

TD 2001/D9 - Income tax: capital gains: what is the first element of the cost base and reduced cost base of a share in a company you acquire in exchange for a share in another company in a takeover or merger?

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This document has been finalised by TD 2002/4.

Draft Taxation Determination

Income tax: capital gains: what is the first element of the cost base and reduced cost base of a share in a company you acquire in exchange for a share in another company in a takeover or merger?

Preamble

Draft Taxation Determinations (DTDs) present the preliminary, though considered, views of the Australian Taxation Office. DTDs should not be relied on; only final Taxation Determinations represent authoritative statements by the Australian Taxation Office.

General

1. If property other than money is given in respect of acquiring a CGT asset, the first element of the asset's cost base and reduced cost base (that is, broadly speaking, the asset's acquisition cost) is the market value of that property at the time of acquisition (paragraph 110-25(2)(b) of the *Income Tax Assessment Act 1997*).
2. If you acquire shares by issue or allotment, the time of acquisition is when you enter into the contract to acquire the shares or, if you acquire them other than under a contract, when the shares are issued or allotted (section 109-10 item 2).

Takeover offer

Unconditional takeover offer

3. If you accept an unconditional takeover offer from a 'bidder' company for your shares in a 'target' company, and the capital proceeds for your 'target' company shares are shares in the 'bidder' company, you are taken to have acquired the 'bidder' company shares for the market value of your 'target' company shares as at the time you enter into the contract to acquire the 'bidder' company shares, that is, when you accept the offer.

Example

4. Aaron owns 100 shares in XYZ Ltd. ABC Ltd makes an unconditional takeover offer to acquire XYZ Ltd, exchanging 2 shares in XYZ Ltd for each share in ABC Ltd. Each share in XYZ Ltd is worth \$4.50 at the time of the offer. Aaron accepts the offer. At the time Aaron accepts the offer the market value of an XYZ Ltd share is \$4.40. The first element of the cost base and reduced cost base of each ABC Ltd share is \$8.80 (i.e., 2 x \$4.40). If the market value of an XYZ Ltd share

was \$4.60 at the time Aaron accepted the offer, the first element of the cost base and reduced cost base for each ABC Ltd share would have been \$9.20.

Effect of contractual conditions

5. The existence of a contractual condition (for example, the contract is subject to the ‘bidder’ company acquiring 90% of the shares in the ‘target’ company) will not generally affect the time when the contract is entered into. The contract will usually be made when the offer is accepted and not when it becomes unconditional.

6. However if an offer from a ‘bidder’ company for shares in a ‘target’ company is one which is subject to a condition precedent to the creation of the contract, the date of acquisition of the ‘bidder’ company shares will be the later of the date that the condition is met or the offer is accepted. [For further information see, for example, *Perri & anor v. Coolangatta Investments Pty Ltd* (1982) 149 CLR 537.]

Scheme of arrangement

7. If the ‘bidder’ company shares are acquired under a court ordered scheme of arrangement, the first element of their cost base and reduced cost base will be determined having regard to the market value of the ‘target’ company shares on the date that the scheme of arrangement becomes effective.

Special scrip for scrip roll-over rules

8. Special rules apply to the calculation of the cost base of shares acquired under a scrip for scrip roll-over if the provisions contained in Subdivision 124-M apply.

9. If a full roll-over is chosen, the first element of the cost base of shares in the ‘bidder’ company is determined by reasonably attributing to them a portion of the cost base of the shares in the ‘target’ company that were exchanged for the ‘bidder’ company shares (subsection 124-785(2)).

Example

10. *Able exchanges 1 share in Small Co. with a cost base of \$9 for a class X share and a class Y share in Big Co. An X class share in Big Co. has a market value of \$5 and a Y class share has a market value of \$10. The first element of the cost base of the shares would be \$3 and \$6 respectively.*

Target company shares acquired before 20 September 1985

11. In some scrip for scrip arrangements if the shares in ‘target’ company were acquired before 20 September 1985, the first element of the cost base and reduced cost base of the shares in the ‘bidder’ company will be their market value just after acquisition (subsection 124-800(1)).

12. The first element of the cost base or reduced cost base of the shares in the ‘bidder’ company is determined in this manner if they were acquired in consequence of an arrangement that satisfies the conditions in subsection 124-780(2). It is not necessary that the arrangement be one for which a shareholder actually chooses a roll-over.

Note 1:

13. This draft Taxation Determination rewrites and, when it is finalised, will replace, CGT Determination TD 39.

Note 2:

14. This draft Taxation Determination does not consider how the first element of the cost base and reduced cost base would be calculated if the capital proceeds for the ‘target’ company shares includes something other than shares in the ‘bidder’ company.

Your comments

15. We invite you to comment on this Draft Taxation Determination. We are allowing 4 weeks for comments before we finalise the Determination. If you want your comments considered, please provide them to us within this period.

Comments by date: 7 December 2001
Contact officer: Lyn Freshwater
E-mail address: lyn.freshwater@ato.gov.au
Telephone: (07) 3213 5554
Facsimile: (07) 3213 5971
Address: GPO Box 9990
BRISBANE QLD 4001

Commissioner of Taxation7 November 2001

Previous draft:

Not previously issued in draft form

Subject references:

- acquisition
- acquisition cost
- capital gain
- contract
- cost base
- exchange
- first element
- merger
- reduced cost base
- roll-over
- share
- scheme of arrangement
- scrip
- scrip for scrip roll-over
- takeover
- time of acquisition

Legislative references:

- ITAA 1997 109-10 item 2
- ITAA 1997 110-25(2)(b)
- ITAA 1997 Subdivision 124-M
- ITAA 1997 124-780(2)
- ITAA 1997 124-785(2)
- ITAA 1997 124-800(1)

Case references:

Perri & anor v. Coolangatta Investments Pty Ltd (1982) 149 CLR 537

ATO references:

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