


# ***CR 2012/52 - Income tax: Gloucester Coal Limited - Special Dividend and Capital Return***

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## Class Ruling

### Income tax: Gloucester Coal Limited – Special Dividend and Capital Return

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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

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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);
- subparagraph 44(1)(a)(i) of the ITAA 1936;
- section 45A of the ITAA 1936;
- section 45B of the ITAA 1936;
- section 45C of the ITAA 1936;
- paragraph 177EA(5)(b) of the ITAA 1936;
- Division 67 of the *Income Tax Assessment Act 1997* (ITAA 1997);
- section 104-25 of the ITAA 1997;
- section 104-135 of the ITAA 1997;

- Division 115 of the ITAA 1997;
- section 202-40 of the ITAA 1997;
- paragraph 204-30(3)(c) of the ITAA 1997;
- subsection 205-15(1) of the ITAA 1997;
- section 207-20 of the ITAA 1997;
- section 207-145 of the ITAA 1997;
- section 207-155 of the ITAA 1997; and
- section 208-195 of the ITAA 1997.

## **Class of entities**

3. The class of entities to which this Ruling applies are shareholders in Gloucester Coal Limited (Gloucester) who:

- held ordinary shares in Gloucester on capital account on the Capital Reduction Record Date of 22 June 2012;
- acquired their Gloucester Shares on, or after, 20 September 1985;
- were 'Australian residents' (within the meaning of subsection 995-1(1) of the ITAA 1997); and
- were not a 'temporary resident' of Australia within the meaning of subsection 995-1(1) of the ITAA 1997.

4. This Ruling does not apply to Gloucester Shareholders for whom gains and losses from the Gloucester Special Dividend and Capital Return are subject to the taxation of financial arrangements rules in Division 230 of the ITAA 1997.

**(Note:** Division 230 of the ITAA 1997 will not generally apply to the financial arrangements of individuals, unless they have made an election for those rules to apply to them.)

5. This Ruling does not apply to Gloucester Shareholders where the Gloucester Special Dividend or the Capital Return is exempt income (within the meaning of section 6-20 of the ITAA 1997) or non-assessable non-exempt income (within the meaning of section 6-23 of the ITAA 1997), in their hands.

6. This Ruling does not consider how the gross-up and tax offset rules in Division 207 of the ITAA 1997 apply to a Gloucester Shareholder that is a partnership or trustee, or to indirect distributions to partners in a partnership, trustees or beneficiaries of a trust.

**Qualifications**

7. The class of entities defined in this Ruling may rely on its contents provided the scheme actually carried out is carried out in accordance with the scheme described in paragraphs 11 to 38 of this Ruling.

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

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

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**Date of effect**

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10. This Ruling applies from 22 June 2012 to 30 June 2013. The Ruling continues to apply after 30 June 2013 to all entities within the specified class who entered into the specified scheme during the term of the Ruling. However, this Ruling will not apply to taxpayers to the extent that it conflicts with the terms of a settlement of a dispute agreed to before the date of issue of this Ruling (see paragraphs 75 and 76 of Taxation Ruling TR 2006/10).

**Scheme**

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11. The following description of the scheme is based on information provided by Minter Ellison Lawyers (Applicant). The following documents, or relevant parts of them form part of, and are to be read with, the description:

- application for class ruling dated 23 February 2012 lodged by the Applicant on behalf of Gloucester;
- Merger Proposal Deed dated 22 December 2011;
- Amendment Deed – Merger Proposal Deed dated 6 March 2012;

- resolution to the Gloucester General Meeting of 4 June 2012;
- Promissory Note Trust Deed;
- Deed of Appointment of Promissory Note Trustee;
- Promissory Note; and
- correspondence from the Applicant providing further particulars.

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

12. In this Ruling, unless otherwise indicated, capitalised terms take on the same meanings as in the documents listed in the previous paragraph. In this context, 'Capital Reduction Amount' refers to the total amount by which the share capital of Gloucester was reduced, and 'Capital Return' is the capital amount per Gloucester share that was returned to Gloucester Shareholders.

13. Gloucester is a public company that has been listed on the Australian Securities Exchange (ASX) since June 1985. As at 30 June 2011, Gloucester had an approximate market capitalisation of \$1.4 billion.

14. On 22 December 2011, Gloucester entered into a Merger Proposal (the Scheme) with Yancoal Australia Limited (Yancoal) and Yanzhou Coal Mining Company Limited (Yanzhou). The terms of the Scheme were amended on 6 March 2012 through the Amendment Deed – Merger Proposal Deed.

15. A Scheme Meeting approving the Scheme was held on 4 June 2012. The Scheme Record Date for determining entitlements to the Scheme Consideration for Gloucester Shareholders was 4 July 2012. The Scheme Consideration being either one Yancoal Share and one contingent value rights share for each Gloucester share, or, if an election is made, one Yancoal Share for each Gloucester Share.

16. A General Meeting followed the Scheme Meeting at which the Capital Return was approved by the Gloucester Shareholders.

17. The ex-entitlement date to the Gloucester Special Dividend and Capital Return for Gloucester shares traded on the ASX was 18 June 2012.

18. On 25 June 2012 (prior to the Implementation Date of the Scheme), Gloucester paid to shareholders listed on the Gloucester Share Register at 7:00pm on 22 June 2012 (Capital Reduction Record Date):

- a Gloucester Special Dividend of \$0.47 per Gloucester Share; and
- a Capital Return of \$2.68356463 per Gloucester Share.

19. At the time that the Gloucester Special Dividend and Capital Return were paid, Gloucester was a resident of Australia under the laws of Australia and of no other jurisdiction.

### **Gloucester Special Dividend**

20. The Gloucester Board announced on 14 June 2012 that Gloucester Shareholders would receive a special dividend of \$0.47 per Gloucester Share payable after the Court's approval of the Scheme but prior to the Effective Date of the Scheme. The Court approved the Scheme on 13 June 2012, and the Effective Date of the Scheme was 27 June 2012.

21. The amount of the Gloucester Special Dividend was calculated based on the amount of retained earnings and current year profits in Gloucester at the Capital Reduction Record Date. The Gloucester Special Dividend will effectively deplete almost all of the balance of Gloucester's retained earnings and current year profits.

22. The payment of the Gloucester Special Dividend was at the absolute discretion of the Gloucester Board and was not conditional on the implementation of the Scheme.

23. Gloucester advised that neither Yancoal nor Yanzhou had any influence or control over the declaration or payment of the Gloucester Special Dividend by Gloucester.

24. The Gloucester Special Dividend was paid out of the retained profits and current year profits of Gloucester and was not sourced directly, or indirectly, from Gloucester's share capital account.

25. The Gloucester Special Dividend is a fully franked dividend and was paid on 25 June 2012 to all Gloucester Shareholders listed on the Gloucester Share Register on the Capital Reduction Record Date.

26. Gloucester has a history of paying franked and unfranked dividends.

### **Capital Return**

27. The Gloucester Board announced on 14 June 2012 that Gloucester Shareholders listed on the Gloucester Share Register on the Capital Reduction Record Date would receive a Capital Return of approximately \$2.68 per Gloucester Share payable on or about 25 June 2012, being after the Court's approval of the Scheme but prior to the Effective Date of the Scheme.

28. The Capital Return required the approval of a simple majority of the votes cast by Gloucester Shareholders present at a general meeting, and was not conditional on the approval of the Scheme. The Capital Return was approved at a General Meeting of Gloucester Shareholders on 4 June 2012.

29. The payment of the Capital Reduction Amount was made by creating a debt on the Capital Reduction Record Date due to each holder of Gloucester Shares as at the Capital Reduction Record Date equal to an amount calculated by the following formula:

$$\text{Eligible Shareholders Debt} = \frac{\text{ESH}}{\text{TGS}} \times \text{Capital Reduction Amount}$$

where:

**ESH** means the total number of Gloucester Shares held by the [eligible] Shareholder as at the Capital Reduction Record Date; and

**TGS** means the total number of Gloucester Shares on issue as at the Capital Reduction Record Date.

30. The Eligible Shareholders Debt (representing a Gloucester Shareholder's entitlement to the Capital Return), was discharged in full by the issue of Promissory Notes drawn by Gloucester for an amount equal to each Eligible Shareholders Debt. The payment date being 25 June 2012.

### **Promissory Note Trust**

31. Pursuant to the Constitution of Gloucester and the terms of the resolution approving the Capital Return, Gloucester appointed a Trustee to hold on trust the Promissory Notes for Gloucester Shareholders (Beneficiaries) in accordance with the Promissory Note Trust Deed.

32. Gloucester delivered the Promissory Notes to the Trustee of the Promissory Note Trust on 26 June 2012.

33. Other than for Joint Holders where there is one separate trust for all Joint Holders, each trust for each Beneficiary is a separate trust to any trust for another Beneficiary under the Promissory Note Trust Deed, and no Beneficiary has any interest in the Entitlement of another Beneficiary (clauses 4.1(c) and 4.1(d) of the Promissory Note Trust Deed).

34. A trust for each Promissory Note arose when the Promissory Note was settled on the Trustee of the Promissory Note Trust.

35. Promissory Notes are payable in full by Gloucester to the Trustee on 7 January 2013 following the presentation of the Promissory Notes by the Trustee. Gloucester bears the responsibility to pay the redemption proceeds of the Promissory Notes to the Beneficiaries on presentation of the Promissory Notes to Gloucester for payment on 7 January 2013.

**Funding of the Gloucester Special Dividend, Capital Reduction Amount and Gloucester Option Amount**

36. Yancoal provided written confirmation to Gloucester (including from the relevant financiers) that it has in place \$700 million of funding enabling Gloucester to pay in full and on time, the:

- (a) Gloucester Special Dividend on 25 June 2012;
- (b) Promissory Notes for payment on 7 January 2013; and
- (c) Gloucester Option Amount (this Ruling does not consider the tax consequences relating to the payment of this amount).

37. Gloucester advised that although Yancoal financed the payment of the Gloucester Special Dividend, the finance:

- was not conditional on the implementation of the Scheme – no negotiations have occurred between Yancoal and Gloucester regarding the final amount of the Gloucester Special Dividend, nor the requirement to pay such dividend;
- was an alternative to Gloucester obtaining third party funding – Yancoal has access to more favourable funding terms due to its size; and
- addressed the requirement that the Gloucester Board be satisfied on reasonable grounds that the payment of the Gloucester Special Dividend would not result in Gloucester trading whilst being insolvent and that it would not materially prejudice Gloucester's ability to pay its creditors.

**Other matters**

38. This Ruling is made on the basis that:

- the documents listed in paragraph 11 of this Ruling provide a complete and accurate description of the scheme;
- the documents listed in paragraph 11 of this Ruling are intended by the parties to have their legal effect, and the scheme will be implemented according to the terms of those documents;
- all parties to the scheme are dealing with each other on arm's length terms;
- Gloucester franked the Gloucester Special Dividend at the same franking percentage as the benchmark for the franking period in which the payment was made;

- for the purposes of determining whether a Gloucester Shareholder is a 'qualified person' under Division 1A of former Part IIIAA of the ITAA 1936, the Gloucester Shareholder and their associates will not have taken any 'positions' (within the meaning of former section 160APHJ of the ITAA 1936) in relation to their Gloucester Shares or an interest in the Gloucester Shares apart from holding those Gloucester Shares, and will not make, or will not be under an obligation to make, a 'related payment' (within the meaning of former section 160APHN of the ITAA 1936) in relation to the Gloucester Special Dividend;
- the Gloucester Shareholders in receipt of the Gloucester Special Dividend will have held their Gloucester Shares for a period of at least 45 days (excluding the day of acquisition and the day of disposal, and any days on which the Gloucester Shareholder has materially diminished risks of loss or opportunities for gain in respect of their Gloucester Shares or an interest in their Gloucester Shares), within the period beginning on the day after the day on which the Gloucester Shareholders acquired their Gloucester Shares and ending on the 45th day after the day on which the Gloucester Shares become ex-dividend; and
- the Gloucester Special Dividend was paid out of the retained profits and current year profits of Gloucester and not sourced, directly or indirectly, from Gloucester's share capital account.

## Ruling

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### **Gloucester Special Dividend**

#### ***Inclusion of the Gloucester Special Dividend in assessable income***

39. The Gloucester Special Dividend of \$0.47 per share paid to Gloucester Shareholders will constitute a dividend as defined in subsection 6(1) of the ITAA 1936.

40. The Gloucester Special Dividend is a 'frankable distribution' within the meaning of section 202-40 of the ITAA 1997.

41. Gloucester Shareholders must include in their assessable income:

- the Gloucester Special Dividend (subparagraph 44(1)(a)(i) of the ITAA 1936); and
- the amount equal to the franking credit that is attached to the Gloucester Special Dividend (subsection 207-20(1) of the ITAA 1997).

***Entitlement to a tax offset***

42. Gloucester Shareholders will be entitled to a tax offset equal to the franking credit that is attached to the Gloucester Special Dividend (subsection 207-20(2) of the ITAA 1997).

43. Gloucester Shareholders, who are entitled to a tax offset under subsection 207-20(2) of the ITAA 1997 in respect of the franking credits attached to the Gloucester Special Dividend, will also be subject to the refundable tax offset rules in Division 67 of the ITAA 1997, unless the Gloucester Shareholders are specifically excluded under section 67-25 of the ITAA 1997.

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

44. The Gloucester Special Dividend made by Gloucester does not fall within one or more of the circumstances listed under section 207-145 of the ITAA 1997, specifically:

- a Gloucester Shareholder is a qualified person in relation to the Gloucester Special Dividend distribution for the purposes of Division 1A of former Part IIIAA of the ITAA 1936, and in this context:
  - the Gloucester Special Dividend will not be considered to be a 'related payment' for the purposes of Division 1A of former Part IIIAA of the ITAA 1936; and
  - the holding period rule under former section 160APHO of the ITAA 1936 will be satisfied for Gloucester Shareholders in respect of the Gloucester Special Dividend if:
    - the Gloucester Shares were acquired on or before 18 May 2012; and
    - during the period when the Gloucester Shares or interest in the shares were held, the Gloucester Shareholders did not have 'materially diminished risks of loss or opportunities for gain' (as defined under former section 160APHM of the ITAA 1936) for a continuous period of at least 45 days;
- the Commissioner has not made a determination under paragraph 177EA(5)(b) of the ITAA 1936 (see paragraph 48 of this Ruling);
- the Commissioner has not made a determination under paragraph 204-30(3)(c) of the ITAA 1936 (see paragraph 47 of this Ruling); and
- the distribution is not made as part of a dividend stripping operation under section 207-155 of the ITAA 1997.

45. As Gloucester is not an exempting entity or former exempting entity, section 208-195 of the ITAA 1997 will not apply to deny the gross-up of a Gloucester Shareholder's assessable income to exclude the franking credit, nor to deny the tax offset to which a Gloucester Shareholder would have been otherwise entitled under Division 207 of the ITAA 1997.

### ***Credit to franking account for certain corporate tax entities***

46. For a Gloucester Shareholder that is a 'franking entity' (within the meaning given in section 202-15 of the ITAA 1997) and is entitled to a tax offset under Division 207 of the ITAA 1997 in respect of the franking credit on the Gloucester Special Dividend, a credit of the franking credit on the dividend will arise in the Gloucester Shareholder's franking account on the day the Gloucester Special Dividend is made (item 3 of the table in subsection 205-15(1) of the ITAA 1997).

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

47. The Commissioner will not make a determination under paragraph 204-30(3)(c) of the ITAA 1997 to deny the whole, or any part, of the imputation benefits in relation to the Gloucester Special Dividend received by Gloucester Shareholders.

### ***General anti-avoidance provision***

48. The Commissioner will not make a determination under paragraph 177EA(5)(b) of the ITAA 1936 to deny the whole, or any part, of the imputation benefits received by Gloucester Shareholders in relation to the Gloucester Special Dividend.

### **Capital Return**

#### ***Distribution is not a dividend***

49. The Capital Return to Gloucester Shareholders is not a 'dividend' as defined in subsection 6(1) of the ITAA 1936.

### ***Application of sections 45A, 45B and 45C of the ITAA 1936***

50. The Commissioner will not make a determination under sections 45A or 45B of the ITAA 1936 that section 45C of the ITAA 1936 applies to the Capital Return.

***Capital gains tax (CGT) consequences****Capital Return*

51. CGT event G1 (section 104-135 of the ITAA 1997) happened when Gloucester paid the Capital Return to a Gloucester Shareholder in respect of a Gloucester Share that they owned at the Capital Reduction Record Date and continued to own at the payment date.

52. CGT event C2 (section 104-25 of the ITAA 1997) happened when Gloucester paid the Capital Return to a Gloucester Shareholder in respect of a Gloucester Share that they owned at the Capital Reduction Record Date, but did not own at the payment date.

53. A capital gain made when CGT event G1 or C2 happened will be eligible to be treated as a discount capital gain under Division 115 of the ITAA 1997 provided that the Gloucester Share was acquired at least 12 months before the payment of the Capital Return and the other conditions of that Division are satisfied (subsection 115-25(1) of the ITAA 1997).

*Promissory Note*

54. CGT event C2 happens when the Promissory Note is redeemed by the Trustee of the Promissory Note Trust where a Beneficiary (Gloucester Shareholder) is absolutely entitled to their Promissory Note (section 104-25 of the ITAA 1997).

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**Commissioner of Taxation**11 July 2012]

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## Appendix 1 – Explanation

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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.*

### **Gloucester Special Dividend**

#### ***Inclusion of the Gloucester Special Dividend in assessable income***

55. The term ‘dividend’ is defined in subsection 6(1) of the ITAA 1936 as a distribution made by a company to shareholders, whether in money or other property.

56. The payment of the Gloucester Special Dividend was a distribution of money by Gloucester to its shareholders.

57. Paragraph (d) of the definition of ‘dividend’ in subsection 6(1) of the ITAA 1936 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 ...

58. The funds for the payment of the Gloucester Special Dividend were sourced from financing facilities. The payment amount was debited against Gloucester’s retained earnings and current year profit accounts and not the share capital account. Therefore, the exclusion in paragraph (d) of the definition of ‘dividend’ in subsection 6(1) of the ITAA 1936 will not apply.

59. Accordingly, the Gloucester Special Dividend constitutes a ‘dividend’ for the purposes of subsection 6(1) of the ITAA 1936.

60. Paragraph 44(1)(a) of the ITAA 1936 provides that the assessable income of a resident shareholder in a company includes dividends that are paid to the shareholder by the company out of profits derived by it from any source.

61. The Gloucester Special Dividend was paid out of Gloucester’s retained profits and current year profits. Accordingly, Gloucester Shareholders must include the amount of the Gloucester Special Dividend in their assessable income.

62. The Gloucester Special Dividend will constitute a ‘distribution’ (within the meaning given in section 960-120 of the ITAA 1997). Section 202-30 of the ITAA 1997 provides that distributions and non-share dividends are frankable unless it is specified that they are unfrankable.

63. Section 202-40 of the ITAA 1997 provides that a distribution or a non-share dividend is a 'frankable distribution' if it is not unfrankable under section 202-45 of the ITAA 1997. Section 202-45 sets out the circumstances under which an amount or distribution is taken to be unfrankable. Based on the information provided by the Applicant, it is considered that none of those circumstances apply to the Gloucester Special Dividend.

64. Accordingly, the Gloucester Special Dividend constitutes a 'frankable distribution' under section 202-40 of the ITAA 1997.

65. Section 207-20 of the ITAA 1997 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 any other 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.

66. In accordance with subsection 207-20(1) of the ITAA 1997, the franking credit attached to the Gloucester Special Dividend must also be included in the Gloucester Shareholder's assessable income for the income year in which the Gloucester Special Dividend was made.

#### ***Entitlement to a tax offset***

67. In accordance with subsection 207-20(2) of the ITAA 1997, a Gloucester Shareholder will be entitled to a tax offset equal to the franking credit on the Gloucester Special Dividend that has been included in their assessable income in the income year in which the dividend was made.

68. Gloucester Shareholders who are entitled to a tax offset under subsection 207-20(2) of the ITAA 1997 in respect of the franking credit on the dividend received will also be subject to the refundable tax offset rules unless the Gloucester Shareholder is specifically excluded under section 67-25 of the ITAA 1997.

69. Entities excluded under section 67-25 of the ITAA 1997 include corporate tax entities (such as companies, corporate limited partnerships, corporate unit trusts and public trading trusts), unless they satisfy the requisite conditions as set out in subsections 67-25(1C) or 67-25(1D) of the ITAA 1997.

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

70. Subdivision 207-F of the ITAA 1997 creates the appropriate adjustment to cancel the effect of the gross-up and tax offset rules where the entity has made a franked distribution in one, or more, of the following circumstances listed in subsection 207-145(1) of the ITAA 1997:

- (a) the entity is not a 'qualified person' in relation to the distribution for the purposes of Division 1A of former Part IIIA of the ITAA 1936;
- (b) the Commissioner has made a determination under paragraph 177EA(5)(b) of the ITAA 1936 that no imputation benefit is to arise in respect of the distribution for the entity;
- (c) the Commissioner has made a determination under paragraph 204-30(3)(c) of the ITAA 1997 that no imputation benefit (within the meaning given by subsection 204-30(6) of the ITAA 1997) is to arise in respect of the distribution for the entity; or
- (d) the dividend is made as part of a dividend stripping operation (within the meaning given by section 207-155 of the ITAA 1997).

## ***Qualified persons***

71. A person who has held shares or an interest in shares on which a dividend has been paid (the holder) is a 'qualified person' for the purposes of Division 1A of former Part IIIA of the ITAA 1936 if, generally speaking, they satisfy the holding period rule and the related payment rule.

72. The 'qualified person' test is contained in former subsection 160APHO(1) of the ITAA 1936 which states that:

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 a 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 period in relation to the dividend.

73. Former subsection 160APHO(2) of the ITAA 1936 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 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*

74. In order to determine the relevant qualification period, it is necessary to determine whether, under the present arrangement, the Gloucester Shareholders were considered to be under an obligation to make a related payment.

75. Former section 160APHN of the ITAA 1936 provides non-definitive examples of what constitutes the making of a related payment for the purposes of Division 1A of former Part IIIAA of the ITAA 1936.

76. It is considered that the payment of the Gloucester Special Dividend is not an integral part of the Scheme. The payment of the Gloucester Special Dividend was not conditional upon Gloucester obtaining approval from the Gloucester Shareholders at the Scheme Meeting for the Gloucester Scheme to be entered into. Further, the payment of any amount of the Gloucester Special Dividend by Gloucester does not have the effect of reducing the Scheme Consideration that Gloucester Shareholders received from Yancoal.

77. In determining whether a Gloucester Shareholder is taken to have made, or be likely to make, a related payment in respect of the Gloucester Special Dividend, it is considered that the circumstances surrounding the payment of the Gloucester Special Dividend would not constitute an act that passes the benefit to another for the purposes of former subsection 160APHN(3) of the ITAA 1936. As such, it is concluded that a Gloucester Shareholder will not be taken to have made, or not be likely to make, a related payment in respect of the Gloucester Special Dividend.

*Holding period rule*

78. As the Gloucester Shareholders are taken, for the purposes of Division 1A of former Part IIIAA of the ITAA 1936, to not have made, or not be likely to make, a related payment in respect of the Gloucester Special Dividend, the relevant holding period is the primary qualification period pursuant to former paragraph 160APHO(1)(a) of the ITAA 1936.

79. The primary 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 the period beginning on the day after the day on which the taxpayer acquired the shares or interest and ending:

- (a) if the shares are not preference shares – on the 45th day after the day on which the shares or interest became ex dividend;

80. The ex-dividend date for tax purposes of the Gloucester Special Dividend for shares traded on the ASX is 18 June 2012 pursuant to former section 160APHE of the ITAA 1936. The primary qualification period thus runs from the day after the date of acquisition of a Gloucester Share until 45 days after the ex-dividend date of 18 June 2012.

81. In practical terms, for those Gloucester Shareholders who have not previously satisfied the holding period rule, this means that the primary qualification period runs from the day after the date of acquisition to 3 August 2012. However, pursuant to former subsection 160APHO(3) of the ITAA 1936, any days on which a taxpayer has materially diminished risks of loss or opportunities for gain in respect of the Gloucester Shares are to be excluded. This would mean that the primary qualification period would run from the day after the date of acquisition until the date that Gloucester Shareholders are no longer at risk for the purposes of Division 1A of former Part IIIAA of the ITAA 1936.

82. In this context, entitlement to participate in the Scheme is determined on the Scheme Record Date on the basis of being a Gloucester Shareholder who is registered on the register as the holder of the relevant Scheme Share on 4 July 2012, being the Scheme Record Date. It is considered that once a Gloucester Shareholder is identified as a Scheme Shareholder, that Gloucester Shareholder would no longer be considered to hold their shares 'at risk' for the purposes of Division 1A of former Part IIIAA of the ITAA 1936, as at that time the Gloucester Shareholder is committed to disposing of their Gloucester Shares and receiving the Scheme Consideration.

83. Accordingly, the primary qualification period would run from the day after the date of acquisition until 3 July 2012 (inclusive). Gloucester Shareholders who receive the Gloucester Special Dividend would need to hold their shares at risk for a continuous period of not less than 45 days during this period in order to be a 'qualified person' for the purposes of Division 1A of former Part IIIAA of the ITAA 1936. Thus, for those Gloucester Shareholders who have not previously satisfied the primary qualification period they would need to have acquired their Gloucester Shares on, or before, 18 May 2012 and hold them at risk until 3 July 2012 in order to be a qualified person.

*Determinations under paragraph 177EA(5)(b) of the ITAA 1936 and paragraph 204-30(3)(c) of the ITAA 1997*

84. The Commissioner has confirmed that a determination under paragraph 177EA(5)(b) of the ITAA 1936 or a determination under paragraph 204-30(3)(c) of the ITAA 1997 will not be made to deny the imputation benefits attached to Gloucester Special Dividend paid by Gloucester to the Gloucester Shareholders (see paragraphs 96 to 115 of this Ruling).

*Dividend stripping operation*

85. A distribution will be taken to be made as part of a 'dividend stripping operation', pursuant to section 207-155 of the ITAA 1997, where the making of the distribution arose out of, or was made in the course of, a scheme that was by way of, or in the nature of dividend stripping, or a scheme that had substantially the effect of a scheme that was by way of, or in the nature of, dividend stripping.

86. The documents listed in paragraph 11 of this Ruling provide no indication that the Gloucester Special Dividend and the associated franking of that dividend to the Gloucester Shareholders in any way constitute a dividend stripping arrangement. As such, the dividend stripping provision will have no application to the Gloucester Shareholders.

*Exempting entity and former exempting entity*

87. Division 207 of the ITAA 1997 does not apply to a distribution by an exempting entity unless it is expressly applied under Subdivision 208-G of the ITAA 1997 (section 208-195 of the ITAA 1997).

88. Section 208-20 of the ITAA 1997 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.

89. Subsection 208-25(1) of the ITAA 1997 provides, in broad terms, that an entity is effectively owned by 'prescribed persons' if not less than 95% of accountable membership interests (broadly direct and indirect ownership interests) are held by, or on behalf of, prescribed persons.

90. Section 208-40 of the ITAA 1997 provides the definition of a 'prescribed person' in relation to another corporate tax entity. The definition includes companies, trustees, partnerships or individuals that are a foreign resident; or, if they were to receive a distribution made by a corporate tax entity, the distribution would be exempt income or non-assessable non-exempt income of the company, trust estate, partnership or individual.

91. Based on Gloucester's shareholder register at 25 June 2012 (date of payment of the Gloucester Special Dividend), the total percentage of non-resident shareholder ownership in the accountable membership interests of Gloucester does not amount to Gloucester being effectively controlled by prescribed persons.

92. Accordingly, Gloucester is not an 'exempting entity', nor is it a 'former exempting entity' because it has never ceased to be an 'exempting entity' (section 208-50 of the ITAA 1997).

### ***Credit to franking account for certain corporate tax entities***

93. Item 3 in the table in subsection 205-15(1) of the ITAA 1997 provides that a credit of the franking credit on a distribution made to an entity arises in the franking account of that entity on the day on which the distribution is made if:

- the distribution is a franked distribution;
- the entity satisfies the residency requirement for the income year in which the distribution is made;
- the entity is a 'franking entity' when it receives the distribution; and
- the entity is entitled to a tax offset under Division 207 of the ITAA 1997 because of the distribution.

94. Pursuant to section 202-15 of the ITAA 1997, an entity is a 'franking entity' at a particular time if:

- it is a corporate tax entity (within the meaning given by section 960-115 of the ITAA 1997) at that time;
- it is not a life insurance company that is a mutual insurance company at that time; and
- in a case where the entity is a company that is a trustee of a trust — it is not acting in its capacity as trustee of the trust at that time.

95. Accordingly, if a Gloucester Shareholder is a 'franking entity' and is entitled to a tax offset under Division 207 of the ITAA 1997 in respect of the franking credit on the Gloucester Special Dividend, a credit of the franking credit on the dividend will arise in the Gloucester Shareholder's franking account on the day the dividend is made.

***Streaming of imputation benefits***

96. Section 204-30 of the ITAA 1997 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 section 204-30 of the ITAA 1997 would be, received by a member of the entity as a result of the distribution or distributions;
- (b) the member would derive a greater benefit from franking credits than another member of the entity; 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.

97. If section 204-30 of the ITAA 1997 applies, the Commissioner has discretion under subsection 204-30(3) of the ITAA 1997 to make a determination in writing:

- (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;
- (b) ...; and
- (c) that no imputation benefit is to arise in respect of any streamed distributions made to a favoured member and specified in the determination.

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

99. Under the arrangement for the payment of the franked Gloucester Special Dividend, all Gloucester Shareholders received an imputation benefit. Australian resident shareholders will receive the benefit of a tax offset (paragraph 204-30(6)(a) of the ITAA 1997), or receive a franking credit to their franking account as a result of the distribution.

100. The non-resident shareholders will receive an imputation benefit in the form of an exemption from dividend withholding tax (paragraph 204-30(6)(e) of the ITAA 1997). Resident shareholders will derive a greater benefit from franking credits than non-resident shareholders.

101. However, as the distribution is franked and paid to all Gloucester Shareholders, it cannot be argued that Gloucester has directed the flow of distributions in such a manner so as to ensure that imputation benefits are derived by Gloucester Shareholders who derive greater benefits from franking credits, while other shareholders receive lesser or no imputation benefits.

102. As the conditions in subsection 204-30(1) of the ITAA 1997 will not be met, the Commissioner will not make a determination under paragraph 204-30(3)(c) of the ITAA 1997 to deny the whole, or any part, of the imputation benefit received in relation to the Gloucester Special Dividend.

### ***General anti-avoidance provision***

103. Section 177EA of the ITAA 1936 is a general anti-avoidance provision that targets franking credit trading and dividend streaming schemes where one of the purposes (other than an incidental purpose) of the scheme is to obtain an imputation benefit.

104. Subsection 177EA(3) of the ITAA 1936 provides that section 177EA of the ITAA 1936 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.

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

106. In the present case, Gloucester is a corporate tax entity. The disposal of the Gloucester Shares in Gloucester pursuant to the Scheme is a scheme for the disposition of membership interests.

107. The Gloucester Special Dividend is a frankable distribution, which was paid to Gloucester Shareholders, who reasonably expected to receive imputation benefits.

108. The conditions of paragraphs 177EA(3)(a) to 177EA(3)(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 on the part of Gloucester, or Gloucester Shareholders, that there is a more than a merely incidental purpose of conferring an imputation benefit under the scheme.

109. 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 encompass a range of circumstances which taken individually or collectively may indicate a purpose which is more than incidental. Due to the diverse nature of these circumstances, some may not be present at any one time in any one scheme.

110. In Gloucester's case, fully franked dividends were paid in the 2007 to 2009 income years. Unfranked dividends were paid in the 2005, 2006 and 2008 income years.

111. The payment of a fully franked Gloucester Special Dividend thus represents a continuation of Gloucester's dividend practice to pay fully franked dividends every few years.

112. The Gloucester Special Dividend was fully franked and paid to the Gloucester Shareholders in proportion to their shareholding on the record date for determining entitlements to the Gloucester Special Dividend. The Gloucester Special Dividend was paid to shareholders irrespective of their ability to utilise the relevant franking credits. Non resident shareholders were not compensated for the inability to utilise franking credits.

113. The Gloucester Special Dividend allowed shareholders to share in the past and current year profits and the delivery of imputation credits to Gloucester Shareholders is a natural incident flowing from the ownership of shares in the company.

114. Having regard to the relevant circumstances of the scheme, the Commissioner has formed the view that the scheme was not entered into for the purpose of enabling Gloucester Shareholders to obtain imputation benefits.

115. 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 dividends.

## **Capital Return**

### ***Distribution is not a dividend***

116. Subsection 44(1) of the ITAA 1936 includes in a shareholder's assessable income any dividend (as defined in subsection 6(1) of the ITAA 1936), paid to shareholders out of profits derived by the company from any source (if the shareholder is a resident of Australia) and from an Australian source (if the shareholder is a non-resident of Australia).

117. The definition of 'dividend' in subsection 6(1) of the ITAA 1936 includes any distribution made by a company to any of its shareholders. However, paragraph (d) of the definition excludes a distribution that is debited against an amount standing to the credit of the company's share capital account.

118. Gloucester has debited the Capital Return against its share capital account. In addition, there have been no transfers to Gloucester's share capital account (as defined in section 975-300 of the ITAA 1997), prior to the Capital Return that would:

- (a) have caused the share capital account to become 'tainted' within the meaning of that term in section 197-50 of the ITAA 1997; or
- (b) have prevented Gloucester's share capital account from being tainted as a share capital account for the purposes of paragraph (d) of the definition of 'dividend' in subsection 6(1) of the ITAA 1936.

119. Accordingly, paragraph (d) of the definition of 'dividend' in subsection 6(1) of the ITAA 1936 applies, and the Capital Return is not a dividend assessable under subsection 44(1) of the ITAA 1936.

***Application of sections 45A, 45B and 45C of the ITAA 1936******Section 45A of the ITAA 1936: streaming of dividends and capital benefits***

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

121. Although Gloucester has provided Gloucester Shareholders with a 'capital benefit', as defined in paragraph 45A(3)(b) of the ITAA 1936, the capital benefit has been provided to all Gloucester Shareholders in direct proportion to their shareholding on the record date. The circumstances of the scheme do not indicate that there is a 'streaming' of capital benefits to advantaged shareholders and of dividends to disadvantaged shareholders.

122. Accordingly, section 45A of the ITAA 1936 does not apply to the Capital Return. Therefore, the Commissioner will not make a determination under subsection 45A(2) of the ITAA 1936 that section 45C of the ITAA 1936 applies in relation to the whole, or a part, of the capital benefit.

***Section 45B of the ITAA 1936: schemes to provide capital benefits in substitution for dividends***

123. Section 45B of the ITAA 1936 applies where certain payments are made to shareholders in substitution for dividends.

124. Subsection 45B(2) of the ITAA 1936 sets out the conditions under which the Commissioner may make a determination under subsection 45B(3) of the ITAA 1936 that section 45C of the ITAA 1936 applies. These conditions are that:

- (a) there is a scheme under which a person is provided with a capital benefit by a company;
- (b) under the scheme, a taxpayer (the relevant taxpayer), who may, or may not, be the person provided with the capital benefit, obtains a tax benefit; 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 (whether or not the dominant purpose but not including an incidental purpose) of enabling the relevant taxpayer to obtain a tax benefit.

125. The Capital Return, in conjunction with the Gloucester Special Dividend is the 'scheme' for the purposes of section 45B of the ITAA 1936.

126. The phrase 'provided with a capital benefit' is defined in subsection 45B(5) of the ITAA 1936. Relevantly, it includes a distribution to a person of share capital. As Gloucester debited the Capital Return against its untainted share capital account, Gloucester Shareholders, under the scheme, have been provided with a capital benefit.

127. A shareholder 'obtains a tax benefit', as defined in subsection 45B(9) of the ITAA 1936, if:

- (a) the amount of tax payable; or
- (b) any other amount payable under the ITAA 1936 or the ITAA 1997,

would, apart from the operation of section 45B of the ITAA 1936,

- (c) be less than the amount that would have been payable; or
- (d) be payable at a later time than it would have been payable,

if the capital benefit had instead been a dividend.

128. Ordinarily, a Capital Return would be subject to the CGT provisions of the income tax law. Unless the amount of the distribution exceeds the cost base of the shares, there will only be a cost base reduction under CGT event G1 (section 104-135 of the ITAA 1997). It is only to the extent (if any) that the distribution exceeds the cost base of the shares that a capital gain arises.

129. A dividend would generally be included in the assessable income of a resident shareholder, or in the case of a non-resident shareholder be subject to dividend withholding tax. Therefore, a Gloucester Shareholder has generally obtained a tax benefit from the scheme.

130. For the purposes of paragraph 45B(2)(c) of the ITAA 1936, the Commissioner is required to consider the 'relevant circumstances' set out in subsection 45B(8) of the ITAA 1936 to determine whether any part of the scheme was entered into for a purpose, other than an incidental purpose, of enabling a relevant taxpayer to obtain a tax benefit.

131. The test of purpose is an objective one. The question is whether, objectively, it would be concluded that a person who entered into or carried out the scheme or any part of the scheme did so for the purpose of obtaining a tax benefit for the relevant taxpayer. The purpose does not have to be the most influential or prevailing purpose, but it must be more than an incidental purpose.

132. The relevant circumstances under subsection 45B(8) of the ITAA 1936 cover the circumstances of the company and the tax profile of the shareholders. In this instance, as the Capital Return has been made to all Gloucester Shareholders regardless of individual circumstances, paragraphs 45B(8)(c) to 45B(8)(h) of the ITAA 1936 do not incline for, or against, a conclusion as to purpose.

133. The circumstances covered by paragraphs 45B(8)(i) and 45B(8)(j) of the ITAA 1936 pertaining to the provision of ownership interests and demerger are not relevant. The relevant matters, however, are those covered by the circumstances described in paragraphs 45B(8)(a), 45B(8)(b) and 45B(8)(k) of the ITAA 1936.

134. Paragraph 45B(8)(a) of the ITAA 1936 refers to the extent to which the capital benefit is attributable to capital and profits (realised or unrealised) of the company or an associate (within the meaning of section 318 of the ITAA 1936) of the company. The Capital Return made to the shareholders is debited to Gloucester's share capital account. Under these circumstances, no requisite purpose exists in which the capital benefit is attributable to profit.

135. Paragraph 45B(8)(b) of the ITAA 1936 refers to the pattern of distributions made by a company or an associate (within the meaning of section 318 of the ITAA 1936) of the company. Gloucester has paid a Gloucester Special Dividend of \$0.47 per share which will effectively deplete almost all of the balance of its retained earnings and current year profits. Consequently, no material further dividends will be able to be paid out of its retained earnings. Therefore, there is no requisite purpose that the capital reduction is in substitution for a dividend.

136. Paragraph 45B(8)(k) of the ITAA 1936 refers to the matters in subparagraphs 177D(b)(i) to 177D(b)(viii) of the ITAA 1936. These are matters by reference to which a scheme is able to be examined from a practical perspective in order to identify and compare its tax and non-tax objectives. The matters include the manner in which the scheme is carried out, its form and substance, and its financial and other implications for the parties involved. In this case, the practical implications of the scheme for Gloucester and the Gloucester Shareholders are consistent with it being, in form and substance, a capital reduction.

137. Therefore, having regard to the relevant circumstances involving the Capital Return, it cannot be concluded that Gloucester has entered into, or carried out, the Capital Return for a purpose other than a merely incidental purpose of enabling the Gloucester Shareholders to obtain a tax benefit. The Commissioner will not make a determination under subsection 45B(3) of the ITAA 1936, that section 45C of the ITAA 1936 applies to the whole, or a part, of the capital benefit represented by the Capital Return.

138. Accordingly, as the Commissioner will not make a determination under paragraph 45B(3)(b) of the ITAA 1936 in relation to the scheme as described, section 45C of the ITAA 1936 will not deem any part of the Capital Return to be an unfranked dividend for the purposes of the ITAA 1936 or the ITAA 1997.

### ***Capital gains tax consequences***

#### *Capital Return: CGT event G1*

139. CGT event G1 happened when Gloucester paid the Capital Return to a Gloucester Shareholder in respect of a share that they owned at the Capital Reduction Record Date and continued to own at the payment date – the payment date being 25 June 2012 (section 104-135 of the ITAA 1997).

140. A Gloucester Shareholder will make a capital gain if the Capital Return is more than the cost base of their Gloucester share. The amount of the capital gain is equal to the excess (subsection 104-135(3) of the ITAA 1997).

141. If a Gloucester Shareholder makes a capital gain when CGT event G1 happens, the cost base and reduced cost base of the Gloucester Share is reduced to nil. A Gloucester Shareholder cannot make a capital loss when CGT event G1 happens (subsection 104-135(3) of the ITAA 1997).

142. If the Capital Return is equal to or less than the cost base of the Gloucester Share at the payment date, the cost base and reduced cost base of the share will be reduced by the amount of the Capital Return (subsection 104-135(4) of the ITAA 1997).

143. A capital gain made when CGT event G1 happens will be eligible to be treated as a discount capital gain under Division 115 of the ITAA 1997 provided that the Gloucester Share was acquired at least 12 months before the payment of the Capital Return (subsection 115-25(1) of the ITAA 1997) and the other conditions of that Division are satisfied.

#### *Capital Return: CGT event C2*

144. The right to receive the Capital Return is one of the rights inherent in a Gloucester Share at the Capital Reduction Record Date. If, after the Capital Reduction Record Date but before the payment date, a Gloucester Shareholder ceased to own a Gloucester Share in respect of which the Capital Return was payable, the right to receive the Capital Return in respect of that share is retained by the shareholder and is a separate CGT asset.

145. CGT event C2 happened when the Capital Return was paid (section 104-25 of the ITAA 1997). The right to receive the payment ended by the right being discharged or satisfied when the payment was made.

146. A Gloucester Shareholder will make a capital gain if the capital proceeds from the ending of the right are more than its cost base. The capital gain is equal to the amount of the excess. A Gloucester Shareholder will make a capital loss if the capital proceeds from the ending of the right are less than its reduced cost base. The capital loss is equal to the amount of the difference (subsection 104-25(3) of the ITAA 1997).

147. In working out the capital gain or capital loss made when CGT event C2 happens, the capital proceeds will be the amount of the Capital Return (subsection 116-20(1) of the ITAA 1997).

148. The cost base of a Gloucester Shareholder's right to receive the Capital Return is worked out under Division 110 of the ITAA 1997 (modified by Division 112 of the ITAA 1997). The cost base of the right does not include the cost base or reduced cost base of the share previously owned by a Gloucester Shareholder that has been applied in working out a capital gain or capital loss made when a CGT event happened to the share – for example, when the Gloucester Shareholder disposes of the share after the Capital Reduction Record Date.

149. Therefore, if the full cost base or reduced cost base of the Gloucester Share has been previously applied in working out a capital gain or capital loss when a CGT event happened to that share, then the right to receive the return of capital is likely to have a nil cost base. As a result, a Gloucester Shareholder will generally make a capital gain equal to the amount of the Capital Return.

150. As the right to receive the payment of the Capital Return was inherent in the Gloucester Share during the time it was owned, the right is considered to have been acquired at the time when the corresponding share was acquired (section 109-5 of the ITAA 1997).

151. Accordingly, if the Gloucester Share was acquired at least 12 months before the payment of the Capital Return, a capital gain made from the ending of the corresponding right will satisfy the requirements of section 115-25 of the ITAA 1997. Such a capital gain may be eligible to be treated as a discount capital gain under Division 115 of the ITAA 1997 provided the other conditions of that Division are satisfied.

#### *Promissory Note*

152. The Beneficiaries (Gloucester Shareholders) will be absolutely entitled to their Promissory Note held by the Trustee of the Promissory Note Trust unless the note is held jointly with another entity (section 106-50 of the ITAA 1997). Joint ownership occurs where the shares to which the Promissory Note relates were held jointly at the Capital Reduction Record Date.

153. Where a Beneficiary is absolutely entitled to their Promissory Note, the first element of the cost base will be equal to the total amount of the Capital Return received for all their Gloucester Shares and the capital proceeds will be equal to the amount received for the redemption of their Promissory Note.

154. CGT event C2 will happen at the time their Promissory Note is redeemed by the Trustee of the Promissory Note Trust (subsection 104-25(1) of the ITAA 1997). When CGT event C2 happens, it is anticipated that each Beneficiary affected by the event will make neither a capital gain nor a capital loss because the redemption proceeds on the Promissory Note will equal its cost base (section 100-45 and subsection 104-25(3) of the ITAA 1997).

155. The CGT discount under Subdivision 115-A of the ITAA 1997 will not apply because each Promissory Note will be redeemed within 12 months of the return of capital that funded its acquisition (section 115-25 of the ITAA 1997).

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

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ATOlaw topic: Income Tax ~~ Assessable income ~~ dividend, interest  
and royalty income  
Income Tax ~~ Return of capital  
Income Tax ~~ Capital Gains Tax ~~ CGT events G1 to  
G3 – shares