


CR 2010/53 - Income tax: demerger of White Rock Minerals Limited by Rex Minerals Limited

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Class Ruling

Income tax: demerger of White Rock Minerals Limited by Rex Minerals Limited

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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.

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);
- section 44 of the ITAA 1936;
- section 45B of the ITAA 1936
- section 45C of the ITAA 1936
- section 104-135 of the *Income Tax Assessment Act 1997* (ITAA 1997);
- section 115-30 of the ITAA 1997;
- Division 125 of the ITAA 1997;
- Division 197 of the ITAA 1997;

- section 975-300 of the ITAA 1997; and
- subsection 995-1(1) of the ITAA 1997.

All subsequent legislative references are to the ITAA 1936 unless otherwise indicated.

Class of entities

3. The class of entities to which this Ruling applies is the ordinary shareholders of Rex Minerals Limited (Rex) who:

- (a) were listed on the share register of Rex as at the Record Date (being 7pm on 11 June 2010);
- (b) were residents of Australia as defined in subsection 6(1) of the ITAA 1936 on that date;
- (c) held their Rex shares on capital account on that date; and
- (d) are not subject to the taxation of financial arrangements (TOFA) rules in Division 230 of the ITAA 1997 in relation to gains and losses on their Rex shares.

(Note – Division 230 of the ITAA 1997 will generally not apply to individuals, unless they have made an election for it to apply to them.)

In this ruling, a person belonging to this class of entities is referred to as a 'Rex shareholder'.

Qualifications

4. The Commissioner makes this Ruling based on the precise scheme as identified in this Ruling.

5. The class of entities defined in this Ruling may rely on its contents provided the scheme actually carried out is carried out in accordance with the scheme described in paragraphs 9 to 27 of this Ruling.

6. If the scheme actually carried out is materially different from the scheme that is described in this Ruling, then:

- this Ruling has no binding effect on the Commissioner because the scheme entered into is not the scheme on which the Commissioner has ruled; and
- this Ruling may be withdrawn or modified.

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Date of effect

8. This Ruling applies from 1 July 2009 to 30 June 2010. The Ruling continues to apply after this date to all entities within the specified class who entered into the specified scheme during the term of the Ruling. 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

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

The restructure of Rex

10. On 30 April 2010, Rex announced a proposed restructure subject to approval at the general meeting on 3 June 2010. The key transactions under the proposed restructure were:

- the demerger of 100% of the ordinary shares in White Rock Minerals Limited (White Rock) to the shareholders of Rex;
- following the demerger, White Rock will undertake to raise approximately \$3 to \$5 million of capital by way of an initial public offer;
- a planned listing of all of its shares on the Australian Securities Exchange (ASX). The proposed demerger is a condition precedent of White Rock's initial public offer; and
- White Rock may also seek strategic tenement acquisitions complementary to its objectives prior to listing.

Relevant entities

Rex

11. Rex is an Australian resident company listed on the ASX. Rex has formed a tax consolidated group for the purposes of Part 3-90 of the ITAA 1997 effective from 1 July 2008 with Rex as the head company and the following subsidiary members at the time of the demerger:

- Rex Minerals (NSW) Pty Limited (Rex NSW);
- White Rock;
- Rex Minerals (SA) Pty Limited (Rex SA);
- Rex Minerals (Iron Ore) Pty Limited; and
- Rex Hillside (Property) Pty Limited.

12. Rex is a resource company who carries on a business of minerals exploration and development. Before the restructure, it was in the position of having 100% ownership of two large projects, one in South Australia (Pine Point Copper Belt) and another in New South Wales (Mt Carrington).

13. Immediately before the demerger, Rex had 114,389,460 ordinary shares on issue, of which approximately 12% were owned by non-resident shareholders.

14. Rex also had 4,520,000 unlisted options on issue. These options have been disregarded for the purposes of subsection 125-70(2) of the ITAA 1997 as they are adjusting instruments as defined in subsection 125-75(4) of the ITAA 1997.

White Rock

15. At the time of the demerger, White Rock was an Australian resident company and a wholly owned subsidiary of Rex. White Rock had approximately 38,130,533 fully paid ordinary shares on issue, all owned by Rex.

16. Under the demerger, White Rock acquired all of Rex's interests in Rex NSW in exchange for an issue of shares in White Rock

17. After the demerger, White Rock indirectly owned the Mt Carrington Project through its investment in Rex NSW, its wholly owned subsidiary.

18. White Rock was funded with approximately \$7 million in cash from Rex, and will undertake an initial public offering (IPO) during the September quarter 2010 to raise an additional \$3 to \$5 million for ongoing exploration at Mt Carrington.

19. An application will be made subsequently to list White Rock on the ASX.

The demerger of White Rock as proposed in the ruling application

20. The broad outline of the demerger of White Rock which was carried out on 15 June 2010 involved the following key steps:

- Rex NSW issued new shares to Rex. Rex NSW applied the funds raised to satisfy in full any outstanding intercompany debt owing to Rex;
- White Rock acquired all of Rex's interests in Rex NSW in exchange for the issue of shares in White Rock; and
- White Rock is now the demerged entity of a demerger group with Rex as the head entity.

21. Rex shareholders voted at a general meeting on 3 June 2010 to approve an ordinary resolution (the White Rock share distribution) to reduce the issued share capital of the company, without cancelling any shares, by an amount equal to the market value of all fully paid ordinary shares in White Rock with effect as at 7.00pm Australian Eastern Standard Time on the Record Date.

22. Under the restructure, a Rex shareholder received an *in specie* distribution of the White Rock shares held by Rex on a one (1) White Rock share for every three (3) Rex shares held at the Record Date. As a result of the demerger, Rex's shareholders now own shares in both Rex and White Rock.

Reasons for the demerger

23. Rex expected that a number of advantages will accrue to its shareholders as a result of the demerger. The Mt Carrington project has a number of key attributes and advantages which support the demerger including:

- established gold and silver resources;
- 100% owned Mining Licences and infrastructure;
- favourable location; and
- considerable exploration upside – gold and silver focussed exploration undertaken since 1994 has been exceedingly limited, providing tremendous opportunity to add significant value through focussed exploration programs.

In addition, the demerger is also expected to result in:

- the creation of a gold-silver focussed company with the ability and funding to explore and develop the 100% owned Mt Carrington asset as a sole entity;
- a better alignment of the management teams of both companies to achieve 100% focus on their respective project needs;

- a transparent valuation and immediate value recognition for the Mt Carrington assets;
- a reduction in the diversity of Rex's exploration assets;
- direct exposure to the gold and silver price; and
- a potential tangible increase in shareholder value in both companies (subsequent to the proposed ASX listing of White Rock).

24. The company considers that the Mt Carrington project is a different type of asset to Rex's other portfolio of assets. The demerger will place White Rock shares directly in the hands of Rex's shareholders whilst creating independence in the trading price of Rex from White Rock. The distribution of the White Rock shares will not diminish Rex's capacity to undertake its exploration and production programs as circumstances require and will enable the shareholders to participate directly in any exploration and production success achieved by Rex outside its interest in White Rock.

25. The exploration activities completed by Rex since late 2007 have been dominated by the discovery of significant copper at Hillside on the Yorke Peninsula in South Australia. The Hillside project and the portfolio of additional copper targets on the Pine Point Copper Belt have evolved to define Rex as a copper entity with a geographic focus in South Australia. Although Rex recognises the significant large scale gold-silver-copper potential associated with the Mt Carrington project in New South Wales, the Board considers that the Mt Carrington project has a negligible influence on Rex's share price. The demerger of the Mt Carrington asset into White Rock as a separate entity is considered to be the best opportunity for shareholders to realise maximum value from both of Rex's core assets.

Other matters

26. No Rex shareholder acquired their shares in Rex before 20 September 1985.

27. Rex has confirmed that no amounts have been transferred to its share capital account (as defined in section 975-300 of the ITAA 1997) from any of its other accounts, and accordingly its share capital account is not tainted (within the meaning of Division 197 of the ITAA 1997).

Ruling

CGT event G1

28. CGT event G1 happened in relation to each share owned by the Rex shareholders at the time Rex made the payment of the capital reduction amount (satisfied by the *in specie* distribution of White Rock shares) (section 104-135 of the ITAA 1997).

29. A Rex shareholder will make a capital gain under CGT event G1 if the proportion of the capital reduction amount received for one Rex shares exceeded the cost base of that share. The capital gain is equal to the amount of the excess. A capital loss cannot be made from CGT event G1 (subsection 104-135(3) of the ITAA 1997).

CGT consequences

Demerger roll-over relief

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

31. A Rex shareholder can choose demerger roll-over under subsection 125-55(1) of the ITAA 1997 for their Rex shares.

CGT consequences of choosing roll-over

32. A Rex shareholder who chooses demerger roll-over will disregard any capital gain made when CGT event G1 happened to their Rex shares under the demerger (subsection 125-80(1) of the ITAA 1997).

Other consequences of choosing roll-over

33. If a Rex shareholder chooses roll-over relief, they must recalculate the cost base and reduced cost base of their Rex and White Rock shares.

34. The first element of the cost base and reduced cost base of each Rex share and corresponding White Rock share received under the demerger is worked out as follows:

- sum of the cost bases of the Rex shares (just before the demerger); and
- apportion that sum over the Rex shares and corresponding new White Rock shares received under the demerger.

35. The apportionment of this sum is done on a reasonable basis having regard to the market values (just after the demerger) of the Rex and White Rock shares, or a reasonable approximation of those market values (subsections 125-80(2) and (3) of the ITAA 1997).

Rex shareholders who do not choose demerger roll-over

36. A Rex shareholder who does not choose demerger roll-over will not disregard any capital gain made when CGT event G1 happened to their Rex shares under the demerger.

37. The first element of the cost base and reduced cost base of each Rex share and corresponding White Rock shares is as described in paragraph 35 of this Ruling (subsections 125-85(1) and (2) of the ITAA 1997).

Acquisition date of White Rock shares for the purposes of the CGT discount

38. For the purpose of determining eligibility to a discount capital gain, the White Rock shares received by a Rex shareholder are taken to have been acquired on the date the shareholder acquired, for CGT purposes, the corresponding Rex shares (item 2 in the table in subsection 115-30(1) of the ITAA 1997). This is the case whether or not demerger roll-over is chosen.

Dividend Consequences

39. The amount distributed to shareholders that is debited to Rex's share capital account is not a dividend within the meaning of subsection 6(1) (see exclusion contained in paragraph (d) of the definition of a dividend contained in subsection 6(1)).

Demerger dividend

40. Any dividend arising under the demerger is a demerger dividend under subsection 6(1).

41. The demerger dividend is neither assessable income nor exempt income of the Rex shareholders (subsections 44(3) and (4)).

Application of sections 45B and 45C

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

Appendix 1 – Explanation

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

CGT event G1

43. CGT event G1 happened in relation to the Rex ordinary shares owned by the Rex shareholders at the time that Rex made the payment of the capital reduction amount. The payment is not a dividend as defined in subsection 995-1(1) of the ITAA 1997, nor an amount taken to be a dividend under section 47 of the ITAA 1936 (section 104-135 of the ITAA 1997).

44. A Rex shareholder will make a capital gain if the capital reduction amount is more than the cost base of their Rex share. The amount of the capital gain is equal to this excess. A capital loss cannot be made from CGT event G1 (subsection 104-135(3) of the ITAA 1997).

45. Any capital gain may be disregarded if the Rex shareholder chooses roll-over relief. Whether or not demerger roll-over relief is chosen, the cost base of the Rex shares and the new White Rock shares will be determined by the demerger roll-over provisions.

Demerger roll-over relief

46. Demerger roll-over relief enables a shareholder to choose to disregard a capital gain made as a result of CGT event G1 happening when a non-assessable payment is made in relation to a share under a demerger.

47. The demerger roll-over provisions in Division 125 of the ITAA 1997 contain a number of conditions that must be satisfied before a taxpayer is eligible to choose demerger roll-over. The main conditions that are relevant to the scheme to which this Ruling relates are:

- (a) a shareholder owns a share in a company;
- (b) the company is the head entity of a demerger group;
- (c) a demerger happens to the demerger group; and
- (d) under the demerger a CGT event happens to the original interest and a new or replacement interest is acquired in the demerged entity.

Demerger dividend

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

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

50. Rex will make an *in specie* distribution of White Rock shares to Rex shareholders and will debit its share capital account with an amount that is equal to the market value of the White Rock shares. Therefore there is no amount that is a dividend. No part of the distribution is included in the shareholder's assessable income as a dividend under subsection 6(1)

51. A demerger dividend is neither assessable income nor exempt income (subsections 44(3) and (4)). A demerger dividend is not subject to withholding tax under section 128B (subsection 128B(3D)).

52. To the extent that there is a dividend, it will be a demerger dividend within the meaning of subsection 6(1). As no part of the distribution is a dividend, no part of the distribution is a demerger dividend.

The application of sections 45B and 45C

Section 45B

53. Section 45B is an anti-avoidance provision which, if applicable, allows the Commissioner to make a determination that all or part of a return of capital to be received by shareholders is to be treated as an unfranked dividend.

54. The purpose of section 45B is to ensure that the relevant amounts distributed to shareholders are treated as dividends for tax purposes if certain payments, allocations and distributions are made in substitution for dividends, or components of a demerger allocation as between capital and profit do not reflect the circumstances of the demerger. Specifically, the provision applies where:

- (a) there is a scheme under which a person is provided with a demerger or capital benefit by a company (paragraph 45B(2)(a));
- (b) under the scheme a taxpayer, who may or may not be the person provided with the demerger or capital benefit, obtains a tax benefit (paragraph 45B(2)(b)); and
- (c) 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, (other than an incidental purpose) of enabling a taxpayer to obtain a tax benefit (paragraph 45B(2)(c)).

55. Where the requirements of subsection 45B(2) are met, subsection 45B(3) empowers the Commissioner to make a determination that either section 45BA applies in relation to a demerger benefit or section 45C applies in relation to the whole or part of a capital benefit.

Scheme, demerger and capital benefit

56. The arrangement involving the *in specie* distribution to Rex shareholders of White Rock shares constitutes a scheme for the purposes of section 45B.

57. The phrase 'provided with a capital benefit' is defined in subsection 45B(5) and includes a distribution to a person of share capital and the provision of ownership interests in a company. As the *in specie* distribution of White Rock shares was recorded by means of a debit to Rex's untainted share capital account, Rex shareholders will be provided with a capital benefit as defined in paragraph 45B(5)(b).

58. The provision of ownership interests to the shareholders in another company (White Rock) also constitutes a demerger benefit within the meaning of subsection 45B(4).

59. There is a tax benefit obtained within the meaning of subsection 45B(9), as the tax liability on the demerger and capital benefit is less than it would be, had the demerger or capital benefit been characterised as a dividend instead.

Purpose

60. For the purposes of paragraph 45B(2)(c), the Commissioner is required to consider the relevant circumstances (as outlined in subsection 45B(8)) of the scheme to determine whether it could be concluded that entities that entered into or carried out the scheme or any part of the scheme did so for a purpose (other than an incidental purpose) of enabling the relevant taxpayer (participating shareholders) to obtain a tax benefit. On the basis of the information surrounding the *in specie* distribution of White Rock shares as described in the Class Ruling application and further information provided by Rex, the Commissioner has formed the view that the demerger and capital benefits provided to the Rex shareholders have not been made for a more than incidental purpose of obtaining a tax benefit.

61. Accordingly, the Commissioner will not make a determination pursuant to paragraph 45B(3)(b) that section 45C applies to the *in specie* distribution of White Rock shares by Rex.

Appendix 2 – Detailed contents list

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References

<i>Previous draft:</i>	- ITAA 1936 45B(3)(b)
Not previously issued as a draft	- ITAA 1936 45B(4)
	- ITAA 1936 45B(5)
<i>Related Rulings/Determinations:</i>	- ITAA 1936 45B(5)(b)
TR 2006/10	- ITAA 1936 45B(8)
	- ITAA 1936 45B(9)
<i>Subject references:</i>	- ITAA 1936 45BA
- capital benefits	- ITAA 1936 45C
- capital gains	- ITAA 1936 47
- capital proceeds	- ITAA 1936 128B
- CGT event G1 – G3 – shares	- ITAA 1936 128B(3D)
- cost base adjustments	- ITAA 1997
- demerger	- ITAA 1997 104-135
- demerger allocation	- ITAA 1997 104-135(3)
- demerger benefit	- ITAA 1997 115-30
- demerger group	- ITAA 1997 115-30(1)
- demerger subsidiary	- ITAA 1997 Div 125
- return of capital on shares	- ITAA 1997 125-55(1)
	- ITAA 1997 125-55(2)
	- ITAA 1997 125-70
<i>Legislative references:</i>	- ITAA 1997 125-70(2)
- ITAA 1936	- ITAA 1997 125-75(4)
- ITAA 1936 6(1)	- ITAA 1997 125-80(1)
- ITAA 1936 44	- ITAA 1997 125-80(2)
- ITAA 1936 44(1)	- ITAA 1997 125-80(3)
- ITAA 1936 44(3)	- ITAA 1997 125-85(1)
- ITAA 1936 44(4)	- ITAA 1997 Division 197
- ITAA 1936 45B	- ITAA 1997 975-300
- ITAA 1936 45B(2)	- ITAA 1997 995-1(1)
- ITAA 1936 45B(2)(a)	- ITAA 1997 Part 3-90
- ITAA 1936 45B(2)(b)	- TAA 1953
- ITAA 1936 45B(2)(c)	- Copyright Act 1968
- ITAA 1936 45B(3)	

ATO references

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