

CR 2014/99 - Income tax: demerger of Jacana Minerals Limited by Syrah Resources Limited

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Class Ruling

Income tax: demerger of Jacana Minerals Limited by Syrah Resources Limited

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ⓘ This publication provides you with the following level of protection:

This publication (excluding appendixes) is a public ruling for the purposes of the *Taxation Administration Act 1953*.

A public ruling is an expression of the Commissioner's opinion about the way in which a relevant provision applies, or would apply, to entities generally or to a class of entities in relation to a particular scheme or a class of schemes.

If you rely on this ruling, the Commissioner must apply the law to you in the way set out in the ruling (unless the Commissioner is satisfied that the ruling is incorrect and disadvantages you, in which case the law may be applied to you in a way that is more favourable for you – provided the Commissioner is not prevented from doing so by a time limit imposed by the law). You will be protected from having to pay any underpaid tax, penalty or interest in respect of the matters covered by this ruling if it turns out that it does not correctly state how the relevant provision applies to you.

What this Ruling is about

1. This Ruling sets out the Commissioner's opinion on the way in which the relevant provisions identified below apply to the defined class of entities, who take part in the scheme to which this Ruling relates.

Relevant provision(s)

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

- subsection 6(1) of the *Income Tax Assessment Act 1936* (ITAA 1936)
- subsection 44(1) of the ITAA 1936
- section 45B of the ITAA 1936
- section 104-135 of the *Income Tax Assessment Act 1997* (ITAA 1997)
- subsection 115-30(1) of the ITAA 1997
- Division 125 of the ITAA 1997, and
- Division 855 of the ITAA 1997.

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

Class of entities

3. The class of entities to which this Ruling applies is the holders of ordinary shares in Syrah Resources Limited (Syrah) who:

- (a) were listed on the share register of Syrah as at the Record Date (8 October 2014 at 7pm Australian Eastern Standard Time) for the demerger of ordinary shares in Jacana Minerals Limited (Jacana)
- (b) on the Record Date did not hold their ordinary shares in Syrah as revenue assets (as defined in section 977-50) or as trading stock (as defined in subsection 995-1(1)) – that is, they held their ordinary shares in Syrah broadly on capital account, and
- (c) are not subject to the taxation of financial arrangements (TOFA) rules in Division 230 in relation to gains and losses on their ordinary shares in Syrah.

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

4. In this Ruling, a person belonging to this class of entities is referred to as a 'Syrah shareholder'.

Qualifications

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

6. The class of entities defined in this Ruling may rely on its contents provided the scheme actually carried out is carried out in accordance with the scheme described in paragraphs 9 to 33 of this Ruling.

7. 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

8. This Ruling applies from 1 July 2014 to 30 June 2015. The Ruling continues to apply after 30 June 2015 to all entities within the specified class who entered into the specified scheme during the term of the Ruling. However, this Ruling will not apply to taxpayers to the extent that it conflicts with the terms of a settlement of a dispute agreed to before the date of issue of this Ruling (see paragraphs 75 and 76 of Taxation Ruling TR 2006/10).

Scheme

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

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

Syrah

10. Syrah is an Australian resident company. Syrah was incorporated on 4 May 2007, and its ordinary shares were listed on the Australian Securities Exchange (ASX) on 11 September 2007.

11. Syrah is a minerals exploration company that is undertaking a significant graphite and vanadium project in northern Mozambique (the Balama project). Immediately before the demerger, Syrah also had exploration projects in Tanzania (the Tanzanian projects). The Tanzanian projects are mainly exploration projects for mineral sands, but also include exploration for graphite and nickel.

12. Immediately before the demerger, Syrah had the following shares and options on issue:

- 164,135,076 ordinary shares, and
- 5,460,005 unlisted options to acquire ordinary shares in Syrah.

13. There were no other ownership interests (as defined in subsection 125-60(1)) in Syrah immediately before the demerger.

14. As at 30 June 2014, Syrah had issued share capital of \$81,444,683, accumulated losses of \$18,670,066, and reserves of \$1,767,544.

15. Syrah has never paid any dividends, issued bonus shares, or returned share capital.

16. Approximately 4% of Syrah's ordinary shares are held by foreign residents (as defined in subsection 995-1(1)).

Jacana

17. Jacana Minerals Limited (Jacana) is an Australian resident company. Jacana was incorporated on 2 July 2014, and immediately before the demerger was wholly owned by Syrah.

18. Immediately before the demerger, Jacana had 50,038,524 ordinary shares on issue.

19. There were no other ownership interests (as defined in subsection 125-60(1)) in Jacana immediately before the demerger.

20. After the demerger, it is proposed that Jacana will complete an initial public offering (IPO) of new ordinary shares and list its ordinary shares on the ASX in late 2014. The IPO may include a sale facility for existing Jacana ordinary shares.

Pre-demerger transactions

21. The Tanzanian projects were conducted through a subsidiary of Syrah called Jacana Resources (Tanzania) Limited. Prior to the demerger, Jacana was incorporated, and all of the shares in Jacana Resources (Tanzania) Limited (owned by a wholly owned subsidiary of Syrah) were transferred to Jacana.

22. There was also an intra-group loan from Syrah to Jacana Resources (Tanzania) Limited. Jacana Resources (Tanzania) Limited's liability to Syrah was assumed by Jacana. Jacana then discharged its liability to Syrah by issuing new shares in itself to Syrah.

The demerger of Jacana ordinary shares

23. To effect the demerger by Syrah of Jacana ordinary shares, the shareholders of Syrah voted at a meeting on 1 October 2014 to approve an ordinary resolution under section 256C of the *Corporations Act 2001* to reduce the share capital of Syrah by \$6,559,855 (the capital reduction amount). This amount was debited to the share capital account of Syrah. The capital reduction amount equates to 4 cents per Syrah ordinary share.

24. The payment of the capital reduction amount was satisfied by an *in specie* distribution to the shareholders of Syrah of 49, 240, 117 ordinary shares in Jacana held by Syrah. The shares were distributed to the shareholders of Syrah on a pro rata basis. Syrah implemented the demerger by transferring the Jacana ordinary shares to the shareholders of Syrah on 15 October 2014. The shareholders of Syrah received 3 Jacana ordinary shares for every 10 Syrah ordinary shares they held at the Record Date for the demerger (8 October 2014). As a result of the demerger, the shareholders of Syrah will own shares in both Syrah and Jacana.

25. A small number of Syrah ordinary shares were held on the Record Date by shareholders who were located overseas. For some of these overseas shareholders, a foreign law impeded, or it was impractical or unreasonably onerous to determine whether a foreign law impeded, the ability of Syrah to transfer Jacana ordinary shares to them. Accordingly, the Jacana ordinary shares they would otherwise have received were transferred to a share sale facility on 15 October 2014. The share sale facility will dispose of those Jacana ordinary shares simultaneously with, or as soon as practicable after, the IPO of new Jacana ordinary shares, and will pay the sale proceeds (less any expenses) to the affected overseas shareholders.

26. The market value of the 49,240,117 Jacana ordinary shares transferred by Syrah to its ordinary shareholders and the share sale facility did not exceed the capital reduction amount of \$6,559,855.

27. Syrah retained a small percentage (1.6%) of Jacana ordinary shares. Syrah intends to sell these shares after Jacana is listed on the ASX.

Reasons for the demerger

28. The reasons for the demerger are based on the success of Syrah's Balama project in Mozambique. The Board of Directors of Syrah believed that this success had overshadowed the Tanzanian projects. By spinning-off the Tanzanian projects, the Board of Directors of Syrah intended to:

- Expose the value of the Tanzanian projects
- Enhance the combined value of the Balama project in Mozambique and the Tanzanian projects in the hands of shareholders
- Make it easier to raise equity for the Tanzanian projects, and
- Speed up the progress of the Tanzanian projects.

Accounting treatment

29. Syrah accounted for the capital reduction and the distribution of Jacana ordinary shares that effected the demerger with the following journal entry:

DR Share Capital	\$6,559,855	
CR Investment in Jacana		\$6,559,855

Other matters

30. No amounts have been transferred to the share capital account (as defined in section 975-300) of Syrah from any of its other accounts. Accordingly, Syrah's share capital account is not tainted (within the meaning of Division 197).

31. No Syrah shareholder acquired their Syrah ordinary shares before 20 September 1985.

32. No Syrah ordinary shares were an indirect Australian real property interest (within the meaning given by section 855-25) at the time of the payment of the capital reduction amount (satisfied through the transfer of the Jacana ordinary shares) on 15 October 2014.

33. The Jacana ordinary shares acquired by foreign resident Syrah shareholders under the demerger were not taxable Australian property (within the meaning given by section 855-15) just after they acquired them.

Ruling

Dividend consequences – all Syrah shareholders

34. No part of the distribution of Jacana ordinary shares to Syrah shareholders is a 'dividend' as defined in subsection 6(1) of the ITAA 1936.

35. As a result, no part of the distribution of Jacana ordinary shares will be included in the assessable income of a Syrah shareholder under subsection 44(1) of the ITAA 1936.

36. The Commissioner will not make a determination under paragraph 45B(3)(a) of the ITAA 1936 that section 45BA of the ITAA 1936 applies to the whole, or any part, of the demerger benefit provided to Syrah shareholders under the demerger of Jacana ordinary shares.

37. The Commissioner will not make a determination under paragraph 45B(3)(b) of the ITAA 1936 that section 45C of the ITAA 1936 applies to the whole, or any part, of the capital benefit provided to Syrah shareholders under the demerger of Jacana ordinary shares.

CGT consequences – Australian resident Syrah shareholders

CGT event G1

38. CGT event G1 in section 104-135 happened in respect of each Syrah ordinary share owned by an Australian resident Syrah shareholder at the time Syrah made the payment of the capital reduction amount (satisfied by distributing the Jacana ordinary shares). This is because Syrah made a payment (which can include giving property) to its shareholders in respect of the shares they owned in Syrah, some or all of the payment is not a dividend, and the payment is not included in the assessable income of shareholders (subsection 104-135(1)).

Capital gain

39. An Australian resident Syrah shareholder will make a capital gain from CGT event G1 happening if the capital reduction amount for each Syrah ordinary share (4 cents) is more than the cost base of the Syrah ordinary share. The capital gain is equal to the amount of the excess. No capital loss can be made from CGT event G1 (subsection 104-135(3)).

Demerger roll-over

40. A demerger, as defined in section 125-70, happened to the Syrah demerger group (which included Syrah and Jacana) under the scheme that is the subject of this Ruling.

41. An Australian resident Syrah shareholder can choose to obtain demerger roll-over under Division 125.

Consequences of choosing demerger roll-over

42. An Australian resident Syrah shareholder who chooses demerger roll-over:

- will disregard a capital gain made when CGT event G1 happened under the demerger to their Syrah ordinary shares (subsection 125-80(1)), and
- must recalculate the first element of the cost base and reduced cost base of their Syrah ordinary shares, and calculate the first element of the cost base and reduced cost base of the Jacana ordinary shares they acquired under the demerger (subsection 125-80(2)).

43. The first element of the cost base and reduced cost base of each Syrah ordinary share and Jacana ordinary share is worked out by:

- taking the total of the cost bases of the Syrah ordinary shares just before the demerger, and
- apportioning that total between the Syrah ordinary shares and the Jacana ordinary shares acquired under the demerger.

44. The apportionment of this total is done on a reasonable basis having regard to the market values (just after the demerger) of the Syrah ordinary shares and Jacana ordinary shares, or a reasonable approximation of those market values (subsections 125-80(2) and 125-80(3)).

45. The Commissioner accepts that a reasonable apportionment is to:

- attribute 98.87% of the total of the cost bases of the Syrah ordinary shares just before the demerger to the Syrah ordinary shares, and
- attribute 1.13% of the total of the cost bases of the Syrah ordinary shares just before the demerger to the Jacana ordinary shares.

Consequences of not choosing demerger roll-over

46. An Australian resident Syrah shareholder who does not choose demerger roll-over:

- cannot disregard a capital gain made when CGT event G1 happened under the demerger to their Syrah ordinary shares, and
- must recalculate the first element of the cost base and reduced cost base of their Syrah ordinary shares, and calculate the first element of the cost base and reduced cost base of the Jacana ordinary shares they acquired under the demerger, in the same way as described in paragraphs 43 to 45 of this Ruling (subsections 125-85(1) and (2)).

Acquisition date of the Jacana ordinary shares for the purpose of making a discount capital gain

47. For the purpose of determining eligibility to make a discount capital gain, a Jacana ordinary share acquired by an Australian resident Syrah shareholder under the demerger will be taken to have been acquired on the date the shareholder acquired, for CGT purposes, the corresponding Syrah ordinary shares (item 2 of the table in subsection 115-30(1)). This will be the case whether or not the Australian resident Syrah shareholder chooses demerger roll-over.

CGT consequences – foreign resident Syrah shareholders

CGT event G1

48. CGT event G1 in section 104-135 happened in respect of each Syrah ordinary share owned by a foreign resident Syrah shareholder at the time Syrah made the payment of the capital reduction amount (satisfied by distributing the Jacana ordinary shares).

Capital gain

49. A foreign resident Syrah shareholder will make a capital gain from CGT event G1 happening if the capital reduction amount for each Syrah ordinary share (4 cents) is more than the cost base of the Syrah ordinary share. The capital gain is equal to the amount of the excess. No capital loss can be made from CGT event G1 (subsection 104-135(3)).

Demerger roll-over is not available

50. A foreign resident Syrah shareholder cannot choose to obtain demerger roll-over under Division 125 because the Jacana ordinary shares they acquired under the demerger were not taxable Australian property just after they acquired them (subsection 125-55(2)).

Foreign resident Syrah shareholders whose Syrah ordinary shares were not taxable Australian property

51. A foreign resident Syrah shareholder can disregard a capital gain made from CGT event G1 happening under the demerger in respect of a Syrah ordinary share, unless:

- the Syrah ordinary share has been used at any time by them in carrying on a business through a permanent establishment in Australia (item 3 of the table in section 855-15), or
- the Syrah ordinary share is covered by subsection 104-165(3) (item 5 of the table in section 855-15).

Cost base and reduced cost base of Syrah ordinary shares and Jacana ordinary shares

52. A foreign resident Syrah shareholder must recalculate the first element of the cost base and reduced cost base of their Syrah ordinary shares, and calculate the first element of the cost base and reduced cost base of the Jacana ordinary shares they acquired under the demerger, in the same way as described in paragraphs 43 to 45 of this Ruling (subsections 125-85(1) and (2)).

Acquisition date of the Jacana ordinary shares for the purpose of making a discount capital gain

53. For the purpose of determining eligibility to make a discount capital gain, a Jacana ordinary share acquired by a foreign resident Syrah shareholder under the demerger will be taken to have been acquired on the date the shareholder acquired, for CGT purposes, the corresponding Syrah ordinary shares (item 2 of the table in subsection 115-30(1)). The discount percentage applied by foreign resident Syrah shareholders will be affected by sections 115-105 to 115-120.

Appendix 1 – Explanation

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

54. The income tax consequences and relevant legislative provisions that arise concerning the scheme that is the subject of this Ruling are outlined in the Ruling part of this document.

Dividend consequences

Distribution of Jacana ordinary shares is not a dividend for income tax purposes

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

56. The term ‘dividend’ is defined in subsection 6(1) of the ITAA 1936, and includes any distribution made by a company to any of its shareholders, whether in money or other property. However, paragraph (d) of the definition of ‘dividend’ in subsection 6(1) of the ITAA 1936 excludes a distribution by a company to its shareholders from being a dividend where the amount of the money 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.

57. The term ‘share capital account’ is defined in section 975-300 as an account which the company keeps of its share capital, or any other account created on or after 1 July 1998 where the first amount credited to the account was an amount of share capital.

58. Subsection 975-300(3) states that an account is not a share capital account if it is tainted.

59. The demerger of Jacana was implemented by Syrah distributing property (Jacana ordinary shares) to shareholders of Syrah. The total market value of the Jacana ordinary shares distributed to the shareholders of Syrah was debited against an amount standing to the credit of Syrah’s share capital account. As Syrah’s share capital account is not tainted within the meaning of Division 197 of the ITAA 1997, the exclusion in paragraph (d) of the definition of ‘dividend’ in subsection 6(1) of the ITAA 1936 applies.

60. As the total market value of the Jacana ordinary shares distributed to the shareholders of Syrah was debited against an amount standing to the credit of Syrah's share capital account, the entire distribution is not a 'dividend' as defined in subsection 6(1) of the ITAA 1936. As a result, the distribution will not be included in the assessable income of a Syrah shareholder under subsection 44(1) of the ITAA 1936 (see also Taxation Ruling TR 2003/8).¹

The application of sections 45B, 45BA and 45C

61. Section 45B of the ITAA 1936 is an anti-avoidance provision which, if applicable, allows the Commissioner to make a determination that all or part of a demerger allocation or return of capital received by shareholders is to be treated as an unfranked dividend.

62. The purpose of section 45B of the ITAA 1936 is to ensure that the relevant amounts distributed to shareholders are treated as dividends for tax purposes if certain payments, allocations and distributions are made in substitution for dividends. Specifically, section 45B of the ITAA 1936 applies where:

- (a) there is a scheme under which a person is provided with a demerger benefit or a capital benefit by a company (paragraph 45B(2)(a) of the ITAA 1936)
- (b) under the scheme a taxpayer, who may or may not be the person provided with the demerger benefit or the capital benefit, obtains a tax benefit (paragraph 45B(2)(b) of the ITAA 1936), and
- (c) having regard to the relevant circumstances of the scheme, it would be concluded that the person, or one of the persons, who entered into or carried out the scheme or any part of the scheme did so for a purpose (other than an incidental purpose) of enabling a taxpayer to obtain a tax benefit (paragraph 45B(2)(c) of the ITAA 1936).

63. The arrangement involving the distribution of Jacana ordinary shares to the shareholders of Syrah constitutes a scheme for the purposes of section 45B of the ITAA 1936.

64. The phrase 'provided with a demerger benefit' is defined in subsection 45B(4) of the ITAA 1936 and includes a company providing a person with ownership interests (such as shares) in that or another company. The phrase 'provided with a capital benefit' is defined in subsection 45B(5) of the ITAA 1936 and includes the provision of ownership interests (such as shares) in a company to a person. The distribution of Jacana ordinary shares to the shareholders of Syrah means that Syrah shareholders were provided with a demerger benefit and provided with a capital benefit.

¹ Taxation Ruling TR 2003/8 *Income tax: distributions of property by companies to shareholders - amount to be included as an assessable dividend.*

65. The Commissioner considers that at least some Syrah shareholders obtained a tax benefit (within the meaning given by subsection 45B(9) of the ITAA 1936) under the scheme.

66. For the purposes of paragraph 45B(2)(c) of the ITAA 1936, the Commissioner is required to consider the relevant circumstances (as outlined in subsection 45B(8) of the ITAA 1936) of the scheme to determine whether it could be concluded that entities that entered into or carried out the scheme or any part of the scheme did so for a purpose (other than an incidental purpose) of enabling the relevant taxpayer (Syrah shareholders) to obtain a tax benefit. Having regard to the relevant circumstances as outlined in subsection 45B(8) of the ITAA 1936, the Commissioner has formed the view that such a purpose did not exist.

67. Accordingly, section 45B of the ITAA 1936 does not apply to the scheme, and the Commissioner will not make a determination:

- under paragraph 45B(3)(a) of the ITAA 1936 that section 45BA of the ITAA 1936 applies to the whole, or any part, of the demerger benefit provided to Syrah shareholders under the demerger of Jacana ordinary shares
- under paragraph 45B(3)(b) of the ITAA 1936 that section 45C of the ITAA 1936 applies to the whole, or any part, of the capital benefit provided to Syrah shareholders under the demerger of Jacana ordinary shares.

CGT consequences – the demerger of Jacana ordinary shares

68. The demerger roll-over provisions in Division 125 contain a number of conditions for eligibility to choose the roll-over. The main conditions that are relevant to the demerger of Jacana ordinary shares by Syrah are:

- (a) an entity owns a share in a company (the original interest)
- (b) the company is the head entity of a demerger group
- (c) a demerger happens to the demerger group
- (d) under the demerger, a CGT event happens to the original interest and the entity acquires a new interest in the demerged entity (which must be a company) only because they own the original interest, and acquires nothing else, and
- (e) the entity owning the original interest must acquire, under the demerger, the same proportion of new interests in the demerged entity as they owned in the head entity just before the demerger.

69. The conditions for choosing demerger roll-over under Division 125 were satisfied in respect of the demerger of Jacana ordinary shares. Accordingly, the demerger concessions in Division 125 are available to Australian resident Syrah shareholders in respect of the demerger of Jacana ordinary shares. A foreign resident Syrah shareholder cannot choose to obtain demerger roll-over under Division 125 because the Jacana ordinary shares they acquired under the demerger were not taxable Australian property just after they acquired them (subsection 125-55(2)).

Appendix 2 – Detailed contents list

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

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References

<i>Previous draft:</i>	- ITAA 1936 45B(9)
Not previously issued as a draft	- ITAA 1936 45BA
	- ITAA 1936 45C
<i>Related Rulings/Determinations:</i>	- ITAA 1997
TR 2003/8; TR 2006/10	- ITAA 1997 104-135
	- ITAA 1997 104-135(1)
	- ITAA 1997 104-135(3)
<i>Subject references:</i>	- ITAA 1997 104-165(3)
- acquisition dates	- ITAA 1997 115-30(1)
- capital benefit	- ITAA 1997 115-105
- capital gains	- ITAA 1997 115-110
- CGT events G1-G3 – shares	- ITAA 1997 115-115
- CGT taxable Australian property	- ITAA 1997 115-120
- cost base adjustments	- ITAA 1997 Div 125
- demerger	- ITAA 1997 125-55(2)
- demerger benefit	- ITAA 1997 125-60(1)
- demerger roll-over	- ITAA 1997 125-70
- dividend income	- ITAA 1997 125-80(1)
- return of capital on shares	- ITAA 1997 125-80(2)
	- ITAA 1997 125-80(3)
	- ITAA 1997 125-85(1)
<i>Legislative references:</i>	- ITAA 1997 125-85(2)
- ITAA 1936	- ITAA 1997 Div 197
- ITAA 1936 6(1)	- ITAA 1997 Div 230
- ITAA 1936 44(1)	- ITAA 1997 Div 855
- ITAA 1936 45B	- ITAA 1997 855-15
- ITAA 1936 45B(2)(a)	- ITAA 1997 855-25
- ITAA 1936 45B(2)(b)	- ITAA 1997 975-300
- ITAA 1936 45B(2)(c)	- ITAA 1997 975-300(3)
- ITAA 1936 45B(3)(a)	- ITAA 1997 977-50
- ITAA 1936 45B(3)(b)	- ITAA 1997 995-1(1)
- ITAA 1936 45B(4)	- TAA 1953
- ITAA 1936 45B(5)	- Corporations Act 2001 256C
- ITAA 1936 45B(8)	

ATO references

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