


# ***CR 2017/29 - Income tax: Suncorp Group Limited: Suncorp Group Limited Capital Notes***

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## Class Ruling

### Income tax: Suncorp Group Limited: Suncorp Group Limited Capital Notes

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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

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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 considered in this Ruling are:

- subsection 6(1) of the *Income Tax Assessment Act 1936* (ITAA 1936)
- section 26BB of the 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 45C of the ITAA 1936
- section 70B of the ITAA 1936
- section 177EA of the ITAA 1936

- Division 1A of former Part IIIAA of the ITAA 1936
- former section 160APHJ of the ITAA 1936
- former section 160APHM of the ITAA 1936
- Division 67 of the *Income Tax Assessment Act 1997* (ITAA 1997)
- section 67-25 of the ITAA 1997
- section 104-10 of the ITAA 1997
- section 104-25 of the ITAA 1997
- section 109-10 of the ITAA 1997
- subsection 110-25(2) of the ITAA 1997
- subsection 110-55(2) of the ITAA 1997
- section 116-20 of the ITAA 1997
- Subdivision 130-C of the ITAA 1997
- section 130-60 of the ITAA 1997
- section 204-30 of the ITAA 1997
- Division 207 of the ITAA 1997
- Subdivision 207-D of the ITAA 1997
- section 207-20 of the ITAA 1997
- section 207-145 of the ITAA 1997
- section 974-75 of the ITAA 1997
- section 974-120 of the ITAA 1997
- subsection 995-1(1) of the ITAA 1997.

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

### **Class of entities**

3. The class of entities to which this Ruling applies are investors who are allotted perpetual, convertible, subordinated and unsecured notes issued by Suncorp Group Limited (SGL) called Suncorp Group Limited Capital Notes (Capital Notes) and who:

- are residents of Australia (within the meaning of that term in subsection 6(1) of the ITAA 1936)
- hold their Capital Notes on capital account, and
- are not subject to the Taxation of Financial Arrangements (TOFA) 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 previous 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 the Capital Notes who acquired their Capital Notes otherwise than by initial application under the Suncorp Group Limited Capital Notes Prospectus dated 27 March 2017 and subsequently replaced with the Suncorp Group Limited Capital Notes Prospectus dated 4 April 2017 (the Prospectus).

### **Qualifications**

6. This Ruling does not deal with:

- how the taxation law applies to SGL in relation to the issue of the Capital Notes
- how the taxation law applies to Holders who hold their Capital Notes as trading stock or revenue assets
- the tax implications of the Exchange of the Capital Notes by Redemption or Resale, or the Conversion of the Capital Notes on a Non-Viability Trigger Event
- how the taxation law applies to the Nominated Purchaser who acquires their Capital Notes under the Resale facility
- 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, and
- the tax implications for Holders for whom gains and losses from the Capital Notes are subject to the TOFA rules in Division 230.

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

8. The class of entities defined in this Ruling may rely on its contents provided the scheme actually carried out is carried out in accordance with the scheme described in paragraphs 11 to 64 of this Ruling.

9. 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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10. This Ruling applies from 1 July 2016 to 30 June 2024. The Ruling continues to apply after 30 June 2024 to all entities within the specified class who entered into the specified scheme during the term of the Ruling. However, this Ruling will not apply to taxpayers to the extent that it conflicts with the terms of a settlement of a dispute agreed to before the date of issue of this Ruling (see paragraphs 75 and 76 of Taxation Ruling TR 2006/10).

## Scheme

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

- application for Class Ruling from SGL dated 3 March 2017
- the Prospectus
- Capital Notes Terms (as included in Appendix A of the Prospectus) (the Terms)
- Suncorp Capital Notes Trust Deed dated 27 March 2017 (the Trust Deed), and
- additional information and correspondence provided by the applicant from 13 February 2017 to 11 April 2017.

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

12. In this Ruling, unless otherwise indicated, capitalised terms take on the same meaning as in the Prospectus.

### SGL

13. During the term of the scheme, SGL will be a resident of Australia under the income tax laws of Australia and of no other jurisdiction.

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

15. Suncorp Group delivers insurance, banking and wealth products and services across Australia and New Zealand. Suncorp Group operates an integrated, customer-centric 'One Suncorp' business model that enables its customers to access any of Suncorp Group's products, services or brands to deliver solutions that meet their needs.

16. Wholly-owned NOHCs have been established for each of the APRA regulated general insurance businesses, regulated life insurance and superannuation businesses, and the regulated banking businesses. SGL also holds capital in respect of centralised corporate service entities.

### **The offer of the Capital Notes**

17. In the Prospectus which was lodged with the Australian Securities and Investments Commission (ASIC) on 4 April 2017 pursuant to section 713(1) of the *Corporations Act 2001* (Cth) (Corporations Act), SGL announced its intention to undertake an offer of Capital Notes to raise \$300 million, with the ability to raise more or less (the Offer).

18. The Prospectus expires on the date which is 13 months after 27 March 2017 (Expiry Date) and no Capital Notes will be issued on the basis of the Prospectus after the Expiry Date.

19. The classes of Applicants who can apply for the Capital Notes as described in the Prospectus, are:

- Securityholder Applicant – a person who is:
  - a registered holder of Ordinary Shares, SML Floating Rate Notes (floating rate capital notes issued by SML in 1998 under a prospectus dated 26 October 1998), CPS2 (convertible preference share issued by SGL in 2012 under a replacement prospectus dated 3 October 2012), CPS3 (convertible preference share issued by SGL in 2014 under a replacement prospectus dated 31 March 2014) or SGL Subordinated Notes (subordinated notes issued by SGL in 2013 under a replacement prospectus dated 18 April 2013) (as applicable) at 7:00pm (Sydney time) on 23 March 2017
  - shown on the Register with an address in Australia, and
  - not in the United States, or acting for the account or benefit of a person in the United States.

- 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 the Capital Notes 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 the Capital Notes in the Bookbuild, provided that such investor was not in the United States or acting for the account or benefit of a person in the United States.

20. The Prospectus states that no action has been taken to register or qualify the Capital Notes or the Offer or to otherwise permit a public offering of the Capital Notes outside Australia. It further states that subject to SGL's approval, the Capital Notes 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.

21. The Capital Notes were issued on 5 May 2017 (Issue Date).

22. SGL has applied for the Capital Notes to be quoted on the ASX and the Capital Notes will trade under ASX code 'SUNPF'.

## **Reasons for issuing the Capital Notes**

23. The Capital Notes are being issued as part of SGL's ongoing funding and capital management strategy, the proceeds of which it expects to use to fund the capital needs of one or more Regulated Entities within the Suncorp Group.

24. SGL will invest all or some of the proceeds of the issue in notes to be issued by one or more Regulated Entities within Suncorp Group.

25. The Offer is part of SGL's continuing capital management strategy and is designed to meet APRA's requirements for instruments to qualify as Eligible Additional Tier 1 capital.

26. It is expected that APRA will permit internal instruments funded by the issue of the Capital Notes to qualify as the relevant subsidiary entities' Additional Tier 1 capital for the purposes of applicable APRA prudential standards.

## **Terms of the Capital Notes**

27. The Capital Notes are perpetual, convertible, subordinated and unsecured notes issued by SGL.

28. The issue price of each Capital Note is \$100 (Issue Price) and on issue is fully paid.

29. The Capital Notes will not have voting rights, except in the limited circumstances described in the Terms and Trust Deed.

***Distribution calculation***

30. Subject to the Distribution Payment Conditions outlined in paragraphs 33 to 36 below, the Holder of each Capital Note will be entitled to receive on the relevant Distribution Payment Date a distribution (Distribution) calculated using the following formula:

$$\text{Distribution} = (\text{Distribution Rate} \times \text{A\$100} \times \text{N}) / 365$$

where:

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

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

where:

**Bank Bill Rate** (expressed as a percentage per annum) means, for a Distribution Period, the rate for prime bank eligible securities having a tenor of 3 months, which is designated as the 'AVG MID' on the Reuters Screen BBSW Page (or any page which replaces that page) at approximately 10:15am, Sydney time (or such other time at which such rate customarily appears on that page) on the relevant day (Publication Time), on the first Business Day of the Distribution Period. However, if such rate does not appear on the Reuters Screen BBSW Page (or any page which replaces that page) by 10:30am, Sydney time, on that day (or such other time that is 15 minutes after the then prevailing Publication Time), or if it does appear but SGL determines that there is an obvious error in that rate, 'Bank Bill Rate' means the rate determined by SGL having regard to comparable indices then available;

**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 Distribution Payment Date; and

**N** means in respect of:

- (a) the first Distribution Payment Date, the number of days from (and including) the Issue Date until (but

not including) the first Distribution Payment Date;  
and

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

31. If a Distribution is not franked to 100%, the Distribution will be calculated according to the following formula:

$$\text{Distribution} = D / (1 - [T \times (1 - F)])$$

where:

**D** means the Distribution calculated under clause 3.1 of the Terms;

**T** has the meaning given under clause 3.1 of the Terms, and

**F** means the applicable Franking Rate.

32. The Distribution Payment Dates are each 17 March, 17 June, 17 September and 17 December, commencing on 18 September 2017 until (but not including) the date on which the Capital Notes are Converted or Redeemed in accordance with the Terms. A Distribution will also be paid on the date on which an Exchange of that Capital Note (other than a Conversion on a Trigger Event Date) occurs in accordance with clause 3.5 of the Terms.

### ***Distribution payment conditions***

33. Pursuant to clause 3.3 of the Terms, payment of a Distribution is subject to:

- SGL's absolute discretion
- paying the Distribution on the Distribution Payment Date not resulting in the Eligible Capital of SGL not complying with APRA's then current prudential capital requirements as they are applied to the Suncorp Group at the time (unless APRA nevertheless approves paying the Distribution in writing)
- paying the Distribution on the Distribution Payment Date 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 Distribution being paid on the Distribution Payment Date.

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

35. Distributions are non-cumulative, as stated in clause 3.4 of the Terms. If all or any part of a Distribution 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.

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

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

37. If a Distribution is not paid in full on a Distribution Payment Date (the Relevant Distribution Payment Date), SGL must not, without the approval of a Special Resolution, until and including the next Distribution Payment Date, declare, determine to pay or pay a dividend on Ordinary Shares, or undertake any Buy-Back or Capital Reduction with respect to any Ordinary Shares, unless the Distribution is paid in full within three Business Days of the Relevant Distribution Payment Date.

38. The restrictions do not apply in certain limited circumstances as described in clause 3.8 of the Terms.

### ***Mandatory Conversion***

39. Pursuant to clause 4.1 of the Terms, subject to the occurrence of a Non-Viability Trigger Event, Optional Exchange or an Acquisition Event, SGL must Convert all (but not some) Capital Notes on issue on the Mandatory Conversion Date into Ordinary Shares in accordance with clauses 4 and 8 of the Terms.

40. 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 4.3 of the Terms are satisfied:

- (a) 17 June 2024 (Scheduled Mandatory Conversion Date), and
- (b) a Distribution Payment Date after the Scheduled Mandatory Conversion Date.

41. The Mandatory Conversion Conditions to be satisfied (as set out in clause 4.3 of the Terms) are:

- (a) the VWAP of Ordinary Shares on the First Test Date being greater than 55.00% of the Issue Date VWAP (First Mandatory Conversion Condition)
- (b) the VWAP during the period of 20 Business Days on which trading in Ordinary Shares took place immediately preceding (but not including) the Relevant Date is greater than 50.51% of 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***

42. Conversion of the Capital Notes may occur at a time before a Scheduled Mandatory Conversion Date on the occurrence of a Non-Viability Trigger Event.

43. SGL must Convert the Capital Notes on the Trigger Event Date, in accordance with clauses 5 and 8 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 or any other conditions being satisfied.

44. A Non-Viability Trigger Event is defined in clause 5.1 of the Terms as an event where APRA provides a written determination to SGL that the conversion to Ordinary Shares or write-off of Relevant Securities (including the Capital Notes) in accordance with their terms or by operation of law is necessary, because:

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

45. If a Non-Viability Trigger Event occurs, SGL must Convert to Ordinary Shares or Write-Off all Relevant Securities or an amount of Relevant Securities that APRA is satisfied would be sufficient to ensure SGL does not become non-viable. Where a Non-Viability Trigger Event occurs because APRA determines that without a public sector injection of capital (or equivalent support) SGL would become non-viable, all Capital Notes must be Converted.

46. Clause 5.2(d) of the Terms requires SGL to give notice to Holders if a Non-Viability Trigger Event occurs. SGL must also determine, among other things, the number of Capital Notes that will Convert and the identity of the Holders whose Capital Notes will Convert. The Non-Viability Trigger Event Notice must state the Trigger Event Date, how many Capital Notes will Convert and the relevant amount of other Relevant Securities that will be Converted or Written-off.

***Write-Off***

47. If for any reason, including an Inability Event (which means that SGL is prevented due to an applicable law, court order, action of government authority or any other reason from Converting the Capital Notes) SGL cannot Convert the Capital Notes, and Conversion has not been effected within five Business Days after the relevant Trigger Event Date, then the Capital Notes will be Written-Off in accordance with clause 5.5 of the Terms.

48. In clause 5.5 of the Terms, 'Written-Off', in respect of the Capital Notes and a Trigger Event Date, is defined as:

- (a) the Capital Note will not be Converted in respect of a Trigger Event Date and will not be Converted, Redeemed or Resold under the Terms on any subsequent date, and
- (b) the relevant Holders' rights (including to payment of Distributions and Redemption Price) in relation to such Capital Note are immediately and irrevocably terminated and written off.

### ***Optional Exchange of the Capital Notes by SGL***

49. Under clause 6.1 of the Terms, SGL may, with APRA's prior written approval, elect to Exchange (Holders of the Capital Notes do not have a right to request Exchange):

- (a) all, or some, Capital Notes on an Exchange Date following the occurrence of a Tax Event or a Regulatory Event
- (b) all (but not some only) Capital Notes on an Exchange Date following the occurrence of a Potential Acquisition Event, or
- (c) all, or some, Capital Notes on the Optional Exchange Date being 17 June 2022.

50. If SGL elects to Exchange the Capital Notes, it must elect which of the following it intends to do, as specified by clause 6.3 of the Terms:

- Convert the Capital Notes into Ordinary Shares in accordance with clause 8 of the Terms
- Redeem the Capital Notes in accordance with clause 9 of the Terms, or
- Resell the Capital Notes in accordance with clause 10 of the Terms.

51. Subject to clauses 6.4 and 6.5 of the Terms, in the election under clause 6.3(a) of the Terms, SGL may specify which of Conversion, Redemption and Resale applies to a particular Capital Note, and:

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

### ***Conversion on an Acquisition Event***

52. Upon the occurrence of an Acquisition Event, SGL must, in accordance with clauses 7 and 8 of the Terms, Convert all (but not only some) of the Capital Notes on the Acquisition Conversion Date by notice to the Trustee and Holders. An Acquisition Event is defined in clause 22.2 of the Terms as:

- (a) a takeover bid being made to acquire all or some Ordinary Shares and the offer is, or becomes, unconditional and either (i) the bidder has a relevant interest (as defined in the Corporations Act) in more than 50% of the Ordinary Shares on issue or (ii) the Directors issue a statement that at least a majority of SGL's directors who are eligible to do so recommend acceptance of the offer; or
- (b) a court approves a scheme of arrangement which, when implemented, will result in a person other than SGL having a relevant interest (as defined in the Corporations Act) in more than 50% of the Ordinary Shares.

### **Conversion Mechanics**

53. 'Conversion' means the conversion of the Capital Notes into Ordinary Shares in accordance with and subject to clause 8 of the Terms.

54. If SGL Converts the Capital Notes, then under clause 8 of the Terms:

- (a) each Holder's rights (including to payment of the Redemption Price and Distributions other than the Distribution, if any, payable on a date on which Conversion is required to occur) in relation to each Capital Note that is being Converted will be immediately and irrevocably terminated in full for an amount equal to the Issue Price
- (b) SGL will apply the amount equal to the Issue Price by way of payment for the subscription for Ordinary Shares to be allotted and issued on Conversion, and
- (c) each Holder will be allotted and issued a number of Ordinary Shares for each Capital Note being Converted on the relevant date equal to the Conversion Number (but no greater than the Maximum Conversion Number), calculated as follows:

**Conversion Number** = Issue Price / (99% x VWAP)

where:

**VWAP** (expressed in dollars and cents) means the VWAP during the VWAP Period;

The Maximum Conversion Number is calculated as follows:

**Maximum Conversion Number** = Issue Price / (Issue Date VWAP x 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.

55. Subject to the operation of the limitation imposed by the Maximum Conversion Number, the total market value of the Ordinary Shares held by a Holder immediately after the Conversion of the Capital Notes will be approximately \$101 (based on the VWAP at the time of Conversion), which is slightly above the Issue Price of the Capital Notes (that is, \$100).

56. Pursuant to clause 8.9 of the Terms, the Ordinary Shares issued upon Conversion will rank equally with all other fully paid Ordinary Shares.

57. Should a Holder not wish to receive Ordinary Shares if SGL has elected or is required to Convert the Capital Notes (and has notified SGL of this fact), under clause 8.11 of the Terms, on the date for Conversion, the relevant Ordinary Shares will be issued to the Trustee and or other nominee appointed by SGL who will sell the Ordinary Shares and pay a cash amount equal to the Proceeds to the relevant Holder.

#### ***Redemption Mechanics***

58. SGL may elect to Redeem the Capital Notes in accordance with the Terms and subject to APRA's prior written approval.

59. The Capital Notes will be Redeemed by payment of an amount equal to the Issue Price (Redemption Price).

60. Where SGL has elected to Redeem the Capital Notes, on the Exchange Date the only right the Holders will have with respect to the Capital Notes 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 Capital Notes will no longer have effect (clause 9.3 of the Terms).

#### ***Resale Mechanics***

61. SGL may (subject to APRA's prior written approval) elect to Resell the Capital Notes by electing one or more Nominated Purchasers as set out in clause 10.11 of the Terms.

62. Under clause 10.4 of the Terms, if an election to Resell is made, each Holder is taken to irrevocably offer to sell the Capital Notes the subject of Resale to the Nominated Purchaser for a cash amount equal to each Capital Note's Issue Price (the Resale Price) on the Exchange Date. In accordance with clause 10.5 of the Terms, subject to payment by the Nominated Purchaser of the Resale Price to the Holders, all right, title and interest in such Capital Note (excluding the right to any Distribution payable on that date) will be transferred to the Nominated Purchaser free from Encumbrances.

## ***Ranking of the Capital Notes on Winding-Up***

63. Under clause 2.1 of the Terms, in a winding-up of SGL, the Capital Notes will rank as follows for the payment of the Redemption Price:

- (a) in priority to Ordinary Shares;
- (b) equally amongst themselves and with all Equal Ranking Instruments; and
- (c) behind the claims of Senior Ranking Creditors.

## **Other matters**

64. The Ruling is made on the basis that:

- (a) The Transaction Documents represent a complete and accurate description of the scheme, are intended by the parties to have their legal effect, and will be implemented according to their terms.
- (b) 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 Capital Notes.
- (c) The Capital Notes are 'equity interests' pursuant to Division 974.
- (d) The Ordinary Shares issued in the event of a Conversion of the Capital Notes will be 'equity interests' pursuant to Division 974.
- (e) Distributions on the Capital Notes will be non-share dividends under section 974-120 and will be frankable distributions pursuant to section 202-40.
- (f) The Distributions are expected to be fully franked; however, if any distribution is not franked or only partially franked, the Distribution will be grossed up to the extent that the franking percentage of the Distribution is less than 100% as calculated in accordance with clause 3.2 of the Terms.
- (g) SGL will not differentially frank distributions payable to different Holders of the Capital Notes, 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.
- (h) The extent to which a Holder receives franked Distributions will be determined solely by each Holder's proportionate ownership of the Capital Notes 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 Distribution.

- (i) The Distributions on the Capital Notes are expected to be franked in the same proportion as dividends paid on Ordinary Shares.
- (j) Any Capital Notes held by non-residents that acquired the Capital Notes under the Institutional Offer will be franked in the same manner as the Capital Notes held by residents.
- (k) The share capital account of SGL will not become tainted within the meaning of Subdivision 197-A by an issue of the Capital Notes or the allotment of Ordinary Shares on Conversion of the Capital Notes.
- (l) No Distributions paid in respect of the Capital Notes will be sourced, directly or indirectly, from SGL's share capital account or its non-share capital account.
- (m) Immediately before payment of a Distribution on the Capital Notes, SGL will have sufficient available profits (worked out under section 215-20) to pay the Distribution.
- (n) The Capital Notes are expected to be characterised as a liability for Australian International Financial Reporting Standard purposes.
- (o) 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, neither a Holder nor an associate of a Holder will take any positions (apart from the holding of the Capital Notes) in relation to their Capital Notes that would cause a Holder not to be a 'qualified person' and will not make, be under an obligation to make, or be likely to make a related payment (within the meaning of former section 160APHN of the ITAA 1936) in relation to the Distributions.
- (p) Holders in receipt of Distributions on the Capital Notes will have held their Capital Notes 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 Capital Notes and ending on the 90<sup>th</sup> day after the day on which the Capital Notes go ex-distribution.
- (q) It is reasonable to expect that the dividend payout ratios and the franking credits in relation to the ordinary share capital or preference share capital of SGL will not change as a result of the issue of the Capital Notes.
- (r) Distributions will not be funded directly or indirectly by SGL issuing new equity interests.

- (s) On Conversion, SGL will debit the Issue Price of Capital Notes to its non-share capital account.
- (t) On the date of Conversion of the Capital Notes into Ordinary Shares, the rights and obligations attached to the Ordinary Shares are the same as those contained in the Constitution of SGL.
- (u) Any internal notes issued by the Regulated Entities would not satisfy the debt test under section 974-20.

## Ruling

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### **Acquisition time of the Capital Notes**

65. Holders acquire their Capital Notes on 5 May 2017, being the date the contract for the issue of the Capital Notes is entered into (item 2 of the table in section 109-10).

### **Cost base and reduced cost base of the Capital Notes**

66. The first element of the cost base and reduced cost base of each Capital Note is \$100, being the money paid by the Holder to acquire the Capital Note from SGL (subsections 110-25(2) and 110-55(2)).

### **Inclusion of Distributions and franking credits in assessable income**

67. Distributions paid in respect of each Capital Note are non-share dividends under section 974-120 and must be included in the Holders' assessable income (subparagraph 44(1)(a)(ii) of the ITAA 1936).

68. Holders must also include in their assessable income an amount equal to the franking credits attached to the Distribution (subsection 207-20(1)).

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

69. Holders will be entitled to a tax offset equal to the franking credit received on Distributions paid in respect of the Capital Notes (subsection 207-20(2)), unless the Distribution is exempt income or non-assessable non-exempt income in the hands of the Holder and none of the exceptions in Subdivision 207-E apply.

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

70. If the Distribution (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 Distribution 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) unless any of the exceptions in Subdivision 207-E apply.

### **Franking credit subject to the refundable tax offset rules**

71. Holders who are entitled to a tax offset under subsection 207-20(2), in respect of the franking credits received in relation to the Capital Notes, will be subject to the refundable tax offset rules in Division 67, unless they are specifically excluded under section 67-25.

### **Imputation benefits – streaming**

72. 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 Distributions paid in respect of the Capital Notes.

### **Section 177EA of the ITAA 1936**

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

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

74. Section 207-145 will not apply to the whole, or any part, of the Distributions paid to 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.

75. For the purposes of determining whether a Holder is a 'qualified person' in relation to the Distributions under Division 1A of former Part IIIAA of the ITAA 1936 (which is relevant to paragraph 207-145(1)(a)), the Resale facility and the Conversion mechanism will not of themselves affect a Holder's risks of loss or opportunities for gain in respect of the Capital Notes. This is because neither the Resale facility nor the Conversion mechanism will constitute separate 'positions' for the purposes of Division 1A of former Part IIIAA of the ITAA 1936 (former sections 160APHJ and 160APHM of the ITAA 1936).

### **Each Capital Note is not a traditional security**

76. Section 26BB of the ITAA 1936 will not apply to include any amount in the assessable income of Holders upon disposal or Redemption of their Capital Notes.

77. Section 70B of the ITAA 1936 will not apply to allow a deduction to Holders upon disposal or Redemption of their Capital Notes.

### **Capital Notes are convertible interests**

78. Each Capital Note is a convertible interest under item 4 of the table in subsection 974-75(1).

### **Conversion of the Capital Notes – CGT implications**

79. CGT event C2 will happen for Holders on Conversion of the Capital Notes into Ordinary Shares (section 104-25).

80. Any capital gain or capital loss made by a Holder from CGT event C2 happening on Conversion of the Capital Notes will be disregarded (subsection 130-60(3)).

### **Cost base and reduced cost base of Ordinary Shares acquired on Conversion**

81. On Conversion of the Capital Notes, Subdivision 130-C will apply so that the first element of the cost base and reduced cost base of each Ordinary Share acquired upon Conversion will be a pro-rata portion of the cost base and reduced cost base of the Capital Notes at the time of Conversion (item 2 of the table in subsection 130-60(1)).

### **Acquisition time of Ordinary Shares received on Conversion**

82. Ordinary Shares received by a Holder on Conversion are taken to be acquired when the Conversion happens on the relevant Exchange Date (subsection 130-60(2)).

### **Allotment of Ordinary Shares on Conversion not a dividend**

83. Other than in respect of a Distribution paid on the Exchange Date, a Holder will not be taken to have received a dividend within the meaning of subsection 6(1) of the ITAA 1936 nor a non-share dividend under section 974-120 as a result of Conversion of the Capital Notes.

### **Section 45 of the ITAA 1936**

84. Section 45 of the ITAA 1936 will not apply to treat an amount equal to the Ordinary Shares issued on Conversion as an unfrankable dividend paid by SGL.

**Section 45A of the ITAA 1936**

85. The Commissioner will not make a determination under subsection 45A(2) of the ITAA 1936 that section 45C of the ITAA 1936 applies to treat the whole, or part of, a capital benefit that arises on Conversion or Redemption of the Capital Notes as an unfranked dividend in the hands of Holders.

**Section 45B of the ITAA 1936**

86. 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 treat the whole, or part of, a capital benefit that arises on Conversion or Redemption of the Capital Notes as an unfranked dividend in the hands of Holders.

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**Commissioner of Taxation**10 May 2017

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## Appendix 1 – Explanation

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

### **Acquisition time of the Capital Notes**

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

88. The Capital Notes are equity interests in SGL. When an investor's application for the Capital Notes is accepted by SGL, this leads to the formation of a contract for the issue of the Capital Notes to the investor (who will become a Holder). The contract is not formed prior to the Issue Date as SGL has the right not to proceed with, or withdraw, the Offer at any time before the Capital Notes are issued. Therefore, for the purposes of item 2 in the table contained in section 109-10, a Holder will acquire their Capital Notes on 5 May 2017.

### **Cost base and reduced cost base of the Capital Notes**

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

90. The Issue Price of each Capital Note is \$100. Accordingly, the first element of the cost base and reduced cost base of each Capital Note is \$100.

### **Inclusion of Distributions and franking credits in assessable income**

91. Subsection 44(1) of the ITAA 1936 provides that the assessable income of a resident shareholder in a company includes all dividends and non-share dividends paid to the shareholder by the company.

92. The Capital Notes are 'non-share equity interests' as defined in subsection 995-1(1) and the Holders are 'equity holders' as defined in subsection 995-1(1). Paragraph 43B(1)(b) of the ITAA 1936 provides that Subdivision D of Division 2 of Part III of the ITAA 1936 (which governs dividends) applies to an equity holder in the same way as it applies to a shareholder.

93. Distributions paid in respect of the Capital Notes are frankable non-share dividends in accordance with sections 202-30 and 974-120. Accordingly, Holders must include Distributions paid in respect of the Capital Notes in their assessable income under subparagraph 44(1)(a)(ii) of the ITAA 1936.

94. Under the Australian imputation system, where an Australian resident company makes a franked distribution directly to a shareholder, the assessable income of the shareholder must also include the amount of the franking credit on the distribution pursuant to subsection 207-20(1). The inclusion of both the dividend and the attached franking credit in a shareholder's assessable income is known as 'grossing-up' the dividend.

95. Distributions on the Capital Notes are expected to be fully franked. Holders must include in their assessable income the amount of any franking credit attached to a Distribution in the income year in which the Distribution is made.

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

96. Holders are entitled to receive a tax offset equal to the franking credit which has been included in their assessable income in respect of Distributions they receive (subsection 207-20(2)).

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

97. If the Distribution is exempt income or non-assessable non-exempt income in the hands of the Holder and none of the exceptions in Subdivision 207-E apply, then:

- the amount of any franking credit on the Distribution 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).

#### **Franking credit subject to the refundable tax offset rules**

98. Holders who are entitled to a tax offset under subsection 207-20(2), in respect of a franking credit received on a Distribution, will also be subject to the refundable tax offset rules in Division 67, unless they are specifically excluded under section 67-25.

99. The refundable tax offset rules ensure that certain taxpayers are entitled to a refund once their available tax offsets have been utilised to reduce any income tax liability to nil.

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

## **Imputation benefits – streaming**

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

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

- (a) an 'imputation benefit' is, or apart from section 204-30 would be, received by a member of the entity as a result of the distribution or distributions (paragraph 204-30(1)(a))
- (b) the member (favoured member) would derive a greater benefit from franking credits than another member of the entity (paragraph 204-30(1)(b)), and
- (c) the other member (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)).

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

104. The Capital Notes will be listed on the ASX and hence will be available for investment by different types of investors. The extent to which a Holder receives franked Distributions will be determined solely by each Holder's proportionate ownership of the Capital Notes 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 Distribution. The dividend payout ratios and the franking credits arising in relation to the ordinary share capital or preference share capital of SGL is not expected to be affected by the issue of the Capital Notes and Distributions on the Capital Notes are expected to be franked in the same proportion as dividends paid on Ordinary Shares.

105. Based on the information provided, the Commissioner has concluded that the requisite element of streaming does not exist in relation to the franked Distributions to be paid by SGL to Holders. Accordingly, 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 Distributions paid in respect of the Capital Notes.

**Section 177EA of the ITAA 1936**

106. Section 177EA of the ITAA 1936 is a general anti-avoidance provision that applies to a wide range of schemes designed to obtain imputation benefits. In essence, it applies to schemes for the disposition of membership interests or an interest in membership interests, where a franked distribution is paid or payable in respect of the membership interests or an interest in membership interests.

107. Where section 177EA of the ITAA 1936 applies, the Commissioner has a discretion pursuant to subsection 177EA(5) of the ITAA 1936 to make a determination to either debit the company's franking account or deny the imputation benefit on the distribution that flowed directly or indirectly to each shareholder.

108. The Commissioner can make a determination if the following conditions in subsection 177EA(3) of the ITAA 1936 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.

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

- the issue of the Capital Notes constitutes a scheme for the disposition of membership interests in a corporate tax entity. Paragraph 177EA(12)(a) of the ITAA 1936 applies to treat non-share equity interests in the same way as membership interests for the purposes of section 177EA of the ITAA 1936

- Distributions are frankable distributions and are expected to be payable to Holders in respect of their Capital Notes
- Distributions are expected to be franked distributions, and
- the Holders could reasonably be expected to receive an imputation benefit as a result of the Distributions, as SGL intends to fully frank the Distributions on the Capital Notes.

110. 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.

111. In arriving at a conclusion, the Commissioner must have regard to the relevant circumstances of the scheme which include, but are not limited to, the factors listed in subsection 177EA(17) of the ITAA 1936.

112. 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 relation to a particular scheme.

113. Based on the information provided and the qualifications set out in this Ruling, and having regard to all of the relevant circumstances of the scheme, the Commissioner has concluded that the purpose of enabling the Holders to obtain imputation benefits is no more than incidental to SGL's purpose of raising capital for the Suncorp Group to meet its capital adequacy / prudential requirements.

114. Accordingly, the Commissioner will not make a determination under paragraph 177EA(5)(b) of the ITAA 1936 to deny the whole, or any part, of the imputation benefits received by Holders in relation to Distributions paid in respect of the Capital Notes.

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

115. 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.

116. Pursuant to subsection 207-145(1), this adjustment will occur where a franked distribution is made to an entity in one or more of the following circumstances:

- the entity is not a 'qualified person' in relation to the distribution for the purposes of Division 1A of former Part IIIAA of the ITAA 1936 (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 respect of the distribution for the entity (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 respect of the distribution for the entity (paragraph 207-145(1)(c)), or
- the distribution is made as part of a dividend stripping operation (paragraph 207-145(1)(d)).

117. Generally, a person is a 'qualified person' for the purposes of Division 1A of former Part IIIAA of the ITAA 1936 if they satisfy the holding period rule in former paragraph 160APHO(1)(a) of the ITAA 1936 or the related payments rule in former paragraph 160APHO(1)(b) of the ITAA 1936).

118. By virtue of former section 160AOA of the ITAA 1936, the holding period rule and the related payments rule apply to non-share equity interests, equity holders and non-share dividends in the same way as they apply to shares, shareholders and dividends respectively.

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

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

121. As this Ruling is made on the basis that neither a Holder, nor associates of the Holder, will make, is under an obligation to make, or is likely to make, a related payment in relation to the Distributions within the meaning of former section 160APHN of the ITAA 1936 (see paragraph 64(o) above), a Holder will be a 'qualified person' in relation to Distributions received in respect of their Capital Notes, provided the Holder continuously held their Capital Notes 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) throughout the primary qualification period. The primary qualification period begins on the day after the day on which the Holder acquired their Capital Notes and ends on the 90th day after the day on which the Capital Notes became ex-dividend (former subsections 160APHO(2) and 160APHO(3) of the ITAA 1936 and former sections 160APHM and 160APHJ of the ITAA 1936).

122. In determining whether a shareholder is a 'qualified person' in relation to a distribution paid on their shares, every 'position' (defined in former subsection 160APHJ(2) of the ITAA 1936) in relation to the shares is taken into account in calculating the 'net position' (defined in former subsection 160APHJ(5) of the ITAA 1936) in relation to the shares. The 'net position' determines whether a shareholder has materially diminished risks of loss or opportunities for gain on a particular day in respect of shares held by the shareholder (former section 160APHM of the ITAA 1936). Under former subsection 160APHJ(2) of the ITAA 1936, a 'position' in relation to shares is anything that has a delta in relation to the shares.

123. 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 TD 2007/29 *Income tax: holding period rule: is an embedded share option a position in relation to the share if it is exercisable by or against a party other than the issuer of the share?*).

124. Under the Terms, SGL may (subject to certain conditions) elect to require the Holders to sell all or some of their Capital Notes to one or more Nominated Purchasers. Until SGL appoints an entity as a Nominated Purchaser, that entity has no right or ability to call for the Capital Notes from the Holders. Holders have no right to elect Resale of the Capital Notes.

125. SGL is not required to elect to Resell the Capital Notes. It follows that the Resale facility is an option that is held by SGL, the issuer of the Capital Notes, and not by a third party. Therefore, the Resale facility does not constitute a separate 'position' in relation to the Capital Notes under former subsection 160APHJ(2) of the ITAA 1936.

126. Similarly, although the Conversion mechanism results in the exchange of Capital Notes for Ordinary Shares, the Conversion mechanism does not constitute a separate 'position' for the purposes of former Division 1A of Part IIIA of the ITAA 1936 as the Holders have no right to elect Conversion.

127. Therefore, for the purposes of determining whether a Holder is a 'qualified person' in relation to the Distributions under Division 1A of former Part IIIA of the ITAA 1936, neither the Resale facility nor the Conversion mechanism, of themselves, affect a Holder's risks of loss or opportunities for gain in respect of the Capital Notes.

128. 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 benefit that arises in

respect of a Distribution that is made (see paragraphs 106 to 114 above).

129. Finally, a distribution will be taken to be made as part of a dividend stripping operation, pursuant to section 207-145, where the distribution arose out of, or was made in the course of, a scheme or substantially similar arrangement that was in the nature of dividend stripping.

130. Section 207-155 defines a dividend stripping operation as a scheme by way of or in the nature of dividend stripping, or that has substantially the effect of a scheme by way of or in the nature of dividend stripping.

131. The term dividend stripping has no precise legal meaning. Paragraph 9 of Income Tax Ruling IT 2627 states that dividend stripping would include a situation where a vehicle entity (the stripper) purchases shares in a target company that has accumulated or current year profits that are represented by cash or other readily-realizable assets. The stripper pays the vendor shareholders a capital sum that reflects those profits and then draws off the profits by having paid to it a dividend (or a liquidation distribution) from the target company.

132. Paragraph 10 of IT 2627 further states that an important element to be looked at will be any release of profits of a company to its shareholders in a non-taxable form, regardless of the different methods that might be used to achieve this result.

133. The Prospectus and Terms provide no indication that the offering of the Capital Notes and the associated payment of franked Distributions to Holders in any way constitutes a dividend stripping arrangement. As such, the dividend stripping provisions do not apply.

134. Accordingly, section 207-145 will not apply to adjust the Holders' assessable income to exclude the franking credit, nor will it deny the tax offset to which the Holders would otherwise be entitled.

### **Capital Notes not traditional securities**

135. A 'traditional security' is defined in subsection 26BB(1) of the ITAA 1936 as a security held by the taxpayer that was acquired by the taxpayer after 10 May 1989, is not a prescribed security within the meaning of section 26C of the ITAA 1936, is not trading stock of the taxpayer, and either does not have an eligible return, or has an eligible return that satisfies the conditions listed in subparagraph (b)(ii) of the definition of traditional security in subsection 26BB(1) of the ITAA 1936.

136. The term 'security' is defined in subsection 26BB(1) of the ITAA 1936 by reference to subsection 159GP(1) of the ITAA 1936. Pursuant to subsection 159GP(1), 'security' means:

- (a) stock, a bond, debenture, certificate of entitlement, bill of exchange, promissory note or other security

- (b) a deposit with a bank or other financial institution
- (c) a secured or unsecured loan, or
- (d) any other contract, whether or not in writing, under which a person is liable to pay an amount or amounts, whether or not the liability is secured.

137. The Capital Notes are not stock, a bond, debenture, certificate of entitlement, bill of exchange, or a promissory note.

138. The term 'or other security' in paragraph (a) of the definition of security in subsection 26BB(1) of the ITAA 1936 only encompasses instruments that evidence an obligation on the part of the issuer or drawer to pay an amount to the holder or acceptor, whether during the term of the instrument or at its maturity. The types of securities referred to in paragraph (a) of the definition will generally be recognised as debt instruments (Taxation Ruling TR 96/14 *Income tax: traditional securities*).

139. Paragraphs (b) and (c) of the definition of security in subsection 26BB(1) of the ITAA 1936 do not apply because the Capital Notes are neither a deposit with a bank or other financial institution, nor a secured or unsecured loan.

140. Only those contracts that have debt like obligations will usually fall under paragraph (d) of the definition of security in subsection 26BB(1) of the ITAA 1936 (TR 96/14).

141. The Terms do not evidence a liability by SGL to pay an amount or amounts to Holders of the Capital Notes during the term of the instrument or at maturity. The Capital Notes are perpetual and Holders do not have a right to require Redemption. The payment by SGL of Distributions is subject to the Distribution Payment Conditions. Distributions are discretionary and non-cumulative and if a Distribution is not paid, SGL has no liability to pay the Distribution and Holders have no claim in respect of non-payment.

142. Upon Conversion, SGL will allot and issue a number of Ordinary Shares based on a formula set out in the Terms for each Capital Note held by the Holder. Each Holder's rights in relation to each Capital Note that is being converted are immediately and irrevocably terminated for an amount equal to the Issue Price and SGL will apply that amount by way of payment for the subscription for Ordinary Shares issued to Holders. SGL cannot be said to have a liability to pay an amount under the Terms of the Capital Notes pursuant to the Conversion.

143. Early Redemption of the Capital Notes is possible. However it is at the option of SGL and will only occur upon the happening of certain events, at SGL's option, and requires the prior written approval of APRA. This does not establish a liability on SGL to pay an amount.

144. SGL will not become liable to pay an amount under the Capital Notes upon a wind-up as it would be expected that, before a wind-up commences, the Capital Notes would either be converted

into Ordinary Shares pursuant to a Non-Viability Trigger Event (in which case any distribution would be made to the Holders as Ordinary Shareholders as opposed to under the terms of the Capital Notes), or Holders' rights would be terminated where SGL is not able to issue Ordinary Shares within the time stated in the Terms.

145. As the Capital Notes are not a security within the meaning of subsection 159GP(1) of the ITAA 1936, the Capital Notes are not traditional securities under subsection 26BB(1) of the ITAA 1936.

146. As the Capital Notes are not 'traditional securities' within the meaning of that term in subsection 26BB(1) of the ITAA 1936:

- subsection 26BB(2) of the ITAA 1936 will not apply to include the amount of any gain in the assessable income of the Holder upon disposal of their Capital Notes, and
- subsection 70B(2) of the ITAA 1936 will not apply to allow a deduction for any loss to Holders upon disposal of their Capital Notes.

### **Capital Notes are convertible interests**

147. Subsection 995-1(1) defines a 'convertible interest' in a company as an interest of the kind referred to in item 4 of the table in subsection 974-75(1). Paragraph (b) of item 4 of the table in subsection 974-75(1) provides that an interest is an equity interest if it is an interest issued by the company and the interest will, or may, convert into an equity interest in the company.

148. Under section 974-165, an interest is an interest that will or may convert into another interest if:

- the interest must be or may be converted into another interest (paragraph 974-165(a)), or
- the interest must be or may be redeemed, repaid or satisfied by the issue or transfer of the other interest (subparagraph 974-165(b)(i)).

149. Each Capital Note is a convertible interest because it will or may be redeemed, repaid or satisfied by the issue of Ordinary Shares upon Conversion.

### **Conversion of the Capital Notes – CGT implications**

150. Under paragraph 104-25(1)(f), CGT event C2 happens if an entity's ownership of an intangible CGT asset ends by the asset (if it is a convertible interest) being converted.

151. The Capital Notes are convertible interests. Conversion of the Capital Notes for Ordinary Shares constitutes the conversion of a convertible interest. Therefore, CGT event C2 will happen to Holders on Conversion of the Capital Notes.

152. Conversion of the Capital Notes happens as part of a conversion to which Subdivision 130-C applies. Under subsection 130-60(3), a capital gain or capital loss made from converting a convertible interest is disregarded.

153. Therefore, any capital gain or capital loss made by a Holder from CGT event C2 happening on Conversion of the Capital Notes is disregarded.

### **Cost base and reduced cost base of Ordinary Shares acquired on Conversion**

154. The first element of the cost base or reduced cost base for shares acquired by converting a convertible interest that is not a traditional security is worked out under item 2 of the table in subsection 130-60(1). Item 2 states that the first element is the sum of:

- (a) the cost of the convertible interest at the time of conversion
- (b) any amount paid to convert the convertible interest, except to the extent that the amount is represented in the paragraph (a) amount, and
- (c) all the amounts that are to be added under subsection 130-60(1A) (concerning amounts to be added back under certain circumstances).

155. On Conversion, Subdivision 130-C will apply so that the first element of the cost base and reduced cost base of each Ordinary Share acquired from Conversion of a Capital Note will be a pro-rata portion of the cost base of the Capital Note at the time of Conversion (item 2 of the table in subsection 130-60(1)).

### **Acquisition time of Ordinary Shares acquired on Conversion**

156. Subsection 130-60(2) states that the shares are acquired when the conversion of the convertible interest happened.

157. Ordinary Shares acquired on Conversion of the Capital Notes (being convertible interests) will be taken to be acquired when the Conversion happens on the relevant Exchange Date (subsection 130-60(2)).

### **Allotment of Ordinary Shares on Conversion not a dividend**

158. The issue of Ordinary Shares to Holders on Conversion is a distribution of property to holders of a non-share equity interest and a non-share distribution under subparagraph 974-115(b)(ii). Subsection 974-120(1) states that, subject to subsection 974-120(2), all non-share distributions are a non-share dividend.

159. Subsection 974-120(2) provides that a non-share distribution is not a non-share dividend to the extent to which the company debits

the distribution against the company's share capital account or non-share capital account.

160. On Conversion, SGL will debit the Issue Price of the Capital Notes to its non-share capital account. Accordingly, the issue of Ordinary Shares on Conversion will not be a non-share dividend and will not be included in a Holder's assessable income under subparagraph 44(1)(a)(ii) of the ITAA 1936.

161. Furthermore, the Ordinary Shares will not be issued to the Holders of the Capital Notes as shareholders of SGL. Therefore, it would not satisfy paragraphs (a) or (b) of the definition of 'dividend' in subsection 6(1) of the ITAA 1936. This means that it will not be included in the assessable income of the Holders under subparagraph 44(1)(a)(i) of the ITAA 1936.

#### **Section 45 of the ITAA 1936**

162. 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 franked to less than 10%.

163. SGL has consistently paid fully franked distributions and has stated that it expects to continue to pay fully franked distributions, including to the Holders, to the extent of the franking credits in its franking account. Furthermore, the Terms do not allow SGL to issue Ordinary Shares to all or some of the Holders in satisfaction of their distribution entitlements in relation to the Capital Notes.

164. Based on the information provided and having regard to the circumstances of the scheme, section 45 of the ITAA 1936 will not apply to treat an amount equal to the value of the Ordinary Shares issued on Conversion as an unfrankable dividend in the hands of Holders.

#### **Section 45A of the ITAA 1936**

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

166. If these conditions are satisfied, the Commissioner may make a determination under subsection 45A(2) of the ITAA 1936 that section 45C of the ITAA 1936 applies. The effect of such a determination is that all or part of the capital benefit is taken to be an unfranked dividend.

167. A provision of capital benefits includes the provision to the shareholder of shares in the company pursuant to paragraph 45A(3)(a) of the ITAA 1936. The issue of Ordinary Shares to Holders on Conversion of the Capital Notes will constitute the provision of capital benefits in the form of shares in substitution for a non-share equity interest. It represents the replacement of one type of equity interest with another.

168. In the absence of any other factors that would contribute to an alternative conclusion, the issue of Ordinary Shares on Conversion will not be considered to be streaming as contemplated by section 45A of the ITAA 1936.

169. The Redemption of the Capital Notes involves the provision of a capital benefit within the meaning of subsection 45A(3) of the ITAA 1936 as it is a non-share capital return (subsection 45A(3A) of the ITAA 1936). The amount paid to Holders on Redemption is limited to the amount of the Issue Price of the Capital Notes and is made in respect of the termination of an equity interest. Any Distribution entitlements on the Capital Notes will be separately paid as Distributions given that each date on which Redemption occurs will also be a Distribution Payment Date under the Terms.

170. Accordingly, it cannot be said that Holders would derive a greater benefit from the receipt of the capital benefits than other SGL shareholders. Therefore, the issue of Ordinary Shares on Conversion or the Redemption of the Capital Notes will not trigger the application of section 45A of the ITAA 1936.

171. As such, the Commissioner will not make a determination under subsection 45A(2) of the ITAA 1936 that section 45C of the ITAA 1936 applies to treat the whole, or part of, a capital benefit that arises on Conversion or Redemption of the Capital Notes as an unfranked dividend in the hands of the Holders.

### **Section 45B of the ITAA 1936**

172. Section 45B of the ITAA 1936 applies where the conditions in subsection 45B(2) of the ITAA 1936 are met and it is concluded that certain capital benefits are provided to shareholders in substitution for dividends.

173. Where the requirements of subsection 45B(2) of the ITAA 1936 are met, paragraph 45B(3)(b) of the ITAA 1936 empowers the Commissioner to make a determination that section 45C applies in relation to the whole, or a part, of the capital benefit such that it will be treated as an unfranked dividend, so that it can be included in the assessable income of the relevant taxpayer.

174. The issue of Ordinary Shares to Holders on Conversion will constitute a scheme under which the Holders are provided with a capital benefit by SGL (paragraph 45B(5)(a) of the ITAA 1936). Similarly, Redemption of the Capital Notes will also constitute a scheme under which the Holders are provided with a capital benefit

by SGL (paragraph 45B(5)(b) of the ITAA 1936 and subsection 45B(7) of the ITAA 1936).

175. For the provision to apply, among other things, paragraph 45B(2)(c) of the ITAA 1936 requires that, having regard to the relevant circumstances of the scheme, it would be concluded that the person, or one of the persons, entered into the scheme or carried out the scheme or any part of the scheme for a purpose, other than an incidental purpose, of enabling a taxpayer to obtain a tax benefit. A non-exhaustive list of relevant circumstances of the scheme are provided in subsection 45B(8) of the ITAA 1936.

176. Having regard to the relevant circumstances surrounding the issue of Ordinary Shares on Conversion and Redemption of the Capital Notes, it cannot be concluded that SGL, the Holders or any other person entered into or carried out the scheme for the purpose of enabling Holders to obtain a tax benefit.

177. The allotment of Ordinary Shares on Conversion is not in satisfaction of the Holders' entitlement to Distributions, but rather a product of the Conversion of the Capital Notes held by the Holders according to the Terms. Conversion simply involves a change in the type of equity interests that are held by the Holder; an instrument paying franked distributions (the Capital Notes) is replaced with another instrument paying franked distributions (Ordinary Shares). Any Distribution entitlements on Conversion will be separately paid as a Distribution given that each date on which Conversion occurs will also be a Distribution Payment Date under the Terms.

178. Similarly, it cannot be said that Redemption involves any benefit provided to Holders that is in substitution for Distributions. The amount paid to Holders on Redemption is limited to an amount equal to the Issue Price of the Capital Notes and any Distribution entitlements on Capital Notes are separately paid as a Distribution given that each date on which Redemption occurs will also be a Distribution Payment Date under the Terms.

179. Accordingly, 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 treat the whole, or part of, a capital benefit that arises on Conversion or Redemption of the Capital Notes as an unfranked dividend in the hands of Holders.

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