


CR 2010/60 - Income tax: Mitchell Communication Group Limited Scheme of Arrangement

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Class Ruling

Income tax: Mitchell Communication Group Limited Scheme of Arrangement

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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);
 - subsection 44(1) of the ITAA 1936;
 - subsection 128B(3) of the ITAA 1936;
 - section 128D of the ITAA 1936;
 - former section 160APHN of the ITAA 1936;
 - Division 1A of the former Part IIIA of the ITAA 1936;
 - section 177EA of the ITAA 1936;
 - section 104-10 of the *Income Tax Assessment Act 1997* (ITAA 1997);
 - section 109-10 of the ITAA 1997;

- section 110-25 of the ITAA 1997;
- section 110-55 of the ITAA 1997;
- section 112-30 of the ITAA 1997;
- Subdivision 115-A of the ITAA 1997;
- Subdivision 115-C of the ITAA 1997;
- section 116-20 of the ITAA 1997;
- Subdivision 124-M of the ITAA 1997;
- section 204-30 of the ITAA 1997;
- section 207-20 of the ITAA 1997;
- section 855-10 of the ITAA 1997; and
- section 855-15 of the ITAA 1997.

All subsequent legislative references are to the ITAA 1997 unless otherwise indicated.

Class of entities

3. The class of entities to which this Ruling applies, in relation to Part 3-1 and Part 3-3 of the, (referred to as participating Mitchell shareholders) consists of the registered holders of fully paid ordinary shares in the capital of Mitchell Communication Group Limited (Mitchell) who:

- (a) hold their shares on capital account;
- (b) participate in the proposed Scheme of Arrangement pursuant to which Aegis Group plc (Aegis) would acquire 100% of the Mitchell shares;
- (c) dispose of their Mitchell shares to Aegis in exchange for Cash Consideration and/or Share Consideration;
- (d) are not 'significant stakeholders' or 'common stakeholders' within the meaning of those expressions in Subdivision 124-M; and
- (e) are not subject to the TOFA rules in Division 230 in relation to gains and losses on their Mitchell shares.

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

Qualifications

4. The Commissioner makes this Ruling based on the precise arrangement 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 2010 to 30 June 2011. The Ruling continues to apply after 30 June 2011 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 following documents, or relevant parts of them form part of and are to be read with the description:

- Application for a Class Ruling, dated 20 August 2010;
- Merger Implementation Agreement, between Mitchell and Aegis, dated 29 July 2010; and
- Scheme Booklet issued by Mitchell to its shareholders, dated 17 September 2010.

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

Mitchell

10. Mitchell is an Australian resident company listed for quotation on the Australian Securities Exchange (ASX).

11. Mitchell is a leading Australian independent marketing communications group. Mitchell offers its clients services including media planning and buying, strategy, digital media and marketing, branded entertainment, public relations, brand experience, sponsorship, sportsground marketing, direct marketing and corporate social responsibility.

12. Mitchell has a single class of share capital on issue being ordinary shares.

13. All Mitchell rights and options were exercised or cancelled prior to the scheme implementation date.

Aegis

14. Aegis is a public limited company incorporated under the laws of England and Wales and is listed for quotation on the London Stock Exchange.

15. Aegis is a leading international marketing communications group operating in 82 countries.

The Scheme of Arrangement

16. Aegis and Mitchell announced on 29 July 2010 that they had entered into a Merger Implementation Agreement (MIA) under which it is proposed that Aegis will acquire all of the issued capital in Mitchell by way of a Scheme of Arrangement under the *Corporations Act 2001*.

17. The Scheme Meeting of Mitchell, as ordered by the Supreme Court of Victoria, will be held on 25 October 2010 at which a resolution will be put to Mitchell shareholders seeking their agreement to implement the Scheme of Arrangement.

18. The Record Date for determining entitlement to the Scheme Consideration pursuant to the Scheme of Arrangement is 9 November 2010 with the Scheme Consideration to be provided on the Scheme Implementation Date of 17 November 2010.

The Scheme Consideration

19. Under the Scheme of Arrangement, participating Mitchell shareholders may elect to receive the consideration from Aegis for their Mitchell shares either in cash, or Aegis shares, or a combination of both, under one of the following formulas:

- 100% cash;
- 75% cash and 25% Aegis shares;
- 50% cash and 50% Aegis shares;
- 25% cash and 75% Aegis shares; or
- 100% Aegis shares.

20. Mitchell shareholders who do not make an election or make an invalid election will be deemed to have elected to receive 100% Cash Consideration.

21. It is proposed that Aegis will acquire all of the issued capital in Mitchell for approximately \$363 million (based on cash consideration of \$1.20 per Mitchell share).

22. Under the Scheme, Mitchell shareholders will receive total consideration of either:

- cash of \$1.20 per share;
- shares calculated as 40 Aegis shares per 67 Mitchell shares; or
- a combination of cash and Aegis shares.

23. The Share Consideration is subject to a cap on the overall quantum of Aegis Shares that may be issued as Share Consideration being limited to approximately 9.9% of the share capital of Aegis.

Ineligible Foreign Mitchell Shareholders

24. Ineligible foreign shareholders are unable to elect to receive Aegis shares so will receive 100% cash consideration for their Mitchell shares. An ineligible foreign shareholder means a Mitchell shareholder whose address shown in the share register at the Record Date is a place outside Australia and its external territories, New Zealand, the United Kingdom or the United States of America, or who is acting on behalf of such a person, except where certain conditions are satisfied.

The Dividend

25. On 18 August 2010, Mitchell announced that, if the Scheme is approved, Mitchell shareholders will receive a payment of \$0.05 per share, fully franked, as the final dividend (the Mitchell Dividend) for the year ended 30 June 2010. If the Scheme is not approved, the final dividend will be a lesser amount.

26. Any Mitchell shareholder who holds their Mitchell shares on the dividend record date of Monday 1 November 2010 will receive the Mitchell Dividend.

27. The Mitchell Dividend reflects a distribution of profits that have accrued prior to the Scheme of Arrangement being implemented. The dividend will be funded by Mitchell from its existing cash reserves and/or existing banking facilities.

Ruling

The Dividend

28. The Mitchell Dividend of \$0.05 per share to be paid to Mitchell shareholders will constitute a 'dividend' as defined in subsection 6(1) of the ITAA 1936.

Assessability of the Dividend

29. Mitchell shareholders who received the fully franked Mitchell Dividend and are residents of Australia as defined in subsection 6(1) of the ITAA 1936 are required to include the Mitchell Dividend as assessable income under subparagraph 44(1)(a)(i) of the ITAA 1936.

Gross up and tax offset

30. Mitchell shareholders who received the fully franked Mitchell Dividend directly will:

- include the amount of the franking credit attached to the Mitchell Dividend in their assessable income; and
- be entitled to a tax offset equal to the amount of the franking credit,

under section 207-20, subject to being a qualified person.

Qualified persons

31. The payment of the Mitchell Dividend as part of the scheme of arrangement will constitute a related payment for the purposes of former section 160APHN of the ITAA 1936.

32. Accordingly, each Mitchell shareholder will need to hold their Mitchell shares at risk for a continuous period of at least 45 days in the secondary qualification period in order to be a qualified person.

33. Those Mitchell shareholders who have held their Mitchell shares 'at risk' for a continuous period of not less than 45 days during the period 18 September 2010 to 8 November 2010 will be qualified persons with respect to the fully franked Mitchell Dividend.

Non-resident shareholders

34. Mitchell shareholders who received the fully franked Mitchell Dividend and are non-residents (other than those carrying on business in Australia at or through a permanent establishment in Australia) will not be required to include the dividend as assessable income under subparagraph 44(1)(b)(ii) of the ITAA 1936 (section 128D of the ITAA 1936) and will not be liable for Australian withholding tax (paragraph 128B(3)(ga) of the ITAA 1936).

Capital Gains Tax (CGT) consequences***CGT event A1***

35. CGT event A1 will happen when a participating Mitchell shareholder disposes of a Mitchell share to Aegis pursuant to the Scheme (subsections 104-10(1) and (2)).

36. The time of the CGT event will be when the change of ownership occurs (subsection 104-10(3)). This is when the Mitchell shares are transferred to Aegis on the Scheme Implementation date, being 17 November 2010.

Capital gain or capital loss

37. A participating Mitchell shareholder will make a capital gain when CGT event A1 happens if the capital proceeds in respect of the disposal of a Mitchell share exceed its cost base. A participating Mitchell shareholder will make a capital loss if the capital proceeds in respect of the disposal of their Mitchell share are less than its reduced cost base (subsection 104-10(4)).

Capital proceeds

38. The capital proceeds from the disposal of each Mitchell share will be the total of any cash consideration and the market value (worked out as at the time of CGT event A1) of the part of the Aegis share (if any) received or entitled to be received by the participating Mitchell shareholder in respect of its disposal (subsection 116-20(1)). The capital proceeds will not include the Mitchell Dividend as it is considered, having regard to all the circumstances of the arrangement, that it is not paid in respect of the CGT event happening (subsection 116-20(1)).

If a capital gain is made

Capital gain referable to Mitchell shares – full or partial scrip for scrip roll-over

39. Subject to the qualification in paragraph 40 of this Ruling, a participating Mitchell shareholder who makes a capital gain from the disposal of a Mitchell share may choose scrip for scrip roll-over for that part of the capital gain that is referable to the receipt of Aegis shares as capital proceeds (sections 124-780 and 124-790).

40. However, scrip for scrip roll-over cannot be chosen if any capital gain the participating Mitchell shareholder might make from the replacement Aegis shares would be disregarded, except because of a roll-over (subsection 124-795(2)).

41. If scrip for scrip roll-over is chosen, that part of the capital gain that is referable to the receipt of Aegis shares is disregarded (subsections 124-785(1)). Any part of the capital gain that is referable to the receipt of cash is not disregarded because it is ineligible proceeds for which roll-over is not available (subsection 124-790(1)).

Discount capital gain

42. If a participating Mitchell shareholder makes a capital gain from the disposal and roll-over is not chosen, or cannot be chosen, for all or part of the gain, they will be eligible to treat that part as a 'discount capital gain' provided that:

- the participating Mitchell shareholder is an individual, complying superannuation entity or, subject to the rules in Subdivision 115-C, a trust (section 115-10);
- the capital gain has been worked out using a cost base that has been calculated without reference to indexation (subsection 115-20(1)); and
- the Mitchell share was acquired at least 12 months prior to CGT event A1 happening.

Cost base of Aegis shares

43. The cost base and reduced cost base of any Aegis shares acquired by a participating Mitchell shareholder in exchange for all or part of their Mitchell shares, is affected by whether the shareholder chooses scrip for scrip roll-over.

Scrip for scrip roll-over is not chosen

44. Where scrip for scrip roll-over is not chosen, the first element of the cost base and reduced cost base of each Aegis share is equal to the market value of the relevant part of the Mitchell shares given in exchange for the acquisition of the Aegis share (subsections 110-25(2), 110-55(2) and 112-30(1)). The market value is worked out as at the time of the acquisition (subsection 110-25(2)). However the market value of the Mitchell shares given in respect of the acquisition of the Aegis share must first be reduced by that part of the market value that is reasonably attributable to any cash consideration (subsection 112-30(1)).

Scrip for scrip roll-over is chosen

45. Where scrip for scrip roll-over is chosen, the first element of the cost base and reduced cost base of a replacement Aegis share is worked out by reasonably attributing to it, the sum of the parts of the cost base of the Mitchell shares exchanged for the Aegis share and for which the roll-over was obtained (subsections 124-785(2) and 124-785(4)). However the cost base of the Mitchell shares must first be reduced by that part of the cost base of the Mitchell shares that is reasonably attributable to any cash consideration (subsection 124-785(3)).

Acquisition date of Aegis shares

46. The acquisition date of the Aegis shares will be the date when the shares are issued or allotted (Item 2 of the table in section 109-10).

47. For the purpose of determining whether a capital gain made from any later disposal of their Aegis shares is a discount capital gain, participating Mitchell shareholders who choose scrip for scrip roll-over are taken to have acquired their Aegis shares when they acquired the corresponding Mitchell shares subject to the roll-over (Item 2 of the table in subsection 115-30(1)).

Foreign resident shareholders

48. A foreign resident Mitchell shareholder who participates in the Scheme disregards any capital gain made when CGT event A1 happens if their share is not 'taxable Australian property' (section 855-10).

49. If their Mitchell share is taxable Australian property, a foreign resident shareholder is not eligible to choose roll-over if the replacement Aegis share is not taxable Australian property (subsection 124-795(1)).

The anti-avoidance provisions – imputation benefits

50. The Commissioner will not make a determination under paragraph 204-30(3)(c) to deny the whole, or any part, of the imputation benefit received in relation to the Mitchell Dividend.

51. 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 benefit received in relation to the Mitchell Dividend.

Commissioner of Taxation

3 November 2010

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.*

The Dividend

Dividend as defined in subsection 6(1)

52. The term 'dividend' is defined in subsection 6(1) of the ITAA 1936 and includes any distribution made by a company to any of its shareholders. The Mitchell Dividend will be a distribution in money made by Mitchell to its ordinary shareholders.

53. Paragraph (d) of the definition of 'dividend' in subsection 6(1) of the ITAA 1936 however excludes from the definition of 'dividend' any:

moneys paid or credited by a company to a shareholder or any other property distributed by a company to shareholders (not being moneys or other property to which this paragraph, by reason of subsection (4), does not apply or moneys paid or credited, or property distributed for the redemption or cancellation of a redeemable preference share), where the amount of the moneys paid or credited, or the amount of the value of the property, is debited against an amount standing to the credit of the share capital account of the company...

54. The Mitchell Dividend will be sourced from Mitchell's retained earnings. Mitchell will not debit the Mitchell Dividend to its share capital account. Therefore, the exclusion in paragraph (d) will not apply and the Mitchell Dividend will constitute a 'dividend' for the purposes of subsection 6(1) of the ITAA 1936.

Section 208-20

55. Section 208-20 states that a corporate tax entity is an exempting entity at a particular time if it is effectively owned by prescribed persons at that time. Subsection 208-25(1) provides in broad terms that an entity is effectively owned by prescribed persons if not less than 95% of accountable membership interests or accountable partial interests (broadly direct and indirect ownership interests) are held by or on behalf of prescribed persons.

56. Section 208-40 provides the definition of a prescribed person in relation to another corporate tax entity. Generally, the definition includes companies, trustees, partnerships or individuals that are a foreign resident or if they were to receive a distribution by the corporate tax entity, the distribution would be exempt income or non-assessable non-exempt income of the company, trust estate, partnership or individual.

57. As at 30 June 2010, 98.89% of the issued capital of Mitchell was held by resident shareholders. As the percentage of non resident shareholder ownership in Mitchell does not amount to Mitchell being effectively controlled by prescribed persons, Mitchell will not be an exempting entity under Division 208.

Assessability of the Dividend

58. Subparagraph 44(1)(a)(i) of the ITAA 1936 includes in the assessable income of an Australian resident shareholder in a company:

dividends (other than non-share dividends) that are paid to the shareholder by the company out of profits derived by it from any source.

59. As the Mitchell Dividend will be paid to Mitchell shareholders out of profits derived by Mitchell, Mitchell shareholders who are residents of Australia as defined in subsection 6(1) of the ITAA 1936 are required to include the Mitchell Dividend as assessable income under subparagraph 44(1)(a)(i).

Non-resident shareholders

60. Subparagraph 44(1)(b)(i) of the ITAA 1936 includes in the assessable income of a non-resident shareholder in a company:

dividends (other than non-share dividends) paid to the shareholder by the company to the extent to which they are paid out of profits derived by it from sources in Australia.

61. Subsection 128B(1) of the ITAA 1936 imposes Australian withholding tax on income that:

- (a) is derived, on or after 1 January 1968, by a non resident; and
- (b) consists of a dividend paid by a company that is a resident.

62. However, subparagraph 128B(3)(ga)(i) of the ITAA 1936 excludes from subsection 128B(1) of the ITAA 1936 income derived by a non-resident that consists of the franked part of a dividend. As the Mitchell Dividend will be fully franked, it will not be subject to Australian withholding tax when derived by non-resident Mitchell shareholders.

63. Additionally section 128D of the ITAA 1936 states that:

Income other than income to which section 128B applies by virtue of subsection (2A), (2C) or (9C) of that section upon which withholding tax is payable, or upon which withholding tax would, but for paragraph 128B(3)(ga) or (jb), section 128F, section 128FA or section 128GB, be payable, is not assessable income and is not exempt income of a person.

64. As the Mitchell Dividend is income that is subject to withholding tax but for paragraph 128B(3)(ga) of the ITAA 1936 it will not be assessable income and will not be exempt income of non-resident Mitchell shareholders pursuant to section 128D.

65. Withholding tax will not apply under section 128B of the ITAA 1936 where:

- the Mitchell Dividend is paid to a shareholder who is a non-resident carrying on business in Australia at or through a permanent establishment of the shareholder in Australia; and
- the dividend income is attributable to the permanent establishment – and the Mitchell Dividend is not paid to the shareholder in the shareholder's capacity as trustee.

66. Subsection 128B(3E) of the ITAA 1936 also ensures that none of the Mitchell Dividend will be non-assessable and non-exempt income under section 128D of the ITAA 1936.

67. Subparagraph 44(1)(c)(i) of the ITAA 1936 includes in the assessable income of a non-resident shareholder of a resident company who is carrying on business in Australia at or through a permanent establishment of the shareholder in Australia:

dividends (other than non-share dividends) that are paid to the shareholder by the company and are attributable to the permanent establishment, to the extent to which they are paid out of profits derived by the company from sources outside Australia.

68. As the Mitchell Dividend will be paid out of profits derived by Mitchell from sources both in and outside of Australia, non-resident Mitchell shareholders carrying on business in Australia at or through a permanent establishment will include the Mitchell Dividend in their assessable income to the extent they are attributable to the permanent establishment of the non-resident shareholder in Australia pursuant to subparagraphs 44(1)(b)(i) and 44(1)(c)(i) of the ITAA 1936.

Gross up and tax offset

69. Section 207-20 provides:

- (1) If an entity makes a *franked distribution to another entity, the assessable income of the receiving entity, for the income year in which the distribution is made, includes the amount of the *franking credit on the distribution. This is in addition to another amount included in the receiving entity's assessable income in relation to the distribution under any other provision of this Act.

- (2) The receiving entity is entitled to a *tax offset for the income year in which the distribution is made. The tax offset is equal to the *franking credit on the distribution.

70. Therefore, subject to satisfying the qualified person rule, where the fully franked Mitchell Dividend is received directly by a Mitchell shareholder, the Mitchell shareholder will:

- include the amount of the franking credit attached to the Mitchell Dividend in their assessable income; and
- be entitled to a tax offset equal to the amount of the franking credit.

71. Where the fully franked Mitchell Dividend is received by a Mitchell shareholder (not being an entity taxed as a corporate tax entity) that is a trustee of a trust (not being a complying superannuation fund) or a partnership, subsection 207-35(1) applies, subject to the trustee or partnership being a qualified person. Subsection 207-35(1) provides:

If:

- (a) a *franked distribution is made in an income year to an entity that is a partnership or the trustee of a trust; and
- (b) the entity is not a *corporate tax entity when the distribution is made; and
- (c) if the entity is the trustee of a trust – the trust is not a *complying superannuation entity or *FHSA trust when the distribution is made;

the assessable income of the partnership or trust for that income year includes the amount of the *franking credit on the distribution.

72. Therefore, a Mitchell shareholder who is a trustee of a trust or a partnership will be required to include the amount of the franking credit attached to the Mitchell Dividend in their assessable income under subsection 207-35(1).

Qualified persons

73. Pursuant to paragraph 207-145(1)(a), an entity must be a 'qualified person' in relation to a dividend in order to be entitled to a tax offset in respect of the franking credit allocated to the dividend.

74. Division 1A of former Part IIIAA of the ITAA 1936 (the former Division 1A) contains the measures known as the holding period rule and the related payment rule. In broad terms, the former Division 1A provides the statutory tests that must be satisfied for a taxpayer to be a 'qualified person' with respect to a franked distribution they have received and thus be entitled to a tax offset for the franking credit attached to the distribution.

75. The test of what constitutes a 'qualified person' is provided in former section 160APHO of the ITAA 1936 as follows:

A taxpayer who has held shares or an interest in shares on which a dividend has been paid is a 'qualified person' in relation to the dividend if:

- (a) where neither the taxpayer nor an associate of the taxpayer has made, is under an obligation to make, or is likely to make, a related payment in respect of the dividend – the taxpayer has satisfied subsection (2) in relation to the primary qualification period in relation to the dividend; or
- (b) where the taxpayer or an associate of a taxpayer has made, is under an obligation to make, or is likely to make, a related payment in respect of the dividend – the taxpayer has satisfied subsection (2) in relation to the secondary qualification in relation to the dividend.

76. Former subsection 160APHO(2) of the ITAA 1936, referred to in paragraph 75 of this Ruling, sets out the holding period requirement. Broadly, if a taxpayer is not under an obligation to make a related payment in relation to a dividend or distribution, the taxpayer will have to satisfy the holding period requirement within the primary qualification period. If a taxpayer makes or is under an obligation to make a related payment in relation to a dividend or distribution, the taxpayer will have to satisfy the holding period requirement within the secondary qualification period.

Related payment rule

77. In order to determine which is the relevant qualification period, it is necessary to determine whether, under the present arrangement, the Mitchell shareholders are considered to have made or be likely to make a related payment in respect of the Mitchell Dividend.

78. Former section 160APHN of the ITAA 1936 provides non-definitive examples of what constitutes the making of a related payment for the purposes of the former Division 1A. Former subsection 160APHN(2) provides:

The taxpayer or associate is taken, for the purposes of this Division, to have made, to be under an obligation to make, or to be likely to make, a related payment in respect of the dividend or distribution if, under an arrangement, the taxpayer or associate has done, is under an obligation to do, or may reasonably be expected to do, as the case may be, anything having the effect of passing the benefit of the dividend or distribution to one or more other persons.

79. Former subsection 160APHN(3) of the ITAA 1936 states:

Without limiting subsection (2), the doing of any of the following by the taxpayer or an associate of the taxpayer in the circumstances mentioned in subsection (4) may have the effect of passing the benefit of the dividend or distribution to one or more other persons:

- (a) causing a payment or payments to be made to, or in accordance with the directions of, the other person or other persons; or
- (b) causing an amount or amounts to be credited to, or applied for the benefit of, the other person or the other persons; or
- (c) causing services to be provided to, or in accordance with the directions of, the other person or other persons; or
- (d) causing property to be transferred to, or in accordance with directions of, the other person or other persons; or
- (e) allowing any property or money to be used by the other person or other persons or by someone nominated by the other person or other persons; or
- (f) causing an amount or amounts to be set off against, or to be otherwise applied in reduction of, a debt or debts owed by the other person or other persons; or
- (g) agreeing to treat an amount or amounts owed to the other person or other persons by the taxpayer or associate as having been increased.

80. Former subsection 160APHN(4) of the ITAA 1936 states:

The circumstances referred to in subsection (3), are where:

- (a) the amount or the sum of the amounts paid, credited or applied; or
- (b) the value or the sum of the values of the services provided, of the property transferred or of the use of the property or money; or
- (c) the amount or the sum of the amounts of the set-offs, reductions or increases;

as the case may be:

- (d) is, or may reasonably be expected to be, equal to; or
- (e) approximates or may reasonably be expected to approximate; or
- (f) is calculated by reference to;

the amount of dividend or distribution.

81. Where a shareholder is not taken to pass the benefit of the dividend to another person in the circumstances set out above, the shareholder will need to satisfy the holding period requirement in respect of the primary qualification period in order to be entitled to a tax offset in respect of the franking credit allocated to the dividend. However, where a shareholder is taken to pass the benefit of the dividend to another person in the circumstances set out above, the shareholder will need to satisfy the holding period requirement in respect of the secondary qualification period in order to be entitled to a tax offset in respect of the franking credit allocated to the dividend.

82. Mitchell has stated that the Mitchell Dividend will only be paid if the proposed Scheme of Arrangement is approved by shareholders making the payment of the dividend conditional on the Scheme proceeding. Further, the payment by Mitchell of a final dividend of up to \$0.05 per share is excluded from being a Mitchell Prescribed Event pursuant to Clause 4 of Schedule 2 of the Merger Implementation Agreement, indicating that the arrangement has specifically contemplated the payment of the dividend. Having regard to these factors, which amount to the Scheme contemplating the payment of a conditional dividend, it can be concluded that Mitchell shareholders will be taken to have made or be likely to make a related payment in relation to the Mitchell Dividend. The relevant holding period is thus the secondary qualification period pursuant to former paragraph 160APHO(1)(b).

Holding period requirement

83. The holding period requirement requires a shareholder to hold the shares, or the interest in the shares, on which a dividend is paid, at risk for a continuous period of at least 45 days during the relevant qualification period.

84. The primary qualification period as provided in the former section 160APHD of the ITAA 1936 begins from the day after the date of acquisition of the share and ends on the 45th day after the day on which the share becomes ex-dividend. In determining whether a shareholder has satisfied the holding period rule, any days during which there is a materially diminished risk in relation to the share are not counted.

85. The secondary qualification period is defined in former section 160APHD of the ITAA 1936 as follows:

In relation to a taxpayer in relation to shares or an interest in shares, means:

- (a) if the shares are not preference shares – the period beginning on the 45th day before, and ending on the 45th day after, the day on which the shares or interest became ex dividend...

86. The concept of 'ex-dividend' is defined by former subsection 160APHE(1) of the ITAA 1936 as follows:

a share in respect of which a dividend is to be paid, or an interest (other than an interest as a beneficiary of a widely held trust) in such a share, becomes ex dividend on the day after the last day on which the acquisition by a person of the share will entitle the person to receive the dividend.

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

88. It is considered that until the Record Date for the Scheme of Arrangement, (9 November 2010), Mitchell shareholders will not, by reason of the Scheme, have done anything to materially diminish their risks of loss or opportunities for gain in respect of their Mitchell shares.

89. It should be noted that no days after the 9 November 2010 for the Scheme of Arrangement will be capable of being counted to satisfy the at risk requirements, nor will the Mitchell shares be considered to be held at risk on the 9 November 2010 of the Scheme of Arrangement.

90. Accordingly, the secondary qualification period would run from 18 September 2010 until 8 November 2010. Those Mitchell shareholders who have held their Mitchell shares 'at risk' for a continuous period of not less than 45 days during this period will be qualified persons with respect to the fully franked Mitchell Dividend. Further, pursuant to former paragraph 160APHO(2)(a) of the ITAA 1936, the date of acquisition or disposal are not included in the relevant 45 day period. This would have the effect in the present circumstances, for example, that the 45 day qualification period could not include 18 September 2010 if this was the date of acquisition of Mitchell shares.

CGT consequences

CGT event A1

91. CGT event A1 (section 104-10) happens if there is a change in the ownership of an asset from one entity to another. This event happens when a contract to dispose of the asset is entered into or, if there is no contract, when the change of ownership occurs (subsection 104-10(3)).

92. A takeover or merger effected by a court approved scheme of arrangement does not involve a disposal of shares under a contract (refer to paragraph 9 of Taxation Determination TD 2002/4)

93. CGT event A1 will therefore happen to participating Mitchell shareholders when the change of ownership occurs. This is when the Mitchell shares are transferred to Aegis under the Scheme, which is on the Implementation date of 17 November 2010.

94. The time when CGT event A1 happens determines the income year in which any capital gain or loss is made and whether the CGT discount applies to any capital gain.

95. A participating Mitchell shareholder will make a capital gain from CGT event A1 happening if the capital proceeds from the disposal of their Mitchell share exceeds its cost base. A participating Mitchell shareholder will make a capital loss if those capital proceeds are less than the Mitchell share's reduced cost base (subsection 104-10(4)).

Capital Proceeds

96. The capital proceeds for CGT event A1 happening to a Mitchell share under the Scheme is the money received or entitled to be received and the market value of any other property received or entitled to be received in respect of the disposal of the Mitchell share (subsection 116-20(1)).

97. A participating Mitchell shareholder will be entitled to receive Scheme Consideration of the total of any cash and the market value (worked out as at the time of CGT event A1, being the Implementation Date) of any Aegis shares received or entitled to be received by the Mitchell shareholder in respect of CGT event A1 happening to their Mitchell shares.

98. The term 'in respect of the event happening' in subsection 116-20(1) requires the relationship between the event and the receipt of the money, or entitlement to receive the money, to be more than coincidental. An amount is not 'capital proceeds' of an event merely because it is received in association with the event.

99. If the Scheme is approved, any Mitchell shareholder who holds Mitchell Shares on the Dividend Record date of 1 November 2010 will receive a \$0.05 per share fully franked final dividend for the period ending 30 June 2010. If the Scheme is not approved, the fully franked final dividend for the period ending 30 June 2010 will be a lesser amount.

100. Although payment of the final dividend in the amount of \$0.05 is conditional upon Mitchell shareholders approving the Scheme of Arrangement, the dividend is not paid as a term or condition of the Scheme of Arrangement. It is therefore not received in respect of the disposal of the Mitchell shares under the Scheme. Accordingly it is not capital proceeds for the disposal of Mitchell shares.

Scrip for scrip roll-over – Subdivision 124-M

101. The significant tax consequence for Mitchell shareholders is the availability of scrip for scrip roll-over under Subdivision 124-M. It allows a shareholder to disregard a capital gain from a share that is disposed of as part of a corporate takeover or merger if the shareholder receives a replacement share in exchange. It does not allow a shareholder to disregard a capital gain to the extent to which the capital proceeds include something other than shares, for example, cash consideration. Subdivision 124-M also provides special rules for calculating the cost base and reduced cost base of the replacement share.

102. Subdivision 124-M contains a number of conditions for, and exceptions to, a shareholder being eligible to choose scrip for scrip roll-over. The main requirements that are relevant to the scheme that is the subject of this Ruling are:

- shares are exchanged for shares in another company;
- the exchange is in consequence of a single arrangement;
- conditions for the roll-over are satisfied;
- further conditions, if applicable, are satisfied; and
- exceptions to obtaining scrip for scrip roll-over are not applicable.

103. Under the Scheme, all of the conditions for roll-over under Subdivision 124-M are satisfied for Mitchell shares that are exchanged for Aegis shares. No further explanation of the application of those laws beyond that contained in the Ruling part of the document is necessary.

Foreign resident shareholders

104. Under subsection 855-10(1), an entity disregards a capital gain or capital loss from a CGT event if they are a foreign resident, or the trustee of a foreign trust for CGT purposes, just before the CGT event happens and the CGT event happens in relation to a CGT asset that is not 'taxable Australian property'.

105. The term 'taxable Australian property' is defined in the table in section 855-15. The table sets out these five categories of CGT assets:

Item 1	taxable Australian real property;
Item 2	an indirect Australian real property interest not covered by item 5;
Item 3	a CGT asset used at any time in carrying on a business through a permanent establishment in Australia and which is not covered by item 1, 2 or 5;
Item 4	an option or right to acquire a CGT asset covered by item 1, 2 or 3; and
Item 5	a CGT asset that is covered by subsection 104-165(3) (choosing to disregard a gain or loss on ceasing to be an Australian resident).

106. A Mitchell shareholder who is a foreign resident, or the trustee of a foreign trust for CGT purposes, just before CGT event A1 happens when they dispose of a Mitchell share pursuant to the Scheme, can not disregard a capital gain or capital loss from CGT event A1 under subsection 855-10(1) if:

- their Mitchell share is an indirect Australian real property interest (item 2 of the table in section 855-15); or
- their Mitchell share has been used at any time by the foreign resident, or the trustee of a foreign trust for CGT purposes, in carrying on a business through a permanent establishment in Australia (item 3 of the table in section 855-15); or
- their Mitchell share is covered by subsection 104-165(3) (item 5 of the table in section 855-15)

107. Subsection 124-795(1) provides that roll-over is not available if, just before the disposal, the original interest holder is a foreign resident unless, just after the acquisition of the replacement interest, the replacement interest is taxable Australian property. This means that foreign resident Mitchell shareholders are not eligible to choose scrip for scrip roll-over if the replacement Aegis shares are not taxable Australian property.

The anti-avoidance provisions

Section 204-30

108. Section 204-30 applies where a corporate tax entity streams the payment of dividends, or the payment of dividends and the giving of other benefits, to its members in such a way that:

- (a) an imputation benefit is, or apart from this section would be, received by a member of the entity as a result of the distribution or distributions (paragraph 204-30(1)(a));
- (b) the member would derive a greater benefit from franking credits than another member of the entity (paragraph 204-30(1)(b)); and
- (c) the other 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)).

109. Relevantly, if section 204-30 applies, the Commissioner is vested with a discretion under subsection 204-30(3) to make a determination in writing either:

- (a) that a specified franking debit arises in the franking account of the entity, for a specified distribution or other benefit to a disadvantaged member (paragraph 204-30(3)(a)); or
- (b) that no imputation benefit is to arise in respect of any distributions made to a favoured member and specified in the determination (paragraph 204-30(3)(c)).

110. For section 204-30 to apply, members to whom distributions are streamed must derive a greater benefit from franking credits than the members who consequently do not receive franking credits, or do not receive the same amount of franking credits as they would have had streaming not occurred.

111. Under the current Scheme for the payment of the Mitchell Dividend, all Mitchell shareholders will receive an imputation benefit as a result of the dividend; the resident shareholders in the form of a tax offset (paragraph 204-30(6)(a)) and the non-resident shareholders in the form of an exemption from dividend withholding tax (paragraph 204-30(6)(e)). The resident shareholders will derive a greater benefit from franking credits than the non-resident shareholders.

112. However, the dividend will be paid to all Mitchell shareholders at the respective Record Dates and will be fully franked with Australian franking credits. Accordingly, it cannot be argued that Mitchell will direct the flow of distributions in such a manner as to stream the imputation benefits such that one class of members will derive a greater benefit from the franking credits attached to the dividends, while the other members will receive lesser or no imputation benefits.

113. As the conditions in subsection 204-30(1) for the provision to apply will not be met, the Commissioner will not make a determination under paragraph 204-30(3)(c) to deny the whole, or any part, of the imputation benefit received in relation to the dividend.

Section 177EA

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

- (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 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, a 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.

115. If section 177EA of the ITAA 1936 applies, the Commissioner may make a determination under subsection 177EA(5) that either a franking debit arises to the company in respect of each distribution paid to the relevant taxpayer (paragraph 177EA(5)(a)) or, in the alternative, that no franking credit benefit arises in respect of a distribution paid to the relevant taxpayer (paragraph 177EA(5)(b)).

116. Mitchell is a corporate tax entity. The disposal of the ordinary shares in Mitchell pursuant to the Scheme is a scheme for the disposition of membership interests. The fully franked Mitchell Dividend is a frankable distribution that will be paid to Mitchell shareholders as a part of this Scheme who could, therefore, reasonably be expected to receive imputation benefits.

117. In the present case, the conditions of paragraphs 177EA(3)(a) to (d) of the ITAA 1936 are satisfied. Accordingly, the issue is whether having regard to the relevant circumstances of the scheme, it would be concluded that, on the part of Mitchell or its shareholders, there is a purpose, more than merely an incidental purpose, of conferring an imputation benefit under the Scheme.

118. In arriving at a conclusion the Commissioner must have regard to the relevant circumstances of the Scheme which include, but are not limited to, the circumstances set out in subsection 177EA(17) of the ITAA 1936. The relevant circumstances listed there 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 not be present at any one time in any one scheme.

119. The relevant circumstances of the Scheme indicate that there is no requisite purpose of conferring an imputation benefit under the Scheme. The dividends have been and will be fully franked, which is a continuation of Mitchell dividend policy to pay fully franked dividends. Mitchell has only ordinary shares on issue and the dividends have been and will be paid to all Mitchell shareholders on a pro-rata basis in proportion to the number of shares that each Mitchell shareholder holds on the relevant Record Dates for the dividends. The amount of the Dividend is largely consistent with dividends previously paid out by Mitchell and allowed Mitchell shareholders to share in the current profits of Mitchell for the income half year ended 30 June 2010. The amount of the Dividend allows Mitchell Shareholders to share in the accumulated profits of Mitchell.

120. In considering the manner, form and substance of the Scheme, it is considered that the Scheme is not being entered into for the purpose of enabling participating members to obtain an imputation benefit. Having regard to the relevant circumstances of the Scheme, the Commissioner has come to the view that the requisite purpose is not present and accordingly 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 benefit received in relation to the dividend.

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References

Previous draft:

Not previously issued as a draft

Related Rulings/Determinations:

TR 2006/10; TD 2002/4

Subject references:

- arrangement
- CGT capital proceeds
- CGT event A1 – disposal of a CGT asset
- dividend streaming arrangement
- dividend stripping
- frankable dividends
- franking credits
- holding period rule
- imputation system
- ordinary shares
- qualified person
- related payment rule
- scrip for scrip roll-over

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Income Tax ~~ Tax integrity measures ~~ dividend streaming and demerger benefits
Income Tax ~~ Tax integrity measures ~~ qualified persons – franking credits