

TR 95/D19 - Income tax: capital gains: roll-over relief following reorganisation of the affairs of a unit trust or company - sections 160ZZPA, 160ZZPB, 160ZZPC and 160ZZPD

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This document has been finalised by TR 97/18.



Draft Taxation Ruling

Income tax: capital gains: roll-over relief following reorganisation of the affairs of a unit trust or company - sections 160ZZPA, 160ZZPB, 160ZZPC and 160ZZPD

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What this Ruling is about

Class of person/arrangement

1. This Ruling covers aspects of the roll-over relief provided by sections 160ZZPA, 160ZZPB, 160ZZPC and 160ZZPD of the *Income Tax Assessment Act 1936* (the Act).

2. The Ruling specifically covers sections 160ZZPA and 160ZZPB of the Act which are the operative provisions that provide for roll-over relief for a scheme for the reorganisation of the affairs of a unit trust where a company is interposed between the trust and its unitholders. Equally, it applies to sections 160ZZPC and 160ZZPD as they modify sections 160ZZPA and 160ZZPB (respectively) to schemes for the reorganisation of the affairs of a company where another company is interposed between the company and its shareholders.

3. This Ruling does not deal with the general income provisions of the Act or the possible application of the general anti-avoidance provisions of Part IVA.

4. The provisions of sections 160ZZPA and 160ZZPB are in many respects similar in their construction. Accordingly, in this Ruling a reference to certain words and phrases in section 160ZZPA, is intended to include a reference to comparable words and phrases in section 160ZZPB. The table below summarises these references:

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Reference to:	Includes reference to:
Section 160ZZPA	Sections 160ZZPB, 160ZZPC and 160ZZPD
Subsections, paragraphs and subparagraphs of section 160ZZPA	Subsections, paragraphs and subparagraphs of section 160ZZPB
units	shares in the original company
units in the unit trust	shares in the original company
unit trust	original company
unitholder	shareholder
disposed of	cancelled or redeemed

Definitions

5. The meanings of key terms used in the legislation and this Ruling are as follows:

Relevant to sections 160ZZPA, 160ZZPB, 160ZZPC and 160ZZPD

exchanging taxpayer: each of the two or more taxpayers who are the holders of all the units in the unit trust and which units are disposed of for shares in the interposed company;

exchange units: all the units in the unit trust and which are disposed of for shares in the interposed company;

interposed company: a resident company that acquires all the units in the unit trust and whose shares are held by the original unitholders;

replacement share: a non-redeemable share in the interposed company received as consideration for the disposal of units in the unit trust;

remaining shares: the five or fewer issued shares in the interposed company that are not replacement shares;

exchanging taxpayer's disposal time: the time when all of the units in the unit trust held by a particular unitholder are disposed of;

completion time: the time when the last of the unitholders disposes of his or her units in the unit trust.

Relevant to section 160ZZPB and section 160ZZPD only

formal units: if the original units are to be disposed of and new units are to be issued to the interposed company, the interposed company may acquire up to five units (formal units) in the unit trust before this disposal takes place;

scheme units: if the original units are to be disposed of and new units issued to the interposed company, then, once this disposal is made, the trustee of the unit trust must issue to the interposed company two or more units (scheme units) in the unit trust.

Relevant to section 160ZZPC and section 160ZZPD only

original company: the existing resident company in which the shareholders originally held shares before disposing of the shares

Key concept

6. Broadly, roll-over relief is available for certain business reorganisations where no change occurs in the economic ownership of a particular underlying asset, or where the underlying assets in which the taxpayer has an economic interest do not change. The provisions were not designed to extend to any other type of arrangement which may involve the introduction of new economic owners into the structure or where the owners obtain an economic interest in underlying assets which they did not previously hold.

7. It is readily observed that if there is a reorganisation of the affairs of a wholly owned group/conglomerate by reconfiguring the group under two main operating companies, there occur changes in cross holdings between each related company **but no change in the overall economic ownership of the underlying assets within the group**. This type of arrangement is common commercial practice and not offensive to the roll-over provisions of section 160ZZO of the Act.

8. Section 160ZZPA was introduced to extend roll-over relief under Division 17 of Part IIIA to schemes where unitholders in a unit trust dispose of their units in consideration for shares in an interposed company. Such a scheme is described in Example 1. The provisions of that section have been drafted to reflect the specific type of scheme for which the extension of roll-over relief was intended.

9. Section 160ZZPA was enacted to extend roll-over relief to a wholly internal reorganisation of a unit trust where a company is interposed between the owners (the unitholders) and the unit trust. The words of the provisions are specifically directed at a scheme for

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the reorganisation of a unit trust, **not** two or more unit trusts. Schemes for the reorganisation of the affairs of more than one entity will typically not be able to satisfy the other operative requirements of the section.

10. This view is supported by the words of these provisions and by the overall scheme of Part IIIA of the Act. The operative requirements of the provisions prescribe a number of requirements that must be satisfied for the roll-over relief to be available. These are all designed to give effect to the clear intention of the provisions. If the interposed company has on issue, in addition to the replacement shares, more than five shares, (or five or fewer shares possessing more than nominal value), then the operative requirements are not met.

11. Subsection 15AA(1) of the *Acts Interpretation Act 1901* provides:

'In the interpretation of a provision of an Act, a construction that would promote the purpose or object underlying the Act (whether that purpose or object is expressly stated in the Act or not) shall be preferred to a construction that would not promote that purpose or object.'

It is with this key concept in mind that the views expressed in this Ruling have been formed.

Ruling

12. It is an essential requirement for roll-over relief under section 160ZZPA that there must be a scheme for the reorganisation of the affairs of a unit trust.

13. A scheme for the reorganisation of the affairs of a unit trust is different from the merger of that unit trust with another unit trust. Roll-over relief under section 160ZZPA is therefore not available for schemes where the merger of two or more unit trusts is effected. In any event, mergers will generally not satisfy the other operative requirements of section 160ZZPA for the availability of roll-over relief.

14. Furthermore, roll-over relief under section 160ZZPA cannot be available for schemes for the reorganisation of the affairs of more than one unit trust as that section is clearly expressed in the singular form.

15. The requirement of paragraph 160ZZPA(1)(k) is satisfied if the proportions obtained by comparing the number of units held by an exchanging taxpayer to the total number of units in the unit trust, is the same as the proportion represented by the exchanging taxpayer's

holding of replacement shares to the **total** replacement shares in the interposed company.

16. The only shares on issue by the interposed company at the completion time must be replacement shares subject only to the exception for remaining shares contained in subsection 160ZZPA(10).

17. The time at which the proportions of units in the unit trust are ascertained for the purposes of paragraph 160ZZPA(1)(k) is immediately before the earliest exchanging taxpayer's disposal time.

18. All replacement shares held by a taxpayer in the capacity of trustee must be held on the same trust as the original units in the unit trust. This means that the trust property must be held for the benefit of the same beneficiaries and upon the same terms and conditions as before the exchange.

19. The 'multiple' of exchange units required by paragraph 160ZZPA(1)(c) [and subparagraph 160ZZPB(1)(a)(vii)] must be a whole number and not a fraction.

20. The only consideration that exchanging taxpayers may receive in respect of the disposal of their units is non-redeemable shares in the interposed company.

Operative requirements

21. In the following tables the summarised references contained in paragraph 4 are incorporated.

Common Features of sections 160ZZPA, 160ZZPB, 160ZZPC and 160ZZPD

Matter	Provision	Requirement
Arrangements covered	(1)(a)	Scheme for the reorganisation of the affairs of a unit trust.
Consideration	(1)(b)	Non-redeemable (replacement) shares in the interposed company issued to the taxpayers.
Numerical Continuity	(1)(c)	The number of replacement shares equals, or is a multiple of, the number of exchange units.
Timing	(1)(d)	Each taxpayer's exchange units are disposed of at the same time.

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Matter	Provision	Requirement
Control	(1)(e)	On completion, the taxpayers are the owners of all, or substantially all, the shares in the interposed company. The 'substantially all' modification results from the Commissioner's discretion in subsection (10) where the number of shares held by others does not exceed five.
Continuity of Ownership	(1)(f)	Each taxpayer owns the replacement shares from disposal time to completion time.
Residence	(1)(g) and (1)(h)	The unit trust and the interposed company are residents for the prescribed income year or period.
Trustee status	(1)(j)	Replacement shares held by a trustee are held upon the same trust as the exchange units.
Proportional Ownership	(1)(k)	Each exchanging taxpayer owns the replacement shares in the interposed company in the same proportion that the exchange units were held in the unit trust.
Proportional Value	(1)(m)	For each exchanging taxpayer: the ratio which so much of the market value, at completion time, of the taxpayer's replacement shares, as is attributable to the exchange (or scheme) units, bears to the market value of all replacement shares attributable to those units must be the same as the ratio which the market value of the taxpayer's units bore to the market value of the exchange units immediately before the exchanging taxpayers disposal time.
Election	(1)(n) and (1)(p)	The interposed company provides a written election within two months after completion time (or such further time as the Commissioner allows) accompanied by a declaration.

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Applicable to sections 160ZZPA and 160ZZPC only

Matter	Provision	Requirement
Elements of scheme	(1)(a)(i)	Two or more taxpayers hold all the units in a unit trust All the units are disposed of to an (interposed) company. The interposed company is not the trustee of a trust estate.

Applicable to sections 160ZZPB and 160ZZPD only

Matter	Provision	Requirement
Elements of scheme	(1)(a)(ii)	An (interposed) company acquires up to five (formal) units in a unit trust. The interposed company is not the trustee of a trust estate.
	(1)(a)(iii)	The interposed company did not previously hold any units in the unit trust.
	(1)(a)(iv)	Two or more taxpayers own the remaining (exchange) units.
	(1)(a)(v)	All exchange units are redeemed or cancelled.
	(1)(a)(vi)	Two or more (scheme) units are issued to the interposed company.
	(1)(a)(vii)	The number of scheme units equals, or is a multiple of, the number of exchange units.

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Applicable to sections 160ZZPA and 160ZZPB only

Matter	Provision	Requirement
Commencing date	(1)(a)(ii)	On or after 9 December 1987.

Applicable to sections 160ZZPC and 160ZZPD only

Matter	Provision	Requirement
Commencing date	(1)(a)(i)	On or after 28 January 1988.

Date of effect

22. This Ruling applies to years commencing both before and after its date of issue. However, the Ruling does 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 the Ruling (see paragraphs 21 and 22 of Taxation Ruling TR 92/20).

23. If a taxpayer has a more favourable private ruling (whether legally or administratively binding), this Ruling applies to that taxpayer to the extent of any inconsistency only in respect of any transactions, arrangements, agreements, acts or events entered into, commenced or occurring from the date of this Ruling.

Explanations

Schemes for the reorganisation of the affairs of a unit trust

24. Paragraph 160ZZPA(1)(a) requires that there must be a scheme for the reorganisation of the affairs of a unit trust.

25. It is plain that subparagraph 160ZZPA(1)(a)(i) separately requires there to be a scheme for the reorganisation of the affairs of a unit trust. The succeeding paragraphs of subsection 160ZZPA(1) then set out further requirements. These further requirements do indicate

what type of reorganisation is contemplated by subparagraph 160ZZPA(1)(a)(i). In other words they show what is meant by a reorganisation of the affairs of a unit trust. What is meant is the interposition of a company between the unit trust and its unitholders.

Mergers

26. The view has been put to us that section 160ZZPA means that, if all other conditions are satisfied, then it follows that the arrangement, even if it is a merger, satisfies the reorganisation requirement. A merger between two companies involves an absorption of the one entity by another, or two or more companies unite or combine. Accordingly we consider that for the purposes of the application of section 160ZZPA a merger cannot constitute a reorganisation. Under a reorganisation no change occurs in the economic ownership of the underlying assets and the underlying assets in which the taxpayer has an economic interest do not change.

27. Our view is that the legislation does not intend that roll-over relief of this type should be available in the case of a merger, but rather should be available for the type of reorganisation where a new company is interposed between the owners of an existing entity and that entity, so that the owners exchange their existing direct interests in the entity for shares in the interposed company, thus retaining their existing economic ownership of the underlying assets indirectly. For example, a new company may be interposed between unitholders and a unit trust where the unitholders exchange their existing unitholdings for shares in the new company and the new company holds 100% of the units in the unit trust.

28. Schemes described as 'mergers' where taxpayers have sought to have roll-over relief available under section 160ZZPA have taken either one of the following forms. The first involves two operating companies with different sets of shareholders. Under this form of scheme both sets of shareholders become the shareholders in one of the companies whilst that company becomes the sole shareholder in the other company (such an arrangement involving a unit trust and a company is described in Example 2).

29. The second form of scheme also involves two operating companies with separate sets of shareholders. The two sets of shareholders become the shareholders in a new company which is the sole shareholder in the two operating companies (such a scheme is described in Example 3).

30. Under both of these arrangements we consider that the scheme involves more than the reorganisation of the affairs of a company. The affairs of both of the operating companies have been

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fundamentally altered. Neither of the companies involved retains the same shareholder ownership as it had before the scheme as, at the very least, some new shareholders are introduced whilst in some cases the entire shareholding in the company is changed. By tracing through the interposed company it will be clear that there has been, at least, a partial change in the economic ownership in the underlying assets, as persons who did not previously hold economic interests in some of the underlying assets of the companies now hold such interests. The economic interests in the underlying assets of shareholders who have not disposed of a share in a company will also have changed because other persons will now also have economic interests in the underlying assets of the company. Again the underlying assets in which the shareholders have an economic interest will have changed.

31. It is not possible to consider parts of these schemes in isolation. In considering a scheme we must look at the entirety of the scheme and its effect in determining whether the scheme is one for the reorganisation of the affairs of a unit trust.

32. If contrary to the view expressed later in this Ruling, it is possible to have a reorganisation at law of the affairs of two or more unit trusts section 160ZZPA does not provide roll-over relief as the section is clearly limited to the reorganisation of the affairs of a single unit trust.

33. Accordingly, it is our opinion that if the scheme is one for the reorganisation of the affairs of more than one unit trust roll-over relief under section 160ZZPA is not available.

34. Case law provides analysis of the meaning of the word 'reorganisation' and how it is distinguished from the word 'amalgamation'. The word 'amalgamation' is a commercial term which has been adopted in various companies legislation and subsection 86(2) of the *Capital Gains Tax Act 1979* (UK).

35. In the English case *Hooper v. Western Counties & South Wales Telephone Company Limited* 68 LT 78 at 80, Chitty J said when considering the terms 'reconstruction' and 'reorganisation' for the purposes of the *Companies Act 1862* (UK):

'Reorganisation, though a less familiar term, can have no wider meaning than reconstruction...I think that the two terms are used as alternative expressions.'

36. Chitty J was of the view that 'reorganisation' of a company means the same as, and not more than, 'reconstruction' of a company. He discussed how a 'reconstruction' differed from an 'amalgamation', by placing reliance on text writers and concluding (at 80) that:

'Lindley LJ in his treatise says that "reconstruction differs from amalgamation in that, as a rule there is only one transferring

company, and the company to which the property is transferred is practically the same company with some alterations in its constitution" (*Law of Companies*, 5th ed at 900); that appears to me to afford a clue to the meaning of the word as used in a clause like the present.'

37. Buckley J in *In re South African Supply & Cold Storage Co; Wild v. Same Company* [1904] 2 Ch 268 at 286 and 287 discussed the difference between the terms 'reconstruction' and 'amalgamation' and (at 286) said:

'What does "reconstruction" mean?...It involves, I think, that substantially the same business shall be carried on, and substantially the same persons shall carry it on...Substantially the business and the persons interested must be the same...You have to see whether substantially the same persons carry on the same business; and if they do, that, I conceive, is a reconstruction.'

38. Buckley J then went on to explain what he considered an 'amalgamation' to be, stating (at 287):

'Now what is an amalgamation? An amalgamation involves, I think, a different idea. There you must have the rolling, somehow or other, of two concerns into one. You must weld two things together and arrive at an amalgam - a blending of two undertakings...The difference between reconstruction and amalgamation is that in the latter is involved the blending of two concerns one with the other, but not merely the continuance of one concern. An amalgamation may take place, it seems to me, either by transfer of undertakings A and B to a new corporation, C, or by the continuance of A and B by B upon terms that the shareholders of A shall become shareholders in B. It is not necessary that you should have a new company. You may have a continuance of one of the two companies upon the terms that the undertakings of both corporations shall substantially be merged in one corporation only.'

39. What Buckley J describes as an amalgamation is representative of cases we describe in this Ruling as mergers.

40. In the High Court of Australia in *The Citizen's and Graziers' Life Assurance Company Limited v. The Commonwealth Life (Amalgamated) Assurances Limited and Anor* (1934) 51 CLR 422, Dixon J said (at 455):

'In spite of the commercial origins of the terms 'amalgamation', 'reconstruction' and 'reorganisation' as descriptions of company transactions, their meaning is not to be ascertained by considering the lay understanding of the expressions but rather

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by referring to the text writers upon company law, who are specially conversant with the subject.'

41. Dixon J in his judgment made reference to *Lindley on Companies*, 6th edition (1902) and *Palmer's Company Precedents*, 13th edition (1927). It is our view that the text writers also support the proposition that a merger or amalgamation is not a reconstruction or reorganisation.

42. In the case of share disposals prompted by takeovers there is a change in the economic ownership of the underlying assets of the target company after takeover. In the course of company amalgamations the economic ownership of the underlying assets also changes. These changes are not consistent with the policy of roll-over relief.

43. In our view, therefore, a merger does not constitute a scheme for the reorganisation of the affairs of a unit trust or company. We consider that a merger does not satisfy the requirement of the provisions that the scheme be for the reorganisation of the affairs of a unit trust within the meaning of subparagraph 160ZZPA(1)(a)(i).

The words used in the legislation are 'singular' not 'plural'

44. As already mentioned (see paragraphs 31 to 33 above), if a scheme is one for the reorganisation of the affairs of more than one unit trust roll-over relief under section 160ZZPA is not available.

45. The provisions of sections 160ZZPA have been carefully drafted using language which is clearly expressed in the singular. The section provides that the reorganisation must be by way of interposing a company (singular) between the unitholders and the unit trust (singular) where all unitholders' units in the unit trust (singular) are disposed of in exchange for non-redeemable shares in the interposed company (singular) in the same proportions that they originally held the exchange units.

46. The legislation was drafted with words in the singular to ensure that the proportional interest of each former unitholder in the ownership of the unit trust was maintained after the reorganisation. This interpretation is within the spirit and intent of roll-over relief under Part IIIA of the Act.

47. Section 23 of the *Acts Interpretation Act 1901* provides:

'In any Act unless the contrary intention appears:

...

- (b) words in the singular number include the plural and words in the plural number include the singular.'

48. However, we consider that a contrary intention does appear here. To adopt the singular construction when it is used and not the plural is appropriate when the character of the legislation would be changed by adopting the plural.

49. In *Blue Metal Industries Ltd v. Dilley* (1969) 117 CLR 651 the Privy Council considered the equivalent provisions of the *Interpretation Act 1899* (NSW). Their Lordships in their judgment said (at 656):

'By s.21 of the *Interpretation Act*, 1899 (NSW) it is enacted that in all Acts, unless the contrary intention appears, words in the singular shall include the plural and words in the plural shall include the singular. Such a provision is of manifest advantage. It assists the legislature to avoid cumbersome and over-elaborate wording. Prima facie it can be assumed that in the processes which lead to an enactment both draughtsman and legislators have such a provision in mind. It follows that the mere fact that the reading of words in a section suggests an emphasis on singularity as opposed to plurality is not enough to exclude plurality. Words in the singular will include the plural unless the contrary intention appears. But in considering whether a contrary intention appears there need be no confinement of attention to any one particular section of an Act. **It must be appropriate to consider the section in its setting in the legislation and furthermore to consider the substance and tenor of the legislation as a whole.** (See *Sin Poh Amalgamated (HK) Ltd v. Attorney-General* [1965] 1 WLR 62)' (emphasis added).

50. And then later, at 658:

'The *Interpretation Act* is a drafting convenience. It is not to be expected that it would be used so as to change the character of legislation. Acquisition of shares by two or more companies is not merely the plural of acquisition by one. It is quite a different kind of acquisition with different consequences. It would presuppose a different legislative policy.'

51. By adopting a plural construction the character of the provisions is altered and anomalies may arise. For example, under paragraphs 160ZZPA(2)(c) and (d) an exchanging taxpayer who holds units in a unit trust that were acquired before 20 September 1985 is allowed to have the replacement shares received under the reorganisation of the affairs of the unit trust also taken to have been acquired before 20 September 1985 for the purposes of Part IIIA.

52. If the scheme is one for the reorganisation of the affairs of two unit trusts, such as in Example 3, and the exchanging taxpayer holds

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units in only one of the unit trusts that were acquired before 20 September 1985 an anomaly arises. If roll-over relief were available, that exchanging taxpayer would be able to treat replacement shares received as also being acquired before 20 September 1985. However, that exchanging taxpayer now has an economic interest in the underlying assets of the unit trust in which such an interest was previously not held. The status of those replacement shares will not reflect the economic reality that under the scheme the taxpayer has newly acquired economic interests in underlying assets. It does not appear reasonable that in these circumstances the taxpayer should be able to treat all the replacement shares as being acquired before 20 September 1985.

53. These roll-over provisions were drafted to cater for situations in which the underlying assets in which the taxpayer has an economic interest have remained the same, being a reorganisation of the affairs of one unit trust where the proportionate ownership is maintained. Schemes for the reorganisation of the affairs of two or more unit trusts are not considered to be covered. The application of the provisions to such schemes would produce a result which is not in keeping with the policy of the roll-over provisions.

54. It is the clear intention of roll-over relief of this type that it be available where the interests of the economic owners of the property are maintained after the reorganisation. To construe terms expressed in the singular to include the plural would, in our view, change the essential character of the provisions and not properly reflect the intention of the Parliament.

In the same proportion

55. Paragraph 160ZZPA(1)(k) requires that immediately after the completion time, each exchanging taxpayer owns replacement shares in the interposed company in the same proportion as he or she held exchange units in the unit trust.

56. The paragraph requires comparison of the proportion held by each exchanging taxpayer of the replacement shares issued in the interposed company with the proportion of the units held by that exchanging taxpayer. This impliedly requires that issued shares, other than replacement shares, in the interposed company not be taken into account in determining whether the requirements of paragraph 160ZZPA(1)(k) are satisfied. However, paragraph 160ZZPA(1)(k) must be read in the context that, subject to the exception contained in subsection 160ZZPA(10), the replacement shares will be **all** the shares of the interposed company on issue at the completion time.

57. The requirement that, subject to the exception contained in subsection 160ZZPA(10), the replacement shares will be all the shares of the company on issue at the completion time is discernible from the entirety of the requirements of section 160ZZPA.

58. An important rule of statutory interpretation requires an Act to be read as a whole with the result that the words must be read in their context. In this regard, reference is made to the joint judgment of Isaacs and Rich JJ in *Metropolitan Gas Co v. Federated Gas Employees' Industrial Union* (1924) 35 CLR 449 at 455 where their Honours state:

'It is a received canon of interpretation that every passage in a document must be read, not as if it were entirely divorced from its context, but as part of the whole instrument: *Ex antecedentibus et consequentibus fir optima interpretatio*. In construing an instrument "every part of it should be brought into action, in order to collect from the whole one uniform and consistent sense, if that may be done; or, in other words, the construction must be made upon the whole instrument, and not merely upon disjointed parts of it; the whole context must be considered, in endeavouring to collect the intention of the parties, although the immediate object of inquiry be the meaning of an isolated clause". (*Broom's Legal Maxims*, 9th ed, pp 367-8, and cases there cited; and per Lord Haldane LC in *Toronto Suburban Railway v. Toronto Corp* [1915] AC 590 at 597).'

59. Roll-over relief of the type under consideration is available in recognition that the economic ownership of the underlying assets is unchanged by the reorganisation. Therefore, the economic interest of each former unitholder in the underlying assets of the unit trust must be maintained immediately after the completion time. If no regard were paid to the totality of the shareholding in the interposed company, it would not be possible to ensure that the economic ownership of the underlying assets was maintained.

60. It is argued by some that the requirement in subparagraph 160ZZPA(1)(e)(i) that 'all the shares' in the interposed company must be owned immediately after the completion time by the exchanging taxpayers will be satisfied in cases where the exchanging taxpayers own not only replacement shares in the interposed company immediately after the completion time but also other shares (existing shares) in that company which they acquired before the commencement of the scheme for reorganisation. However, when the specific requirements of paragraphs 160ZZPA(1)(b), (c), (d), (e), (f), (k) and (m) are looked at it is clear that what subsection 160ZZPA(1) is directed towards is ensuring that the proportional interest of each

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exchanging taxpayer in the interposed company will be the same as the proportional interest of that exchanging taxpayer in the unit trust.

61. If subparagraph 160ZZPA(1)(e)(i) had referred to all the 'replacement shares' instead of 'all the shares' in the interposed company there would have been a clear inference that the interposed company could have on issue at the completion time shares other than the replacement shares. By using the expression 'all the shares' in the interposed company it is made clear that the shares being referred to are the shares, and only the shares, acquired by the exchanging taxpayers under paragraph 160ZZPA(1)(b). The replacement shares are the only shares in the interposed company referred to in subsection 160ZZPA(1), other than in subparagraph 160ZZPA(1)(e)(i), and are, therefore, the relevant shares for the purposes of subsection 160ZZPA(1).

62. It would be odd, to say the least, if the interposed company could have existing shareholdings by the exchanging taxpayers before the exchange of units. If this were the case, after the exchange, despite complying with the various operative requirements of subsection 160ZZPA(1) designed to ensure that the value of an exchanging taxpayer's replacement shares attributable to exchange (or scheme) units was the same as the proportional value of his or her interest in the units exchanged for replacement shares (see paragraph 160ZZPA(1)(m)), the interest of an exchanging taxpayer in the underlying property of the unit trust could be altered. This would occur where the existing shareholding of that exchanging taxpayer in the interposed company before the reorganisation was a different proportion of the existing total shareholdings from the proportion of units held by the exchanging taxpayer in the unit trust.

63. For example, before implementation of a scheme a taxpayer holds 10% of the issued units in a unit trust (10 units of 100 units issued) and already holds 20% of issued capital of the company to be interposed (20 shares of 100 shares issued). Under the scheme the taxpayer receives 10% of replacement shares (10 shares of 100 shares issued). After the scheme the taxpayer has 30 shares of the 200 shares issued in the interposed company being 15% of the issued capital. The economic interest of the taxpayer in the underlying assets has changed from the 10% held in the unit trust and the 20% held in the company to 15% in the consolidated group.

64. The above view is further supported by subsection 160ZZPA(10). Subsection 160ZZPA(10) operates where, after the completion time, the exchanging taxpayers are the owners of some but not all of the shares in the interposed company.

65. Subsection 160ZZPA(10) modifies the requirements of subparagraph 160ZZPA(1)(e)(i) to enable shares held in the interposed

company by persons other than the exchanging taxpayers immediately after the completion time being the remaining shares to be disregarded for the purposes of establishing compliance with those provisions. The circumstances in which the Commissioner may disregard the remaining shares are detailed in paragraphs 160ZZPA(10)(a) to (c): Paragraph 160ZZPA(10)(a) requires that immediately after the completion time the exchanging taxpayers will not be the owners of all the shares in the interposed company. Paragraph 160ZZPA(10)(b) requires that there be no more than five remaining shares. Paragraph 160ZZPA(10)(c) states that the Commissioner is to have regard to the ratio of the market value of those shares to the market value of the replacement shares, and also to any other matter considered relevant.

66. Paragraphs 160ZZPA(10)(a) to (c) provide recognition that small shareholdings of nominal value may exist in the interposed company immediately after the completion time to facilitate the reorganisation.

67. In the situation envisaged by paragraph 160ZZPA(10)(a), it is obvious that not all the shares on issue by the interposed company immediately after the completion time will be replacement shares. Replacement shares can only be owned by an exchanging taxpayer.

68. If the shares not owned by the exchanging taxpayers (the remaining shares) meet the requirements of paragraph 160ZZPA(1)(b) and (c), the exchanging taxpayers shall be treated, for the purposes of subparagraph 160ZZPA(1)(e)(i), as if, immediately after the completion time, they were the owners of all the shares in the interposed company (paragraph 160ZZPA(10)(d)). It is also further provided, in paragraph 160ZZPA(10)(e), that the remaining shares shall be disregarded for the purposes of paragraph 160ZZPA(1)(k).

69. It will be noted that paragraph 160ZZPA(1)(k) refers to each exchanging shareholder owning the **replacement shares** in the interposed company in the same proportion as that taxpayer held units in the unit trust. In other words, the relevant proportionate shareholding of the exchanging taxpayer in the interposed company is **not** the taxpayer's proportionate shareholding in **all** the issued shares of the interposed company but in the **replacement shares**. However, paragraph 160ZZPA(10)(e) provides that the remaining shares, which are not, and cannot be, the replacement shares, shall be disregarded for the purposes of paragraph 160ZZPA(1)(k).

70. Paragraph 160ZZPA(10)(e) can only, therefore, be seen as necessary or relevant if it is accepted that there is an underlying assumption in subsection 160ZZPA(1) that the only shares of the interposed company on issue immediately after the completion time were, subject to the exception in subsection 160ZZPA(10), replacement shares.

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71. Further, it would seem illogical that whilst paragraph 160ZZPA(10)(d) specifically provided for the remaining shares not to be taken into account for the purposes of subparagraph 160ZZPA(1)(e)(i), any existing shares in the interposed company held by the exchanging taxpayers would not cause that subparagraph to be breached even though their presence could (and in many cases would) change the proportion of the economic interests of the exchanging taxpayers in the underlying property of the unit trust.

72. Paragraph 15AB(1)(a) of the *Acts Interpretation Act 1901* provides:

'Subject to subsection (3), in the interpretation of a provision of an Act, if any material not forming part of the Act is capable of assisting in the ascertainment of the meaning of the provision, consideration may be given to that material -

- (a) to confirm that the meaning of the provision is the ordinary meaning conveyed by the text of the provision taking into account its context in the Act and the purpose or object underlying the Act.'

73. The Explanatory Memorandum to the *Taxation Laws Amendment Act (No 5) 1987* states, in respect of paragraph 160ZZPA(1)(k):

'Paragraph (k) stipulates that immediately after the completion time, each exchanging taxpayer must own the **replacement shares** in the interposed company in the same proportion as the exchange units were held in the unit trust. For example, a taxpayer who held 10 per cent of the issued units of the unit trust would be required to own 10 per cent of **the shares** in the interposed company' (emphasis added).

74. The passage quoted from the Explanatory Memorandum clearly confirms our view that, subject to the exception in subsection 160ZZPA(10), the only issued shares in the interposed company at completion time, must be the replacement shares. A taxpayer who held ten percent of the units in the unit trust would not necessarily own ten percent of the shares in the interposed company (so as to own replacement shares in the same proportion as he owned the exchange units) merely because he owned ten percent of the shares in the interposed company, unless the only shares on issue were replacement shares.

75. Paragraph 160ZZPA(1)(d) requires that **each** exchanging taxpayer dispose of **all** of his or her individual holding of exchange units at the same time. However, it is not a requirement of the section that **all** exchanging taxpayers dispose of **all** of their exchange units at the same time. Paragraph 160ZZPA(1)(k) requires a comparison to be

made of the number of units held by an exchanging taxpayer to the total number of units in the unit trust (see paragraph 15). The time at which the proportion of each exchanging taxpayer's units to the total units in the unit trust for the purposes of this comparison is immediately before the earliest exchanging taxpayer's disposal time, being the only practical and reliable time. At any earlier time, there may be persons holding units that affect the relevant proportions who will not be disposing of those units under the scheme. Any time after the earliest exchanging taxpayer's disposal time and before the completion time would produce proportions that are distorted by the earlier disposals of exchange units by exchanging taxpayers.

Same trust

76. Paragraph 160ZZPA(1)(j) deals with exchanging taxpayers who are acting in the capacity of a trustee. This paragraph deals with the situation where the exchanging taxpayer is the trustee of a trust estate. This paragraph requires that the taxpayer, immediately after the disposal time, hold the replacement shares on the same trust as the exchange units had been held. This means that the trust property must be held for the same beneficiaries and on the same terms and conditions as before the reorganisation. This paragraph seeks to adopt a tracing rule to ensure that underlying economic ownership is maintained.

77. These provisions may cause some difficulty in the case of a public company or unit trust listed on a stock exchange. The requirement of establishing that this provision is met may involve a tracing of beneficial ownership of a unit or share back to natural persons. For example, the power exists under Part 6.8 of the *Corporations Law* which allows a listed company to enquire as to the beneficial ownership of its shares.

78. We expect that in the case of a public company, the company would take all reasonable steps to ascertain whether beneficial ownership is maintained upon the same trust.

Multiple

79. The word 'multiple' is used in paragraph 160ZZPA(1)(c) and subparagraph 160ZZPB(1)(a)(vii). These provisions require that a certain number of either replacement shares or scheme units are issued.

80. The *Macquarie Dictionary* defines the word 'multiple' to mean: 'a number which contains another number some number of times without a remainder: *12 is a multiple of 3.*'

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81. The Explanatory Memorandum to the *Taxation Laws Amendment Act (No 5) 1987* states, in respect of paragraph 160ZZPA(1)(c):

'Paragraph (c) requires that the total number of replacement shares in the interposed company received by the former unitholders as a result of the re-organisation, equals, or is a multiple of, the total number of exchange units. If there were, for example, 10,000 exchange units, the number of replacement shares needed would be 10,000 or a whole number multiple of 10,000.'

82. The requirement is that the 'multiple' must be a whole number. A fraction being less than one, or a figure which is greater than one and not a whole number, does not satisfy the provision (see Example 4).

Consideration must be non-redeemable shares

83. Section 160ZZPA(1)(b) requires that the consideration in respect of the disposal of the units consist only of non-redeemable shares in the interposed company. These replacement shares must be the only type or form of consideration received by the exchanging taxpayers. The receipt by the exchanging taxpayer of any additional form of consideration, such as 'stapled units', or 'piggyback options', which may be attached or linked to the shares, will not satisfy the requirements of the section (see Example 5).

Consequences of the roll-over relief being unavailable

84. Where roll-over relief is not available we consider that there is a disposal of the units on the reconstruction and that the general provisions of the Act, including Part IIIA, apply.

85. The general income provisions such as subsection 25(1) or section 25A of the Act may apply to the disposal of the units in the unit trust.

86. If the units were acquired by the taxpayer before 20 September 1985, in general, Part IIIA will not apply to the disposal of the shares under the scheme. However, a capital gain may be deemed to accrue to the taxpayer if section 160ZZT applies.

87. If the units were acquired on or after 20 September 1985, their disposal under the scheme will be subject to the provisions of Part IIIA. The consideration in respect of the disposal of these units will be determined under section 160ZD.

88. Further, a change in the underlying ownership of the assets of the unit trust, due to the introduction of persons who did not hold an economic interest in the underlying property before the reconstruction, may cause section 160ZZS to apply on the disposal of the underlying assets previously held by the unit trust.

89. The shares acquired in the interposed company will be subject to the provisions of Part IIIA on their later disposal. The cost base of those shares will be determined under section 160ZH.

90. In the case of a merger, the schemes may effect a change in the underlying interests held by natural persons in the assets of either, or both, of the merging entities. This may cause section 160ZZS to apply to those assets.

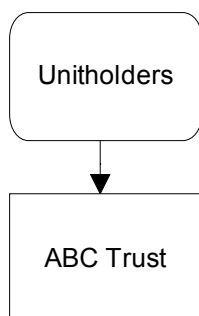
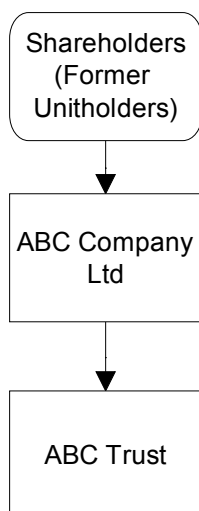
Examples

Example 1

91. A publicly trading unit trust, ABC Trust, proposes to incorporate.

92. This is achieved by the ABC Trust issuing units to a newly formed company with only two issued shares and assets of two dollars, ABC Company Ltd. ABC Trust then cancels all the remaining units and in consideration for the cancellation, ABC Company Ltd issues the same number of shares to the former unitholders as the number of units that were cancelled.

93. The respective structures appear as follows:

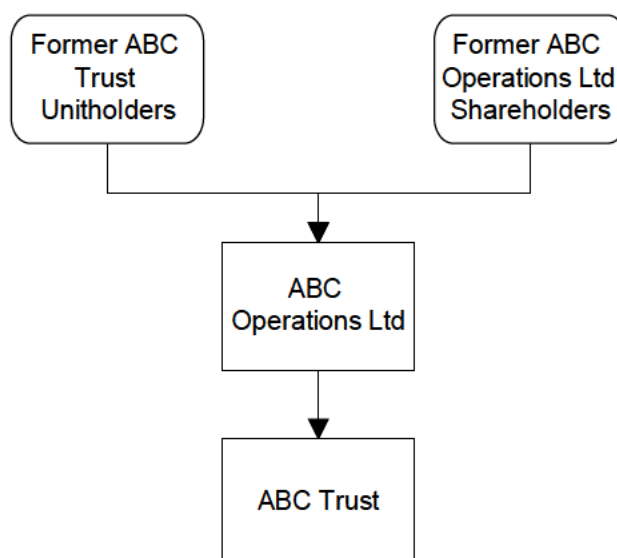
TR 95/D19Pre ReorganisationPost Reorganisation

94. In these circumstances, we consider that roll-over relief under section 160ZZPB is available because the scheme for the reorganisation of the affairs of the unit trust meets all of the operative requirements of the section. In particular, the economic interests of each former unitholder in the underlying assets of the interposed company are maintained after reconstruction.

Example 2

95. The merger is proposed of a publicly listed trading unit trust, ABC Trust, and a public company, ABC Operations Ltd.

96. The first step is for all shareholders in ABC Operations Ltd to acquire units in ABC Trust. These units are acquired by way of dividend declared by the company after the company subscribes for the units. The dividend is satisfied by the distribution of those units in specie to the shareholders. ABC Operations Ltd then acquires all the issued units of the ABC Trust thereby wholly owning the trust. In consideration for the acquisition of the units, ABC Operations Ltd will issue a proportionate number of shares to the former unitholders of the ABC Trust. The resultant structure appears as follows:



97. In these circumstances, we consider that roll-over relief under section 160ZZPA is **not** available for the proposed arrangement. Apart from the fact that this merger is not considered to be for the reorganisation of the affairs of a unit trust, the operative requirements of section 160ZZPA are not satisfied. Before the reorganisation the former ABC Trust unitholders held 100% of the trust. However, as the shareholders in ABC Operations Ltd maintain their shares in the interposed company (ABC Operations Ltd) the requirement that the only shares of the interposed company on issue at the completion time is not met.

98. It is noted that the requirement of subparagraph 160ZZPA(1)(e)(i) is only satisfied because the original shareholders in ABC Operations Ltd acquired the units by way of a dividend declared immediately before the time at which identification of the exchanging taxpayers is made.

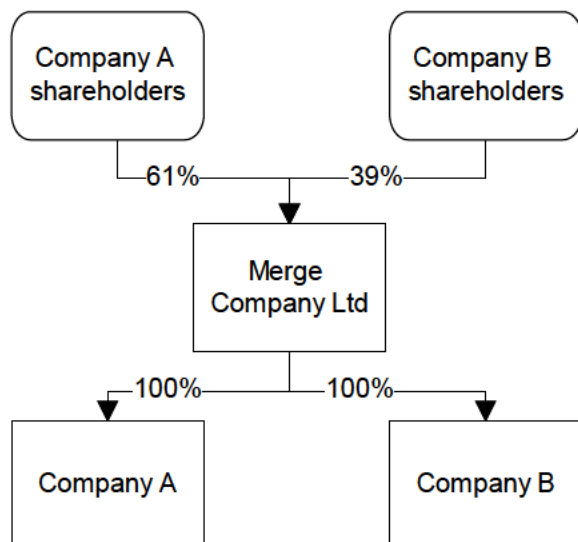
Example 3

99. It is proposed that two Schemes of Arrangement (one for each company) be undertaken independently, under section 411 of the *Corporations Law*, in order to effect a merger.

100. This is achieved by Company A issuing a nominal number of shares (but less than five) to Merge Company Ltd. Company A then cancels the other issued capital, and in consideration for the cancellation, Merge Company Ltd issues shares to the former shareholders in proportion to their former shareholdings in Company A. Company A then issues to Merge Company Ltd the same number of shares that were cancelled. The same process is repeated by Company B.

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101. The resultant structure appears as follows:



102. In these circumstances, we consider that roll-over relief under section 160ZZPB is not available for the proposed arrangement. Because the former shareholders in both Company A and Company B become the shareholders in Merge Company Ltd it is not possible for them to maintain the proportionate interests they previously held in the respective companies before the change. Further, the requirement of subparagraph 160ZZPB(1)(e)(i) is not satisfied because the exchanging taxpayers in respect of each company are not the holders of all the shares in Merge Company Ltd, shares also being held by the exchanging taxpayers of the other company. In addition, the scheme does not meet the requirement of being a reorganisation of the affairs of a company, as there is more than one company involved in these schemes.

Example 4

103. A scheme is proposed whereby a company will be interposed between a unit trust and its unitholders. To effect the interposition the following steps are taken. The trustee of the unit trust issues five formal units in the trust to the company. The company issues shares in the company to the unitholders in the unit trust as consideration for the redemption of their units. The trustee of the unit trust redeems all existing units currently held in the unit trust with the exception of those issued to the company. The trustee of the unit trust issues new units to the company. Before the scheme the 75 units on issue in the

unit trust were held by Jack (10 units), Ted (15 units) and Patricia (50 units).

104. The number of shares to be issued is determined in accordance with the trust deed which stipulates a formula which takes into account the current value of a unit (U), stamp duty in respect of the redemption and allotments required under the scheme (S) and the value of a replacement share (R). The result is then rounded down to the nearest whole number.

The formula is: Number of shares per unit = (U-S)/R

105. The value of the units is \$1, the attributable stamp duty to each unitholder \$0.02 and the value of a share \$2. The result is that, for every unit held in the unit trust, a multiplication factor of 0.49 is applied in determining the number of shares each unitholder is to be allotted.

106. For this reason, it is not possible to satisfy the requirement of paragraph 160ZZPB(1)(c) as the requirement is that the multiple be a whole number.

107. Further, the act of rounding down will mean that the 'same proportion' test of paragraph 160ZZPB(1)(k) is not met. The former unitholders will not hold the replacement shares in the company in the same proportions as they held the units in the unit trust that were redeemed. The table below illustrates this point:

	Units	%	Units times 0.49	Rounded down (Shares)	%
Jack	10	13.3	4.9	4	11.4
Ted	15	20	7.35	7	20
Patricia	50	66.7	24.5	24	68.6
Total	75	100		35	100

Example 5

108. Sunshine Unit Trust wholly owns the asset-rich company Paradise Pty Ltd. Acme Ltd wants to acquire Paradise Pty Ltd from Sunshine Unit Trust. It uses a shelf company, Leon Pty Ltd as the acquisition vehicle.

The steps in acquisition of Paradise Pty Ltd involved the cancellation of the shares held by Sunshine Unit Trust in Paradise Pty Ltd and the

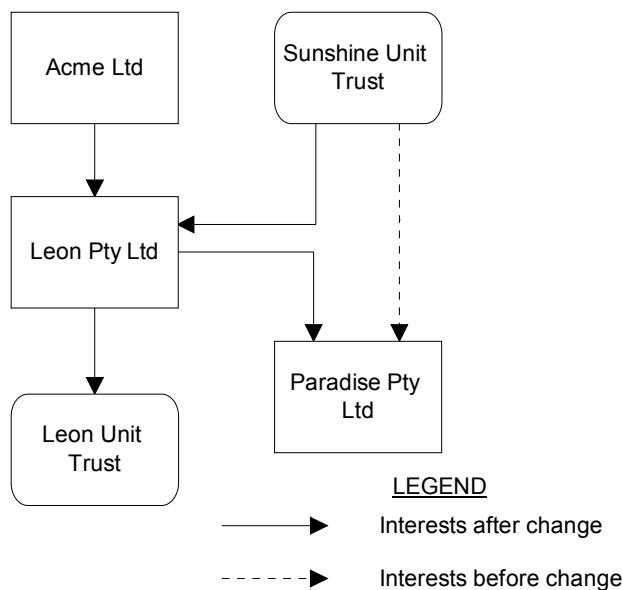
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replacement of those shares with Leon Pty Ltd shares stapled to units in a unit trust (Leon Unit Trust) wholly owned by Leon Pty Ltd.

The shares and units are able to be traded as a single security, or may be traded independently.

Following the reorganisation Acme Ltd and Sunshine Unit Trust had effectively merged (due to the merging of the securities).

The unitholders in Sunshine Unit Trust and the shareholders in Acme Ltd have acquired new interests.



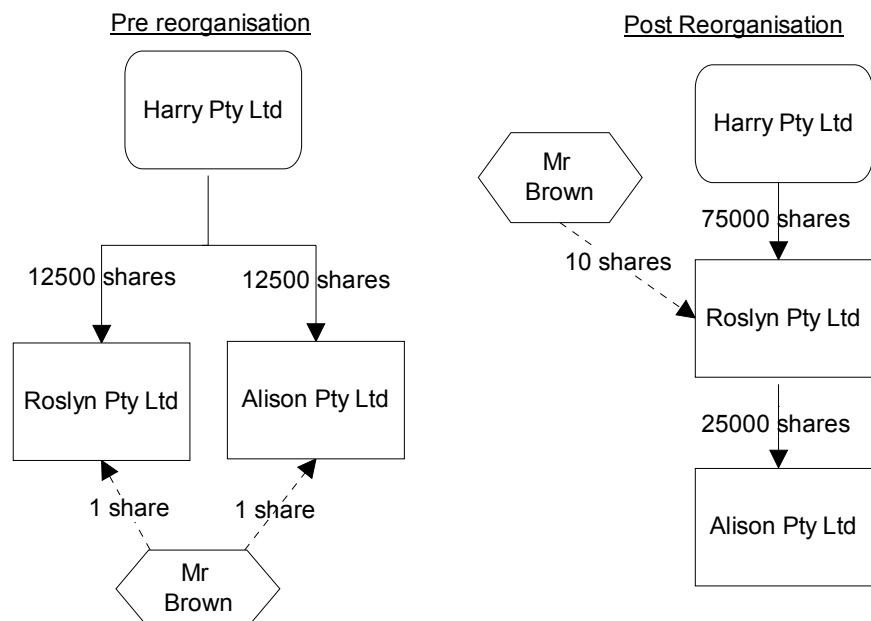
109. This scenario does not qualify for roll-over relief as three requirements of subsection 160ZZPB(1) have not been satisfied. Paragraphs 160ZZPB(1)(b) [only non redeemable shares], (e)[the exchanging unitholders do not hold all the Leon Pty Ltd shares] and (m) [market value ratios] have not been satisfied.

Example 6

110. The Harry Group reorganises its internal structure in order to facilitate the acquisition of key assets. The details of the actions of the group are:

- Dec 1989 Harry Pty Ltd purchased a shelf company Roslyn Pty Ltd by acquiring the two shares on issue.
- Oct 1990 Alison Pty Ltd issued 12501 shares. 12500 shares to Harry Pty Ltd and 1 share to Mr Brown who is acting as trustee for Harry Pty Ltd.

- June 1991 Roslyn Pty Ltd issued 12499 shares. 12498 shares to Harry Pty Ltd and 1 share to Mr Brown who is acting as trustee for Harry Pty Ltd.
- July 1991 Roslyn Pty Ltd's board of directors approved that company's acquisition of Alison Pty Ltd. The consideration for the acquisition consisted of 5 shares in Roslyn Pty Ltd for every share in Alison Pty Ltd held.



111. In these circumstances roll-over relief is not available, as the proportions test contained in paragraph 160ZZPC(1)(k) has not been satisfied (refer to paragraph 16 of this Ruling). Not all shares on issue by Roslyn Pty Ltd are replacement shares.

NOTE: provided the conditions of section 160ZZO have been satisfied, roll-over relief is available under that section for this scheme.

Your comments

112. If you wish to comment on this Draft Ruling, please send your comments by: 13 October 1995

to:

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FOI status: draft only - for comment

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Commissioner of Taxation

30 August 1995

ISSN	1039 - 0731	- ITAA 160ZZPA(1)
		- ITAA 160ZZPA(1)(a)
		- ITAA 160ZZPA(1)(a)(i)\
ATO references		- ITAA 160ZZPA(1)(b)
NO	NAT 95/6430-6	- ITAA 160ZZPA(1)(c)
BO	BAN TR 3	- ITAA 160ZZPA(1)(d)
		- ITAA 160ZZPA(1)(e)
Not previously released to the public in draft form		- ITAA 160ZZPA(1)(e)(i)
		- ITAA 160ZZPA(1)(f)
		- ITAA 160ZZPA(1)(j)
Price	\$2.80	- ITAA 160ZZPA(1)(k)
		- ITAA 160ZZPA(1)(m)
FOI index detail		- ITAA 160ZZPA(2)(c)
<i>reference number</i>		- ITAA 160ZZPA(2)(d)
		- ITAA 160ZZPA(10)
		- ITAA 160ZZPA(10)(a)
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