

CR 2011/106 - Income tax: DEXUS Property Group - Capital Reallocation

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Class Ruling

Income tax: DEXUS Property Group – Capital Reallocation

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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 provisions identified below apply to the defined class of entities, who take part in the scheme to which this Ruling relates.

Relevant provision(s)

2. The relevant provisions dealt with in this Ruling are:

- section 6-5 of the *Income Tax Assessment Act 1997* (ITAA 1997);
- section 104-70 of the ITAA 1997;
- section 110-25 of the ITAA 1997;
- section 110-55 of the ITAA 1997;
- Division 725 of the ITAA 1997;
- Division 727 of the ITAA 1997; and
- section 855-10 of the ITAA 1997.

All subsequent legislative references in this Ruling are to the ITAA 1997 unless otherwise stated.

Class of entities

3. The class of entities to which this Ruling applies are the stapled security holders (Securityholders) of DEXUS Property Group (DXS) who:

- (a) are registered on the DXS unit register on the record date of 19 December 2011 for the return of capital;
- (b) hold their units in DEXUS Office Trust, DEXUS Diversified Trust, DEXUS Industrial Trust and DEXUS Operations Trust on capital account;
- (c) participate in the capital reallocation (Capital Reallocation) to be announced on 8 December 2011 and described in the Scheme part of this Ruling; and
- (d) are not subject to the taxation of financial arrangements rules in Division 230 in relation to gains and losses on their units.

(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 scheme 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 24 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 2011 to 30 June 2012. The Ruling continues to apply after 30 June 2012 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 in the following documents:

- application for class ruling dated 12 September 2011 lodged by Greenwoods & Freehills;
- appendix A – the proposed capital reallocation flow charts;
- appendix B – class ruling checklist;
- appendix C – draft class ruling;
- appendix D – marked up proposed amendments to the DEXUS Industrial Trust Consolidated Constitution (identical changes will be made to each constitution for the Trusts involved in the scheme);
- DEXUS Property Group Financial Report 2011;
- DEXUS Industrial Trust Financial Statements 2011;
- DEXUS Office Trust Financial Statements 2011;
- DEXUS Operations Trust Financial Statements 2011;
- correspondence from Greenwoods & Freehills dated 17 October 2011.

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

10. In this Ruling, unless otherwise defined, capitalised terms take on the same meaning as provided in the above documentation.

The DEXUS Property Group

11. DXS is an Australian property group that specialises in owning, managing and developing office industrial properties and retail properties, primarily in Australia and the US. In Australia, DXS has interests in office and industrial properties and manages and develops shopping centres.

12. DXS consists of four trusts:

- DEXUS Funds Management Limited (DXFM) as the responsible entity of the DEXUS Office Trust (DOT);
- DXFM as the responsible entity of the DEXUS Diversified Trust (DDF);
- DXFM as the responsible entity of the DEXUS Industrial Trust (DIT); and
- DXFM as the responsible entity of the DEXUS Operations Trust (DXO).

13. DOT, DDF, DIT and DXO trade on the Australian Securities Exchange as a single (quadruple) stapled security (ASX:DXS). DXS has been listed since 6 October 2004.

The Capital Reallocation

14. Securityholders will be asked to approve a capital reallocation which will include a return of trust capital by:

- DDF to all Securityholders of \$0.03616 per unit; and
- DOT to all Securityholders of \$0.03616 per unit.

15. There are currently approximately 4.8 billion DDF and DOT units on issue (each included in the DXS staple). Consequently, the aggregate capital return will be approximately \$175 million each for DDF (DDF Capital Reduction Amount) and DOT (DOT Capital Reduction Amount) (together, Capital Reduction Amounts).

16. Both the DDF Capital Reduction Amount and the DOT Capital Reduction Amount will be debited to the contributed equity of DDF and DOT respectively.

17. These capital returns will be compulsorily applied on behalf of each Securityholder as a further capital contribution in respect of a Securityholder's existing units in:

- DIT, as to \$0.03616 per unit; and
- DXO, as to \$0.03616 per unit.

18. A DXS Securityholder will not receive any cash as part of the Capital Reallocation.

19. There are currently approximately 4.8 billion DIT and DXO units on issue (each included in the DXS staple). Consequently, the aggregate capital contribution will be approximately \$175 million for each of DIT (DIT Contribution Amount) and DXO (DXO Contribution Amount).
20. The DIT Contribution Amount and the DXO Contribution Amount are to be contributed in respect of the existing units in DIT and DXO respectively. No new units will be issued in DIT or DXO under the Capital Reallocation.
21. DXFM as the responsible entity will resolve that the distribution of the DDF Capital Reduction Amount and the DOT Capital Reduction Amount will be distributions of trust capital. DXFM will distribute the Distributable Income (clause 9.2 of the Consolidated Constitution) of DDF and DOT for the year ended 30 June 2012 to the Securityholders in the usual manner.
22. Approval will be sought from DXS Securityholders to amend the constitutions of DOT, DDF, DIT and DXO to facilitate the Capital Reallocation. The amendments would permit DXFM to receive the DDF Capital Reduction Amount and the DOT Capital Reduction Amount as attorney for the Securityholders and to apply those amounts towards a contribution of additional equity in DIT and DXO respectively.
23. The internal flow of funds under the Capital Reallocation will be facilitated through DXS Group's internal funding vehicle, DEXUS Finance Pty Limited (DXF), utilising an existing Intra-Group Master Facility Agreement by which DXF may make loans to and borrow from each of DOT, DDF, DIT and DXO.
24. In respect of DXS no entity, or no entity and its associates between them, has the right to receive at least 40% of any distribution of trust income, or trust capital, as beneficiaries of DXS.

Ruling

Non-assessable payment

25. Neither the DDF return of capital of \$0.03616 per unit nor the DOT return of capital of \$0.03616 per unit will be included in a Securityholder's assessable income under section 6-5.

CGT event E4

26. CGT event E4 happens in respect of each DDF unit when DDF pays \$0.03616 per unit to a Securityholder (section 104-70). For the purposes of section 104-70, the entire amount of \$0.03616 per DDF unit is a non-assessable part.

27. CGT event E4 happens in respect of each DOT unit when DOT pays \$0.03616 per unit to a Securityholder (section 104-70). For the purposes of section 104-70, the entire amount of \$0.03616 per DOT unit is a non-assessable part.

Capital gain – DDF

28. A Securityholder will make a capital gain if the non-assessable amount of \$0.03616 per DDF unit made by DDF during the income year in respect of the DDF unit exceeds the cost base of the unit (subsection 104-70(4)).

29. However, this capital gain will be disregarded if the relevant DDF unit was acquired (within the meaning of section 109-1) on or before 19 September 1985 (subsection 104-70(7)).

Cost base reduction – DDF

30. Where a Securityholder makes a capital gain when CGT event E4 happens, the cost base and reduced cost base of the DDF unit will be reduced to nil (subsection 104-70(5)).

31. If the non-assessable amount of \$0.03616 per DDF unit is less than or equal to the cost base of the DDF unit, the cost base and reduced cost base of the DDF unit are reduced by that amount (subsection 104-70(6)).

Capital gain – DOT

32. A Securityholder will make a capital gain if the non-assessable amount of \$0.03616 per DOT unit made by DOT during the income year in respect of the DOT unit exceeds the cost base of the unit (subsection 104-70(4)).

33. However, this capital gain will be disregarded if the relevant DOT unit was acquired (within the meaning of section 109-1) on or before 19 September 1985 (subsection 104-70(7)).

Cost base reduction – DOT

34. Where a Securityholder makes a capital gain when CGT event E4 happens, the cost base and reduced cost base of the DOT unit will be reduced to nil (subsection 104-70(5)).

35. If the non-assessable amount of \$0.03616 per DOT unit is less than or equal to the cost base of the DOT unit, the cost base and reduced cost base of the DOT unit are reduced by that amount (subsection 104-70(6)).

Foreign resident Securityholders

36. A foreign resident Securityholder who is paid the DDF Capital Reduction Amount and DOT Capital Reduction Amount disregards any capital gain made from CGT event E4 if their DDF and DOT units do not constitute 'taxable Australian property' (section 855-10).

Capital Contribution***Cost base – DXO***

37. The fourth element of the cost base and reduced cost base of a DXO unit will increase by \$0.03616 per unit, which is the DXO Contribution Amount (subsections 110-25(5) and 110-55(2)).

Cost base – DIT

38. The fourth element of the cost base and reduced cost base of a DIT unit will increase by \$0.03616 per unit, which is the DIT Contribution Amount (subsections 110-25(5) and 110-55(2)).

Value Shifting

39. There will be no consequences for a Securityholder under Divisions 725 and 727.

Commissioner of Taxation7 December 2011

Appendix 1 – Explanation

ⓘ *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.*

Non-assessable payment

40. Subsection 6-5(1) provides that a taxpayer's assessable income includes income according to ordinary concepts (ordinary income). In *Scott v. Federal Commissioner of Taxation* (1966) 117 CLR 514; (1966) 10 ATR 367; (1966) 14 ATD 286, Windeyer J stated that:

Whether or not a particular receipt is income depends upon its quality in the hands of the recipient.

41. The DDF Capital Reduction Amount and the DOT Capital Reduction Amount will be a distribution of trust capital for the year ending 30 June 2012, (being a payment of corpus) and does not have the quality of income in the hands of the Securityholders and is not ordinary income under section 6-5.

CGT event E4

42. Under section 104-70, CGT event E4 happens if the trustee of a trust makes a payment to a unitholder in respect of their unit in the trust and some or all of the payment is not included in the unitholder's assessable income (non-assessable payment).

43. The consequences of CGT event E4 happening are determined on an annual basis, that is, having regard to all such CGT events that happen to a unit during an income year (subsection 104-70(3)).

44. CGT event E4 happens in respect of each DDF unit when DDF pays \$0.03616 per unit to a Securityholder (section 104-70). For the purposes of section 104-70, the entire amount of \$0.03616 per DDF unit is a non-assessable part.

45. CGT event E4 happens in respect of each DOT unit when DOT pays \$0.03616 per unit to a Securityholder (section 104-70). For the purposes of section 104-70, the entire amount of \$0.03616 per DOT unit is a non-assessable part.

Capital gain

46. If CGT event E4 happens during an income year, a unitholder will make a capital gain if the total value of the non-assessable payments made by the trustee during the income year in respect of their unit exceeds its cost base (subsection 104-70(4)).

47. A Securityholder will make a capital gain if the non-assessable amount of \$0.03616 made for each of their DDF units during the income year exceeds the cost base of the unit (subsection 104-70(4)).

48. A Securityholder will make a capital gain if the non-assessable amount of \$0.03616 made for each of their DOT units during the income year exceeds the cost base of the unit (subsection 104-70(4)).

49. However, this capital gain will be disregarded if the relevant DDF unit or DOT unit was acquired (within the meaning of section 109-1) on or before 19 September 1985 (subsection 104-70(7)).

Cost base reduction

50. When a unitholder makes a capital gain from CGT event E4 happening, the cost base and reduced cost base of the unit are reduced to nil (subsection 104-70(5)).

51. However, if the sum of the non-assessable payments is less than or equal to the cost base of the unit, the cost base and reduced cost base of the unit are reduced by that amount. A unitholder cannot make a capital loss when CGT event E4 happens (subsection 104-70(6)).

52. Where the Securityholder makes a capital gain, the cost base and reduced cost base of their DDF or DOT unit are reduced to nil (subsection 104-70(5)).

53. If the non-assessable amount of \$0.03616 per DDF or DOT unit is less than or equal to the cost base of the respective unit, the cost base and reduced cost base of the DDF or DOT is reduced by that amount (subsection 104-70(6)).

54. The CGT event in respect of a capital reduction will occur just before the end of the income year in which DXFM pays that Capital Reduction Amount or, if another CGT event other than CGT event E4, happens in relation to the unit after DXFM pays that Capital Reduction but before the end of that income year – just before the time of that other CGT event.

Foreign resident Securityholders

55. Under subsection 855-10(1), an entity disregards a capital gain or capital loss made 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 in relation to a CGT asset that is not 'taxable Australian property'.

56. 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).

57. A foreign resident, or the trustee of a foreign trust for CGT purposes, just before CGT event E4 happens, cannot disregard under subsection 855-10(1) a capital gain from CGT event E4 happening if:

- *their DDF of DOT unit was an 'indirect Australian real property interest' (item 2 of the table in section 855-15);*
- *their DDF or DOT unit had been used at any time by the foreign resident in carrying on a business through a permanent establishment in Australia (item 3 of the table in section 855-15); or*
- *their DDF or DOT unit was covered by subsection 104-165(3) (item 5 of the table in section).*

Capital contribution and cost base

58. The return of trust capital on each DDF and DOT units has been applied to each DXO and DIT units as a capital contribution. This capital contribution represents capital expenditure incurred by a Securityholder for the purpose of increasing the value of their DXO and DIT units.

59. The fourth element of the cost base and reduced cost base of each DXO and DIT unit includes the amount of the capital contribution that is referable to that unit (subsection 110-25(5) and 110-55(2)).

Value Shifting

60. There is a direct value shift under a scheme involving equity or loan interests in an entity where there is a decrease in the market value of some equity or loan interest and an increase or issue at a discount of other equity or loan interests (section 725-145).

61. There is an indirect value shift where there is an unequal exchange of economic benefits between two entities – the losing entity and gaining entity (subsection 727-150(3)).

62. There can only be consequences for a direct value shift if there is any entity that controls the target entity for value shifting purposes at some time during the scheme period as defined in section 725-55 (paragraph 725-50(b)). Section 727-355 sets out the relevant tests for whether an entity controls a company for value shifting purposes. Section 727-360 sets out the relevant tests for whether an entity controls a fixed trust for value shifting purposes.

63. There can only be consequences for an indirect value shift if the entities between which the value is shifted (the losing entity and the gaining entity) satisfy an ultimate controller test and/or a common ownership nexus test at some time during the indirect value shift period defined in subsection 727-150(7) (paragraph 727-100(c) and sections 727-105 and 727-110).

64. There are no consequences for any direct value shift or indirect value shift that happens under the arrangement involving the capital reallocation. There are no consequences for any direct value shift as there is no entity that controls (for value shifting purposes) DXS at any time from when the arrangement is entered into until when it is carried out (paragraph 725-50(b) and section 725-55). There are no consequences for any indirect value shift as no entity would, together with DXS, meet the ultimate controller test or common ownership nexus test (paragraphs 727-100(c) and 727-110(1)(a) and section 727-355).

Appendix 2 – Detailed contents list

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

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References

Previous draft:

Not previously issued as a draft

Related Rulings/Determinations:

TR 2006/10

Subject references:

- capital gains
- Capital Gains Tax
- CGT assets
- CGT cost base
- CGT events
- CGT events E1-E9 – trusts
- CGT reduced cost base
- present entitlement
- trusts
- value shifting – entity interests
indirect value shifting rules

Legislative references:

- ITAA 1997 6-5(1)
- ITAA 1997 104-70(1)

- ITAA 1997 104-70(1)(b)
- ITAA 1997 104-70(4)
- ITAA 1997 104-70(5)
- ITAA 1997 104-70(6)
- ITAA 1997 104-70(7)
- ITAA 1997 104-165(3)
- ITAA 1997 109-1
- ITAA 1997 110-25(5)
- ITAA 1997 855-10
- ITAA 1997 855-15
- ITAA 1997 855-25(1)
- ITAA 1997 855-30
- ITAA 1997 960-195
- TAA 1953
- Copyright Act 1968

Case references:

- *Scott v. Federal Commissioner of Taxation* (1966) 117 CLR 514; (1966) 10 AITR 367; (1966) 14 ATD 286

ATO references

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