


CR 2016/69 - Income tax: scheme of arrangement - merger of Royal Automobile Club of Queensland Limited and QT Mutual Bank Limited

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Class Ruling

Income tax: scheme of arrangement – merger of Royal Automobile Club of Queensland Limited and QT Mutual Bank 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

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 Provisions

2. The relevant provisions considered in this Ruling are:

- section 104-10 of the *Income Tax Assessment Act 1997* (ITAA 1997)
- section 109-10 of the ITAA 1997
- section 110-25 of the ITAA 1997
- section 110-35 of the ITAA 1997
- section 110-55 of the ITAA 1997
- section 115-30 of the ITAA 1997
- section 116-20 of the ITAA 1997

- section 124-780 of the ITAA 1997
- section 124-785 of the ITAA 1997, and
- section 124-795 of the ITAA 1997.

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

Class of entities

3. The class of entities to which this Ruling applies consists of QT Mutual Bank Limited (QTMB) Members who, on the Implementation Date of the Scheme:

- exchange their QTMB share for a Legacy Share in Club Finance Holdings Limited
 - are a 'resident' of Australia as defined in subsection 6(1) of the *Income Tax Assessment Act 1936*
 - are not a 'temporary resident' of Australia as defined in section 995-1
 - acquired their QTMB share on or after 20 September 1985
 - hold their QTMB share on capital account for income tax purposes, and do not hold the share as a revenue asset nor trading stock, and
 - are not subject to the taxation of financial arrangements rules in Division 230 in relation to gains and losses on their QTMB share.
- (**Note:** Division 230 will generally not apply to individuals, unless they have made an election for it to apply.)

Qualifications

4. The Commissioner makes this Ruling based on the proposed scheme precisely identified in this Ruling.

5. The class of entities defined in this Ruling may rely on its contents provided the scheme actually carried out is carried out in accordance with the scheme described in paragraphs 8 to 32 of this Ruling.

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

- this Ruling has no binding effect on the Commissioner because the scheme entered into is not the scheme on which the Commissioner has ruled, and

- this Ruling may be withdrawn or modified.

Date of effect

7. This Ruling applies from 1 July 2016 to 30 June 2017. The Ruling continues to apply after 30 June 2017 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

8. The following description of the scheme is based on information provided by the applicant. The following documents, or relevant parts of them, form part of and are to be read with the description:

- application for a class ruling dated 13 July 2016 on behalf of QTMB
- Merger Implementation Agreement dated 31 March 2016
- Deed of Amendment and Reinstatement dated 2 June 2016
- Constitution of the Royal Automobile Club of Queensland Limited 20 November 2014
- By-laws of the Royal Automobile Club of Queensland Limited 10 December 2015
- QT Mutual Bank Limited Constitution 5 November 2014
- disclosure documents for a Merger between QT Mutual Bank Limited and the Royal Automobile Club of Queensland Limited dated 12 August 2016
- Notices of Meeting and Scheme Booklet
- constitution of Club Finance Holdings Limited, and
- Independent Expert's Report dated 3 August 2016.

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

Overview

9. The scheme that is the subject of the Ruling involves the acquisition of all of the QTMB shares by Club Finance Holdings Limited, a majority owned subsidiary of the RACQ Group.

Background of key entities

RACQ

10. RACQ is an Australian resident company limited by guarantee. RACQ operates as a mutual motoring club that, through its subsidiaries (the RACQ Group), provides the following services to its members in Australia:

- motor and road side assistance services
- insurance services, including home, vehicle, travel and compulsory third party insurance
- financial services, including car and personal loans, and
- home assistance services, including household repairs.

11. RACQ Membership is granted to those who purchase eligible products as defined in RACQ's By-Laws, which include *inter alia*:

- roadside assistance
- RACQ insurance, and
- RACQ home assistance.

Club Finance Holdings Limited

12. Club Finance Holdings Limited (Club Finance Holdings) is an Australian resident company and majority-owned subsidiary of RACQ Investments No 2 Pty Ltd (a company within the RACQ Group).

13. Club Finance Holdings has been established to be the non-operating holding company of QTMB in accordance with the Australian Prudential Regulation Authority's (APRA) guidelines. A third party outside the RACQ Group will, prior to the Implementation Date, hold all the A class non-voting redeemable preference shares in Club Finance Holdings.

QTMB

14. QTMB is an Australian resident company limited by shares and owned by its members. It operates as an authorised deposit taking institution (ADI) and provides the following services to its members:

- financial services, including deposit taking and the provision of loans, and

- insurance services, including home, vehicle and travel insurance.

15. A QTMB Member is issued with a QTMB share on the payment of the subscription price of \$10.

16. Under the QTMB Constitution, QTMB Members are entitled to the following:

- right to vote
- right to participate in the distribution of profits or assets on winding up, and
- redemption of their QTMB share upon giving notice or when they cease to hold a QTMB product.

Proposed Transaction: Merger of RACQ and QTMB

17. On 18 April 2016, QTMB announced a proposal to merge with RACQ.

18. The merger will occur by means of a members' scheme of arrangement under Part 5.1 of the *Corporations Act 2001*, as approved by order of a court for the purposes of paragraph 411(4)(b) of that Act.

Pre-merger steps

19. QTMB will obtain QTMB Member approval of a demutualisation proposal and demutualise in accordance with QTMB's Constitution to become a non-mutual public company.

20. Following approval of the demutualisation, QTMB will apply to the Supreme Court of Queensland for orders convening the Scheme Meeting at which QTMB Members will be asked to approve the members' scheme of arrangement.

21. Subject to the QTMB Members voting in favour of the resolutions approving the merger, including the amendment of the QTMB Constitution to facilitate the merger, QTMB will return to the Court to seek orders approving the scheme of arrangement.

The Merger of RACQ and QTMB

22. Once demutualised, and following court approval, the scheme of arrangement will be implemented.

23. Under the merger, all of the QTMB shares will be transferred from the QTMB Members to Club Finance Holdings.

24. In consideration for the transfer of the QTMB Shares, existing QTMB Members as at the Record Date (who do not have a registered address outside Australia at the Record Date) will each be issued one

redeemable preference share (Legacy Share) in Club Finance Holdings.

25. Each Legacy Share confers upon its holder the right to payment in cash of the Preserved Surplus Amount upon the earlier to occur of:

- a QTMB disposal
- the insolvency of Club Finance Holdings or QTMB
- the winding up of Club Finance Holdings or QTMB, and
- an RACQ demutualisation.

26. The Preserved Surplus Amount means the amount each Legacy Share equates to the total equity as recorded in the audited annual financial statements for QTMB as at 30 June 2016, divided by the number of shares on issue in QTMB as at the issue date.

27. The issue of the Legacy Shares will occur on the Implementation Date and will have the following terms:

- no entitlement to dividends
- a right to the distribution of a proportional share in the 30 June 2016 Preserved Surplus Amount on the happenings of certain events (as outlined at paragraph (25) above)
- Club Finance Holdings has the discretion to redeem the Legacy Shares for \$10 when either the member has not held any QTMB product in the past three months, or there has been a distribution of the Preserved Surplus Amount, and
- all Legacy Shares not otherwise redeemed will be mandatorily redeemed on or within three months after the seventh anniversary of the issue date.

28. QTMB Members with a registered address outside Australia at the Record Date (Overseas Holders) will not be issued a Legacy Share. They will instead each be entitled to a payment of \$10 as consideration for their QTMB share, together with the agreement to make the payment of the Preserved Surplus Amount on the occurrence of an event giving rise to that entitlement for those holders of Legacy Shares (as outlined at paragraph (26) above).

29. Other than the Legacy Share (or the \$10 payment to Overseas Holders), no additional consideration is paid to QTMB Members for the transfer of their QTMB shares to Club Finance Holdings.

Other matters

30. RACQ will amend its By-Laws prior to the Implementation Date to ensure that QTMB Members, who are not currently RACQ

members at the Record Date, will be entitled to become RACQ members following the merger.

31. Following the merger, RACQ membership will be granted to new QTMB customers (who are not already RACQ members) that hold or purchase a merged eligible product.

32. Club Finance Holdings will not make a choice under subsection 124-795(4) preventing QTMB Members from making a choice to obtain scrip for scrip roll-over.

Ruling

33. CGT event A1 will happen as a result of the disposal by a QTMB Member of their QTMB share to Club Finance Holdings (subsection 104-10(1)).

34. The time of the event is when the QTMB share is transferred to Club Finance Holdings on the Implementation Date (paragraph 104-10(3)(b)).

Capital gain or loss

35. A QTMB member will make a capital gain from CGT event A1 happening if the capital proceeds from the disposal of their QTMB share exceed its cost base. A QTMB Member will make a capital loss if those capital proceeds are less than the share's reduced cost base (subsection 104-10(4)).

36. The only capital proceeds received by a QTMB Member is a Legacy Share in Club Finance Holdings. The capital proceeds from the disposal of a QTMB share is equal to the market value of the Legacy Share worked out at the time CGT event A1 happened (subsection 116-20(1)).

37. The cost base (or reduced cost base) of a QTMB share is comprised of the \$10 paid to acquire the share, plus any incidental costs incurred by the member to acquire the share or in relation to the disposal (subsections 110-25(2) and 110-25(3), section 110-35 and subsection 110-55(2)).

Availability of scrip for scrip roll-over

38. Subject to the qualification in paragraph 39 of this Ruling, a QTMB Member who makes a capital gain from the disposal of their QTMB share may choose scrip for scrip roll-over under Subdivision 124-M (section 124-780).

39. Scrip for scrip roll-over cannot be chosen if any capital gain the QTMB Member might make from the disposal of their QTMB share would be disregarded, except because of a roll-over (paragraph 124-795(2)(a)).

CGT consequences if roll-over chosen

40. If a QTMB Member chooses scrip for scrip roll-over, any capital gain made from the disposal of a QTMB share is disregarded (subsection 124-785(1)).

41. As the shares are exchanged on a one for one basis, the first element of cost base and reduced cost base of the Legacy Share is an amount equal to the cost base of the QTMB share (subsections 124-785(2) and 124-785(4)).

CGT consequences if roll-over is not chosen

42. A QTMB Member who does not, or cannot, choose scrip for scrip roll-over must take into account any capital gain or capital loss made from the disposal of their QTMB share in calculating their net capital gain for the income year.

43. For these members, the first element of the cost base and reduced cost base of the Legacy Share is equal to the market value of the QTMB share worked out at the time of the exchange (subsections 110-25(2) and 110-55(2)).

Acquisition date of Legacy Shares

44. A Legacy Share is acquired by the QTMB Member on the date the shares are issued by Club Finance Holdings (item 2 of the table in section 109-10).

45. However, for the purposes of determining eligibility to a discount capital gain, QTMB Members who choose scrip for scrip roll-over will be taken to have acquired their Legacy Share when they acquired their original QTMB share (item 2 of the table in subsection 115-30(1)).

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.*

46. The 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.

47. The significant tax consequence that is the subject of this Ruling is the availability of scrip for scrip roll-over under Subdivision 124-M. It enables the holder of a share in a company to disregard a capital gain from a share that is disposed of if the holder receives a replacement share in another company in exchange. It also provides special rules for calculating the cost base and reduced cost base of the replacement share.

Scrip for scrip roll-over

48. Subdivision 124-M contains a number of conditions for, and exceptions to, a shareholder being eligible to choose scrip for scrip roll-over. The main requirements that are relevant to the scheme that is the exchange of a QTMB share for a Legacy Share in Club Finance Holdings are:

- shares in a company are exchanged for shares in another company (replacement of shares))
- the exchange occurs in consequence of a single arrangement that satisfies subsection 124-780(2) or 124-780(2A) (conditions for arrangement)
- the conditions for roll-over in subsection 124-780(3) are satisfied (conditions for roll-over)
- further conditions (if applicable) are satisfied (further conditions), and
- exceptions to obtaining scrip for scrip roll-over in section 124-795 are not applicable (exceptions).

Replacement of shares

49. A QTMB Member will receive a Legacy Share in Club Finance Holdings in exchange for the disposal of their QTMB share in QTMB (the original entity) (paragraph 124-780(1)(a)).

Conditions for arrangement

50. Paragraph 124-780(1)(b) requires that shares in the original entity be exchanged as a consequence of a single arrangement, under either subsections 124-780(2) or 124-780(2A).

51. The exchange of QTMB shares for Legacy Shares is considered to be a consequence of a single arrangement for the purposes of paragraph 124-780(1)(b) and satisfies the conditions in subsection 124-780(2A):

- Club Finance Holdings, an entity that is not a member of a wholly-owned group, becomes the owner of more than 80% of the voting shares in QTMB.
- The Scheme will constitute a compromise or arrangement entered into by QTMB under Part 5.1 of the *Corporations Act 2001* and approved by order of a Court made for the purposes of paragraph 411(4)(b) of that Act.

Conditions for roll-over are satisfied

52. Paragraph 124-780(1)(c) requires the conditions for roll-over outlined in subsection 124-780(3) to be satisfied.

53. In this case, the conditions in subsection 124-780(3) are satisfied as:

- a QTMB Member acquired their QTMB share on or after 20 September 1985
- where the market value of a Legacy Share exceeds the cost base of a QTMB Share, that QTMB Member would make a capital gain on the disposal of their share. The exact amount of any capital gain would depend on the individual circumstances of each QTMB Member
- the Legacy Share is issued in Club Finance Holdings, being the company that acquires the QTMB shares and that is not a member of a wholly-owned group
- the QTMB Member chooses to obtain the roll-over under Subdivision 124-M, and
- Section 124-782 has no application to the Scheme as there are no significant stakeholders or common stakeholders under the arrangement for the purposes of section 124-783.

Further conditions are not applicable

54. Subsection 124-780(4) provides that the additional requirements in subsection 124-780(5) must be satisfied if the original interest holder and the acquiring entity did not deal with each other at arm's length and:

- (a) neither the original entity nor the replacement entity had at least 300 members just before the arrangement started, or

- (b) the original interest holder, the original entity and an acquiring entity were all members of the same linked group just before that time.

55. Subsection 124-780(4) does not apply because the QTMB Members and Club Finance Holdings are dealing with each other at arm's length.

Exceptions to obtaining scrip for scrip roll-over are not applicable

56. Section 124-795 contains a number of exceptions where scrip for scrip roll-over cannot be chosen.

57. Scrip for scrip roll-over under Subdivision 124-M cannot be chosen if:

- just before the exchange of shares, the holder of the share is a foreign resident, unless the replacement interest is taxable Australian property just after it is acquired
- the holder of the share and the acquiring entity are members of the same wholly-owned group and the acquiring entity is a foreign resident
- roll-over can be chosen under Division 122 (which deals with the disposal of assets to a wholly-owned company) or Division 615 (which deals with roll-overs for business restructure) for the CGT event happening in relation to the exchange of the original shares, and
- the replacement entity made a choice to the effect that the holder could not obtain Subdivision 124-M scrip for scrip roll-over in relation to the exchange.

58. The circumstances of the QTMB share exchange are such that none of the exceptions listed in the paragraph above apply (the exception in paragraph 124-795(2)(a) is discussed in paragraph 40 of this Ruling).

Appendix 2 – Detailed contents list

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

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References

Previous draft:

Not previously issued as a draft

Related Rulings/Determinations:

TR 2006/10

Legislative references:

- ITAA 1936
- ITAA 1936 6(1)
- ITAA 1997
- ITAA 1997 104-10
- ITAA 1997 104-10(1)
- ITAA 1997 104-10(3)(b)
- ITAA 1997 104-10 (4)
- ITAA 1997 109-10
- ITAA 1997 110-25
- ITAA 1997 110-25(2)
- ITAA 1997 110-25(3)
- ITAA 1997 110-35
- ITAA 1997 110-55
- ITAA 1997 110-55(2)
- ITAA 1997 115-30
- ITAA 1997 115-30(1)
- ITAA 1997 116-20
- ITAA 1997 116-20(1)
- ITAA 1997 Div 122
- ITAA 1997 Subdiv 124-M
- ITAA 1997 124-780
- ITAA 1997 124-780(1)(a)
- ITAA 1997 124-780(1)(b)
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- ITAA 1997 124-780(3)
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- ITAA 1997 124-780(5)
- ITAA 1997 124-782
- ITAA 1997 124-783
- ITAA 1997 124-785
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- ITAA 1997 124-785(2)
- ITAA 1997 124-785(4)
- ITAA 1997 124-795
- ITAA 1997 124-795(2)(a)
- ITAA 1997 124-795(4)
- ITAA 1997 Div 230
- ITAA 1997 Div 615
- ITAA 1997 995-1
- TAA 1953
- Corporations Act 2001
- Corporations Act 2001 Part 5.1
- Corporations Act 2001 411(4)(b)

ATO references

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Income tax ~~ Capital gains tax ~~ Rollovers ~~ Scrip for scrip - Subdivision 124-M

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