


CR 2017/27 - Income tax: Restructure of PRP Investment Trust

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Class Ruling

Income tax: Restructure of PRP Investment Trust

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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.

Summary – 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 provisions

2. The relevant provisions dealt with in this Ruling are:
- section 104-10 of the *Income Tax Assessment Act 1997* (ITAA 1997)
 - section 104-25 of the ITAA 1997
 - section 104-155 of the ITAA 1997
 - section 115-30 of the ITAA 1997
 - section 115-45 of the ITAA 1997
 - section 124-10 of the ITAA 1997
 - Division 615 of the ITAA 1997
 - Division 725 of the ITAA 1997
 - Division 727 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 the Class A, Class B and Class E units (together the Class Units) in PRP Investment Trust (PRPIT) who:

- will participate in the exchange of their Class Units in PRPIT in return for ordinary shares in PRP Diagnostic Imaging Holdings Limited (PDIHL)
- are residents of Australia within the meaning of subsection 6(1) of the *Income Tax Assessment Act 1936* (ITAA 1936)
- acquired their Class Units in PRPIT on or after 20 September 1985
- hold their Class Units in PRPIT on capital account for tax purposes
- will hold their ordinary shares in PDIHL on capital account for tax purposes, and
- are not subject to the taxation of financial arrangements rules in Division 230 in relation to gains and losses on their Class Units in PRPIT.

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

In this Ruling, this class of entities is referred to as 'participating unitholders'.

Qualifications

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

5. The class of entities defined in this Ruling may rely on its contents provided the scheme actually carried out is carried out in accordance with the scheme described in paragraphs 8 to 23 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 on behalf of PRPIT. The following documents, or relevant parts of them, form part of and are to be read with the description:

- application for Class Ruling dated 7 November 2016
- the PRPIT Trust Deed entitled 'Sixth Deed of Amendment – PRP Investment Trust' dated 5 September 2016, and
- further correspondence and 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.

Background

9. PRPIT is a public trading trust which is taxed under Division 6C of Part III of the ITAA 1936.

10. PRPIT will make a choice, under sections 703-50 and 713-130, to form a tax consolidated group on 1 July 2016 with itself as the head company (PRPIT income tax consolidated group). Upon PRPIT making this choice, PRPIT is generally treated as a company and in turn its units treated as shares for the purposes of applying the ITAA 1997 and ITAA 1936.

11. PRPIT was established in March 2008 and operates multiple radiology practices in New South Wales, Australia.

12. PRP Diagnostic Imaging Pty Ltd is the current trustee of PRPIT (Trustee).

13. PRPIT is governed by the trust deed entitled 'Sixth Deed of Amendment – PRP Investment Trust' dated 5 September 2016 (Trust Deed).

14. PRPIT is owned and operated by radiologists who work in the business as well as by members of the management team.
15. The unitholders are the radiologists, the chief executive officer (CEO), senior management, and their related entities.
16. Immediately prior to that part of the reorganisation considered in this Ruling, PRPIT will have three classes of units on issue:
 - (a) Class A units: issued to the radiologists and/or entities related to them
 - (b) Class B units: issued to the CEO and/or entities related to the CEO, and
 - (c) Class E units: issued to senior management and/or entities related to them.
17. The rights attached to the Class A, Class B and Class E units are identical.
18. The Class Units have rights to capital distributions, income distributions and capital profits distributions and to vote.
19. None of the participating unitholders, currently or as a result of the reorganisation and for 12 months following the reorganisation, will individually, or in aggregate with associates, hold at least 10% of the Class Units in PRPIT or the shares in PDIHL.

The restructure

20. The arrangement that is the subject of this Ruling involves a simplification of the unitholdings in PRPIT in order to facilitate the interposition of a new holding company, PDIHL, between PRPIT and the participating unitholders for the purpose of corporatising the structure of the Trustee's business.
21. The restructure will broadly involve the following steps:
 - (a) The income distribution rights attached to the Class Units will be varied.

They will be varied through an amendment to the rights attaching to these units, and not through the cancellation or redemption of units in exchange for the new, varied Class Units.
 - (b) A new interposed company, PDIHL, which will be an Australian resident for tax purposes, will be incorporated with one ordinary share on issue to a nominee who is not a participating unitholder.
 - (c) The participating unitholders will exchange each of their Class Units in PRPIT for one ordinary share in PDIHL and nothing else.

To effect this exchange, each participating unitholder will enter into a unit transfer agreement with PDIHL. On

the same date, the Trustee will approve this transfer by issuing a written consent as required under the Trust Deed.

- (d) Simultaneously with the exchange, PDIHL will buy back the one ordinary share held by the nominee shareholder so that the participating unitholders will own all the ordinary shares in PDIHL.

Other matters

22. PDIHL will make a choice pursuant to subsection 615-30(2) for the PRPIT income tax consolidated group to continue its existence at and after the 'completion time'. The 'completion time' is defined in section 615-15 to mean the time at which each participating unitholder disposes of their Class Units in PRPIT pursuant to the terms of the reorganisation.

23. The choice made by PDIHL referred to in paragraph 22 will be made within 28 days after the completion time pursuant to paragraph 615-30(3)(b).

Ruling

Variation of Class Unit rights

CGT event C2

24. CGT event C2 will not happen to participating unitholders pursuant to subsection 104-25(1) when the income distribution rights attached to the Class Units are varied.

CGT event H2

25. CGT event H2 will happen to participating unitholders pursuant to subsection 104-155(1) when the income distribution rights attached to the Class Units are varied. However, no participating unitholder will make a capital gain as a result of the event happening as they will not receive capital proceeds.

Value shifting

26. Neither Division 725 nor Division 727 will apply as a result of the variation of the income distribution rights attached to the Class Units.

Exchange of Class Units for PDIHL shares

CGT event A1

27. CGT event A1 will happen pursuant to subsection 104-10(1) when the participating unitholders dispose of each of their Class Units in PRPIT in exchange for a PDIHL share.

Division 615 roll-over

28. A participating unitholder will be taken to have chosen to obtain roll-over under Division 615 in relation to the exchange of their Class Units for PDIHL shares on a one-for-one basis (subsection 615-5(2)).

29. A participating unitholder who obtains roll-over under Division 615 will disregard any capital gain or capital loss made from the disposal of their Class Units in PRPIT under the exchange (section 615-40 with subsection 124-10(2)).

30. The first element of the cost base or reduced cost base of each PDIHL share acquired by a participating unitholder under the exchange will be equal to the cost base of the corresponding Class Unit that was exchanged (section 615-40 with subsection 124-10(3)).

Acquisition date of shares in PDIHL

31. For the purpose of determining any discount capital gains under Division 115 on a future disposal of their PDIHL shares acquired under the scheme, a participating unitholder who obtains roll-over will be taken to have acquired those PDIHL shares on the same date they had acquired their corresponding Class Units (item 2 of the table in subsection 115-30(1)).

Application of section 115-45

32. Section 115-45 will not apply to a participating unitholder, who disposes of their PDIHL shares acquired under the scheme within 12 months of the reorganisation, provided that, at the time of the relevant CGT event, the participating unitholder, together with their associates, will not beneficially own at least 10% by value of the shares in PDIHL.

Appendix 1 – Explanation

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

Unit trust considerations

33. At the time of the implementation of the scheme that is the subject of this Ruling, PRPIT was a public trading trust which was taxed under Division 6C of Part III of the ITAA 1936. PRPIT has made a choice, under sections 703-50 and 713-130, to form an income tax consolidated group on 1 July 2016 with itself as the head company.

34. As a consequence of making this choice, PRPIT will generally be treated as a company for the purposes of applying the ITAA 1997 and ITAA 1936 and in effect the units and unitholders treated as shares and shareholders respectively.

Variation of Class Unit rights

CGT event C2

35. CGT event C2 happens if the ownership of an intangible CGT asset, such as a share, ends by that share being redeemed or cancelled (paragraph 104-25(1)(a)).

36. Shares are comprised of a bundle of rights, however, those rights are not separate pieces of property capable of being divided out and held separately. Accordingly, for CGT purposes, the rights attaching to shares do not constitute individual assets as defined in section 108-5, but rather combine to make up the ultimate asset, being the share (refer to Taxation Ruling TR 94/30).

37. The variation of the income distribution rights attached to the Class Units will not constitute a redemption or cancellation of the units for CGT purposes and therefore CGT event C2 under paragraph 104-25(1)(a) will not happen.

CGT event H2

38. CGT event H2 happens if an act, transaction or event occurs in relation to a CGT asset and the act, transaction or event does not result in an adjustment being made to the asset's cost base or reduced cost base (section 104-155). The variation of the income distribution rights attached to the Class Units is an act, transaction or event in relation to those units. Therefore, the variation will result in CGT event H2 happening in respect of them.

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

40. Capital proceeds are the money or other consideration received, or entitled to be received, because of the act, transaction or event (subsection 116-20(2)). Paragraph 29 of Taxation Ruling TR 95/3 provides that 'consideration' for these purposes can include the benefit of mutual promises flowing to parties even if those promises are not in themselves property.

41. Participating unitholders will not receive or be entitled to receive any capital proceeds in respect of the variation of the income distribution rights attached to the Class Units. Therefore, although CGT event H2 will happen in respect of the Class Units, the participating unitholders will not make a capital gain.

Value shifting

42. There can be income tax consequences where there is a direct value shift, as defined in section 725-145, or an indirect value shift, as defined in section 727-150. However, there are only consequences where threshold control tests are satisfied.

43. The direct value shifting rules in Division 725 do not apply unless there is any entity that controls the target entity for value shifting purposes at some time during the scheme period (paragraph 725-50(b) and section 725-55).

44. The indirect value shifting rules in Division 727 do not apply unless the entities between which the value is shifted (the losing entity and the gaining entity) satisfy an ultimate controller test and/or a common ownership nexus test (paragraph 727-100(c) and sections 727-105 and 727-110).

45. On the basis of the information provided, there is no entity individually, or combined with their associates, that will control PRPIT for value shifting purposes or that will satisfy the ultimate controller test and/or the common ownership nexus test as described above.

46. Accordingly, there will be no consequences under Division 725 or Division 727 for any direct value shift or indirect value shift that may occur as a result of the variation of the income distribution rights attached to the Class Units.

Exchange of Class Units for PDIHL shares

CGT event A1

47. CGT event A1 will happen as a result of the disposal by the participating unitholders of each of their Class Units in PRPIT for shares in PDIHL.

48. The time of CGT event A1 will be the date the unit transfer agreement is signed by the participating unitholder and the written instrument is issued by the Trustee (paragraph 104-10(3)(a)).

Division 615 roll-over

49. The participating unitholders will be taken, under subsection 615-5(2), to have chosen to obtain the roll-over because:

- (a) the exchange satisfies the necessary conditions in subsection 615-5(1) and Subdivision 615-B discussed below
- (b) immediately before the completion time PRPIT is the head company of the consolidated group, and
- (c) immediately after the completion time, PDIHL is the head company of the consolidated group.

50. Division 615 contains a number of conditions for eligibility to choose roll-over. The main conditions that are relevant to the participating unitholders exchanging their Class Units in PRPIT for shares in PDIHL on a one-for-one basis are:

- at least two entities must own all the shares or units in the 'original entity' (paragraph 615-5(1)(b))
- there must be a scheme for reorganising the original entity's affairs, and consideration for the disposal of the shares or units in the original entity must consist only of receiving shares in another company, called the 'interposed company', and nothing else (paragraph 615-5(1)(c))
- the interposed company must own all the shares or units in the original entity immediately after the completion time (section 615-15)
- immediately after the completion time, each exchanging member must own a whole number of shares in the interposed company (paragraph 615-20(1)(a))
- immediately after the completion time, each exchanging member must own a percentage of the shares in the interposed company that were issued to all the exchanging members of the original entity that is equal to the percentage of the shares or units in the original entity that the exchanging member owned (paragraph 615-20(1)(b))
- the market value ratio test in subsection 615-20(2) is met
- the shares issued in the interposed company must not be redeemable shares (subsection 615-25(1)), and

- the exchanging members must own all the shares in the interposed company until the completion time (subsection 615-25(2)), or entities other than those members must own no more than 5 shares in the interposed company and the market value of those shares is such that it is reasonable to treat the exchanging members as owning all the shares (subsection 615-25(3)).

51. Under the reorganisation, the participating unitholders will receive ordinary shares in PDIHL in exchange for all of their Class Units in PRPIT on a one-for-one basis and nothing else. Following the reorganisation, PDIHL will own all the units in PRPIT, and the participating unitholders will have the same percentage interest and value in PDIHL immediately after as they had in PRPIT immediately before. All shareholders will own a whole number of shares in PDIHL. All other relevant conditions under Division 615 will also be satisfied under the scheme.

52. Accordingly, the capital gains tax consequences of obtaining roll-over under Division 615 for the participating unitholders are set out in paragraphs 28 to 30 of this Ruling.

Application of section 115-45

53. A capital gain, arising from a CGT event happening in respect of participating unitholders, who dispose of their shares in PDIHL within 12 months of the proposed reorganisation, will not be considered a discount capital gain, if it falls within the scope of section 115-45.

54. Subsection 115-45(2) provides that a capital gain made from a CGT event happening to a share in a company is not a discount capital gain if the following conditions are satisfied:

- just before the CGT event the taxpayer and their associates beneficially owned at least 10% by value of the shares in the company (subsection 115-45(3))
- the total of the cost bases of CGT assets that the company owned at the time of the CGT event and had acquired less than 12 months before then is more than half of the total of the cost bases of all the CGT assets that the company owned at the time of the CGT event (subsection 115-45(4)), and
- the notional net capital gain of the company worked out under subsection 115-45(6) is more than half of the notional capital gain worked out under subsection 115-45(7) of the ITAA 1997 (subsection 115-45(5)).

55. As a result of the reorganisation, participating unitholders in PRPIT will become owners of shares in PDIHL in the same proportion as they owned their Class Units in PRPIT. Accordingly, none of the participating unitholders who become shareholders in PDIHL at the completion time, together with their associates, will beneficially own at least 10% by value of the shares in PDIHL.

56. It is further taken as a fact for the purposes of this Ruling that, for 12 months following the reorganisation, no participating unitholder who will become a shareholder in PDIHL at the completion time, together with their associates, will beneficially own at least 10% by value of the shares in PDIHL. On this basis, the requirements in subsection 115-45(3) will not be met and therefore section 115-45 will not apply to a capital gain that arises from a CGT event happening to a participating unitholder who disposes of their shares in PDIHL within 12 months of the proposed reorganisation.

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 95/3; TR 2006/10

Legislative references:

- TAA 1953
- ITAA 1936
- ITAA 1936 6(1)
- ITAA 1936 Pt III Div 6C
- ITAA 1997
- ITAA 1997 104-10
- ITAA 1997 104-10(1)
- ITAA 1997 104-10(3)(a)
- ITAA 1997 104-25
- ITAA 1997 104-25(1)
- ITAA 1997 104-25(1)(a)
- ITAA 1997 104-155
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- ITAA 1997 108-5
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- ITAA 1997 Div 115-30
- ITAA 1997 115-30(1)
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- ITAA 1997 Div 615
- ITAA 1997 615-5(1)
- ITAA 1997 615-5(1)(b)
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- ITAA 1997 615-15
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- ITAA 1997 615-20(1)(b)
- ITAA 1997 615-20(2)
- ITAA 1997 615-25(1)
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ATO references

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Income tax ~~ Capital gains tax ~~ Rollovers ~~ Business restructures – Division 615

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