


# ***CR 2014/40 - Income tax: issue of convertible preference shares (CPS3) by Suncorp Group Limited***

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## Class Ruling

### Income tax: issue of convertible preference shares (CPS3) by Suncorp Group Limited

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**❶ 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:
- section 6BA of the *Income Tax Assessment Act 1936* (ITAA 1936)
  - subsection 44(1) of the ITAA 1936
  - section 45 of the ITAA 1936
  - section 45A of the ITAA 1936
  - section 45B of the ITAA 1936
  - section 177EA of the ITAA 1936
  - Division 1A of former Part IIIA of the ITAA 1936

- section 6-5 of the *Income Tax Assessment Act 1997* (ITAA 1997)
- Division 67 of the ITAA 1997
- Division 104 of the ITAA 1997
- section 109-5 of the ITAA 1997
- section 109-10 of the ITAA 1997
- section 110-25 of the ITAA 1997
- section 110-55 of the ITAA 1997
- Subdivision 130-A of the ITAA 1997
- section 204-30 of the ITAA 1997
- Division 207 of the ITAA 1997, and
- section 960-130 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 investors who were allotted perpetual, convertible, unguaranteed and unsecured preference shares issued by Suncorp Group Limited (SGL) called Suncorp Group Limited Convertible Preference Shares (CPS3) and who:

- are Australian residents (within the meaning of subsection 6(1) of the *Income Tax Assessment Act 1936* (ITAA 1936))
- hold their CPS3 on capital account, and
- are not subject to the Taxation of Financial Arrangements rules in Division 230 in relation to financial arrangements under the scheme.

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

4. The investors described in the above paragraph are referred to in this Ruling as Holders.

5. The class of entities to which this Ruling applies does not extend to Holders of CPS3 who acquire their CPS3 otherwise than by initial application under the Suncorp Group Limited CPS3 Prospectus dated 31 March 2014 and subsequently replaced with the Suncorp Group Limited CPS3 Prospectus dated 8 April 2014 (the Prospectus).

**Qualifications**

6. The Ruling does not deal with how the taxation law applies to Holders who hold their CPS3 as trading stock or revenue assets.

7. The Ruling does not consider the tax implications of the Exchange of CPS3 by Redemption or Resale.

8. The Ruling does not consider how the taxation law applies to the Nominated Purchaser who acquires their CPS3 under the Resale facility.

9. The Ruling does not consider how the gross-up and tax offset rules in Division 207 apply to partnership or trustee Holders, or to indirect distributions to partners in a partnership, or beneficiaries or trustees of a trust.

10. The Ruling does not deal with how the taxation law applies to SGL in relation to the issue of the CPS3.

11. 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 14 to 68 of this Ruling.

12. 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.

**Date of effect**

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13. This Ruling applies from 8 May 2014 to 30 June 2022. The Ruling continues to apply after 30 June 2022 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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14. The following description of the scheme is based on the following 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 Class Ruling dated 24 March 2014 (Application)
- the Prospectus

- CPS3 Terms (as included in Appendix A of the Prospectus) (the Terms)
- Australian Stock Exchange (ASX) Announcement dated 31 March 2014 (ASX Announcement)
- letter from the Australian Prudential Regulatory Authority (APRA) dated 26 March 2014 (APRA Letter)
- additional information and correspondence provided by SGL up to 10 April 2014.

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

15. In this Ruling, unless otherwise defined, capitalised terms take on the same meaning as in the Terms.

## **SGL**

16. SGL is an Australian resident company.

17. SGL is a non-operating holding company (NOHC) that is the ASX listed parent company of the Suncorp Group. SGL is also authorised in Australia as a NOHC of the Suncorp Group under the *Insurance Act 1973* (Cth) and is subject to prudential regulation by the APRA.

18. The Suncorp Group is comprised of three separate lines of business, being General Insurance, Banking and Life. Each business line has its own NOHC and a corporate shared services group.

19. Each business line NOHC is owned 100% by SGL. Suncorp Insurance Holdings Limited (SIHL) is the business NOHC for the General Insurance business line and the parent company of the Australian regulated Insurer, AAI Limited (AAIL).

## **The Offer of CPS3**

20. SGL announced an offer of convertible preference shares (CPS3) to raise \$360 million with the ability to raise more or less (the Offer).

21. The Offer was made under the Prospectus which was lodged with the Australian Securities and Investments Commission (ASIC) on 31 March 2014 pursuant to section 713(1) of the *Corporations Act 2001* (Corporations Act).

22. The Issue Date for the CPS3 is 8 May 2014.

23. This Prospectus expires on the date which is 13 months after 31 March 2014 (Expiry Date) and no CPS3 will be issued on the basis of this Prospectus after the Expiry Date.

24. The classes of applicants for CPS3 and how they apply for the CPS3 are:

- Securityholder Applicant – a registered holder of SGL Ordinary Shares, Floating Rate Capital Notes (floating rate capital notes issued by SML in 1998 under a prospectus dated 26 October 1998), CPS2 (convertible preference share issued by SML in 2012 under a replacement prospectus dated 3 October 2012) or Subordinated Notes (Suncorp Subordinated Notes issued by SGL in 2013 under a replacement prospectus dated 18 April 2013) shown on the Register with an address in Australia and who applies through the Securityholder Offer
- Broker Firm Applicant – an Australian resident retail or high net worth client of a Syndicate Broker invited to participate through the Broker Firm Offer, and
- Institutional Investors – an investor to whom offers or invitations in respect of CPS3 can be made without the need for a lodged prospectus (or other formality, other than a formality which SGL is willing to comply with), including in Australia a person to whom offers or invitations can be made without the need for a lodged prospectus under section 708 of the Corporations Act and who has been invited by the Joint Lead Managers to bid for CPS3 in the Bookbuild, provided that such investor may not be in the United States.

25. The Prospectus states that no action has been taken to register or qualify the CPS3 or the Offer or to otherwise permit a public offering of the CPS3 outside Australia. It further states that subject to SGL's approval, the CPS3 may be offered in certain permitted jurisdictions outside Australia under the Institutional Offer where such offer is made, and accepted in accordance with the laws of such jurisdictions.

### **Reasons for issuing CPS3**

26. The capital raised from the Offer will be used for general corporate, funding and capital management purposes of the Suncorp Group, including maintaining the appropriate levels of gearing following the proposed redemption of certain of AAIL's regulatory capital instruments.

27. It will help protect depositors, policy holders and other creditors of the relevant Regulated Entity by providing a loss-absorbing capital buffer.

28. SGL will invest all or some of the proceeds of the issue in notes to be issued by SIHL (SIHL Notes), with SIHL then investing the proceeds from the issue of the SIHL Notes in the issue of back to back notes by AAIL (AAIL Notes), which will be used by AAIL to refinance existing transitional Tier 2 capital held by AAIL, scheduled to be called in September 2014.

29. It will also be used to fund share buybacks by SIHL and AAIL to return Common Equity Tier 1 capital to SGL. The Offer is part of SGL's continuing capital management strategy within the guidelines prescribed by APRA.

30. In the APRA Letter, APRA has confirmed that the CPS3 will constitute Additional Tier 1 Capital of SGL under SGL's NOHC conditions (dated 14 May 2013) until the implementation of APRA's Supervision of Conglomerate Groups framework and the subsequent revision of SGL's NOHC conditions. APRA has also confirmed that it has no objection to SGL's intention to use the proceeds of CPS3 to fund its investment in Additional Tier 1 Capital issued by other APRA regulated entities within the Suncorp Group (noting that any such issue of Additional Tier 1 Capital by other APRA regulated entities will need to meet the requirements of the relevant prudential standard).

### **Terms of the CPS3**

31. CPS3 are perpetual, fully paid, mandatorily convertible non-cumulative preference shares in the capital of SGL.

32. The issue price of each CPS3 is \$100.

33. The CPS3 generally do not have voting rights, except in the limited circumstances as set out in clause 12.1 of the Terms.

34. The CPS3 are expected to be listed on the ASX and to trade under the ASX code 'SUNPE'.

### **Dividend calculation**

35. Subject to the Dividend Payment Conditions set out below, pursuant to clause 2.1 of the Terms, the Holder of each CPS3 is entitled to receive, on the relevant Dividend Payment Date, a dividend (Dividend) calculated using the following formula:

$$\text{Dividend} = \frac{\text{Dividend Rate} \times \text{A\$}100 \times \text{N}}{365}$$

where:

**Dividend Rate** (expressed as a percentage per annum) is calculated as follows:

$$\text{Dividend Rate} = (\text{Bank Bill Rate} + \text{Margin}) \times (1 - T)$$

where:

**Bank Bill Rate** (expressed as a percentage per annum) means, for a Dividend Period, the average mid-rate for bills of a term of 90 days which average mid-rate is displayed on Reuters page BBSW (or any page which replaces that page) on the first Business Day of the Dividend Period or, if there is a manifest error in the calculation of that average mid-rate or that average mid-rate is not displayed by 10:16am (Sydney time) on that date, the rate specified in good faith by SGL at or

around 10:30am (Sydney time) on that date having regard, to the extent possible, to:

- (a) the rates otherwise bid and offered for bills of a term of 90 days or for funds of that tenor displayed on Reuters page BBSW (or any page which replaces that page) at that time on that date, or
- (b) if bid and offer rates for bills of a term of 90 days are not otherwise available, the rates otherwise bid and offered for funds of that tenor at or around that time on that date

**Margin** (expressed as a percentage per annum) means the margin determined under the Bookbuild

**T** (expressed as a decimal) means the Australian corporate tax rate applicable to the franking account of SGL at the relevant Dividend Payment Date, and

**N** means in respect of:

- (a) the first Dividend Payment Date, the number of days from (and including) the Issue Date until (but not including) the first Dividend Payment Date, and
- (b) each subsequent Dividend Payment Date, the number of days from (and including) the preceding Dividend Payment Date until (but not including) the relevant Dividend Payment Date.

### ***Dividend Payment Conditions***

36. The Dividend Payment Dates are 17 March, 17 June, 17 September and 17 December, commencing on 17 June 2014 until (but not including) the date on which the CPS3 is Converted or Redeemed in accordance with the Terms.

37. Under clause 2.3 of the Terms, payment of a Dividend is subject to:

- the Directors, at their absolute discretion, resolving to pay the Dividend on the relevant Dividend Payment Date
- paying the Dividend on the Dividend Payment Date not resulting in the Eligible Capital of the Suncorp Group not complying with APRA's then current prudential capital requirements as they are applied to the Suncorp Group at the time
- paying the Dividend not resulting in SGL becoming, or being likely to become, insolvent for the purposes of the Corporations Act, and
- APRA not otherwise objecting to the Dividend being paid on the Dividend Payment Date.

38. A Dividend is only payable to those persons registered as the Holders on the Record Date for that Dividend.

39. Dividends are non-cumulative, as stated in clause 2.4 of the Terms. If all or any part of a Dividend is not paid, SGL has no liability to pay the unpaid amount, and the Holders have no claim or entitlement in respect of the non-payment, nor will it constitute an event of default.

40. No interest will accrue on any unpaid Dividends and the Holders have no claim or entitlement in respect of interest on any unpaid Dividends.

### ***Ranking of Dividends***

41. Under clause 10.1 of the Terms, the CPS3 rank, in respect of payment of Dividends:

- (a) in priority to ordinary shares in SGL (SGL Ordinary Shares)
- (b) equally amongst themselves and with all Equal Ranking Instruments, and
- (c) behind:
  - (i) any securities or instruments that rank in priority to the CPS3, and
  - (ii) all SGL's debt and liabilities to its creditors, both subordinated and unsubordinated, other than indebtedness that by its terms ranks equally with or behind the CPS3.

### ***Restrictions in the case of non-payment of Dividends***

42. If a Dividend is not paid in full on a Dividend Payment Date (the Relevant Dividend Payment Date), SGL is prevented, without the approval of a Special Resolution, from declaring or determining to pay or paying a dividend, making a distribution on SGL Ordinary Shares, or buying back or reducing capital on any SGL Ordinary Shares, unless the Dividend is paid in full within 3 Business Days of the Relevant Dividend Payment Date (clause 2.7 of the Terms).

43. The restrictions do not apply in certain limited circumstances as described in clause 2.8 of the Terms.

### ***Mandatory Conversion***

44. Pursuant to clause 3.1 of the Terms, subject to the occurrence a Non-Viability Trigger Event, Optional Exchange or an Acquisition Event, SGL must Convert all (but not some) CPS3 on issue on the Mandatory Conversion Date into SGL Ordinary Shares in accordance with clauses 3 and 7 of the Terms. The Mandatory Conversion Date will be the first of the following dates (each a Relevant Date) on which

the Mandatory Conversion Conditions set out in clause 3.3 of the Terms are satisfied:

- (a) 17 June 2022 (Scheduled Mandatory Conversion Date), and
- (b) a Dividend Payment Date after the Scheduled Mandatory Conversion Date.

45. The Mandatory Conversion Conditions to be satisfied (as set out in clause 3.3 of the Terms), are:

- (a) the VWAP of the SGL Ordinary Shares on the 25<sup>th</sup> Business Day immediately preceding the Relevant Date being greater than 110% of the Relevant Fraction, multiplied by the Issue Date VWAP (First Mandatory Conversion Condition)
- (b) the VWAP of the SGL Ordinary Shares during the period of 20 Business Days on which trading in SGL Ordinary Shares took place immediately preceding the Relevant Date is greater than 101.01% of the Relevant Fraction, multiplied by the Issue Date VWAP (Second Mandatory Conversion Condition), and
- (c) no Delisting Event applies in respect of the Relevant Date (Third Mandatory Conversion Condition).

### ***Non-Viability Conversion***

46. SGL must convert the CPS3 on the Non-Viability Conversion Date, in accordance with clauses 4 and 7 of the Terms, should a Non-Viability Trigger Event occur. Conversion due to a Non-Viability Trigger Event is not subject to the Mandatory Conversion Conditions set out in clause 3.3 of the Terms.

47. A Non-Viability Trigger Event is defined in clause 4.1 of the Terms as an event where APRA provides a written determination to SGL that the conversion or write-off of Relevant Preference Securities is necessary, because:

- without the conversion or write-off, APRA considers that SGL would become non-viable, or
- without a public sector injection of capital or equivalent capital support, APRA considers that SGL would become non-viable.

48. If a Non-Viability Trigger Event occurs, SGL must convert to SGL Ordinary Shares or write-off all Relevant Preference Securities or an amount of Relevant Preference Securities that APRA is satisfied would be sufficient to ensure SGL does not become non-viable.

49. Clause 4.2(a) requires SGL to give notice to Holders if a Non-Viability Trigger Event occurs. SGL must also determine the number of CPS3 that will Convert or be written off and the identity of the Holders whose CPS3 will Convert. The Non-Viability Trigger Event Notice must state the Non-Viability Conversion Date, how many CPS3 will Convert and the relevant amount of Relevant Preference Securities that will be converted or written off.

## **Write Off**

50. If an Inability Event (which means that SGL is prevented due to an applicable law, court order, action of a government authority or any other reason from Converting the CPS3) subsists so that SGL cannot Convert CPS3, and Conversion has not been effected within five Business Days after the Non-Viability Conversion Date, then the CPS3 will be Written Off in accordance with clause 7.14 of the Terms.

51. In clause 7.14 of the Terms 'Written Off', in respect of the CPS3 and a Non-Viability Conversion date, is defined as:

- (a) the CPS3 will not be Converted in respect of a Non-Viability Trigger Event and will not be Converted, Redeemed or Resold under the Terms on any subsequent date. and
- (b) on and from the sixth Business Day after the Non-Viability Conversion Date:
  - (i) in a winding-up of SGL, the Liquidation Sum is the sum which would have been paid in respect of CPS3 out of the surplus available to shareholders in a winding-up as if the CPS3 were the Conversion Number of SGL Ordinary Shares
  - (ii) subject to clauses 2.3, 2.4, 14.8 and 14.9 of the Terms and to the requirements of APRA applicable to the payment of dividends on SGL Ordinary Shares, a non-cumulative dividend is payable in respect of the CPS3 if and when a dividend is paid on SGL Ordinary Shares, in an amount determined as if the CPS3 were a number of SGL Ordinary Shares equal to the Conversion Number

in each case with that Conversion Number being finally determined as if the CPS3 had Converted on the Non-Viability Conversion Date, and

- (c) on and from the sixth Business Day after the Non-Viability Conversion Date clauses 2.1, 2.2, 2.5, 2.7, 3, 4 (other than clause 4.3(c)), 5, 6, 7 (other than clause 7.14 and any provisions in clause 7 required to give effect to clause 7.14) and 8 will no longer apply in respect of that CPS3.

***Optional Exchange of CPS3 by SGL***

52. Under clause 5.1 of the Terms, SGL, with APRA's prior written approval, may elect to Exchange:

- (a) all or some CPS3 on an Exchange Date following a Tax Event or a Regulatory Event
- (b) all (but not some only) CPS3 on an Exchange Date following a Potential Acquisition Event, or
- (c) all or some CPS3 on the Optional Exchange Date.

53. If SGL elects to Exchange CPS3, it must elect which of the following it intends to do, as specified by clause 5.3 of the Terms:

- (a) Convert CPS3 into SGL Ordinary Shares in accordance with clause 7 of the Terms
- (b) Redeem CPS3 in accordance with clause 8 of the Terms, or
- (c) Resell CPS3 in accordance with clause 9 of the Terms.

54. Subject to clauses 5.4 and 5.5, in the election under clause 5.3(a) of the Terms, SGL may specify which of Conversion, Redemption and Resale applies to a particular CPS3, and:

- (a) SGL may select any one or more of Conversion, Redemption or Resale to apply to the CPS3 held by a Holder, and
- (b) SGL may select a different combination of Conversion, Redemption and Resale in respect of CPS3 held by different Holders.

***Conversion on Acquisition Event***

55. Upon the occurrence of an Acquisition Event, SGL must, in accordance with clause 6 and 7 of the Terms, Convert all (but not only some) of the CPS3 on the Acquisition Conversion Date. An Acquisition Event is defined in clause 19.2 of the Terms as:

- (a) a takeover bid being made to acquire all or some SGL Ordinary Shares and the offer is, or becomes, unconditional and the bidder either has an interest in more than 50% of the SGL Ordinary Shares on issue or the Directors issue a statement recommending acceptance of the offer; or
- (b) a court approves a scheme of arrangement which will result in a person other than SGL having a relevant interest in more than 50% of the SGL Ordinary Shares.

***Conversion Mechanics***

56. If SGL Converts the CPS3, then under clause 7 of the Terms:

- (a) each CPS3 that is being Converted will Convert into one SGL Ordinary Share on the relevant date, and

- (b) each Holder will be allotted, for no consideration, an additional number of SGL Ordinary Shares for each CPS3 being Converted on the relevant date equal to one less than the Conversion Number (but no greater than the Maximum Conversion Number), calculated as follows:

$$\text{Conversion Number} = \frac{\text{Issue Price}}{99\% \times \text{VWAP}}$$

where:

**VWAP** (expressed in dollars and cents) means the Volume Weighted Average Price during the VWAP Period;

The Maximum Conversion Number is calculated as follows:

$$\text{Maximum Conversion Number} = \frac{\text{Issue Price}}{(\text{Issue Date VWAP} \times \text{Relevant Fraction})}$$

where:

**Relevant Fraction** means, in the case of a Mandatory Conversion, 0.5, or in the case of any other Conversion, 0.2.

57. Subject to the operation of the limitation caused by the Maximum Conversion Number, the total market value of the SGL Ordinary Shares held by a Holder immediately after the Conversion of CPS3 will be approximately the Issue Price of the CPS3 (\$100).

58. Pursuant to clause 7.1(d), a CPS3, upon Conversion, confers all of the rights attaching to one SGL Ordinary Share, and at the times specified in the clause:

- (a) all other rights conferred or restrictions imposed on that CPS3 under the Terms will no longer have effect (except for rights relating to a Dividend which has been determined to be payable but has not been paid before the Conversion takes place, which rights will continue); and
- (b) the SGL Ordinary Share resulting from the Conversion will rank equally with all other SGL Ordinary Shares.

59. Clause 7.1 of the Terms states that the Conversion does not constitute a redemption, buy-back, cancellation or termination of CPS3 or an issue, allotment or creation of a new SGL Ordinary Share (other than under clause 7.1(b)).

60. Should a Holder not wish to receive SGL Ordinary Shares if SGL has elected or is required to Convert CPS3 (and has notified SGL of this fact), under clause 7.11 of the Terms, on the date for Conversion, the relevant SGL Ordinary Shares will be issued to a nominee appointed by SGL who will sell the SGL Ordinary Shares and pay a cash amount equal to the Proceeds to the relevant Holder.

***Redemption mechanics***

61. SGL may Redeem the CPS3 in accordance with the Terms and subject to APRA's prior written approval.
62. For the purposes of clause 8 of the Terms, 'Redeem' means redeem, buy-back (other than an on market buy-back within the meaning of the Corporations Act) or reduce capital, or any combination of these activities.
63. Where the CPS3 are Redeemed, SGL will pay the Issue Price plus any amount payable under 8.3(a)(iii) of the Terms, pursuant to which the Directors may, in their absolute discretion, determine that the consideration payable for each CPS3 by way of buy-back will include an amount equal to a Dividend calculated in accordance with clause 2 of the Terms for the Dividend Period (together, the Redemption Price).
64. On the Exchange Date the only right the Holders will have with respect to the CPS3 will be to obtain the Redemption Price payable in accordance with the Terms and, upon payment of the Redemption Price all other rights conferred, or restrictions imposed, by the CPS3 will no longer have effect (pursuant to clause 8.3 of the Terms).

***Resale mechanics***

65. SGL can elect to Resell the CPS3 by electing one or more Nominated Purchasers as set out in clause 9.2 of the Terms.
66. Under clause 9.4 of the Terms, if an election to Resell is made, each Holder is taken to irrevocably offer to sell CPS3 the subject of Resale to the Nominated Purchaser for the Resale Price on the Exchange Date. In accordance with clause 9.5 of the Terms, subject to payment by the Nominated Purchaser of the Resale Price to the Holders, all right, title and interest in such CPS3 (excluding the right to any Dividend payable on that date) will be transferred to the Nominated Purchaser free from Encumbrances.

***Ranking of CPS3 on Winding-Up***

67. Under clause 10.2 of the Terms, in a winding-up of SGL, a CPS3 gives the Holder the right to payment in cash of the Liquidation Sum (an amount out of surplus assets of SGL equal to \$100 plus the amount of any Dividend determined to be paid but unpaid) out of the surplus (if any) available for distribution to shareholders. The CPS3 will rank as follows for payment of the Liquidation Sum:
- (a) in priority to SGL Ordinary Shares;
  - (b) equally amongst themselves and with all Equal Ranking Instruments; and
  - (c) behind:

- (i) any securities or instruments that rank in priority to the CPS3;
- (ii) all SGL's debt and liabilities to its creditors, both subordinated and unsubordinated, other than indebtedness that by its terms ranks equally or behind the CPS3 in a winding-up.

## Other Matters

68. This Ruling is made on the basis that:

- (a) the documents provided by SGL (refer to paragraph 14 of this Ruling) represent a complete and accurate description of the Transaction, are intended by the parties to have their legal effect and will be implemented according to their terms
- (b) during the term of the Transaction, SGL will be a resident of Australia under the income tax laws of Australia and no other jurisdiction
- (c) all parties to the Transaction are dealing with each other on arm's length terms and fair value consideration will be provided by the Holders to acquire the CPS3
- (d) the CPS3 are 'equity interests' pursuant to Division 974
- (e) the additional SGL Ordinary Shares issued in the event of a Conversion of CPS3 will be 'equity interests' pursuant to Division 974
- (f) dividends on the CPS3 will be frankable distributions pursuant to section 202-40
- (g) the Dividends are expected to be fully franked, however, if any Dividend is not franked or only partially franked, the Dividend will be grossed up to the extent that the franking percentage of the Dividend is less than 100% as calculated in accordance with clause 2.2 of the Terms
- (h) SGL will frank the distributions on the CPS3 at the same franking percentage as the benchmark for the franking period in which the payments are made
- (i) the extent to which a Holder receives franked Dividends will be determined solely by each Holder's proportionate ownership of the CPS3 irrespective of the Holder's tax profile and regardless of the extent to which any particular Holder will actually benefit from the franking credits attached to the Dividend
- (j) the dividends on the CPS3 are expected to be fully franked in the same proportion as dividends paid on SGL Ordinary Shares

- (k) SGL will not differentially frank distributions payable to different Holders of the CPS3, or to holders of any other frankable interest in SGL, according to the tax status of the holders of those respective instruments or on any other basis
- (l) any CPS3 held by non-residents that acquired the CPS3 under the Institutional Offer will be franked in the same manner as the CPS3 held by residents
- (m) the share capital of SGL will not become tainted within the meaning of Subdivision 197-A by an issue of the CPS3 or allotment of additional SGL Ordinary Shares on Conversion of the CPS3
- (n) no dividends paid in respect of the CPS3 will be sourced, directly or indirectly, from SGL's share capital account or its non-share capital account
- (o) SGL reasonably expects to have sufficient available profits from which to pay Dividends, and have net assets in excess of ordinary share capital, immediately before the payment of any Dividends payable in respect of the CPS3
- (p) no debit will be made to any SGL reserve in respect of CPS3 dividends
- (q) dividend payments in respect of the CPS3 will satisfy the requirements of section 254T of the Corporations Act
- (r) dividend payments in respect of the CPS3 will not be an exercise of powers under Division 1 of Part 2J.1 of the Corporations Act
- (s) the CPS3 are expected to be treated as a liability for AIFRS purposes
- (t) for the purposes of determining whether a Holder is a 'qualified person' in relation to a distribution for the purposes of Division 1A of former Part IIIAA of the ITAA 1936, a Holder has taken no positions (apart from the holding of the CPS3) in relation to their CPS3 and will not be under an obligation or is likely to make a related payment (within the meaning of former section 160APHN of the ITAA 1936) in relation to the Dividends
- (u) the Holders in receipt of Dividends on the CPS3 will have held their CPS3 for a period of at least 90 days (excluding the day of disposal), within the period beginning on the day after the day on which the Holder acquired the CPS3 and ending on the 90th day after the day on which the CPS3 go ex-dividend
- (v) it is reasonable to expect that the dividend payout ratios or the franking credits in relation to the ordinary

- share capital or other preference share capital of SGL will not change as a result of the issue of the CPS3
- (w) on the date of Conversion of the CPS3 into SGL Ordinary Shares, the rights and obligations attached to the SGL Ordinary Shares are the same as those contained in the Constitution of SGL as at the time of issue of the CPS3, and
  - (x) the SIHL Notes and the AAIL Notes would not satisfy the debt test under section 974-20 of the ITAA 1997.

## Ruling

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69. The Ruling addresses the tax implications for Holders of the conversion of CPS3 into ordinary shares in the non-operating holding company SGL (SGL Ordinary Shares).

### Acquisition time of the CPS3

70. Pursuant to section 109-10, the Holders are taken to have acquired the CPS3 on the date of issue of the CPS3, being 8 May 2014.

### CPS3 cost base and reduced cost base

71. Pursuant to sections 110-25 and 110-55, the first element of the cost base and reduced cost base of each CPS3 is \$100.

### Inclusion of Dividends and franking credits in assessable income

72. The Holders must include in their assessable income all Dividends received under paragraph 44(1)(a) of the ITAA 1936, and an amount equal to the franking credit received on those Dividends under Division 207, unless the Holder is an entity whose ordinary or statutory income is exempt income.

### Entitlement to a tax offset

73. The Holders will generally be entitled to a tax offset equal to the franking credit received on the Dividends under subsection 207-20(2) for the income year in which the distribution is made, unless Subdivision 207-D applies. This entitlement will be subject to the circumstances listed in section 207-145 not arising (see paragraph 78 of this Ruling).

74. The Holders who are entitled to a tax offset under Division 207, in respect of franking credits received, will also be subject to the refundable tax offset rules in Division 67, unless specifically excluded under section 67-25 (and who are not excepted from the exclusion). Such excluded entities include certain trustees and corporate tax entities under subsections 67-25(1A) to (1D).

#### **Exempt income or non-assessable non-exempt income**

75. If the Dividend (or a part of it) is either exempt income or non-assessable non-exempt income in the hands of the relevant Holder, then the amount of any franking credit on the Dividend is not included in the assessable income of the Holder and the Holder is not entitled to a tax offset under Division 207 (Subdivision 207-D).

#### **Section 177EA**

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

#### **Imputation benefits – streaming**

77. The Commissioner will not make a determination under paragraph 204-30(3)(c) to deny the whole, or any part, of the imputation benefits received by a Holder in relation to the Dividends received by the Holders.

#### **Gross-up and tax offset rules**

78. Provided an entity is a 'qualified person', section 207-145 will not apply to the whole, or any part, of the Dividends received by the Holders. Accordingly, section 207-145 will not adjust the gross-up of the Holders' assessable income to exclude the franking credit, nor will it deny the tax offset to which the Holders would have otherwise been entitled.

#### **Qualified person and the Resale facility**

79. Under the former definition of 'qualified person' contained in Division 1A of former Part IIIA of the ITAA 1936, the Resale facility contained in clause 9 of the Terms will not of itself affect a Holder's risk of loss or opportunities for gain in respect of the CPS3 on the basis that it does not constitute a separate position for the purposes of that Division.

#### **Written Off CPS3**

80. Capital Gains Tax (CGT) event H2 will occur pursuant to section 104-155 when the CPS3 are Written Off.

81. However a Holder will not make a capital gain or a capital loss as a result of CGT Event H2 happening as there will be no capital proceeds or incidental costs incurred because of the CPS3 being Written Off.

82. No other CGT event will occur when the CPS3 are Written Off.

### **Conversion of CPS3 and allotment of additional SGL Ordinary Shares – CGT implications**

83. The Conversion of each CPS3 into SGL Ordinary Shares and the allotment of additional SGL Ordinary Shares under the Terms will not result in any CGT event occurring.

### **Cost base of additional SGL Ordinary Shares**

84. Section 6BA of the ITAA 1936 and Subdivision 130-A will apply to apportion the first element of the cost base and reduced cost base of the CPS3 over the SGL Ordinary Shares, including any additional SGL Ordinary Shares, allotted by SGL pursuant to a Conversion.

### **Acquisition time of additional SGL Ordinary Shares**

85. Under subsection 130-20(3), any additional SGL Ordinary Shares received by a Holder as part of a Conversion are taken to have been acquired at the time the CPS3 were originally acquired by the Holders, which is 8 May 2014.

### **Allotment of additional SGL Ordinary Shares – dividend**

86. The allotment of any additional SGL Ordinary Shares on Conversion of the CPS3 will not be assessable as dividend income in the hands of the Holders.

### **The value of additional SGL Ordinary Shares – ordinary income**

87. The value of any additional SGL Ordinary Shares issued on Conversion of the CPS3 will not be assessable as ordinary income in the hands of the Holders under subsection 6-5(1).

### **Section 45**

88. Section 45 of the ITAA 1936 will not apply to treat the additional SGL Ordinary Shares acquired on Conversion of the CPS3, as an unfrankable dividend paid by SGL.

**Section 45A**

89. The Commissioner will not make a determination, under subsection 45A(2) of the ITAA 1936, such that section 45C applies in relation to the whole or a part of the capital benefit represented by the SGL Ordinary Shares acquired on Conversion of the CPS3 under the Terms, so to treat it as an unfranked dividend in the hands of the Holders.

**Section 45B**

90. The Commissioner will not make a determination under subsection 45B(3) of the ITAA 1936, such that section 45C applies in relation to the whole or a part of the capital benefit represented by the SGL Ordinary Shares acquired on Conversion of the CPS3 under the Terms, so as to treat it as an unfranked dividend in the hands of the Holders.

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**Commissioner of Taxation**30 April 2014

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## Appendix 1 – Explanation

**①** *This Appendix is provided as information to help you understand how the Commissioner's view has been reached. It does not form part of the binding public ruling.*

### **Acquisition time of the CPS3**

91. An equity interest that is issued or allotted by a company is acquired when the contract is entered into or, if no contract exists, when the equity interests are issued or allotted (item 2 of the table in section 109-10).

92. The CPS3 will be issued on 8 May 2014. Therefore, for the purposes of item 2 in the table contained in section 109-10, the CPS3 are acquired on 8 May 2014.

### **CPS3 cost base and reduced cost base**

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

94. The Issue Price of each CPS3 is \$100. Accordingly, when the CPS3 are issued, the first element of the cost base and reduced cost base of each CPS3 is \$100.

### **Inclusion of Dividends and franking credits in Assessable Income**

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

96. Any dividends paid in respect of the CPS3 will be paid out of SGL's profits and will not be sourced, directly or indirectly, from SGL's share capital account. Accordingly, Holders must include any Dividends paid in their assessable income.

97. All Dividends are expected to be fully franked.

98. Subsection 207-20(1) provides that if a corporate tax entity makes a franked distribution to a shareholder, then an amount equal to the franking credit is included in the shareholder's assessable income, in addition to any other amount included in the shareholder's assessable income in relation to the distribution. As such, any franking credits attached to a Dividend that are received by a Holder must be included in the Holder's assessable income.

**Entitlement to a tax offset**

99. Subsection 207-20(2) provides that an entity is entitled to a tax offset equal to the amount of the franking credit on a distribution in the income year in which the distribution is made. Provided the Holder satisfies the requirements of Division 1A of former Part IIIAA of the ITAA 1936, the Holder will also be entitled to a tax offset equal to the amount of the franking credit received by the Holder, in the income year in which the Holder receives the Dividend.

100. The Holders who are entitled to a tax offset under Division 207, in respect of franking credits received, will also be subject to the refundable tax offset rules in Division 67, unless specifically excluded under section 67-25 (and not excepted from the exclusion). Such excluded entities include certain trustees and corporate tax entities under subsections 67-25(1A) to (1D).

**Exempt income or non-assessable non-exempt income**

101. Subdivision 207-D creates the appropriate adjustment to cancel the effect of the gross-up and tax offset rules where the Holder receives a franked distribution, and the franked distribution (or share of it) is, or would be, exempt income or non-assessable non-exempt income in the hands of the relevant Holder.

**Section 177EA**

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

- imposing a franking debit or an exempting debit on the distributing entity's franking account, or
- denying the imputation benefit on the distribution that flowed directly or indirectly to the relevant taxpayer.

103. Pursuant to subsection 177EA(3) of the ITAA 1936, the provision applies if the following conditions are satisfied:

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

- (c) the distribution was, or is expected to be, a franked distribution or a distribution franked with an exempting credit, and
- (d) except for this section, the person (the relevant taxpayer) would receive, or could reasonably be expected to receive, imputation benefits as a result of the distribution, and
- (e) having regard to the relevant circumstances of the scheme, it would be concluded that the person, or one of the persons, who entered into or carried out the scheme or any part of the scheme did so for a purpose (whether or not the dominant purpose but not including an incidental purpose) of enabling the relevant taxpayer to obtain an imputation benefit.

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

- (a) the issue of CPS3 constitutes a scheme for the disposition of a membership interest (paragraph 177EA(3)(a) of the ITAA 1936). Pursuant to paragraph 177EA(14)(a) of the ITAA 1936, a 'scheme for a disposition of membership interests or an interest in membership interests' includes a scheme that involves the issuing of membership interests. The issuance of CPS3 on the terms set out in the Prospectus is a scheme that involves the issuing of membership interests because, once the CPS3 are issued, the Holders are members of SGL and the CPS3 are not debt interests (sections 960-130 and 960-135)
- (b) frankable distributions are expected to be payable to the Holders (paragraph 177EA(3)(b) of the ITAA 1936). The Commissioner accepts that Dividends payable on the CPS3 will be frankable distributions to the extent that the Dividends on the CPS3 do not fall within the list of unfrankable distributions in section 202-45
- (c) franked distributions are expected to be paid to the Holders (paragraph 177EA(3)(c) of the ITAA 1936). Furthermore, SGL advised that it will continue its policy of fully franking all frankable distributions made by it, to the extent of the franking credits available in its franking account, and
- (d) it is reasonable to expect that an imputation benefit will be received by the relevant taxpayers as a result of distributions made to the Holders given that SGL expects to frank the distributions on the CPS3 (paragraph 177EA(3)(d) of ITAA 1936).

105. Accordingly, the issue is whether having regard to the relevant circumstances of the scheme, it would be concluded that a person, or one of the persons who entered into or carried out 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.

106. Circumstances which are relevant in determining whether any person has the requisite purpose include, but are not limited to, the factors listed in subsection 177EA(17) of the ITAA 1936.

107. The relevant circumstances listed encompass a range of circumstances which taken individually or collectively could indicate the requisite purpose. Due to the diverse nature of these circumstances, some may or may not be present at any one time in any one scheme.

108. SGL advised that the primary purpose for the issue of the CPS3 is to provide the Suncorp Group with capital for prudential purposes. The CPS3 will be issued on arm's length terms, and the Holders will provide fair value consideration for the issue of the CPS3.

109. The Commissioner considers that a number of the relevant circumstances of the present arrangement go some way towards indicating a non-incidental purpose of enabling a relevant taxpayer to obtain an imputation benefit. In particular, the calculation of the Dividend by reference to the corporate tax rate, and the franking adjustment that arises if the Dividend is not fully-franked, would be matters going to paragraph (f) of subsection 177EA(17) and are of significance for the ascertainment of the relevant purpose.

110. However, based on the information provided and the qualifications set out in this Ruling, the Commissioner's consideration of all of the relevant circumstances of the scheme would not, on balance, lead to a conclusion that the purpose of enabling Holders to obtain imputation benefits is more than incidental to SGL's purpose of raising capital to meet its prudential capital requirements.

111. Accordingly, the Commissioner will not make a determination under paragraph 177EA(5)(b) of the ITAA 1936 to deny the imputation benefits to the Holders.

### **Imputation benefits – streaming of imputation benefits**

112. Subdivision 204-D broadly enables the Commissioner to make a determination when distributions with attached imputation benefits are streamed to a member of a corporate tax entity in preference to another member.

113. Section 204-30 prescribes the circumstances that are required to exist before the Commissioner may make such a determination, and applies where an entity 'streams' the payment in such a way that:

- an imputation benefit is received by a member of the entity as a result of the distribution (paragraph 204-30(1)(a))

- the member (the favoured member) derives a greater benefit from the franking credits than another member of the entity (paragraph 204-30(1)(b)), and
- the other member (the disadvantaged member) of the entity will receive lesser imputation benefits, or will not receive any imputation benefits, whether or not the other member receives other benefits (paragraph 204-30(1)(c)).

114. 'Streaming' is not defined for the purposes of Subdivision 204-D. However, the Commissioner has understood it to refer to a company 'selectively directing the flow of franked distributions to those members who can most benefit from imputation credits' (paragraph 3.28 of the Explanatory Memorandum to the New Business Tax System (Imputation) Bill 2002).

115. It is expected that the CPS3 will be listed on the ASX and hence will be available for investment by different types of investors. The Dividends will be paid irrespective of the Holders tax profiles and will be paid in proportion to Holders' ownership interest in the CPS3. Additionally, the extent to which a Holder receives franked Dividends will be determined solely by each Holder's proportionate ownership of the CPS3 and regardless of the extent to which any particular Holder will actually benefit from the franking credits attached to the Dividend.

116. With respect to the franking of the Dividends, SGL has also expressed an intention to fully or substantially frank all Dividends in the same proportion as the SGL Ordinary Shares. Furthermore, the CPS3 will be offered to certain non-resident investors under the Institutional Offer, and any CPS3 held by non-residents investors will be franked in the same manner as the CPS3 held by residents. These factors suggest that the requisite element of directing the flow franked distributions to those members of the entity that can most benefit from them, at the expense of those that cannot, is not present in respect of Dividends.

117. Accordingly, the Commissioner will not make a determination under paragraph 204-30(3)(c) to deny imputation benefits to the Holders.

## **Gross-up and tax offset rules**

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

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

- the entity is not a 'qualified person' in relation to the distribution (paragraph 207-145(1)(a))

- the Commissioner has made a determination under paragraph 177EA(5)(b) of the ITAA 1936 that no imputation benefit is to arise in relation to the dividend (paragraph 207-145(1)(b))
- the Commissioner has made a determination under paragraph 204-30(3)(c) that no imputation benefit is to arise in relation to the distribution (paragraph 207-145(1)(c)), or
- the dividend is made as part of a dividend stripping operation (paragraph 207-145(1)(d)).

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

121. The holding period rule applies where neither the taxpayer nor an associate has made, is under an obligation to make, or is likely to make, a related payment in respect of the dividend, and requires the shares to have been continuously held at risk throughout the primary qualification period (former paragraph 160APHO(1)(a) of the ITAA 1936).

122. The related payments rule applies where the taxpayer or an associate, has made, is under an obligation to make, or is likely to make, a related payment in respect of the dividend and requires the shares to have been continuously held at risk throughout the secondary qualification period (former subsection 160APHO(1) of the ITAA 1936 and former section 160APHN of the ITAA 1936).

123. The Holders will be 'qualified persons', if:

- the Holders will have held their CPS3 at risk for a period of at least 90 days (excluding the day of acquisition and the day of disposal, and any days on which the Holder has materially diminished risks of loss or opportunities for gain in respect of the shares or interest), in the period, beginning on the day after the day on which the Holders acquired the CPS3 and ending on the 90th day after the day on which the CPS3 become ex-dividend (former subsections 160APHO(2) and 160APHO(3) of the ITAA 1936 and former sections 160APHM and 160APHJ of the ITAA 1936), and
- neither the Holders, nor associates of the Holders, have made, are under an obligation to make, or are likely to make a related payment in relation to the Dividends on CPS3 (former paragraph 160APHO(1)(a) of the ITAA 1936 and former section 160APHN of the ITAA 1936).

124. If either or both of the above two considerations are not met, the Holders will not be a 'qualified person' for the purposes of Division 1A of former Part IIIA of the ITAA 1936. Subdivision 207-F will create the appropriate adjustment to cancel the effect of the gross-up and tax offset rules for the Holders in relation to payments of Dividends.

125. The Commissioner has confirmed that he will not make a determination under paragraph 177EA(5)(b) of the ITAA 1936 or paragraph 204-30(3)(c) to deny the imputation benefits attached to Dividends paid by SGL to the Holders (see paragraphs 76 and 77 of this Ruling).

126. A distribution to a member of a corporate tax entity will be taken to be made as part of a dividend stripping operation, pursuant to section 207-155, where the distribution arose out of, or was made in the course of, a scheme that was by way of or in the same nature of dividend stripping, or had substantially the effect of a scheme by way of or in the nature of dividend stripping.

127. The documents provided by the taxpayer provide no indication that the offering of the CPS3 and the associated payment of franked Dividends to the Holders in any way constitute a scheme by way of or in the nature of dividend stripping or a scheme having substantially the effect of a scheme by way of or in the nature of dividend stripping. As such, the scheme will not be taken to constitute a dividend stripping arrangement and the dividend stripping provision will have no application to the Holders in the present circumstances.

128. Therefore, in the absence of any evidence of the manipulation of the imputation system, section 207-145 will not apply to deny Holders a gross-up or tax offset in respect of the whole or any part of the franked Dividends received by them.

## **Qualified person and the Resale facility**

129. In determining whether a Holder is a 'qualified person', all of the Holder's 'positions' in respect of the CPS3 are taken into account in determining if there has been a material diminution in the risks of loss or opportunities for gain (see former section 160APHJ and subsection 160APHM(3) of the ITAA 1936). A position relating to a share is anything that has a 'delta' in relation to the shares (see former subsection 160APHJ(2) of the ITAA 1936).

130. An embedded share option is a position in relation to a share if it is exercisable by or against a party other than the issuer of the share (Taxation Determination 2007/29).

131. Under the Resale facility (clause 9 of the Terms), SGL can elect to require all the Holders to sell their CPS3 to a Nominated Purchaser. A Nominated Purchaser (a third party) will not have the right or ability to trigger redemption of the CPS3, and, until nominated by SGL, will not have the right or ability to acquire the CPS3 from the Holders.

132. SGL is not required to exercise the Resale facility and has not appointed any Nominated Purchaser. The Resale facility is an option that is held by SGL, the issuer of the share, and not by a third party. The Resale facility therefore does not represent a separate position in relation to the CPS3 for the purposes of Division 1A of former Part IIIAA of the ITAA 1936.

133. Therefore it is considered that the Resale facility does not affect a Holder's risk of loss or opportunity for gain in respect of the CPS3.

### **Written Off CPS3**

134. Each CPS3 is a bundle of rights, however, those rights are not separate pieces of property capable of being divided out and held separately. Accordingly, the rights attaching to the CPS3 do not constitute individual assets as defined by section 108-5, but rather combine to make up the ultimate asset, being the share (Taxation Ruling TR 94/30 (TR 94/30)).

135. Under section 104-25, CGT event C2 happens if, among other things, the ownership of an intangible asset, such as a preference share, ends by the share:

- being redeemed or cancelled (paragraph 104-25(1)(a)), or
- if the share is a convertible interest – being converted (paragraph 104-25(1)(f)).

136. The mere variation of rights attaching to a share is not a 'redemption' or 'cancellation' of the share for the purposes of paragraph 104-25(1)(a). Further, it does not result in the ownership of a CGT asset coming to an end under paragraph 104-25(f).

137. Under the Terms, when CPS3 are Written Off, a mere variation of rights attaching to the CPS3 will occur. Consequently, CGT event C2 will not occur when the CPS3 are Written Off.

138. Under section 104-155, CGT event H2 happens if:

- (a) an act, transaction or event occurs in relation to a CGT asset that you own, and
- (b) the act, transaction or event does not result in an adjustment being made to the asset's cost base or reduced cost base.

139. Although CGT event C2 will not occur when the CPS3 are Written Off, the variation of rights under the Terms is an act, transaction or event in relation to the CPS3. As the variation of rights will not result in any adjustment to the cost base or reduced cost base of the CPS3, CGT event H2 will occur when the CPS3 are Written Off.

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

141. Subsection 116-20(2) provides that the capital proceeds from CGT event H2 will be the money or other consideration you received, or are entitled to receive, because of the act, transaction or event.

142. There will be no capital proceeds and no incidental costs will be incurred as a result of the CPS3 being Written Off under the Terms. Accordingly, when the CPS3 are Written Off, Holders will make no capital gain or capital loss because of CGT event H2.

143. No other CGT event will happen when the CPS3 are Written Off under the Terms.

## **Conversion of CPS3 and allotment of additional SGL Ordinary Shares – CGT implications**

144. Under the Transaction, each CPS3 will convert into one SGL Ordinary Share through a variation of the rights attaching to each CPS3. The Holders will also receive an allotment of additional SGL Ordinary Shares in accordance with the Terms.

145. As stated at paragraphs 134 to 136 of this Ruling, each CPS3 is a bundle of rights, however, those rights are not separate pieces of property capable of being divided out and held separately, and do not constitute individual assets as defined by section 108-5. Rather, the rights combine to make up the ultimate asset, being the share (TR 94/30).

146. The mere variation of rights attaching to the CPS3 and the allotment of an additional number of SGL Ordinary Shares for no consideration does not result in the ownership of an intangible CGT asset coming to an end by the share being 'redeemed' or 'cancelled' under paragraph 104-25(1)(a).

147. Further, the Conversion of the CPS3 to SGL Ordinary Shares by the variation of the rights attaching to the CPS3 does not result in the ownership of an intangible CGT asset coming to an end by the CPS3 being converted under paragraph 104-25(1)(f).

148. The relinquishment by the Holders of some of the rights attaching to the CPS3 is not a CGT event that happens to part of the CGT asset comprised by each CPS3 under section 112-30 (paragraphs 40 to 42 of TR 94/30).

149. Consequently, CGT event C2 will not occur on Conversion of the CPS3 into SGL Ordinary Shares, and, as a result, Subdivision 130-C will not have application.

150. Further, the Conversion of the CPS3 involving the allotment of additional SGL Ordinary Shares will result in an adjustment to the cost base and reduced cost base of the CPS3 under section 6BA of the ITAA 1936 and Subdivision 130-A.

151. Accordingly, CGT event H2 will not happen on the Conversion of CPS3 involving the allotment of additional SGL Ordinary Shares.

152. No other CGT event in Division 104 will occur as a result of the Conversion of the CPS3 under the Terms.

**Cost base of additional SGL Ordinary Shares**

153. Section 6BA of the ITAA 1936 and Subdivision 130-A will apply to apportion the first element of the cost base and reduced cost base of CPS3 over the SGL Ordinary Shares and any additional ordinary shares allocated by SGL.

154. Section 6BA of the ITAA 1936 applies if a shareholder holds shares in a company (the original shares) and the company issues other shares (the bonus shares) in respect of the original shares.

155. Pursuant to subsection 6BA(3) of the ITAA 1936, as the additional SGL Ordinary Shares will be issued to Holders for no consideration and will not be a dividend nor be taken to be a dividend, the issue price of CPS3 will be apportioned over the Converted CPS3 and any additional SGL Ordinary Shares allotted.

156. Subdivision 130-A applies in a similar manner. It provides special rules relating to the time of acquisition and the cost base of bonus equities for CGT purposes.

157. Section 130-20 sets out what happens if an entity owns shares in a company (the original equities) and the company issues other shares (the bonus equities) in relation to the original equities.

158. Under item 1 of the table in subsection 130-20(3), as the additional SGL Ordinary Shares are not a dividend nor taken to be a dividend, the first element of the cost base and reduced cost base of each CPS3 are apportioned over both the Converted CPS3 and any additional SGL Ordinary Shares issued to the Holders by SGL.

**Acquisition time of additional SGL Ordinary Shares**

159. The Holders will be taken to have acquired the additional SGL Ordinary Shares at the time when the CPS3 were originally acquired by the Holders (subsection 130-20(3)), which is 8 May 2014.

**Allotment of additional SGL Ordinary Shares – dividend**

160. Subsection 6(1) of the ITAA 1936 defines a 'dividend' to include any distribution made by a company to any of its shareholders, whether in money or other property, and any amount credited by a company to any of its shareholders as shareholders.

161. Although the additional SGL Ordinary Shares issued on Conversion of the CPS3 will constitute 'property' in the hands of the Holders, the allotment is not a disposition of property in the ordinary meaning of that expression (*Ord Forrest Pty Ltd v. Federal Commissioner of Taxation* (1974) 130 CLR 124; (1973) 74 ATC 4034; (1973) 4 ATR 230, per Barwick CJ and McTiernan J). As there is no disposition there cannot be a distribution of property by SGL.

162. The allotment of additional SGL Ordinary Shares does not constitute a dividend under subsection 6BA(5) of the ITAA 1936 as the Terms do not provide Holders with a choice of being paid a dividend or being issued shares.

163. Furthermore, no amount is credited to the Holders, nor is an amount paid out of profits.

164. Accordingly, the allotment of additional SGL Ordinary Shares does not constitute a dividend within the meaning of subsection 6(1) of the ITAA 1936.

## **Allotment of additional SGL Ordinary Shares – ordinary income**

165. The allotment of additional SGL Ordinary Shares will be a bonus issue of shares within the meaning of paragraph 254A(1)(a) of the Corporations Act, that is, an issue of shares for which consideration is not payable to SGL. The issue of additional SGL Ordinary Shares will result in a re-expression of the Holder's interest in the share capital of SGL.

166. Accordingly, the value of any additional SGL Ordinary Shares issued on Conversion of the CPS3 will not be assessable as ordinary income under subsection 6-5(2) (*Commissioner of Taxation v. McNeil* (2007) 229 CLR 656; 2007 ATC 4223; (2007) 64 ATR 431).

## **Section 45**

167. Section 45 of the ITAA 1936 applies where a company streams the provision of shares and the payment of minimally franked dividends to its shareholders in such a way that the shares are received by some shareholders and minimally franked dividends are received by other shareholders. Minimally franked dividends are dividends which are not franked or are franked to less than 10%.

168. SGL has consistently paid fully franked dividends and has stated it will pay fully franked dividends to all its shareholders, including the Holders, to the extent of the franking credits in its franking account. Furthermore, the Terms do not allow SGL to issue SGL Ordinary Shares to all or some of the Holders in satisfaction of their dividend entitlements in relation to the CPS3.

169. Upon Conversion of the CPS3 under the Terms, Holders may receive additional SGL Ordinary Shares. The issue of additional SGL Ordinary Shares in these circumstances will not be an alternative to the receipt of any dividends payable by SGL, nor will there be any link between the issue of the additional SGL Ordinary Shares and the timing of the declaration or payment of any dividends by SGL.

170. Therefore, section 45 of the ITAA 1936 will not apply to any of the SGL Ordinary Shares that will be acquired on Conversion of the CPS3.

**Section 45A**

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

172. The receipt of SGL Ordinary Shares by the Holders will be a provision of capital benefits pursuant to paragraph 45A(3)(a) of the ITAA 1936.

173. Upon Conversion of the CPS3 under the Terms, each CPS3 will Convert to one SGL Ordinary Share. Furthermore, in accordance with the Terms, Holders may be allotted additional SGL Ordinary Shares. However, a Holder's entitlement to SGL Ordinary Shares under the Terms will not be determined based upon their preference for the receipt of capital benefits in lieu of dividends. In the absence of other additional factors that would contribute to an alternative conclusion, the allotment of SGL Ordinary Shares upon Conversion will not constitute the streaming of capital benefits.

174. Therefore, the receipt of SGL Ordinary Shares by all Holders upon Conversion under the Terms will not trigger the application of section 45A of the ITAA 1936. The Commissioner will not make a determination under subsection 45A(2) of the ITAA 1936 such that section 45C of the ITAA 1936 will apply to treat all or part of the capital benefit as an unfranked dividend in the hands of the Holders.

**Section 45B**

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

176. Upon Conversion of the CPS3 under the Terms, each CPS3 will Convert to one SGL Ordinary Share. Furthermore, in accordance with the Terms, Holders may be allotted additional SGL Ordinary Shares. This would constitute a scheme under which a capital benefit, as defined in paragraph 45B(5)(a) of the ITAA 1936, is provided to the Holders. A CPS3 represents a fully paid preference share in the capital SGL. Consequently, its Conversion under the Terms represents a re-expression of a Holder's interest in SGL's share capital, rather than a distribution of a profit disguised as capital.

177. For the provision to apply paragraph 45B(2)(c) requires that, having regard to the relevant circumstances of the scheme, it would be concluded that the person, or one of the persons, who entered into the scheme or carried out the scheme or any part of the scheme did so for a purpose, other than an incidental purpose, of enabling a taxpayer (the relevant taxpayer) to obtain a tax benefit. The relevant circumstances of the scheme are listed in subsection 45B(8) of the ITAA 1936.

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178. Therefore, having regard to the relevant circumstances of the scheme, it cannot be concluded that any of the parties to the scheme entered into or carried out the scheme for a more than incidental purpose of enabling the Holders to obtain a tax benefit.

Consequently, section 45B of the ITAA 1936 will not apply to treat the SGL Ordinary Shares acquired upon Conversion under the Terms as an unfranked dividend in the hands of the Holders.

179. Accordingly the Commissioner will not make a determination under subsection 45B(3) of the ITAA 1936.

**Appendix 2 – Detailed contents list**

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## References

*Previous draft:*

Not previously issued as a draft

*Related Rulings/Determinations:*

TR 94/30; TR 2006/10;  
TD 2007/29

*Subject references:*

- acquisition of CGT assets
- allotment & issue of securities
- banking, finance & securities
- capital gains tax
- CGT assets
- CGT cost base
- CGT events
- CGT events C1-C3 - end of a CGT asset
- CGT events H1-H2 – special capital receipts
- company tax
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- financial instruments
- frankable dividends
- franked dividends
- franking accounts
- franking credits
- imputation system
- preference shares
- redeemable preference shares
- securities
- securities transactions
- shares

*Legislative references:*

- ITAA 1936 6
- ITAA 1936 44(1)
- ITAA 1936 45
- ITAA 1936 45A
- ITAA 1936 45B
- ITAA 1936 PT IIIAA Div 1A
- ITAA 1936 177EA

- ITAA 1997 6-5
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- Copyright Act 1968
- Corporations Act 2001

*Case references:*

- Ord Forrest Pty Ltd v. Federal Commissioner of Taxation (1974) 130 CLR 124 (1973) 74 ATC 4034 (1973) 4 ATR 230
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- Explanatory Memorandum to New Business Tax System (Imputation) Bill 2002

## ATO references

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