. It is designed to curb the inappropriate use of franking credits through streaming arrangements. It permits the Commissioner to make determinations where an entity streams one or more distributions, whether in a single franking period or in a number of franking periods, in such a manner whereby:

- an imputation benefit is, or apart from section 204-30 would be, received by the member of the entity as a result of a distribution or distributions; and
- that member derives a greater benefit from franking credits than another member of the entity; and
- the other member of the entity receives a lesser imputation benefit, or receives no imputation benefits, whether or not the other member receives other benefits.

76. For section 204-30 of the ITAA 1997 to apply, members to whom distributions are streamed must derive a greater benefit from imputation benefits than other members. The words 'derives a greater benefit from franking credits' (imputation benefits) are defined in subsection 204-30(8) by reference to the ability of the members to fully utilise imputation benefits.

77. The St George Final Dividend and the Special Dividend will be paid to all holders of St George ordinary shares. The current proposal does not have any regard to the ability of the recipient shareholders to effectively utilise the franking credits in determining which shareholders will receive the franked distribution.

78. Therefore, it cannot be concluded that the dividends involve the payment of franked distributions in a selective manner to favoured members to the exclusion of disadvantaged members. Consequently, section 204-30 will not apply to the distribution.

Section 177EA

79. Section 177EA of the ITAA 1936 is a general anti-avoidance provision that applies to a wide range of schemes to obtain a tax advantage in relation to imputation benefits. Subsection 177EA(3) of the ITAA 1936 provides relevantly that the section applies if:

- (a) there is a scheme for a disposition of membership interests in a corporate tax entity; and
- (b) a frankable distribution has been paid, or is payable or expected to be payable, to a person in respect of the membership interests; and
- (c) the distribution was, or is expected to be, a franked distribution; and

- (d) except for this section, the person would receive, or could reasonably be expected to receive, imputation benefits as a result of the distribution; and
- (f) having regard to the relevant circumstances of the scheme, it would be concluded that the person, or one of the persons, who entered into or carried out the scheme or any part of the scheme did so for a purpose (whether or not the dominant purpose but not including an incidental purpose) of enabling the relevant taxpayer to obtain an imputation benefit.

80. In this instance, the Final Dividend and the Special Dividend are both frankable and are also a part of a scheme which includes the disposition of St George Shares. Therefore, section 177EA of the ITAA 1936 will apply if, having regard to the relevant circumstances of the scheme, it would be concluded that the person, or one of the persons, who entered into or carried out the scheme, did so for a non-incidental purpose of enabling the shareholders to obtain an imputation benefit.

81. Subsection 177EA(17) of the ITAA 1936 provides a non-exclusive list of 'relevant circumstances' to which one must have regard. The list includes a variety of matters (including the eight matters in subparagraphs 177D(b)(i) to (viii) of the ITAA 1936) which individually and collectively could indicate the requisite purpose; however not all of the circumstances listed will be relevant to every case.

82. The key circumstances of the Final Dividend and the Special Dividend are that they will be debited against St George's retained profits and will be payable indiscriminately to all of its shareholders. Furthermore, the declaration and payment of the Dividends are independent of the merger. These circumstances, individually and collectively, suggest that the requisite purpose for the application of section 177EA of the ITAA 1936 is not present and therefore the section will not apply in this case. Accordingly, the Commissioner will not seek to make a determination pursuant to paragraph 177EA(5)(b) of the ITAA 1936.

Appendix 2 – Detailed contents list

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References

Previous draft:

Not previously issued as a draft

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- takeovers & mergers

Legislative references:

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- ITAA 1997 104-10(2)
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ATO references

NO: 2008/16522

ISSN: 1445-2014

ATOlaw topic: Income Tax ~~ Assessable income ~~ dividend, interest and royalty income
 Income Tax ~~ Capital Gains Tax ~~ CGT event A1 - disposal of a CGT asset
 Income Tax ~~ Capital Gains Tax ~~ roll-overs - scrip for scrip