

# **CR 2009/78 - Income tax: Commonwealth Bank of Australia - Perpetual Exchangeable Resaleable Listed Securities**

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! The Deed entered into between the Commissioner and the Commonwealth Bank of Australia referred to in this Ruling can be accessed [here](#).

! This document has changed over time. This is a consolidated version of the ruling which was published on *1 October 2014*



## Class Ruling

# Income tax: Commonwealth Bank of Australia – Perpetual Exchangeable Resaleable Listed Securities

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### **ⓘ 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, 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.

**[Note:** This is a consolidated version of this document. Refer to the Legal Database (<http://law.ato.gov.au>) to check its currency and to view the details of all changes.]

## 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:

- subsection 6(1) of the *Income Tax Assessment Act 1936* (ITAA 1936);
- subsection 6(4) of the ITAA 1936;
- subsection 44(1) of the ITAA 1936;
- section 45 of the ITAA 1936;
- section 45A of the ITAA 1936;
- section 45B of the ITAA 1936;

- Division 1A of former Part IIIA of the ITAA 1936;
- section 177EA of the ITAA 1936;
- Schedule 2C of the ITAA 1936;
- Division 67 of the *Income Tax Assessment Act 1997* (ITAA 1997);
- Division 104 of the ITAA 1997;
- section 108-5 of the ITAA 1997;
- section 109-5 of the ITAA 1997;
- subsection 110-25(2) of the ITAA 1997;
- subsection 110-55(2) of the ITAA 1997;
- Subdivision 130-C of the ITAA 1997;
- section 204-30 of the ITAA 1997;
- section 207-20 of the ITAA 1997;
- section 207-30 of the ITAA 1997;
- section 207-35 of the ITAA 1997;
- section 207-145 of the ITAA 1997;
- subsection 974-75(1) of the ITAA 1997;
- subsection 974-120 of the ITAA 1997; and
- section 974-165 of the ITAA 1997.

### **Important: scope of this Ruling**

3. This Ruling should be read with the Deed (to which a link is attached in this Ruling) entered into between the Commissioner and the Commonwealth Bank of Australia (CBA) (the Deed). Nothing in this Ruling should be construed inconsistently with the Deed, and this Ruling is without prejudice to the rights of any person under the Deed.

4. This Ruling considers how the law applies to the scheme as set out in paragraphs 13 to 47 of this Ruling, but in some respects is dependent on the Commissioner not making a determination under paragraph 177EA(5)(b) of the ITAA 1936 in relation to the class of entities.

5. The Commissioner will not, subject to the Deed, and Clause 16 of the Note Terms or Clause 17 of the Preference Share Terms make a determination pursuant to paragraph 177EA(5)(b) of the ITAA 1936 in respect of frankable distributions on the Perpetual Exchangeable Resaleable Listed Securities (PERLS V) that are paid, payable or expected to be payable to any Holder, other than the Nominated Investor.

**Class of entities**

6. The class of entities to which this Ruling applies are the Australian resident individuals, companies, partnerships, trusts and complying superannuation entities who acquired the PERLS V issued by CBA from an Initial Holder (IH) and who hold the PERLS V on capital account.

7. The class of entities to which this Ruling applies are referred to as the 'Holders'.

8. The class of entities to which this Ruling applies excludes:

- Holders who do not acquire the PERLS V by way of submitting the Application Form attached to the PERLS V Prospectus for the offer of the PERLS V (that is, this Ruling only applies to Holders who have acquired the PERLS V from an IH under the PERLS V Prospectus);
- Holders who exercise their rights under Clause 5.1 of the Note Terms;
- Holders who make an election under Clause 16(b) of the Note Terms;
- Holders to whom a determination is made under paragraph 177EA(5)(b) of the ITAA 1936; and
- the Nominated Investor, as defined in the Deed.

**Qualifications**

9. 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 47 of this Ruling.

10. 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

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12. This Ruling applies from 1 July 2009 to 30 June 2016. The Ruling continues to apply after 30 June 2016 to all entities within the specified class who entered into the specified scheme during the term of the Ruling. However, this Ruling will 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 this Ruling (see paragraphs 75 and 76 of Taxation Ruling TR 2006/10).

## Scheme

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13. The following description of the scheme is based on information provided by Greenwoods & Freehills Pty Limited on behalf of CBA as the Applicant. These documents, or the relevant part/s of them, as the case may be, form part of and are to be read in conjunction with this description.

14. The relevant documents, or parts of documents, to be read in conjunction with this description are:

- the application for a Class Ruling dated 1 May 2009 and Revised application for a Class Ruling dated 18 August 2009;
- the PERLS V Prospectus dated 28 August 2009;
- the PERLS V Replacement Prospectus dated 7 September 2009 (PERLS V Prospectus);
- the Offer Management Subscription Agreement dated 17 August 2009;
- the PERLS V Note Deed Poll provided on 1 May 2009;
- the Preference Share Terms provided on 27 August 2009;
- the Note Terms provided on 27 August 2009;
- Deed of Settlement between CBA and the Commissioner executed 27 August 2009;
- Australian Prudential Regulation Authority (APRA) submission dated 1 May 2009;
- APRA submission dated 13 July 2009;
- Deed of Indemnity between CBA and CBA (New Zealand Branch) received 26 August 2009;
- CBA Media Release dated 7 September 2009;
- CBA Media Release dated 29 September 2009;

- application dated 16 September 2014 for an Addendum to Class Ruling CR 2009/78 from the Applicant on behalf of CBA; and
- amended Appendix B-Note Terms of the PERLS V Prospectus dated 7 September 2009 provided on 16 September 2014.

**Note:** certain information which relates to the affairs of CBA which is not in the public domain has been taken into account in determining the Commissioner's opinion set out in this Ruling (including the application of certain anti-avoidance provisions). This information has been provided on a commercial-in-confidence basis and will not be disclosed or released under the Freedom of Information legislation.

15. In this Ruling, unless otherwise defined, capitalised terms take their meaning as per the PERLS V Prospectus.

16. CBA is an authorised deposit-taking institution (ADI) and is required to comply with the capital requirements of APRA, which includes the maintenance of mandatory levels of Tier 1 Capital.

17. CBA has obtained approval from APRA that the PERLS V are Non-innovative Residual Tier 1 Capital and that they assist CBA in meeting its Tier 1 Capital requirement.

18. Each PERLS V is an instrument consisting of a bundle of rights which have the features of a Note and a Preference Share. The Holders will acquire the PERLS V from an IH for a price of \$200 each on 14 October 2009. Pursuant to the terms of the Offer in the PERLS V Prospectus, the Holder will acquire the PERLS V subject to the Note Deed Poll, the Note Terms and the Preference Share Terms. In doing so, the Holder is bound by, and subject to the terms of the offer made by the relevant IH to assign the Notes to CBA on the occurrence of a defined Assignment Event.

19. The PERLS V are listed on the Australian Securities Exchange (ASX) as stapled securities. When an Assignment Event occurs, the PERLS V will be destapled (that is the Notes will be destapled and transferred to CBA, or with the written approval of APRA, any other entity nominated by CBA that is (broadly) deemed to be part of CBA for the purposes of APRA guidelines (assignee)) without any further action being required by the Holder. After destapling, the PERLS V consisting solely of the Preference Shares then outstanding (as applicable) will remain listed on the ASX.

### **Main Features of the PERLS V**

#### ***Distributions in respect of the PERLS V***

20. Distributions payable in respect of the PERLS V are expected to be fully franked. To the extent that the Interest or Dividends are not franked to 100% under Part 3-6 of the ITAA 1997, the Holder will generally receive a gross-up of the distribution payable to the amount that would have been fully franked.

21. Generally, Interest and Dividends are scheduled to be paid quarterly in arrears on the Interest Payment Dates and Dividend Payment Dates. Interest will also be paid on 8 October 2014 for the period from 31 July 2014 to 30 September 2014. Where a Holder holds their PERLS V until 31 October 2014 they will also receive Interest, on that date, for the period from (and including) 1 October 2014 to 30 October 2014. Interest and Dividends are non-cumulative.

22. Dividends on the Preference Shares will only become payable after an Assignment Event (other than Conversion or Repurchase) has occurred, as the PERLS V will be comprised solely of the Preference Shares then outstanding. The Preference Shares will begin to accrue Dividends at the same rate as Interest that was payable on the Notes from and including:

- (a) the last Interest Payment Date for the Notes before the date on which the Assignment Event occurred; or
- (b) if no Interest Payment date has yet occurred, the date the Preference Shares were issued.

23. Distributions will not be paid to Holders of the PERLS V if the relevant conditions in the terms of the PERLS V are not satisfied.

24. If a distribution is not paid in full because the relevant conditions in the terms of the PERLS V are not satisfied, CBA has no liability to pay that distribution and Holders have no claim in respect of non-payment, notwithstanding the ability for an Optional Dividend to be paid (subject to APRA approval). However, if the unpaid amount is unpaid Interest, an Assignment Event may occur.

25. No interest accrues on any unpaid distribution, and the Holder has no claim or entitlement in respect of interest on any unpaid distribution.

26. Subject to certain exceptions, non-payment of a distribution will restrict CBA from paying certain distributions in respect of other specific instruments issued by CBA. The Holder of the PERLS V does not have a right to require redemption of the Notes for cash prior to the winding up of CBA.

### ***Deed between CBA and the Commissioner***

27. Subject to arrangements entered into between CBA and the Commissioner, franking credits will be allowed as a tax offset to Holders. The Commissioner expressed the view, prior to the issue of the PERLS V that paragraph 177EA(5)(b) of the ITAA 1936 may entitle him to make a determination that no imputation benefit is to arise to Holders in respect of distributions made on the PERLS V prior to the Assignment Event Date. CBA does not agree with the Commissioner's view that paragraph 177EA(5)(b) of the ITAA 1936 may apply. As a result the parties agreed that following the issue of the PERLS V, if the Commissioner forms the view that a determination would be made that paragraph 177EA(5)(b) of the

ITAA 1936 would apply, and the Holder might otherwise be denied franking credits, the dispute will be resolved in the manner set out in the Deed (to which a link is attached in this Ruling).

28. Essentially CBA intends to have the Commissioner's view tested in Court. CBA and the Commissioner have agreed to certain arrangements that will ensure that neither Holders nor the revenue will be impacted by this process. If the Commissioner's view is sustained in the representative case, CBA has agreed to indemnify the revenue for the amount that would be collected if each Holder's claim for a franking credit were to be denied. In practice, franking credits as a tax offset will be allowed to Holders, and will not be denied unless individual taxpayers request the Commissioner to do so.

29. Subject to paragraph 30 of this Ruling, each Holder agrees that pursuant to the Note Terms and the Preference Share Terms, if the Commissioner makes a determination under paragraph 177EA(5)(b) of ITAA 1936 in respect of any distribution relating to the Nominated Investor, each Holder:

- (a) will be bound, and will treat itself as bound, by the outcome of any administrative or judicial proceedings between CBA and the Commissioner in respect of the determination;
- (b) will not seek:
  - (i) an amended assessment of its taxation position in respect of the availability of the benefit of franking credits on any distributions on the PERLS V; or
  - (ii) a determination from the Commissioner under paragraph 177EA(5)(b) of the ITAA 1936 in respect of any distributions on the PERLS V, and
- (c) will, if CBA is required under any arrangement with the Commissioner to make a payment to the Commissioner in respect of any tax liability relating to any distributions on the PERLS V (whether received or expected to be received by that Holder), direct CBA to pay that amount to the Commissioner.

30. A Holder may elect by written notice to CBA not to be bound by these agreements in Clause 17 of the Preference Share Terms and Clause 16 of the Note Terms.

### ***Destapling of the PERLS V – Assignment Event***

31. On the Assignment Event Date, and if CBA accepts the Holder's offer to assign the relevant Notes to it, the following will broadly occur in relation to the PERLS V:

- (a) CBA and each Holder will be deemed to enter into an assignment agreement on the Assignment Event Date;

- (b) the relevant Notes will be destapled from the Preference Share to which they are stapled;
- (c) the Notes and the Holder's right, title and interest in the Notes are assigned to CBA on that date; and
- (d) all amounts payable in respect of the Notes after the occurrence of an Assignment Event will be payable to CBA, or the assignee.

32. If the Assignment Event is not a Conversion or Repurchase of the Preference Shares, the Holders will continue to hold the Preference Shares and the Preference Shares will become Dividend paying.

33. If the Assignment Event is a Conversion of the Preference Shares, the Preference Shares will be redeemed and the Holders will be issued a number of Ordinary Shares. The Conversion method is detailed in paragraph 36 of this Ruling.

34. An Assignment Event is defined in the Note Terms. An Assignment Event means the occurrence of any of the following events after the issue of the Preference Shares comprising part of the PERLS V:

- (a) a Default Event;
- (b) an APRA Event occurring (other than where it occurs because APRA appoints a statutory manager to the ADI) and APRA requiring that such APRA Event be an Assignment Event;
- (c) APRA appoints a statutory manager to the ADI;
- (d) APRA requiring that an Assignment Event occur (to the extent required by APRA);
- (e) CBA electing that an Assignment Event occur (to the extent elected by CBA);
- (f) the date the Preference Shares are Repurchased or converted prior to the Repurchase or Conversion taking effect;
- (g) Interest on the Notes or an Assignment Prevention Optional Dividend on the Preference Shares has not been paid in full to Holders within 20 Business Days of an Interest Payment Date; or
- (h) the Face Value of the Preference Shares has not been paid in full to Holders where the Preference Shares are to be Repurchased.

35. If CBA elects for an Assignment Event to occur, it may at its discretion, subject to APRA's prior written approval, in respect of some or all of the Preference Shares (and Notes which are attached), give notice to Holders to Repurchase for cash, convert into Ordinary Shares, or Resell if a Tax Event, Regulatory Event or Non-Operating Holding Company (NOHC) Event occurs.

**Conversion**

36. On the date for Conversion (a Relevant Date), CBA will convert all Preference Shares on issue at that date into CBA Ordinary Shares (Ordinary Shares). The Holders have no right to seek or initiate Conversion or Redemption of the Preference Shares. Any Dividend that is due and payable, but has not been paid on or before a Relevant Date, must be paid by CBA to the Holders. The Conversion of the PERLS V will be effected by way of:

- (a) An issue of a number of Ordinary Shares to the Holders with a 1% discount, in return for the issue and delivery of a Promissory Note from the Holders to CBA. Under the terms of the Promissory Note, each Holder agrees to pay CBA an amount (calculated in accordance with Clause 8.2(a) of the Preference Share Terms) that is equal to the Face Value per PERLS V. However, under no circumstances will any cash be payable by the Holder under the Promissory Note or otherwise.
- (b) Redemption of the PERLS V (that is, Redemption of the Preference Shares following the assignment of the Notes to CBA). The consideration for redemption payable by CBA (an amount equal to the Face Value per PERLS V) will be provided out of the proceeds of issue of the Ordinary Shares referred to in Clause 8.1 of the Preference Share Terms and by transferring the Promissory Note to the Holders and cancelling the Holders' obligations under the Promissory Note.

37. This Conversion mechanism was implemented by CBA to allow it to comply with the requirements of the current New Zealand taxation laws and the Australian *Corporations Act 2001*.

38. The Relevant Date will be the earlier of:

- (a) 31 October 2014, subject to the satisfaction of the Conversion Conditions; or
- (b) each Dividend Payment Date after 31 October 2014, on which the Conversion Conditions are satisfied.

39. In addition, CBA may elect to Resell all of the Preference Shares by giving a Resale Notice not less than 21 Business Days prior to the Relevant Date.

**Exchange**

40. CBA may, subject to APRA's prior written approval, give an optional Exchange Notice to Holders after the occurrence of a Regulatory Event, NOHC Event or Tax Event, to exchange all (but not some) of the Preference Shares.

41. Where an Acquisition Event occurs, CBA must give an Acquisition Event Notice to Holders as soon as practicable after becoming aware of that event. In such event and on the Exchange Date, subject to APRA's prior written approval, all (and not some) of the Preference Shares must be Exchanged. The Acquisition Exchange Notice provides for the Preference Shares to be either Repurchased or converted to Ordinary Shares.

## **Resale**

42. CBA may require all of the Holders to Resell their Preference Shares (and, if there has not been an Assignment Event, any corresponding Note forming part of the PERLS V) to a third party Purchaser. Once CBA has negotiated with the Purchaser, it will affect the Resale facility by issuing a Resale Notice, not less than 21 Business Days prior to the Relevant Date.

43. If CBA issues a Resale Notice:

- (a) each Holder is taken irrevocably to offer to sell the Preference Shares (and any corresponding Note forming part of the PERLS V) which CBA has elected to Resell to the Purchaser on the Exchange Date for a cash amount equal to the Face Value; and
- (b) on the Exchange Date, subject to payment by the Purchaser of the Face Value to the Holders, all right, title and interest in such Preference Shares (and any corresponding Note forming part of the PERLS V) will be transferred to the Purchaser.

## **The Offer**

44. The Offer to subscribe through the Prospectus for the PERLS V was available to:

- (a) Eligible Securityholders;
- (b) certain institutional investors; and
- (c) Australian clients of brokers to the PERLS V offer.

45. A Holder is an Eligible Securityholder if they have a registered Australian address and was a:

- (a) registered holder of PERLS II on 16 March 2009 (being the PERLS II redemption date);
- (b) holder of PERLS III;
- (c) holder of PERLS IV; or
- (d) holder of CBA Ordinary Shares.

46. The Offer to subscribe for PERLS V through the Prospectus for existing CBA holders without a registered Australian address was limited to certain institutional investors outside Australia, at the sole discretion of CBA and its Joint Lead Managers.

47. The PERLS V is listed on the ASX and trades under the ASX code CBAPA.

## Other matters

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48. This Ruling is made on the basis that:

- (a) the documents listed in paragraph 14 of this Ruling provide a complete and accurate description of the scheme;
- (b) the documents listed in paragraph 14 of this Ruling were intended by parties to have their legal effect and the scheme was implemented according to the terms of these documents;
- (c) during the term of the scheme, CBA will be a resident of Australia under the income tax laws of Australia;
- (d) distributions paid in respect of the PERLS V are frankable distributions under section 202-40 of the ITAA 1997 and are not unfrankable under section 202-45 of the ITAA 1997;
- (e) distributions on the PERLS V will, until the security is destapled, be paid on the Notes issued from the New Zealand Branch and, thereafter will be paid on the Preference Shares;
- (f) each PERLS V is an 'equity interest' in CBA under Division 974 of the ITAA 1997. This is because upon applying the debt/equity test embodied in Division 974 of the ITAA 1997, the PERLS V satisfies the equity test and does not satisfy the debt test;
- (g) CBA will frank the distributions in respect of the PERLS V at the same franking percentage as the benchmark for the franking period in which the payments are made;
- (h) the Ordinary Shares in CBA are 'equity interests' in CBA under Division 974 of the ITAA 1997;
- (i) a Holder, and their associates, do not have any positions (within the meaning of former section 160APHJ of the ITAA 1936) in relation to the PERLS V apart from the holding of the PERLS V themselves that would cause a Holder not to be a 'qualified person' for the purposes of Division 1A of former Part IIIAA of the ITAA 1936;

- (j) a Holder and their associates will not make any related payments (within the meaning of former section 160APHN of the ITAA 1936) in relation to distributions payable in respect of the PERLS V;
- (k) Holders will not dispose of their PERLS V before a period of at least 90 days (excluding the day of acquisition and the day of disposal) beginning the day after the acquisition of the PERLS V;
- (l) CBA will not differentially frank distributions to different Holders in respect of the PERLS V according to the tax status of the Holders or on any other basis;
- (m) the dividend payout ratios or CBA's policies in relation to the franking of Ordinary Share capital or other Preference Share capital of CBA are not expected to change as a result of the issue of the PERLS V;
- (n) distributions and any gross-up amounts payable in respect of the PERLS V, and Dividends and any gross-up amounts payable in respect of the PERLS V following an Assignment Event (other than Conversion or Repurchase), will not be debited to CBA's share capital account, or its non-share capital account;
- (o) the share capital of CBA will not become tainted by an issue of the PERLS V or the Ordinary Shares of CBA on Conversion of the PERLS V within the meaning of Subdivision 197-A of the ITAA 1997; and
- (p) no Interest, Dividends or any gross-up amounts will be sourced, directly or indirectly, from CBA's share capital account.

## Ruling

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**❶** *To be read with the 'Scope of this Ruling' section contained in paragraphs 3 to 5 of this Ruling*

### **Single CGT asset**

49. Each PERLS V is a single CGT asset (section 108-5 of the ITAA 1997), arising from a single contract between CBA and the Holder.

### **Acquisition time of the PERLS V**

50. Each Holder acquired the PERLS V from an IH on the date the contract was entered into (section 109-5 of the ITAA 1997).

**Cost base and reduced cost base**

51. The first element of the cost base and reduced cost base for each PERLS V is \$200, being the amount paid by the Holder to acquire the PERLS V from an IH (subsections 110-25(2) and 110-55(2) of the ITAA 1997).

**Inclusion of Interest and Dividends in assessable income**

52. Distributions described as 'Interest' and 'Dividends' payable in respect of each PERLS V are non-share dividends under section 974-120 of the ITAA 1997 and dividends under subsection 6(1) of the ITAA 1936 respectively. Holders must include in their assessable income all non-share dividends and dividends received in respect of the PERLS V (paragraph 44(1)(a) of the ITAA 1936). The Holders must also include in their assessable income an amount equal to the franking credits attached to the non-share dividends and dividends respectively (subsection 207-20(1) of the ITAA 1997).

**Entitlement to a tax offset**

53. Holders will be entitled to a tax offset equal to the franking credit received on the non-share dividends and dividends paid in respect of the PERLS V (subsection 207-20(2) of the ITAA 1997) unless and until a determination is made under paragraph 177EA(5)(b) of the ITAA 1936 in the circumstances described in paragraphs 3 to 5 and 27 to 30 of this Ruling.

**Franking credit subject to the refundable tax offset rules**

54. Holders who are entitled to a tax offset under subsection 207-20(2) of the ITAA 1997, in respect of the franking credits received in relation to the PERLS V, will be subject to the refundable tax offset rules in Division 67 of the ITAA 1997, unless they are specifically excluded under section 67-25 of the ITAA 1997.

**Gross-up and tax offset denied in certain circumstances**

55. For the purposes of Division 1A of former Part IIIAA of the ITAA 1936, a Holder will be considered to be a 'qualified person' in relation to the non-share dividends and dividends payable in respect of the PERLS V provided that, pursuant to former section 160APHO of the ITAA 1936:

- the Holder holds the PERLS V at risk for a continuous period of at least 90 days (excluding the day of acquisition and the day of disposal, and any days on which the Holder has materially diminished risks of loss or opportunities for gain in respect of the shares or interest within the meaning of former sections 160APHM and 160APHJ of the ITAA 1936); and

- neither the Holder, nor an associate of the Holder, has made or is under an obligation to make a related payment (within the meaning of former section 160APHN of the ITAA 1936) in respect of the non-share dividends and dividends payable in respect of the PERLS V.

56. The following will not affect whether the PERLS V are held 'at risk' for the purposes of Division 1A of former Part IIIAA of the ITAA 1936:

- the irrevocable offer by Holders to assign the Notes on the occurrence of an Assignment Event date, and
- the irrevocable offer by Holders to sell their PERLS V (or Preference Shares, where an Assignment Event that is not a Conversion or Repurchase has occurred) to a Purchaser if CBA issues a Resale Notice.

57. The following product features do not affect a Holder's risks of loss or opportunities for gain in respect of the PERLS V for the purposes of being qualified persons under former section 160APHO of the ITAA 1936:

- the Resale facility, and
- the Conversion process.

58. Section 207-145 of the ITAA 1997 will not apply to the whole, or any part, of the non-share dividends or dividends received by the relevant Holders. Accordingly, the franking credits will not be excluded from the Holders' assessable income under sections 207-30 and 207-35 of the ITAA 1997.

## **Imputation integrity provisions**

59. The Commissioner will not make a determination under paragraph 204-30(3)(c) of the ITAA 1997 to deny the whole, or any part, of the imputation benefits received in relation to the non-share dividends and dividends received by the Holders in respect of the PERLS V.

60. The Commissioner will not make a determination under paragraph 177EA(5)(b) of the ITAA 1936 to deny the whole, or any part, of the imputation benefits received in relation to the dividends received by Holders in respect of the Preference Shares on issue (following the occurrence of an Assignment Event that is not a Conversion or Repurchase) or an issue of Ordinary Shares (following a Conversion of PERLS V).

## **PERLS V are convertible interests**

61. The PERLS V is a convertible interest under item 4 of the table in subsection 974-75(1) of the ITAA 1997 and within the meaning of section 974-165 of the ITAA 1997.

**Assignment Event – CGT implications**

62. CGT event H2 (section 104-155 of the ITAA 1997) will happen to the Holders when an Assignment Event occurs. However, no Holder will make a capital gain or capital loss, as there are no capital proceeds because of the event, and no incidental costs are incurred in respect of the event. No other CGT event will happen to the Holders when an Assignment Event other than Conversion occurs.

**Conversion of the PERLS V – CGT implications**

63. CGT event C2 (section 104-25 of the ITAA 1997) will happen to the Holders because of the Conversion of the PERLS V. As part of the Conversion, each PERLS V (consisting solely of a Preference Share at that time) will be redeemed by CBA.

64. Any capital gain or capital loss made by a Holder from CGT event C2 happening on redemption of the PERLS V will be disregarded (subsection 130-60(3) of the ITAA 1997).

**Issue of Ordinary Shares – assessable income**

65. Pursuant to subsection 6(4) of the ITAA 1936, the value of the issued Ordinary Shares on Conversion of the PERLS V will not be a 'dividend' as defined in subsection 6(1) of the ITAA 1936. As such, the value of the issued Ordinary Shares will not be included in the Holder's assessable income under subsection 44(1) of the ITAA 1936.

**Section 45**

66. Section 45 of the ITAA 1936 will not apply to treat the Ordinary Shares issued on an occurrence of an Assignment Event that is a Conversion as an unfranked dividend paid by CBA.

**Section 45A**

67. The Commissioner will not make a determination under subsection 45A(2) of the ITAA 1936 that the whole or part of the capital benefit that arises upon a Conversion of Preference Shares is an unfranked dividend in the hands of the Holders.

**Section 45B**

68. The Commissioner will not make a determination under subsection 45B(3) of the ITAA 1936 that the whole or part of the capital benefit that arises upon an Assignment Event occurring is an unfranked dividend in the hands of the Holders.

## **Cost base of the Ordinary Shares**

69. The PERLS V are convertible interests. When an Assignment Event occurs that results in the Conversion of the PERLS V, Subdivision 130-C of the ITAA 1997 will apply so that the first element of the cost base and reduced cost base of the converted PERLS V (being Ordinary Shares in CBA) will be the cost base of the PERLS V at the time of the Conversion (item 2 of the table in subsection 130-60(1) of the ITAA 1997).

## **Cost base of the PERLS V (consisting solely of Preference Shares)**

70. When an Assignment Event occurs that does not result in the Conversion of the PERLS V, the cost base and reduced cost base of the PERLS V (consisting solely of Preference Shares) will remain the same.

## **Date of acquisition of the Ordinary Shares**

71. The PERLS V are convertible interests. When an Assignment Event occurs that results in the Conversion of the PERLS V, the converted PERLS V (being Ordinary Shares in CBA) are taken to have been acquired by the Holder when the Conversion of the PERLS V happened (subsection 130-60(2) of the ITAA 1997).

## **Commercial debt forgiveness**

72. When CBA transfers a Promissory Note (being a debt owed by a Holder) to a Holder and cancels the Holder's obligations under it, a commercial debt of the Holder is forgiven. However, there is no forgiven amount in respect of the debt. Subdivisions 245-D to 245-G of Schedule 2C to the ITAA 1936 do not apply in respect of the debt (paragraph 245-75(2)(b) of Schedule 2C to the ITAA 1936). Certain tax attributes that would be taken into account in calculating a Holder's taxable income will not be modified by Schedule 2C to the ITAA 1936.

## **Appendix 1 – Explanation**

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**①** *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.*

### **Acquisition time of the PERLS V**

73. Where an entity disposes of a CGT asset to you (except where you compulsorily acquire it), you acquire the CGT asset at the time when the disposal contract is entered into or, if no contract is entered into, when the entity stops being the asset's owner (item 1 of the table in subsection 109-5(2) of the ITAA 1997).

74. Each PERLS V is a single CGT asset, arising from a single contract between CBA and the Holder. By acquiring the PERLS V from an IH on the terms offered by CBA in its Prospectus for the issue of the PERLS V, each Holder has agreed to be bound by the Constitution of CBA, the Note Deed Poll, the Note Terms, the Preference Share Terms and the terms and conditions of the Offer as set out in the PERLS V Prospectus.

75. Each PERLS V was acquired by the Holder from an IH on the issue date, being 14 October 2009.

76. Each PERLS V is a single CGT asset consisting of a bundle of rights. The Assignment Event does not result in the acquisition of any new CGT asset. Rather each PERLS V takes on the features of a simple Preference Share. Accordingly, the Preference Share is not a new CGT asset acquired by the Holder upon the assignment of the Note, and the acquisition date of the Preference Share is the acquisition date of the PERLS V, being 14 October 2009.

### **Cost base and reduced cost base**

77. The first element of the cost base and reduced cost base of a CGT asset includes the money paid, or required to be paid, in respect of acquiring a CGT asset (paragraph 110-25(2)(a) and subsection 110-55(2) of the ITAA 1997).

78. The Holder acquired each PERLS V from an IH for \$200. Accordingly, the first element of the cost base and reduced cost base of each PERLS V is \$200.

79. The occurrence of an Assignment Event does not modify the cost base and reduced cost base of each PERLS V. Accordingly, the first element of the cost base and reduced cost base of each PERLS V is \$200.

## **Inclusion of Interest and Dividends in assessable income**

80. By virtue of paragraph 44(1)(a) of the ITAA 1936, the assessable income of a resident shareholder in a company includes all dividends and non-share dividends that are paid to the shareholder by the company.

81. Interest and Dividends payable in respect of the PERLS V are non-share dividends under section 974-120 of the ITAA 1997 and dividends under subsection 6(1) of the ITAA 1936 respectively. Accordingly, the Holders will include in their assessable income Interest and Dividends payable in respect of the PERLS V under paragraph 44(1)(a) of the ITAA 1936.

82. Furthermore, as this Ruling is made on the basis that:

- the non-share dividends and dividends payable in respect of the PERLS V are frankable distributions pursuant to section 202-40 of the ITAA 1997 and are not unfrankable under section 202-45 of the ITAA 1997; and
- where CBA franks a frankable distribution payable in respect of the PERLS V in accordance with section 202-5 of the ITAA 1997, the distribution will be a franked distribution,

it therefore follows that the franking credits attached respectively to the non-share dividends and dividends must also be included in the Holder's assessable income under subsection 207-20(1) of the ITAA 1997.

## **Entitlement to a tax offset**

83. In accordance with subsection 207-20(2) of the ITAA 1997, the Holders are entitled to receive a tax offset equal to the value of the franking credit which has been included in their assessable income in respect of the non-share dividends and dividends they received (subject to paragraphs 3 to 5 and 27 to 30 of this Ruling). The Commissioner has confirmed that subject to the circumstances mentioned in the Deed referred to at paragraphs 3 to 5 of this Ruling he will not make a determination under paragraph 177EA(5)(b) of the ITAA 1936 or paragraph 204-30(3)(c) of the ITAA 1997 to deny the imputation benefits attached to non-share dividends or dividends paid to the Holders in respect of their PERLS V.

## **Franking credit subject to the refundable tax offset rules**

84. Holders who are entitled to a tax offset under subsection 207-20(2) of the ITAA 1997, in respect of the franking credit received, will also be subject to the refundable tax offset rules in Division 67 of the ITAA 1997, unless they are specifically excluded under section 67-25 of the ITAA 1997. Certain trustees and corporate tax entities are not subject to the refundable tax offset rules because of subsections 67-25(1A) to 67-25(1D) of the ITAA 1997.

85. The refundable tax offset rules ensure that certain taxpayers are entitled to a refund once their available tax offsets have been utilised to reduce any income tax liability to nil.

### **Imputation integrity provisions**

#### ***Streaming of imputation benefits***

86. Subdivision 204-D of the ITAA 1997 broadly enables the Commissioner to make a determination where distributions with attached imputation benefits are streamed to members of a corporate tax entity.

87. Section 204-30 of the ITAA 1997 prescribes the circumstances that are required to exist before the Commissioner may make such a determination. Section 204-30 applies where an entity 'streams' the payment of distributions in such a way that:

- an 'imputation benefit' is, or apart from section 204-30 would be, received by a member of the entity as a result of the distribution or distributions (paragraph 204-30(1)(a) of the ITAA 1997);
- the member (favoured member) would derive a greater benefit from franking credits than another member of the entity (paragraph 204-30(1)(b) of the ITAA 1997); and
- the other member (disadvantaged member) of the entity will receive lesser imputation benefits, or will not receive any imputation benefits, whether or not the other member receives other benefits (paragraph 204-30(1)(c) of the ITAA 1997).

88. The existence of these conditions enables the Commissioner, under paragraph 204-30(3)(c) of the ITAA 1997, to make a determination that no imputation benefit is to arise in respect of the distributions made to those favoured members.

89. The primary issue is whether there will be a 'streaming' of distributions in such a way described in section 204-30 of the ITAA 1997. The expression 'streams' is not defined in the ITAA 1997.

90. Paragraphs 3.28 and 3.29 of the Explanatory Memorandum to the New Business Tax System (Imputation) Bill of 2002 provide that:

Streaming is selectively directing the flow of franked distributions to those members who can most benefit from imputation credits... The law uses an essentially objective test for streaming, although purpose may be relevant where future conduct is a relevant consideration. It will normally be apparent on the face of an arrangement that a strategy for streaming is being implemented. The distinguishing of members on the basis of their ability to use franking benefits is a key element of streaming.

91. If streaming were to exist, the remaining issue would be whether there is an 'imputation benefit'. 'Imputation benefit' is defined in subsection 204-30(6) of the ITAA 1997 to include an entitlement to a 'tax offset under Division 207 of the ITAA 1997 as a result of the distribution'. As the distributions payable in respect of the PERLS V are 'frankable distributions' (refer to paragraph 82 of this Ruling) it is reasonable to expect that the Holders of the PERLS V will receive an 'imputation benefit' as defined in subsection 204-30(6) of the ITAA 1997 as a result of receiving the distributions.

92. The Applicant submitted that:

- foreign residents will not be precluded from participating in the Offer, where the Offer is made in accordance with the laws of their jurisdiction;
- all Holders of the PERLS V will receive fully-franked distributions regardless of their tax attributes or their individual tax position;
- the dividend payout ratios or CBA's policies in relation to the franking of Ordinary Share capital or other Preference Share capital of CBA are not expected to change as a result of the issue of the PERLS V;
- as CBA is a listed public company with a large number and variety of equity holders, it is difficult to reasonably conclude that CBA would be capable of having sufficient knowledge as regards the tax profiles of its equity holders to 'stream' franking credits to particular equity holders who would derive a greater benefit from franking credits than other equity holders;
- Holders may also hold Ordinary Shares or other frankable equity interests in CBA. In such circumstances, CBA could not stream imputation benefits in respect of such equity holders as it is a requirement of streaming that the imputation benefits are streamed from one equity holder to another. As the same equity holder would hold both interests, there could be no streaming in such a situation; and
- the purpose of the transaction is not to enable CBA to stream franking credits to the Holders over holders of Ordinary Shares and other equity instruments issued by CBA. The principal purpose of the transaction is to raise Tier 1 Capital in a timely and cost-effective manner and to take advantage of conditions existing in the domestic market, where there is considered to be demand for equity-like investments, such as the PERLS V. CBA wishes to raise as much equity as practicable in Australia.

93. Based on the facts submitted, 'streaming' cannot be concluded to exist in relation to the franked distributions to be paid by CBA to the Holders of the PERLS V. Accordingly, the Commissioner will not make a determination under paragraph 204-30(3)(c) of the ITAA 1997 to deny imputation benefits of distributions made on the PERLS V to its Holders.

***General anti-avoidance rule – imputation***

94. **Note:** the commentary under this heading relates to the Dividends received by Holders in respect of the Preference Shares on issue (following the occurrence of an Assignment event that is not a Conversion or Repurchase) or an issue of Ordinary Shares (following a Conversion of PERLS V). It does not apply to the stapled security; refer to 'Scope of this Ruling' at paragraphs 3 to 5 of this Ruling.

95. Section 177EA of the ITAA 1936 is a general anti-avoidance provision that applies where one of the purposes (other than an incidental purpose) of the scheme is to obtain an imputation benefit. Where these circumstances arise, subsection 177EA(5) of the ITAA 1936 enables the Commissioner to make a determination with the effect of either:

- imposing franking debits or exempting debits on the distributing entity's franking account generally; or
- denying the imputation benefit on the distribution that flowed directly or indirectly to the relevant taxpayer.

96. Pursuant to subsection 177EA(3) of the ITAA 1936, and in conjunction with subsection 177EA(12) of the ITAA 1936 (which extends the application of section 177EA of the ITAA 1936 to non-share equity interests, equity holders and non-share dividends), section 177EA applies if the following conditions are satisfied:

- (a) there is a scheme for a disposition of membership interests, or an interest in membership interests, in a corporate tax entity; and
- (b) either:
  - (i) a frankable distribution has been paid, or is payable or expected to be payable, to a person in respect of the membership interests; or
  - (ii) a frankable distribution has flowed indirectly, or flows indirectly or is expected to flow indirectly, to a person in respect of the interest in membership interests, as the case may be;
- (c) the distribution was, or is expected to be, a franked distribution or a distribution franked with an exempting credit;

- (d) except for this section, the person (the relevant taxpayer) would receive, or could reasonably be expected to receive, imputation benefits as a result of the distribution; and
- (e) 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.

97. Membership interests include both equity interests and non-share equity interests.

98. It is considered that the conditions in paragraphs 177EA(3)(a) to 177EA(3)(d) of the ITAA 1936 are satisfied because:

- (a) subsection 177EA(14) of the ITAA 1936 provides that a 'scheme for a disposition of membership interests or an interest in membership interests' includes but is not limited to issuing the membership interests. The scheme for the PERLS V can be particularised by the relevant documents and descriptions provided by the Applicant. The application of section 177EA of the ITAA 1936 considers the purpose and relevant circumstances of the scheme, and the imputation benefits that arise during the course of the implementation of the scheme. After the Assignment Event has occurred and the PERLS V will be destapled (that is, the Notes will have been detached and transferred to CBA) without any further action being required by the Holder. The issuance of the PERLS V as a stapled security, the destapling of the Note leaving the Preference Shares and/or the acquisition of Ordinary Shares (following a Conversion of the PERLS V) on the terms set out in the PERLS V Prospectus are all aspects of a scheme that involve the issuing of membership interests. Holders of the PERLS V, as a stapled instrument, destapled Preference Shares or Ordinary Shares are equity holders of CBA at all times throughout the scheme; succeeding paragraphs consider the application of section 177EA to the scheme after the point at which the security is destapled.

- (b) frankable distributions are expected to be paid to the Holders of the Preference Shares (following an Assignment Event that is not a Conversion or Repurchase) or the Ordinary Shares (following a Conversion of the PERLS V) (paragraph 177EA(3)(b) of the ITAA 1936). This Ruling is made on the basis that the distributions payable in respect of the Preference Shares on issue (following an Assignment Event that is not a Conversion or Repurchase) or the Ordinary Shares (following a Conversion of the PERLS V) will be frankable distributions under section 202-40 of the ITAA 1997 and not be unfrankable distributions under section 202-45 of the ITAA 1997;
- (c) franked distributions are expected to be paid to the Holders of the Preference Shares (following an Assignment Event that is not a Conversion or Repurchase) or the Ordinary Shares (following a Conversion of the PERLS V) (paragraph 177EA(3)(c) of the ITAA 1936). It is expected that the franked distribution payable in respect of the Preference Shares (following an Assignment Event that is not a Conversion or Repurchase) will be made on a quarterly basis and that franked distributions will be payable twice a year in respect of the Ordinary Shares. Furthermore, CBA has advised that it will continue its policy of fully franking all frankable distributions made by it, to the extent of the franking credits available in its franking account; and
- (d) it is reasonable to expect that an imputation benefit will be received by the relevant taxpayers as a result of distributions made to the Holders given that CBA expects to frank the distributions on the Preference Shares (following an Assignment Event that is not a Conversion or Repurchase) or the Ordinary Shares (following a Conversion of the PERLS V) (paragraph 177EA(3)(d) of the ITAA 1936).

99. Accordingly, the issue is whether, having regard to the relevant circumstances of the scheme, it would be concluded that it was entered into or carried out for the purpose (which is not merely an incidental purpose) of enabling the relevant taxpayer to obtain an imputation benefit under the scheme.

100. Circumstances which are relevant in determining whether any person has the requisite purpose include, but are not limited to, the factors listed in subsection 177EA(17) of the ITAA 1936. The relevant circumstances listed encompass a range of circumstances which taken individually or collectively could indicate the requisite purpose. Due to the diverse nature of these circumstances, some may or may not be present at any one time in any one scheme.

101. Based on the information provided, and having regard to the factors listed in subsection 177EA(17) of the ITAA 1936, the qualifications set out in this Ruling and the relevant circumstances of the scheme, it would not be reasonable to conclude that in entering into the scheme, CBA and/or the Holders of the Preference Shares (following the occurrence of an Assignment Event that is not a Conversion or Repurchase) or the Ordinary Shares (following a Conversion of the PERLS V) demonstrate a more than incidental purpose of securing imputation benefits for the Holders of the Preference Shares or the Ordinary Shares, after the stapled security has been destapled and the Holders no longer have as a part of the PERLS V security any interest in a Note. To the extent that any imputation benefits are secured at that time, those benefits are considered to be incidental.

102. Accordingly, the Commissioner will not make a determination under paragraph 177EA(5)(b) of the ITAA 1936 that would deny the imputation benefits attached to the Dividends paid to the Holders in respect of their Preference Shares (following the occurrence of an Assignment Event that is not a Conversion or Repurchase) or the Ordinary Shares (following a Conversion of the PERLS V).

***Gross-up and tax offset denied in certain circumstances***

103. Subdivision 207-F of the ITAA 1997 creates the appropriate adjustment to cancel the effect of the gross-up and tax offset rules where the entity concerned has manipulated the imputation system in a manner that is not permitted under the income tax law.

104. Section 207-145 of the ITAA 1997 provides the circumstances that must exist before this adjustment can occur. Pursuant to subsection 207-145(1) of the ITAA 1997 a 'manipulation of the imputation system' may occur where:

- the entity is not a 'qualified person' in relation to the distribution (paragraph 207-145(1)(a) of the ITAA 1997);
- the Commissioner has made a determination under paragraph 177EA(5)(b) of the ITAA 1936 that no imputation benefit is to arise in relation to the dividend (paragraph 207-145(1)(b) of the ITAA 1997);
- the Commissioner has made a determination under paragraph 204-30(3)(c) of the ITAA 1997 that no imputation benefit is to arise in relation to the distribution (paragraph 207-145(1)(c) of the ITAA 1997); or
- the dividend is made as part of a dividend stripping operation (paragraph 207-145(1)(d) of the ITAA 1997).

105. A person is a 'qualified person' for the purposes of Division 1A of former Part IIIAA of the ITAA 1936 if, generally speaking, they satisfy the holding period rule and the related payments rule (see former section 160APHO of the ITAA 1936).

106. By virtue of the former section 160AOA of the ITAA 1936, the holding period rule and the related payments rule apply to non-share equity interests, equity holders and non-share dividends in the same way as they apply to shares, shareholders and dividends respectively.

107. The holding period rule applies where no related payment has been, or will be made, in respect of the non-share dividend or dividend, and requires the non-share equity interest or share to have been continuously held at risk throughout the primary qualification period (former paragraph 160APHO(1)(a) of the ITAA 1936).

108. The related payments rule applies where the taxpayer or an associate has made or will make a related payment in respect of the non-share dividend or dividend and requires the non-share equity interest or share to have been continuously held at risk throughout the secondary qualification period (former subsection 160APHO(1) of the ITAA 1936 and former section 160APHN of the ITAA 1936).

109. The Commissioner has concluded that the Holders are qualified persons, because:

- the Holders in receipt of non-share dividends and dividends in respect of the PERLS V will have held their PERLS V at risk for at least 90 days (excluding the day of acquisition and the day of disposal, and any days on which the Holder has materially diminished risks of loss or opportunities for gain in respect of the shares or interest), in the period beginning on the day after the day on which the Holder acquired the PERLS V and ending on the 90<sup>th</sup> day after the day on which the PERLS V became ex-dividend (former subsections 160APHO(2) and 160APHO(3) of the ITAA 1936 and former sections 160APHM and 160APHJ of the ITAA 1936); and
- neither the Holders, nor associates of the Holders, are under an obligation to make, or are likely to make a related payment in relation to the non-share dividends or dividends (former paragraph 160APHO(1)(a) of the ITAA 1936 and former section 160APHN of the ITAA 1936).

110. However, if either or both of the above two considerations are not met, the Holder will not be a 'qualified person' for the purposes of Division 1A of former Part IIIAA of the ITAA 1936. Subdivision 207-F of the ITAA 1997 would then create the appropriate adjustment to cancel the effect of the gross-up and tax offset rules for the Holder.

111. Subject to the circumstances mentioned in the Deed referred to at paragraphs 3 to 5 of this Ruling, the Commissioner has confirmed that he will not make a determination under paragraph 177EA(5)(b) of the ITAA 1936 or paragraph 204-30(3)(c) of the ITAA 1997 to deny the imputation benefits attached to non-share dividends or dividends paid to the Holders in respect of their PERLS V.

112. A distribution will be taken to be made as part of a dividend stripping operation, pursuant to section 207-155 of the ITAA 1997, where the distribution arose out of, or was made in the course of, a scheme or substantially similar arrangement that was in the nature of dividend stripping.

113. The PERLS V Prospectus provides no indication that the offering of the PERLS V and the associated payment of franked distributions to the Holders in any way constitute a dividend stripping arrangement. As such, the dividend stripping provision will have no application to the Holders.

114. Therefore, section 207-145 of the ITAA 1997 may apply to deny imputation benefits to Holders where one or more conditions outlined in paragraphs 103 and 104 of this Ruling are met.

115. In addition, based on the facts and additional matters stated by the Applicant, and the reasoning contained in paragraphs 105 to 110 of this Ruling that the Holders are qualified persons, the Commissioner has concluded that the following do not affect whether the PERLS V are held 'at risk' for the purposes of Division 1A of former Part IIIAA of the ITAA 1936:

- the irrevocable offer by Holders to assign the Notes on the occurrence of an Assignment Event Date; or
- the irrevocable offer by Holders to sell their PERLS V (or Preference Shares, where an Assignment Event that is not a Conversion or Repurchase has occurred) to a Purchaser if CBA issues a Resale Notice.

116. This is because 'held', as provided within the qualified persons test outlined in paragraphs 105 to 109, is explained within paragraph 4.29 of the Explanatory Memorandum to the Taxation Laws Amendment Bill (No. 2) of 1999. The paragraph provides that an equity interest is held during the period between acquisition and disposal.

117. Former subsection 160APHH(1) of the ITAA 1936 provides that, where shares are disposed of for a fixed price under a conditional contract, the taxpayer is taken to have disposed of shares at the time the condition has been complied with. The contract would take effect from the time the condition has been complied with.

118. This means that Holders will continue to hold the PERLS V at 'risk' for the purposes of Division 1A of former Part IIIAA of the ITAA 1936 after the relevant irrevocable offers are made by Holders. Accordingly, Holders will only be treated as disposing of the PERLS V on the Assignment Event Date or the Exchange Date, and will therefore cease to hold the PERLS V 'at risk' at that time.

119. The Commissioner has concluded that the following product features do not affect a Holder's risks of loss or opportunities for gain in respect of the PERLS V for the purposes of being qualified persons under former section 160APHO of the ITAA 1936. This is also on the basis of the following paragraphs, that the Holders hold long positions, and not separate positions, and that the Holders' net positions on any day are not less than 30% of those risks or opportunities for the purposes of former subsections 160APHJ(4) and 160APHM(2) of the ITAA 1936 respectively:

- the Resale facility; and
- the Conversion process.

120. Paragraph 13 of Taxation Determination TD 2007/29 provides that:

If the issuer of an equity interest has the ability to redeem the interest then that redemption option is not taken into account in determining whether there has been a material diminution in the risks of loss or opportunities for gain in holding the interest.

121. Paragraphs 16 and 17 of TD 2007/29 further provide that:

... subsection 160APHJ(4) operates to treat the rights and obligations held as between the issuing company and the investor as a single position, but that it does not preclude the recognition of rights of third parties as separate positions... An option to redeem or acquire a share which is granted to a party other than the issuer of the share does not represent an obligation of the shareholder as against the company in which they are the shareholder. Rather the option represents a separate position in relation to the share.

122. In considering the reasoning of paragraph 13 of TD 2007/29 and the operation of the Resale facility, CBA may elect to issue a Resale Notice specifying that all of the PERLS V will be acquired by a Purchaser on an Exchange Date for a cash amount equal to the Face Value of each PERLS V. However, this is a right that is held by CBA as against a Holder of the PERLS V to nominate a Purchaser to acquire the PERLS V. This means that this is a right to nominate by CBA and will not be taken into account to give rise to a diminution in the risks of loss or opportunities for gain in holding the PERLS V for the purposes of former subsection 160APHM(2) of the ITAA 1936.

123. Further, in considering the reasoning of paragraphs 16 and 17 of TD 2007/29 and the operation of the Resale facility, the Preference Share Terms do not provide the nominated Purchaser any right or ability to trigger redemption or call for the PERLS V from the Holders. That is, there is no right or obligation between a nominated Purchaser and the Holder to acquire the PERLS V. Only CBA may call for the PERLS V from the Holders and nominate a Purchaser as an acquirer of the PERLS V. Therefore, no separate position arises in relation to the PERLS V for the purposes of former subsection 160APHJ(4) of the ITAA 1936.

124. Similarly, the right for CBA to elect for an Assignment Event that is a Conversion to occur, which would effect the redemption of Preference Shares and the issue of Ordinary Shares, will not give rise to a diminution in the risks of loss or opportunities for gain in holding the PERLS V, and will not represent a separate position, for the purposes of former subsections 160APHM(2) and 160APHJ(4) of the ITAA 1936. This is because only CBA has the right to elect for the Assignment Event that is a Conversion to occur, and there is no right or obligation for a Purchaser or a Holder to convert the PERLS V.

### **Characterisation of the PERLS V for CGT purposes**

125. Each PERLS V is a single CGT asset, arising from a single contract, the terms of which are to be found in the Constitution of CBA, the Note Deed Poll, the Note Terms, the Preference Share Terms and the terms and conditions of the Offer as set out in the PERLS V Prospectus.

### **Assignment Event – CGT implications**

126. Each PERLS V is a single CGT asset, arising from a single contract between CBA and the Holder. The assignment of the Notes on an Assignment Event Date will not affect the continued existence of this CGT asset, although the PERLS V will then take on the features of simple Preference Shares.

127. Subsection 104-155(1) of the ITAA 1997 provides that CGT event H2 happens if an act, transaction or event occurs in relation to a CGT asset that you own and the act, transaction or event does not result in an adjustment being made to the asset's cost base or reduced cost base.

128. CGT event H2 will happen when an Assignment Event occurs. This is an act, transaction or event in relation to the PERLS V that does not result in an adjustment being made to the cost base or reduced cost base of the PERLS V.

129. A capital gain is made if the capital proceeds from CGT event H2 are more than the incidental costs incurred in relation to the event. A capital loss is made if the capital proceeds are less than the incidental costs (subsection 104-155(3) of the ITAA 1997).

130. Subsection 116-20(2) of the ITAA 1997 provides that the capital proceeds from CGT event H2 happening is the money or other consideration received, or entitled to be received, because of the act, transaction or event.

131. Holders will make no capital gain or capital loss from the happening of CGT event H2 as there are no capital proceeds because of the event and no incidental costs are incurred by the Holders that relate to the event.

132. No other CGT event will happen when an Assignment Event other than Conversion occurs.

**PERLS V are convertible interests**

133. Subsection 995-1(1) of the ITAA 1997 defines a 'convertible interest' in a company as an interest of the kind referred to in item 4 of the table in subsection 974-75(1) of the ITAA 1997. Paragraph (b) of item 4 of the table in subsection 974-75(1) provides that an interest is an equity interest if it is an interest issued by the company that is an interest that will, or may, convert into an equity interest in the company.

134. Section 974-165 of the ITAA 1997 provides that an interest (the first interest) is an interest that will or may convert into another interest (the second interest) if:

- (b) the first interest, or a part of the first interest, must be or may be redeemed, repaid or satisfied by:
  - (i) the issue or transfer of the second interest (whether to the holder of the first interest or to some other person); or
  - ...
- (c) the holder of the first interest has, or is to have, a right to have allotted or transferred to the holder or for the holder to acquire:
  - (i) the second interest; or
  - ...

135. Paragraph 2.2 of the Explanatory Memorandum to the New Business Tax System (Debt and Equity) Bill of 2001 (Debt and Equity EM) provides that the interest in a company is classified according to the economic substance of the rights and obligations of an arrangement rather than its mere legal form. It is also relevant to have regard to the pricing, terms and conditions of the arrangement under which the interest is issued.

136. Example 2.8 of the Debt and Equity EM provides an example in which a stapled instrument comprising an unpaid preference share and a note whose terms provide that, if the face value of the note is redeemed, a call is made on the unpaid amount of the preference share. The example provides that in such a situation, there is an effective, but not an actual, conversion of the note into a preference share.

137. In considering paragraph 2.2 and example 2.8 of the Debt and Equity EM, the Commissioner has concluded that an effective conversion will occur:

- (a) where an Assignment Event is not a Conversion or Repurchase. This is because the economic substance of destapling each PERLS V is that each Note will effectively be consideration for the fully paid up amount on each Preference Share. Therefore, the Holders will no longer hold Notes or be entitled to receive Interest on the Notes. The Holders will consequently hold Preference Shares and be entitled to receive Dividends on the Preference Shares equal to the amount they would have received as Interest on the Notes; or
- (b) where an Assignment Event is a Conversion. This is because, whilst Conversion is carried out after destapling by way of a Promissory Note, the result created by the Conversion mechanism would be to effectively achieve a conversion. This is also consistent with the terms and conditions provided. This means that the economic substance of the arrangement would cause the Holders to no longer hold the Preference Shares and to no longer be entitled to receive Dividends on them. The Preference Shares are redeemed and a number of Ordinary Shares are issued accordingly. The Holders would then be entitled to receive dividends on the Ordinary Shares. As discussed earlier, this Conversion mechanism was implemented by CBA to allow it to comply with the requirements of the current New Zealand taxation laws and the Australian *Corporations Act 2001*.

138. Paragraph 4 of Taxation Determination TD 2007/26 provides that:

whether it (a share) qualifies as a convertible interest depends on whether there is anything in Division 974 (or any other provision of the ITAA 1997) which prevents a share satisfying both item 1 and item 4 of the table.

139. Consistent with the reasoning provided in TD 2007/26, there is no ground to prevent the PERLS V from satisfying both item 1 and item 4 of the table in subsection 974-75(1) of the ITAA 1997. That is, the PERLS V would be both a member interest in CBA and a convertible interest.

140. Accordingly, under subparagraph 974-165(c)(i) of the ITAA 1997, when an Assignment Event is not a Conversion or Repurchase, and the PERLS V destaple, an effective conversion will occur and the Holders will solely hold Preference Shares and be entitled to receive Dividends.

141. Under subparagraph 974-165(b)(i) of the ITAA 1997 and pursuant to the terms of the PERLS V, if an Assignment Event is a Conversion, each PERLS V (consisting at that time of only a Preference Share) will effectively convert into Ordinary Shares through the issue of Ordinary Shares to the Holders and the redemption of the PERLS V.

142. Therefore, the PERLS V is a convertible interest under item 4 of the table in subsection 974-75(1) of the ITAA 1997 and within the meaning of section 974-165 of the ITAA 1997.

### ***Conversion of the PERLS V***

143. The PERLS V will convert at the earlier of:

- 31 October 2014, subject to the satisfaction of the Conversion Conditions; or
- the first Dividend Payment Date after 31 October 2014 on which the Conversion Conditions are satisfied.

144. The PERLS V may convert before the Relevant Date at CBA's discretion where certain defined events have occurred.

145. CGT event C2 will happen to the Holders on the Conversion of the PERLS V.

146. Under section 104-25 of the ITAA 1997, CGT event C2 happens if, among other things, the ownership of an intangible CGT asset (the PERLS V) ends:

- by being redeemed or cancelled (paragraph 104-25(1)(a) of the ITAA 1997); or
- if the PERLS V is a convertible interest – by being converted (paragraph 104-25(1)(f) of the ITAA 1997).

147. The PERLS V will be redeemed for the purposes of paragraph 104-25(1)(a) of the ITAA 1997. As part of the Conversion, each PERLS V (consisting solely of a Preference Share at that time) will be redeemed by CBA.

148. Under subsection 104-25(3) of the ITAA 1997, the Holders will make a capital gain if the capital proceeds from CGT event C2 are more than the asset's cost base. The Holders will make a capital loss if the capital proceeds are less than the asset's reduced cost base.

149. The PERLS V are convertible interests. Under subsection 130-60(3) of the ITAA 1997, a capital gain or capital loss made by a Holder from converting a 'convertible interest' is disregarded. The redemption of each PERLS V (consisting solely of a Preference Share at that time) happens as part of the Conversion. Any capital gain or capital loss made by a Holder from CGT event C2 happening on redemption of the PERLS V will be disregarded.

## **Sections 45, 45A and 45B**

150. Sections 45, 45A and 45B of the ITAA 1936 are anti-avoidance provisions which, if they apply, either deem the value of shares or other capital benefits received by a shareholder to be an unfranked dividend paid by the company out of profits of that company, to the shareholder or allow the Commissioner to make a determination to that effect.

### ***Section 45***

151. Section 45 of the ITAA 1936 applies where a company streams the provision of shares and the payment of minimally franked dividends to its shareholders in such a way that the shares are received by some shareholders and minimally franked dividends are received by other shareholders. Minimally franked dividends are dividends which are franked to less than 10%.

152. CBA has consistently paid fully franked dividends and intends to continue paying fully franked dividends to all its shareholders into the foreseeable future. Based on the information provided and having regard to the circumstances of the scheme, section 45 of the ITAA 1936 will not apply to treat the issue of Ordinary Shares as an unfranked dividend in the hands of the Holders.

### ***Section 45A***

153. Section 45A of the ITAA 1936 applies in circumstances where capital benefits are streamed to certain shareholders who derive a greater benefit from the receipt of capital (the advantaged shareholders) and it is reasonable to assume that the other shareholders have received or will receive dividends (the disadvantaged shareholders).

154. The issue of Ordinary Shares to Holders as a result of a Conversion of the Preference Shares will constitute the provision of ownership interests in CBA to the Holders, which falls within the definition of 'provision of capital benefits' within the meaning of subsection 45A(3) of the ITAA 1936.

155. The issue of Ordinary Shares on Conversion of the Preference Shares is in effect a restatement of the Holder's interest in the capital of CBA. In the absence of any other factors that would contribute to an alternative conclusion, there will not be any streaming of capital benefits.

156. Accordingly, it cannot be said that Holders derive a greater benefit from capital benefits than other CBA shareholders. Therefore, the issue of Ordinary Shares does not trigger the application of section 45A of the ITAA 1936.

157. The Commissioner will not make a determination under subsection 45A(2) of the ITAA 1936 that the whole or part of the capital benefit that arises upon a Conversion of the Preference Shares is an unfranked dividend in the hands of the Holders.

### **Section 45B**

158. Section 45B of the ITAA 1936 applies where certain capital benefits are provided to shareholders in substitution for dividends.

159. The issue of Ordinary Shares to Holders as a result of a Conversion of Preference Shares will constitute the provision of ownership interests in CBA to the Holders, which falls within the definition of 'provision of capital benefits' within the meaning of subsection 45B(5) of the ITAA 1936.

160. For the provision to apply, among other things, paragraph 45B(2)(c) of the ITAA 1936 requires that, having regard to the relevant circumstances of the scheme, it would be concluded that any part of the scheme would be entered into for a purpose, other than an incidental purpose, of enabling a relevant taxpayer to obtain a tax benefit. A non-exhaustive list of relevant circumstances of the scheme are provided in subsection 45B(8) of the ITAA 1936.

161. Having regard to the relevant circumstances surrounding the issue of the PERLS V, it cannot be concluded that CBA, the Holders or any other person entered into or carried out the issue of the PERLS V for the purpose of enabling the Holders to obtain a capital benefit in substitution for dividends. The terms of the arrangement do not disclose that the Ordinary Shares issued upon a Conversion will be provided in substitution for any Dividend payment in respect of the PERLS V. Further, the issue of Ordinary Shares cannot be said to be attributable to the profits of the company.

162. Accordingly, the Commissioner will not make a determination under paragraph 45B(3)(b) of the ITAA 1936 that subsection 45C(3) of the ITAA 1936 applies to the whole or part of the capital benefit under the transaction.

### **Cost base of the Ordinary Shares**

163. Subdivision 130-C of the ITAA 1997 governs the time of acquisition and the cost base of shares acquired by converting a convertible interest for CGT purposes.

164. PERLS V are convertible interests. Upon the Conversion of the PERLS V, Subdivision 130-C of the ITAA 1997 will apply. As the Holders will acquire shares by converting a convertible interest that is not a traditional security, the first element of the cost base and reduced cost base of the converted PERLS V (being CBA Ordinary Shares) will be the cost base of the PERLS V at the time of the Conversion (item 2 of the table in subsection 130-60(1) of the ITAA 1997).

## **Date of acquisition of the Ordinary Shares**

165. PERLS V are convertible interests. On the Conversion of the PERLS V, the converted PERLS V (being CBA Ordinary Shares) are taken to have been acquired by the Holder when the Conversion of the PERLS V happened (subsection 130-60(2) of the ITAA 1997), that is, on the Exchange Date of the Conversion.

## **Commercial debt forgiveness**

166. The Promissory Note issued by a Holder to CBA is a commercial debt of the Holder (section 245-25 of Schedule 2C to the ITAA 1936).

167. When CBA transfers the Promissory Note to the Holder who issued it, and cancels the Holder's obligations under it, a Holder's commercial debt is forgiven by being extinguished (subsection 245-35(1) of Schedule 2C to the ITAA 1936).

168. As a result of the forgiveness, Subdivision 245-C of Schedule 2C to the ITAA 1936 must be applied in calculating the gross forgiven amount of the debt. This amount is the notional value of the debt less the consideration in respect of the forgiveness.

169. Under section 245-55 of Schedule 2C to the ITAA 1936, the notional value of the debt (the Promissory Note issued by each Holder) at the time when it will be forgiven will be the face value of the debt evidenced by the Promissory Note.

170. Under section 245-65 of Schedule 2C to the ITAA 1936, the consideration in respect of the forgiveness of the debt (the Promissory Note issued by each Holder) will be the Face Value of the PERLS V (consisting solely of a Preference Share at the time of the forgiveness of the debt) multiplied by the number of PERLS V owned by each Holder. This equals the face value of the debt evidenced by the Promissory Note.

171. Therefore, the notional value of the debt at the time when the debt is forgiven will be equal to the consideration that is, or is taken to be, paid or given in respect of the forgiveness of the debt. As a result, paragraph 245-75(2)(b) of Schedule 2C to the ITAA 1936 provides that there is no forgiven amount in respect of the debt.

Subdivisions 245-D to 245-G of Schedule 2C to the ITAA 1936 do not apply in respect of the debt. Certain tax attributes that would be taken into account in calculating a Holder's taxable income will not be modified by Schedule 2C to the ITAA 1936.

## **Appendix 2 – Detailed contents list**

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Not previously issued as a draft

### *Related Rulings/Determinations:*

TR 2006/10; TD 2007/26;

TD 2007/29

### *Subject references:*

- acquisition dates
- anti avoidance measures
- capital gains tax
- CGT cost base
- conversion of securities
- convertible notes
- debt forgiveness
- dividend imputation
- franking rebates
- preference shares
- qualified person
- share capital streaming

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