


CR 2021/55 - Sunrise Energy Metals Limited - demerger of Clean TeQ Water Limited

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Class Ruling

Sunrise Energy Metals Limited – demerger of Clean TeQ Water Limited

1 Relying on this Ruling

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

If this Ruling applies to you, and you correctly rely on it, we will apply the law to you in the way set out in this Ruling. That is, you will not pay any more tax or penalties or interest in respect of the matters covered by this Ruling.

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What this Ruling is about

1. This Ruling sets out the tax consequences of the demerger of Clean TeQ Water Limited (Clean TeQ Water) by Sunrise Energy Metals Limited (Sunrise) which was implemented on 1 July 2021 (Implementation Date).
2. Full details of the demerger are set out in paragraphs 29 to 56 of this Ruling.
3. All legislative references in this Ruling are to the *Income Tax Assessment Act 1997* unless otherwise indicated.

Who this Ruling applies to

4. This Ruling applies to you if you held ordinary shares in Sunrise and you:
 - were registered on the Sunrise share register on 24 June 2021 (Record Date)
 - did not hold your shares in Sunrise as revenue assets (as defined in section 977-50) nor as trading stock (as defined in subsection 995-1(1)) on the Record Date – that is, you held your shares on capital account, and
 - were a resident of Australia (as defined in subsection 6(1) of the *Income Tax Assessment Act 1936* (ITAA 1936)) or a foreign resident that held less than 10% of the ordinary shares in Sunrise.

5. This Ruling does not apply to anyone who is subject to the taxation of financial arrangements rules in Division 230 in relation to the scheme outlined in paragraphs 29 to 56 of this Ruling.

Note: Division 230 will not apply to individuals, unless they have made an election for it to apply.

When this Ruling applies

6. This Ruling applies from 1 July 2021 to 30 June 2022.

Ruling

Demerger happened

7. A demerger, as defined in section 125-70, happened to the Sunrise demerger group (which included Sunrise and Clean TeQ Water) under the scheme described in paragraphs 29 to 56 of this Ruling.

Capital gains tax consequences – Australian-resident Sunrise Energy Metals Limited shareholders

CGT event G1

8. CGT event G1 happened when you were paid an amount by Sunrise in respect of your Sunrise shares by way of the transfer to you of Clean TeQ Water shares on the Implementation Date (section 104-135).

9. You will make a capital gain from CGT event G1 happening if the amount of the reduction of share capital for each Sunrise share (33.4 cents) was more than the cost base of the Sunrise share. If so, the capital gain is equal to the amount of the excess. No capital loss can be made from CGT event G1 (subsection 104-135(3)).

Choosing demerger roll-over

10. You can choose to obtain demerger roll-over under subsection 125-55(1) for your Sunrise shares.

11. If you choose demerger roll-over for your Sunrise shares:

- any capital gain you made when CGT event G1 happened to your Sunrise shares under the demerger is disregarded (subsection 125-80(1)), and
- you must recalculate the first element of the cost base and reduced cost base of your Sunrise shares, and calculate the first element of the cost base and reduced cost base of the corresponding Clean TeQ Water shares you acquired under the demerger (subsection 125-80(2)) – see paragraphs 13 to 15 of this Ruling for more details.

Not choosing demerger roll-over

12. If you do not choose demerger roll-over for your Sunrise shares:

- you cannot disregard any capital gain you made when CGT event G1 happened to your Sunrise shares under the demerger, and

- you must recalculate the first element of the cost base and reduced cost base of your Sunrise shares, and calculate the first element of the cost base and reduced cost base of the corresponding Clean TeQ Water shares you acquired under the demerger (subsections 125-85(1) and (2)) – see paragraphs 13 to 15 of this Ruling.

Cost base and reduced cost base of your Sunrise Energy Metals Limited and Clean TeQ Water Limited shares

13. The first element of the cost base and reduced cost base of each Sunrise share and corresponding Clean TeQ Water share is worked out by:

- taking the total of the cost bases of your Sunrise shares just before the demerger, and
- apportioning that total between your Sunrise shares and the Clean TeQ Water shares you acquired under the demerger.

14. The apportionment is done on a reasonable basis having regard to the market values (just after the demerger) of the Sunrise shares and Clean TeQ Water shares, or an anticipated reasonable approximation of those market values (subsections 125-80(2) and (3)) – see paragraph 55 of this Ruling about the market values of these shares.

15. The Commissioner accepts that a reasonable apportionment is to attribute:

- 81.82% of the total of the cost bases of your Sunrise shares just before the demerger to the Sunrise shares, and
- 18.18% of the total of the cost bases of your Sunrise shares just before the demerger to the corresponding Clean TeQ Water shares.

Acquisition date of the Clean TeQ Water Limited shares for discount capital gain purposes

16. For the purpose of determining whether you can make a discount capital gain from a future CGT event that happens to a Clean TeQ Water share you acquired under the demerger, you will be taken to have acquired the Clean TeQ Water share on the date you acquired, for capital gains tax (CGT) purposes, the corresponding Sunrise share (table item 2 in subsection 115-30(1)). This will be the case whether or not you choose demerger roll-over.

Capital gains tax consequences – foreign-resident Sunrise Energy Metals Limited shareholders***CGT event G1***

17. CGT event G1 happened when you were paid an amount by Sunrise in respect of your Sunrise shares by way of the transfer to you of Clean TeQ Water shares on the Implementation Date (section 104-135).

18. You will make a capital gain from CGT event G1 happening if the amount of the reduction of share capital for a Sunrise share (33.4 cents) is more than the cost base of that Sunrise share. If so, the capital gain is equal to the amount of the excess. No capital loss can be made from CGT event G1 (subsection 104-135(3)).

19. However, any capital gain you make from CGT event G1 is disregarded unless the Sunrise share was taxable Australian property (section 855-10). A Sunrise share was taxable Australian property if it:

- was an indirect Australian real property interest (table item 2 in section 855-15)
- was used by you (the foreign-resident shareholder) in carrying on a business through a permanent establishment in Australia (table item 3 in section 855-15), or
- is a CGT asset that is covered by subsection 104-165(3) (choosing to disregard a capital gain or capital loss on ceasing to be an Australian resident (table item 5 in section 855-15)).

Limited availability of demerger roll-over

20. If you are a foreign resident, you cannot choose to obtain demerger roll-over under subsection 125-55(1) for your Sunrise shares unless the Clean TeQ Water shares you acquired under the demerger were taxable Australian property just after you acquired them (subsection 125-55(2)).

Cost base and reduced cost base of your Sunrise Energy Metals Limited and Clean TeQ Water Limited shares

21. Whether or not you choose demerger roll-over, or demerger roll-over is available to you, you must work out the first element of the cost base and reduced cost base of each Sunrise share and corresponding Clean TeQ Water share in the same way as described in paragraphs 13 to 15 of this Ruling (subsections 125-80(2) and (3), and 125-85(1) and (2)).

Acquisition date of the Clean TeQ Water Limited shares

22. For the purpose of determining whether you can make a discount capital gain from a future CGT event that happens to a Clean TeQ Water share you acquired under the demerger, you will be taken to have acquired the Clean TeQ Water share on the date you acquired, for CGT purposes, the corresponding Sunrise share (table item 2 of subsection 115-30(1)). This will be the case whether or not you choose demerger roll-over.

Sale of Clean TeQ Water Limited shares under the Sale Facility

23. If you are an Ineligible Overseas Shareholder, or if you are a Small Shareholder who chose to participate in the Sale Facility, CGT event A1 happened to you on the Implementation Date in relation to the Clean TeQ Water shares that were transferred to the sale agent for sale through the Sale Facility (section 104-10).

24. The capital proceeds from the disposal of each such share were the net sale proceeds for the share received by you from participating in the Sale Facility.

Not a dividend

25. No part of the value of a Clean TeQ Water share transferred to you under the demerger will be included in your assessable income under subsection 44(1) of the ITAA 1936. Although any part of the value of a Clean TeQ Water share that exceeds the amount debited to the share capital account of Sunrise is a 'dividend' under

subsection 6(1) of the ITAA 1936, it will be a 'demerger dividend' under subsections 44(3) to (5) of the ITAA 1936. A demerger dividend is non-assessable non-exempt income for you.

No dividend withholding tax for non-resident Sunrise Energy Metals Limited shareholders

26. If you are not a resident of Australia (as defined in subsection 6(1) of the ITAA 1936), no part of the value of a Clean TeQ Water share transferred to you under the demerger will be subject to dividend withholding tax (subsection 128B(3D) of the ITAA 1936).

The anti-avoidance provisions in sections 45B, 45BA and 45C of the ITAA 1936 will not apply to deem an assessable dividend

27. The Commissioner will not make a determination under paragraph 45B(3)(a) of the ITAA 1936 that section 45BA of the ITAA 1936 applies to the whole, or any part, of the demerger benefit provided to you under the demerger. This is because the purpose test in paragraph 45B(2)(c) of the ITAA 1936 is not satisfied. Therefore, you will not include any part of the amount of the demerger benefit (the market value of the Clean TeQ Water shares) in your assessable income under subsection 44(1) of the ITAA 1936.

28. The Commissioner will not make a determination under paragraph 45B(3)(b) of the ITAA 1936 that section 45C of the ITAA 1936 applies to the whole, or any part, of the capital benefit provided to you under the demerger. This is because the purpose test in paragraph 45B(2)(c) of the ITAA 1936 is not satisfied. Therefore, you will not include any part of the amount of the capital benefit (the market value of the Clean TeQ Water shares to the extent that it is not a demerger dividend you receive) in your assessable income under subsection 44(1) of the ITAA 1936.

Scheme

29. The following description of the scheme is based on information provided by the applicant. If the scheme is not carried out as described, this Ruling cannot be relied upon.

Sunrise Energy Metals Limited

30. Sunrise is an Australian-resident company incorporated on 10 September 2007 and listed on the Australian Securities Exchange (ASX) on 9 November 2007.

31. Sunrise operated two business divisions:

- Water – provides wastewater treatment solutions for the power, mining and industrial sectors, as well as treating ground, surface and grey water for use as potable water suitable for municipalities.
- Metals – engages in the exploration and development of metal deposits in Australia. The Metals Division commenced its operations during the income year ended 30 June 2015.

32. Immediately before the demerger, Sunrise had on issue:

- 89,333,793 fully-paid ordinary shares, and

- unlisted rights and options issued to directors and employees, representing less than 3% of the total value of ownership interests (as defined in subsection 125-60(1)) in Sunrise.
33. There were no other ownership interests (as defined in subsection 125-60(1)) in Sunrise.
34. Immediately before the demerger, Sunrise had \$326,447,478 credited to its share capital account.

The demerger of Clean TeQ Water Limited

35. On 22 February 2021, Sunrise announced to the ASX the proposed demerger of Clean TeQ Water.
36. Immediately before the demerger, Clean TeQ Water was a wholly-owned subsidiary of Sunrise and owned the companies that made up the Water division.
37. The demerger of Clean TeQ Water was undertaken by a reduction of share capital under section 256B of the *Corporations Act 2001*.
38. The shareholders of Sunrise voted at a meeting on 18 June 2021 to approve:
- an ordinary resolution under section 256C of the *Corporations Act 2001* to reduce the share capital of Sunrise as an equal capital reduction, which equated to \$0.334 per Sunrise share, and
 - the demerger being implemented in the manner described.
39. The date for determining the entitlement of Sunrise shareholders to receive Clean TeQ Water shares was the Record Date.
40. On the Implementation Date, the aggregate of the amount of the reduction of share capital (see paragraph 45 of this Ruling) was applied by Sunrise on behalf of Sunrise shareholders as payment to acquire the Clean TeQ Water shares from Sunrise. Shares in Clean TeQ Water were transferred by Sunrise to Sunrise shareholders.
41. Sunrise shareholders received one Clean TeQ Water share for every two Sunrise shares they held on the Record Date, and nothing else.
42. After the demerger, Sunrise will not own any shares in Clean TeQ Water.
43. As a result of the demerger, Sunrise shareholders owned shares in both Sunrise and Clean TeQ Water.
44. Shares in Clean TeQ Water were listed for quotation on the ASX on 2 July 2021.

Accounting treatment

45. Sunrise accounted for the demerger by debiting its:
- share capital account by \$29,836,850 (the capital reduction amount), and
 - demerger reserve account by \$5,284,567 (the demerger dividend).
46. The demerger dividend was calculated as the difference between the market value of the Clean TeQ Water shares distributed and the capital reduction amount.

Reasons for the demerger

47. The directors of Sunrise formed the view that the demerger would:
- better enable distinct business plans and growth strategies to be pursued for each business
 - enable each business to adopt a capital structure and financial policies appropriate to its needs
 - deliver to shareholders an investment choice depending on their individual investment objectives and strategies – in this regard, shareholders will obtain greater flexibility to choose their level of investment in the Water division and Metals division, as the two businesses have different characteristics, assets and risk profiles, and
 - result in two independent businesses trading separately on the ASX and create two distinct core earnings streams which can be clearly valued by the market.

Sale Facility

48. Ineligible Overseas Shareholders had the Clean TeQ Water shares to which they were entitled sold by Sunrise through a sale agent on the ASX (Sale Facility), who remitted the net sale proceeds to the relevant shareholders. The shares of Ineligible Overseas Shareholders were transferred to the sale agent on the Implementation Date.

49. Ineligible Overseas Shareholders were shareholders who were not Eligible Shareholders at the Record Date.

50. Eligible Shareholders were shareholders whose registered address on the Sunrise share register on the Record Date was in Australia, New Zealand, Canada, China, France, Germany, The Netherlands, Japan, Malaysia, Singapore, Taiwan, Thailand, the United Arab Emirates, the United Kingdom, the United States of America or any other jurisdiction in which Sunrise reasonably believes it is not prohibited or unduly onerous or impractical to implement the demerger and to transfer the Clean TeQ Water shares to those shareholders.

51. Small Shareholders, being Eligible Shareholders who held less than 5,000 Sunrise shares as at the Record Date, were able to choose to participate in the Sale Facility. Small Shareholders participating in the Sale Facility had their Clean TeQ Water shares transferred to the sale agent on the Implementation Date and they received the net sale proceeds.

Other matters

52. Just before the Implementation Date, two foreign residents held 10% or more of the shares in Sunrise – a resident of Singapore held 13.41% and a resident of Hong Kong held 11.70%.

53. Immediately before the Implementation Date, Sunrise's share capital account was not tainted (within the meaning of Division 197).

54. Sunrise did not elect under subsection 44(2) of the ITAA 1936 that subsections 44(3) and (4) of the ITAA 1936 will not apply to the demerger dividend for all Sunrise shareholders.

55. Just after the demerger, CGT assets owned by Clean TeQ Water and its demerger subsidiaries representing at least 50% by market value of all the CGT assets owned by

those entities were used in carrying on a business by those entities (subsection 44(5) of the ITAA 1936).

56. For the purposes of the cost base and reduced cost base apportionment under subsections 125-80(2) and (3), a reasonable approximation of the market values of a Sunrise share and a Clean TeQ Water share just after the demerger has been calculated as:

- \$1.7690 for each Sunrise share, being the volume weighted average price of Sunrise shares as traded on the ASX over the first five trading days from (and including) 2 July 2021.
- 78.63 cents for each Clean TeQ Water share, being the volume weighted average price of Clean TeQ Water shares as traded on the ASX over the first five trading days from (and including) 2 July 2021.

Commissioner of Taxation4 August 2021

References

<i>Previous draft:</i>	- ITAA 1997 104-135(3)
Not previously issued as a draft	- ITAA 1997 104-165(3)
	- ITAA 1997 115-30(1)
<i>Related Rulings/Determinations:</i>	- ITAA 1997 125-55(1)
TR 2006/10	- ITAA 1997 125-55(2)
	- ITAA 1997 125-60(1)
	- ITAA 1997 125-70
<i>Legislative references:</i>	- ITAA 1997 125-80(1)
- ITAA 1936 6(1)	- ITAA 1997 125-80(2)
- ITAA 1936 44(1)	- ITAA 1997 125-80(3)
- ITAA 1936 44(2)	- ITAA 1997 125-85(1)
- ITAA 1936 44(3)	- ITAA 1997 125-85(2)
- ITAA 1936 44(4)	- ITAA 1997 Div 197
- ITAA 1936 44(5)	- ITAA 1997 Div 230
- ITAA 1936 45B	- ITAA 1997 855-10
- ITAA 1936 45B(2)(c)	- ITAA 1997 855-15
- ITAA 1936 45B(3)(a)	- ITAA 1997 977-50
- ITAA 1936 45B(3)(b)	- ITAA 1997 995-1(1)
- ITAA 1936 45BA	- TAA 1953
- ITAA 1936 45C	- Corporations Act 2001 256B
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ATO references

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