



# ***PR 2018/7 - Income tax: tax consequences of investing in PTrackERS***

 This cover sheet is provided for information only. It does not form part of *PR 2018/7 - Income tax: tax consequences of investing in PTrackERS*

 This document has changed over time. This is a consolidated version of the ruling which was published on *5 September 2018*



## Product Ruling

# Income tax: tax consequences of investing in PTrackERS

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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.

## **No guarantee of commercial success**

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The Commissioner **does not** sanction or guarantee this product. Further, the Commissioner gives no assurance that the product is commercially viable, that charges are reasonable, appropriate or represent industry norms, or that projected returns will be achieved or are reasonably based.

Potential participants must form their own view about the commercial and financial viability of the product. The Commissioner recommends a financial (or other) adviser be consulted for such information.

This Product Ruling provides certainty for potential participants by confirming that the tax benefits set out in the **Ruling** part of this document are available, **provided that** the scheme is carried out in accordance with the information we have been given, and as described below in the **Scheme** part of this document. If the scheme is not carried out as described, participants lose the protection of this Product Ruling.

## **Terms of use of this Product Ruling**

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This Product Ruling has been given on the basis that the entity(s) who applied for the Product Ruling, and their associates, will abide by

strict terms of use. Any failure to comply with the terms of use may lead to the withdrawal of this Product Ruling.

## **What this Ruling is about**

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1. This Product Ruling sets out the Commissioner's opinion on the way in which the relevant provisions identified in the Ruling section are applied to the defined class of entities, who take part in the scheme to which this Ruling relates.
2. All legislative references in this Ruling are to the *Income Tax Assessment Act 1997* (ITAA 1997) unless otherwise indicated. In this Product Ruling, terms defined in the documents listed at paragraph 18 have been capitalised.
3. In this Product Ruling, the scheme is an investment in exchangeable notes called Portfolio Tracking Exchangeable Redeemable Securities (Converting Security), (PTrackERS), which are offered under the Prospectus by PM Capital GO 2025 Limited (the Company), a newly incorporated company which is a wholly owned Australian subsidiary of PM Capital Global Opportunities Fund Limited (the Parent Company).
4. This Product Ruling does not address:
  - (a) the tax consequences of any financial accommodation or borrowing funds to acquire a PTrackERS, including the deductibility of interest on funds borrowed to acquire the PTrackERS.
  - (b) the tax consequences of a transfer of the PTrackERS.
  - (c) the tax consequences if the Offer is withdrawn and Application Monies are refunded to Applicants.
  - (d) the tax consequences of a Securityholder upon the occurrence of a Change in Control Event.
  - (e) the tax consequences of how the gross-up and tax offset rules in Division 207 apply where a franked Distribution is made to a partnership or trustee or an entity to whom a franked Distribution flows indirectly (as defined in subsection 995-1(1)).

### **Class of entities**

5. This part of the Product Ruling specifies which entities can rely on the Ruling section of this Product Ruling and which entities cannot rely on the Ruling section. Those entities that can rely on the Ruling section are referred to in this Product Ruling as the Securityholder.

6. The class of entities who can rely on the Ruling section of this Product Ruling consists of those entities:

- that are accepted to participate in the scheme specified below on or after the date this Product Ruling is made and on or before the later of the Entitlement, General Public or Broker Firm Offer Closing Date, and
- that have a purpose of staying in the scheme until it is completed (that is, being a party to the terms of the PTrackERS until the Maturity Date).

7. The class of entities who can rely on the tax benefits set out in the Ruling section of this Product Ruling does not include entities that:

- intend to terminate their involvement in the scheme prior to its completion
- are accepted into this scheme before the date of this Ruling or after the later of the Entitlement, General Public or Broker Firm Offer Closing Date
- are non-residents for Australian taxation purposes
- trade in financial instruments or securities and are treated for taxation purposes as trading in PTrackERS, carrying on a business of investing in the PTrackERS, or holding the PTrackERS as trading stock
- are subject to Division 230 in respect of this scheme. Division 230 will generally not apply to individuals, unless they have made an election for it to apply to them, or
- participate in the scheme through offers made other than through the Prospectus, or who enter into an undisclosed arrangement with the promoter or a promoter associate, or an independent adviser that is interdependent with scheme obligations and/or scheme benefits (which may include tax benefits) in any way.

### ***Superannuation Industry (Supervision) Act 1993***

8. This Product Ruling does not address the provisions of the *Superannuation Industry (Supervision) Act 1993* (SISA). The Commissioner gives no assurance that the scheme is an appropriate investment for a superannuation fund. The trustees of superannuation funds are advised that no consideration has been given in this Product Ruling as to whether investment in this scheme may contravene the provisions of SISA.

## Qualifications

9. The class of entities defined in this Product Ruling may rely on its contents provided the scheme actually carried out is carried out in accordance with the scheme described in paragraphs 18 to 45 of this Ruling.

10. If the scheme actually carried out is materially different from the scheme that is described in this Product Ruling, then:

- This Product Ruling has no binding effect on the Commissioner because the scheme entered into is not the scheme on which the Commissioner has ruled
- This Product Ruling may be withdrawn or modified.

## Date of effect

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11. This Product Ruling applies prospectively from 11 July 2018, the date it published. It therefore applies only to the specified class of entities that enter into the scheme from 11 July 2018 until 30 June 2021, being its period of application. This Product Ruling will continue to apply to those entities even after its period of application has ended for the scheme entered into during the period of application.

12. However the Product Ruling only applies to the extent that there is no change in the scheme or in the entity's involvement in the scheme.

## Changes in the law

13. Although this Product Ruling deals with the income tax laws enacted at the time it was issued, later amendments may impact on this Product Ruling. Any such changes will take precedence over the application of this Product Ruling and, to that extent, this Product Ruling will have no effect.

14. Entities who are considering participating in the scheme are advised to confirm with their taxation adviser that changes in the law have not affected this Product Ruling since it was issued.

## Note to promoters and advisers

15. Product Rulings were introduced for the purpose of providing certainty about tax consequences for entities in schemes such as this. In keeping with that intention the Commissioner suggests that promoters and advisers ensure that participants are fully informed of any legislative changes after the Product Ruling has issued.

## Ruling

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16. Subject to paragraph 4 of this Product Ruling and the assumptions in paragraph 45 of this Ruling:

- (a) The Securityholder's interest in the Company (being the PTrackERS) is a non-share equity interest (as defined in subsection 995-1(1)).
- (b) The scheme as described in paragraphs 18 to 45 of this Product Ruling gives rise to the Securityholders having an equity interest in the Company for the purpose of Division 974.
- (c) A Distribution not paid out of Taxable Profits is a non-share capital return as defined in section 974-125, to the extent to which it is not a non-share dividend as defined in section 974-120.
- (d) A Distribution received by the Securityholder, which is not paid out of Taxable Profits, is not assessable and is a recoupment and will not form part of any element of the cost base (or reduced cost base) of the PTrackERS under subsections 110-45(3) and 110-55(6). This effectively means that the part of the Issue Price returned to the Securityholder by way of this Distribution is taken to have never formed part of the cost base (or reduced cost base) of the PTrackERS.
- (e) Distributions paid out of Taxable Profits which are non-share dividends under section 974-120 are included as assessable income of the Securityholder under section 44 of the *Income Tax Assessment Act 1936* (ITAA 1936).
- (f) The Securityholder will include in their assessable income an amount equal to the franking credits attached to the franked distribution as per subsection 207-20(1).
- (g) The Securityholder will be entitled to a tax offset equal to the franking credit received on Distributions paid in respect of the PTrackERS under subsection 207-20(2), where the Securityholder is a qualified person for the purposes of former Division 1A of Part IIIAA of the ITAA 1936 in respect of a franked distribution.
- (h) Securityholders who are entitled to a tax offset under subsection 207-20(2), in respect of the franking credits received in relation to the PTrackERS, will be subject to the refundable tax offset rules in Division 67, unless they are specifically excluded under section 67-25.

- (i) The Distributions paid in respect of the PTrackERS are not part of a dividend stripping operation under section 207-155 of the ITAA 1997.
- (j) 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 Securityholder in relation to the Distributions paid in respect of the PTrackERS.
- (k) PTrackERS are not considered to have sufficient debt like obligations to be contracts to which the definition of security under paragraph 159GP(1)(d) of the ITAA 1936 applies, nor do they fall within paragraphs (a), (b) or (c) of that definition.
- (l) For the purpose of section 26BB and section 70B of the ITAA 1936, the PTrackERS are not considered to be traditional securities.
- (m) PTrackERS held by the Securityholder are CGT assets under subsection 108-5(1). Each PTrackERS is a convertible interest.
- (n) CGT event C2 (section 104-25 of the ITAA 1997) will happen for Securityholders on redemption of the PTrackERS.
- (o) CGT event C2 (section 104-25 of the ITAA 1997) will happen for Securityholders on Exchange of the PTrackERS for Shares. However any capital gain or capital loss made by a Securityholder from CGT event C2 happening on Exchange of the PTrackERS will be disregarded (subsection 130-60(3) of the ITAA 1997).
- (p) The cost base or reduced cost base of the Parent Company shares acquired by a Securityholder should include the Issue Price (subsection 130-60(1) of the ITAA 1997).
- (q) The Securityholder will be taken to have acquired the Shares when the Exchange happens (subsection 130-60(2)) of the ITAA 1997).
- (r) Section 45 of the ITAA 1936 will not apply to treat the Shares issued on Exchange as an unfrankable dividend paid by the Parent Company.
- (s) 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 any part, of a capital benefit that arises on Exchange or Redemption of the PTrackERS as an unfranked dividend in the hands of Securityholders.

- (t) The Commissioner will not make a determination under subsection 45B(3)(b) of the ITAA 1936 that section 45C of the ITAA 1936 applies to treat the whole, or any part, of a capital benefit that arises on Exchange or Redemption of the PTrackERS as an unfranked dividend in the hands of Securityholders.

17. Provided the scheme ruled on is entered into and carried out as described in this Product Ruling, the anti-avoidance provisions in Part IVA of the ITAA 1936 will not apply to the Securityholder. The Commissioner will therefore not make a determination under paragraph 177EA(5)(b) of the ITAA 1936 to deny any imputation benefits referred to in subparagraphs 16(g) and 16(h) of this Product Ruling which arises in respect of a franked distribution that flows directly or indirectly to the Securityholder.

## Scheme

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18. The scheme that is the subject of this Product Ruling is identified and described in the following documents:

- Application for a Product Ruling as constituted by documents and information received on 28 March 2018.
- Draft PTrackERS terms contained in Annexure 1 of Exchangeable Securities Trust Deed received on 22 June 2018 (**Conditions**).
- Draft Prospectus for the PTrackERS received on 21 June 2018.

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

19. All Australian Securities and Investments Commission (ASIC) requirements are, or will be, complied with for the term of the agreements.

20. For the purposes of describing the scheme to which this Ruling applies, there are no other agreements, whether formal or informal, and whether or not legally enforceable, which a Securityholder, or any associate of a Securityholder, will be a party to, which are a part of the scheme.

### The offer of PTrackERS

21. In the Prospectus, the Company announced its intention to undertake an offer of up to 350,909,977 PTrackERS to raise up to AUD \$491,273,967.80 (the Offer).

22. The PTrackERS are fully paid, unsecured exchanging securities.
23. The classes of applicants who may apply for PTrackERS are:
- (a) Parent Company Shareholder Applicant – a holder of ordinary shares in the Parent Company as of the relevant record date with a registered address in Australia (or New Zealand) as disclosed on Parent Company’s register of shareholders applying through the Entitlement Offer by the Entitlement Offer Closing Date.
  - (b) General Public Offer or Broker Offer Applicant – other applicants with a registered address in Australia or New Zealand that apply through the General Public Offer or who receive a firm allocation from their stockbroker or financial adviser through the Broker Firm Offer.
24. PTrackERS shall only be offered to Securityholders who are Australian residents or domiciled in Australia except where required by Australian Securities Exchange (ASX) Listing Rule 7.7 to be offered to New Zealand domiciled investors: see Condition 2.2(d) of the Conditions.

## **Reasons for issuing PTrackERS**

25. The Parent Company is an ASX-listed company (LIC) (ASX code: PGF).
26. The Parent Company’s investment objective is to provide long term capital growth over a seven year plus investment horizon through investment in a portfolio of global equities and other investment securities.
27. The primary objective of the proposed transaction is to provide investors an economic interest which resembles LIC common equity, whereby it provides direct exposure to the investment performance of an underlying portfolio of shares, but, after a time period consistent with the investment manager’s investment horizon of seven years, has a catalyst to trade on the stock exchange at a value which is reflective to the portfolio’s net asset value (NAV) per security.
28. In this regard, while there is no certainty as to whether the NAV may increase or decrease over seven years, the only catalyst to cause the security price to trade at NAV in seven years’ time, whatever the NAV may be, is for the Company to buy back the securities at NAV where the Securityholder elects to participate. Furthermore, by bringing the trading price of the proposed LIC securities in line with NAV over the long term, this is intended to provide a positive stimulus to the trading level of the Parent Company’s shares generally.

29. The secondary objective of the proposed transaction is to facilitate the raising of non-dilutionary capital by the fresh issue of interests in (or associated with) the current PM LICs.
30. The proposed strategy includes the issue of a new series of interests which will track a portfolio which is similar (but not identical) to the current PM Capital LIC portfolios, managed with a seven year horizon, consistent with the PM Capital LIC's recommended investment horizon.
31. The PTrackERS are intended to function, in economic terms, as if Securityholders were the holders of a class of the Parent Company shares (with the value calculated by reference to the Company's portfolio).
32. The Parent Company has established the Company to issue the PTrackERS.
33. The Company will use the funds raised from the issue of the PTrackERS to acquire a portfolio of interests in undervalued companies (Portfolio) which track a portfolio similar (but not identical) to Parent Company's portfolio.
34. There will be a dividend stopper (Dividend Stopper) in respect of common shares of the Company while the PTrackERS remain outstanding.

### **Terms of PTrackERS**

35. The details of the PTrackERS are summarised as follows:
- (a) The Issue Price of each PTrackERS is \$1.40 and on issue is fully paid.
  - (b) The investment term is approximately seven years (except to the extent that the Securityholder exchange their PTrackERS at the Maturity Date).
  - (c) PTrackERS shall be transferable at any time in accordance with Condition 5 of the Conditions.
  - (d) Pursuant to Condition 3.1, a Securityholder may elect that the PTrackERS be redeemed by the Company in the manner and at the times provided by Conditions 3.2 to 3.7.
  - (e) Subject to the Securityholder making a redemption election (see paragraphs 42 and 44 of this Product Ruling), the PTrackERS held by a Securityholder will automatically exchange in the manner and at the times provided by Condition 3 of the Conditions into Shares at the Exchange Rate (see paragraphs 40 and 41 of this Product ruling).
  - (f) PTrackERS are not redeemable at the option of the Company, unless required by law or Listing Rules, in

accordance with Condition 3.16 or if the Parent Company is delisted.

- (g) If a Change in Control Event occurs prior to the Maturity Date, PTrackERS may be redeemed or exchanged before the Maturity Date, in accordance with Condition 3.7 of the Conditions. This Ruling does not consider the tax consequences of an early redemption or exchange as a result of a Change in Control Event.
- (h) A Securityholder can apply to acquire the PTrackERS by submitting a completed Application Form to the Company by the Entitlement Offer Closing Date, General Public Offer Closing Date or Broker Firm Offer Closing Date. On payment by the Taxpayer of the Application Monies to the Company, the Taxpayer agrees to be bound by the terms of the PTrackERS set out in Section 6 of the Prospectus.
- (i) If the Company or the Parent Company becomes an externally-administered body corporate (within the meaning of the *Corporations Act 2001*) and notwithstanding any other provision of the PTrackERS terms, there will be automatic early redemption, with the redemption to occur within 10 Business Days (and any other future entitlements to Exchange or redemption shall thereupon cease).

## **Distributions (other than the Final Distribution)**

36. At each Distribution Payment Date, the Board of the Company will determine, at its discretion, whether or not:

- (a) subject to the Company having profits, a Distribution will be paid out of profits of the Company, and/or
- (b) a Distribution will be paid as a return of Capital Amount in respect of the PTrackERS

with the total Distributions payable (if any) not to exceed the Target Distribution.

37. The Board of the Company cannot make Distributions to a Securityholder more frequently than semi-annually. Generally the Company intends to target a yield between 3% to 4% per annum based on an expected semi-annual Distribution Payment Amount equal to the Target Distribution (being between 1.5% to 2% multiplied by the average of the previous 6-month end NTA After Tax Liabilities But Before Tax Assets per PTrackERS, prior to declaration of the Distribution).

38. Subject to paragraph 37 above, the commercial objective is to make Distributions (other than the Final Distribution) every six months, around March and September each year consistent with

when Parent Company pays its common equity interim and final dividends.

39. Payments made by the Company in respect of the PTrackERS which are non-share dividends, will be made where the amount of the non-share dividend is equal to or greater than the available frankable profits of the Company.<sup>1</sup>

### **Exchange**

40. Unless the Securityholder elects for the Company to redeem the PTrackERS, the Securityholder agrees to exchange the PTrackERS with the Parent Company for Shares in the Parent Company.

41. Upon exchange by the Securityholder, the Parent Company will hold the PTrackERS. Following an Exchange Date, the Parent Company will have the same redemption rights as Securityholders prior to the Exchange Date, except that the Maturity Date will be replaced by a date nominated by the Parent Company.

### **Redemption and Final Distribution**

42. If the Securityholder makes an election to have the Company redeem the PTrackERS:

- (a) Subject to the discretion of the Board of the Company and the Company having sufficient profits, prior to redemption a Final Distribution may be paid by the Company calculated as the greater of:
  - (i) NTA After Tax Liabilities But Before Tax Assets per PTrackERS – Capital Amount, and
  - (ii) Zero.
- (b) The Company will redeem the PTrackERS for the Redemption Price. The Redemption Price means the lesser of:
  - (i) The Capital Amount less \$0.01 per redeeming PTrackERS, or
  - (ii) The NTA After Tax Liabilities But Before Tax Assets per redeeming PTrackERS.

43. For those Securityholders that elect to redeem their PTrackERS, the Company intends to announce the Final Distribution, within 3 Business Days after the Maturity Date.

44. All PTrackERS that are redeemed by the Company will be cancelled and not re-issued.

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<sup>1</sup> Section 215-15 provides that where the available frankable profits of the entity is nil, less than nil or less than the amount of the non-share dividend amount, then the whole or a portion of the non-share dividend will be an unfrankable distribution.

## Assumptions

45. This Product Ruling is made on the basis of the following assumptions:

- (a) The Distributions on the PTrackERS will be frankable distributions pursuant to section 202-40 of the ITAA 1997 and are not unfrankable under section 202-45 of the ITAA 1997, except to the extent debited to the Company's non-share capital account and except to the extent that the distributions are unfrankable under section 215-15 of the ITAA 1997 as non-share dividends that exceed available frankable profits.
- (b) The share capital account of the Company will not become tainted by an issue of the PTrackERS.
- (c) The Securityholders are not traders in financial instruments or securities and are not treated for taxation purposes as trading in PTrackERS or Shares, carrying on a business of investing in the PTrackERS or Shares, or holding the PTrackERS or Shares as trading stock.
- (d) Any Distribution paid out of Taxable Profits will not be debited against the Company's share capital account or non-share capital account, and these Distributions will not be sourced, directly or indirectly from the Company's share capital account or non-share capital account.
- (e) The Issue Price will be credited to the Company's non-share capital account: see Division 164 of the ITAA 1997.
- (f) Any Distribution which is paid as a return of Note Capital in accordance with Condition 3.19(b) of Annexure 1 of the Deed and the Redemption Price will be debited to the Company's non-share capital account.
- (g) Neither a Securityholder, nor its associates, will have any 'positions' (within the meaning of former section 160APHJ of the ITAA 1936) in relation to their PTrackERS that would cause the Securityholder not to be a 'qualified person' for the purpose of Division 1A of former Part IIIA of the ITAA 1936.
- (h) Neither a Securityholder, nor its associates, will make any related payments, or be under an obligation to make any related payments, or be likely to make any related payments (within the meaning of former section 160APHN of the ITAA 1936) in relation to the Distributions on the PTrackERS.

- (i) Securityholders in receipt of Distributions on the PTrackERS will have held their PTrackERS 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 Securityholder acquired the PTrackERS and ending on the 90th day after the day on which the PTrackERS go ex-distribution.
- (j) The dividend payout ratios and the franking credits arising in relation to the Parent Company ordinary shares are not expected to change as a result of the issue of PTrackERS.
- (k) Neither Parent Company nor the Company are authorised deposit-taking institutions (ADI): see the *Banking Act 1959*.
- (l) The ASX will grant permission for the PTrackERS to be quoted on the ASX under the ASX code 'P25PA'.
- (m) The Company will not issue any other securities.
- (n) The Company intends to frank PTrackERS distributions of Taxable Profits to the maximum extent possible (and at a minimum of 10%).
- (o) The Company cannot claim a tax deduction in another country for the returns on the PTrackERS.
- (p) The scheme will be executed in the manner described in the Scheme section of this Ruling and the scheme documentation mentioned in paragraph 18 of this Ruling.

## 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.*

### Debt Interest v. Equity Interest

46. A non-share equity interest is defined under section 995-1 to mean an equity interest in the company that is not solely a share.

47. Paragraph (b) of item 4 of the table in subsection 974-75(1) of the ITAA 1997 provides that an interest is an equity interest if it is an interest issued by the company that is an interest that will, or may, convert into an equity interest in the company or a connected entity of the company.

48. The PTrackERS may be converted into an ordinary share in the Parent Company of the Company. Therefore PTrackERS are equity interests under paragraph (b) of item 4 of the table in subsection 974-75(1).

49. For the PTrackERS to be an equity interest, the scheme must be a 'financing arrangement' for the company, and the relevant interest may take the form of a proprietary right, a chose in action or any other form (subsection 974-75(2) and subsection 974-75(3)).

50. The PTrackERS satisfy the equity test in relation to Company because:

- (a) the Securityholder has the right to an ordinary share in a connected entity, the Parent Company, and
- (b) the 'scheme' is a 'financing arrangement' for the Company as it enables the Company to raise finance similar to the example in paragraph 974-130(2)(c)).

51. The PTrackERS can only be an equity interest if they are not a debt interest. An important requirement of a debt interest is that the entity that issues the debt instruments will have an effectively non-contingent obligation (ENCO) (as defined in section 974-135) to provide benefits under the scheme and if it is substantially more likely than not that the value of the financial benefits provided will be at least equal to the value of the financial benefits received (paragraph 974-20(1)(d)).

52. The PTrackERS do not have an ENCO requirement in relation to any Distributions which are from Taxable Profits as they are conditional on the board exercising their discretion to declare the Distributions and on the Company having sufficient Taxable Profits.

53. However the Company has an ENCO to pay the Redemption Price to Securityholders because the Redemption Price is not contingent on the Company making profits or the Board exercising its discretion. The mere fact that the Securityholder has the right to exchange the PTrackERS for shares in Parent Company does not

make the Company's obligation to pay the Redemption Price contingent: subsection 974-135(4).

54. Distributions on the PTrackERS paid by the Company which are not paid out of Taxable Profits may reduce the Redemption Price. However, the Company has an ENCO – and this cannot be reduced by paying a portion of this Redemption Price prior to Redemption as a periodic Distribution.

55. Section 974-35 sets out the manner in which the value of a financial benefit to be provided or received under the scheme is to be calculated.

56. Paragraph 974-35(1)(a) of the ITAA 1997 provides that the value of a financial benefit to be provided or received is to be calculated in nominal terms, if the performance period ends no later than 10 years after the interest arising from the scheme is issued or, in present value terms if the performance period must, or may, end more than 10 years after the interest arising from the scheme is issued.

57. As the PTrackERS has a 7 year term, the financial benefits provided can be determined in nominal terms.

58. The amount of the Redemption Price depends on the NTA. The Redemption Price may be less than the Capital Amount as a result of poor performance of the Company's investment portfolio such that the NTA After Tax liabilities But Before Tax Assets may fall below the Capital Amount. In this regard, it should be noted that in the extreme, the Redemption Price may fall to zero, yet the Company would not be in default of its obligations.

59. It is not substantially more likely than not that the returns paid by the Company to the Securityholders will be at least equal to the Issue Price, given that the total of the Redemption Price and any Distributions which are not paid out of Taxable Profits will always be less than the Issue Price of the PTrackERS.

60. Therefore the PTrackERS are equity interests under Division 974.

61. The Commissioner will not make a determination under section 974-65 that the PTrackERS constitute debt interests for tax purposes.

### **Security**

62. 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.

63. The term 'security' is defined in subsection 26BB(1) of the ITAA 1936 by reference to subsection 159GP(1) of the ITAA 1936. Under 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.

64. The types of securities referred to in paragraph (a) of the definition of 'security' are generally recognised as debt instruments (Taxation Ruling TR 96/14 *Income tax: traditional securities*).

65. Only those contracts that have debt like obligations usually fall under paragraph (d) of the definition of 'security' (TR 96/14).

66. The obligations under the terms of issue of the PTrackERS are not considered to have sufficient debt like obligations to be contracts to which paragraph (d) of the definition of security in subsection 159GP(1) of the ITAA 1936 applies, nor do they fall within paragraphs (a), (b) or (c) of that definition. Therefore, the PTrackERS do not meet the definition of security under subsection 159GP(1).

## **Distributions (including Final Distribution)**

67. Any Distributions made by the Company from Taxable Profits to the Securityholder will be included as assessable income of the Securityholder.

## **Section 44: Dividends**

68. 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.

69. The PTrackERS are 'non-share equity interests' as defined in subsection 995-1(1) of the ITAA 1997. Paragraph 43B(1)(a) of the ITAA 1936 provides that Subdivision D of Division 2 of Part III of the ITAA 1936 (which governs dividends) applies to a non-share equity interest in the same way that it applies to a share.

70. The Securityholders are 'equity holders' as defined in subsection 995-1(1) of the ITAA 1997 whereby the Securityholders are an entity that holds an equity interest in the company. Paragraph 43B(1)(b) of the ITAA 1936 provides that Subdivision D of Division 2 of Part III of the ITAA 1936 applies to an equity holder in the same way as it applies to a shareholder.

71. Distributions paid in respect of the PTrackERS which are paid out of Taxable Profits are non-share dividends under section 974-120

of the ITAA 1997. Accordingly, Securityholders must include in their assessable income Distributions paid out of Taxable Profits under subparagraph 44(1)(a)(ii) of the ITAA 1936.

### ***Distributions not paid out of taxable profits***

72. It is considered that any Distributions received by the Securityholder which are not paid out of Taxable Profits is a non-share capital return defined under section 974-125, to the extent to which it is not a non-share dividend as defined under section 974-120.

73. A Distribution received by the Securityholder, which is not paid out of Taxable Profits, should not be included in the assessable income of the Securityholder. A CGT event will not happen as a result of the Securityholder receiving a Distribution which is not paid out of Taxable Profits. Such a Distribution is a recoupment of a loss or outgoing incurred, for the purposes of section 20-25 of the ITAA 1997 and will not form part of any element of the cost base (or reduced cost base) of the PTrackERS under subsection 110-45(3) or subsection 110-55(6). This effectively means that the part of the Issue Price returned to the Securityholder by way of this Distribution is taken to have never formed part of the cost base (or reduced cost base) of the PTrackERS.

### ***Franking credits***

74. It is considered Distributions paid out of Taxable Profits are expected to be franked. If a company makes a franked distribution to another entity, subsection 207-20(1) of the ITAA 1997 requires that the assessable income of the receiving entity include the amount of the franking credit on the distribution in addition to the amount of the franked distribution. Subsection 207-20(2) of the ITAA 1997 provides that the receiving entity is entitled to a tax offset equal to the franking credit on the distribution.

75. In accordance with subsection 207-20(1) of the ITAA 1997, any franking credit attached to a Distribution must also be included in the relevant Securityholder's assessable income for the income year in which the Distribution is made.

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

76. In accordance with subsection 207-20(2) of the ITAA 1997, Securityholders 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.

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

77. Securityholders who are entitled to a tax offset under subsection 207-20(2) of the ITAA 1997, in respect of the franking credit received, will also be subject to the refundable tax offset rules in Division 67 of the ITAA 1997, unless they are specifically excluded under section 67-25 of the ITAA 1997.

78. 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.

79. Entities excluded under section 67-25 of the ITAA 1997 include corporate tax entities (such as companies, corporate limited partnerships, corporate unit trusts and public trading trusts), unless they satisfy the requisite conditions as set out in subsections 67-25(1C) or 67-25(1D) of the ITAA 1997.

## ***Imputation benefits – streaming of imputation benefits***

80. Subdivision 204-D of the ITAA 1997 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.

81. Section 204-30 of the ITAA 1997 prescribes that the Commissioner may make such a determination in circumstances where an imputation benefit is received by a member of the entity, whereby that member would derive a greater benefit from franking credits than another disadvantaged member of the entity, who will receive lesser or no imputation benefits.

82. The Commissioner confirms that section 204-30 of the ITAA 1997 will not apply to deny the whole, or any part, of the imputation benefits received by a Securityholder in relation to Distributions paid on the PTrackERS, as it cannot be determined that members excluded from being paid Distributions will receive a lesser benefit from franked distributions than the Securityholders.

## ***Gross-up and tax offset denied in certain circumstances***

83. Subdivision 207-F of the ITAA 1997 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. Section 207-145 is relevant to the Securityholders that are subject to this Ruling.

84. Pursuant to subsection 207-145(1) of the ITAA 1997, this adjustment will occur where a franked distribution is made to an entity in one or more of the following circumstances:

- (a) 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.
- (b) 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.
- (c) the Commissioner has made a determination under paragraph 204-30(3)(c) of the ITAA 1997 that no imputation benefit is to arise in respect of the distribution for the entity, and
- (d) the distribution is made as part of a dividend stripping operation.

85. A person is a 'qualified person' for the purposes of Division 1A of former Part IIIAA of the ITAA 1936 if, generally speaking, they satisfy the holding period rule and the related payments rule (see former section 160APHO of the ITAA 1936).

86. Therefore, a Securityholder will be a 'qualified person' in relation to a Distribution received in respect of their PTrackERS, provided that:

- (a) if the Securityholder, or an associate of the Securityholder, has made, is under an obligation to make, or are likely to make a related payment in relation to Distributions on their PTrackERS, the Securityholder held their PTrackERS at risk for a period of at least 90 days as required under the holding period rule (excluding the day of acquisition and the day of disposal, and any days on which the Securityholder has materially diminished risks of loss or opportunities for gain in respect of the shares or interest), within each period beginning 90 days before and ending 90 days after the day on which the PTrackERS became ex-dividend, or
- (b) if (a) does not apply, the Securityholder held their PTrackERS at risk for a period of at least 90 days as required under the holding period rule (excluding the day of acquisition and the day of disposal, and any days on which the Securityholder has materially diminished risks of loss or opportunities for gain in respect of the shares or interest), in the period beginning on the day after the day on which the Securityholder acquired the PTrackERS and ending on the 90<sup>th</sup> day after the day on which the PTrackERS became ex-dividend.

87. In determining whether a shareholder is a 'qualified person' in relation to dividends paid on their shares, all 'positions' in respect of the shares are taken into account in identifying a 'net position' to

ensure that there is no material diminution in the risks of loss or opportunities for gain.

88. If either, or both, of the above two considerations in paragraph 86 are not met, the Securityholders will not be a 'qualified person' for the purposes of Division 1A of former Part IIIAA of the ITAA 1936.

89. The Commissioner has confirmed that no determination will be made under paragraph 177EA(5)(b) of the ITAA 1936 or paragraph 204-30(3)(c) of the ITAA 1997 to deny the imputation benefits attached to Distributions paid to Securityholders in respect of the PTrackERS.

90. A distribution will be taken to be made as part of a dividend stripping operation, pursuant to section 207-145 of the ITAA 1997, 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.

91. In considering whether there is a dividend stripping operation in this case, based on the information provided, the Company is a newly formed company that will acquire the Portfolio with the issue proceeds and will have its own franking account, separate from Parent Company.

92. Therefore, section 207-145 of the ITAA 1997 will not apply to the Distributions received by the Securityholders in respect of the PTrackERS. Accordingly, section 207-145 will not adjust the Securityholder's assessable income to exclude the amount of the franking credit on the Distributions, nor will it deny the tax offset to which the Securityholder would otherwise be entitled.

## **Redemption of the PTrackERS**

93. Section 26BB and section 70B of the ITAA 1936 assesses gains or allows a deduction for a loss on the disposal or redemption of a traditional security respectively.

94. For the purpose of these sections, the PTrackERS are not considered to be traditional securities and therefore, the Securityholders will not be entitled to a deduction upon redemption under section 70B.

95. As the PTrackERS are a CGT asset as defined in subsection 108-5(1) of the ITAA 1997, the redemption of the PTrackERS will give rise to a CGT event C2 (paragraph 104-25(1)(a) of the ITAA 1997).

96. The Securityholder will make a capital gain from this CGT event if their capital proceeds from the ending of the ownership of their asset are more than the asset's cost base or a capital loss if those capital proceeds are less than the asset's reduced cost base (subsection 104-25(3)). Any Distributions received by the Securityholder which is not paid out of Taxable Profits is effectively

the return of part of the Issue Price to the Securityholder and is taken to have never formed part of the cost base (or reduced cost base) of the PTrackERS (subsection 110-45(3) or subsection 110-55(6) of the ITAA 1997).

### **Exchange of the PTrackERS**

97. Under section 104-25 of the ITAA 1997, CGT Event C2 happens if, among other things, the ownership of an intangible asset that is a convertible interest ends by the conversion of the asset into another asset (paragraph 104-25(1)(f)).

98. Section 995-1(1) of the ITAA 1997 defines a convertible interest in a company by reference to Item 4 of the table in subsection 974-75(1) of the ITAA 1997.

99. Item 4 of the table in subsection 974-75(1), more specifically paragraph (b), refers to an interest that will, or may, convert into an equity interest in the company or a connected entity of the company. An interest is an interest (the first interest) that may convert into another interest (the second interest) if, for example, the holder of the first interest has a right or option to have allotted to the holder the second interest (section 974-165).

100. The Conditions provide that on Maturity if the Securityholder does not make a Redemption election, the Securityholder's PTrackERS will automatically be exchanged for new Shares in Parent Company.

101. PTrackERS will meet the definition in paragraph (b) in item 4 of the table in subsection 974-75(1) of the ITAA 1997 being an interest that may convert into equity interest in the company or an associate and will, therefore, meet the definition of a convertible interest as defined in subsection 995-1(1) of the ITAA 1997.

102. Therefore, CGT Event C2 occurs on the Exchange of PTrackERS pursuant to paragraph 104-25(1)(f) of the ITAA 1997.

103. Subsection 130-60(3) of the ITAA 1997 provides that any capital gain or capital loss made from converting a convertible interest is disregarded. Accordingly, upon Exchange, Securityholders will disregard any capital gain or loss arising from that Exchange pursuant to subsection 130-60(3).

### **Section 130-60(1): cost base of Shares**

104. Item 2 of the table in subsection 130-60(1) of the ITAA 1997 modifies the first element of the cost base and reduced cost base of shares acquired by converting a convertible interest that is not a traditional security.

105. Subsection 130-60(1) provides in these circumstances that the first element of the cost base and reduced cost base of the PTrackERS will be:

- (a) the cost base of the convertible interest at the time of Exchange.
- (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 to be added under subsection (1A).

106. Therefore, no additional amount is expected to be paid upon Exchange.

107. Subsection 130-60(1A) of the ITAA 1997 provides that an amount is to be added if a capital gain from a convertible interest has been reduced under section 118-20 of the ITAA 1997, which reduces capital gains if the amount is otherwise assessable. No capital gain is assessable to the Securityholders of PTrackERS upon Exchange.

108. Accordingly, the first element of the cost base and reduced cost base of each PTrackERS acquired upon Exchange will include the Issue Price (subsection 130-60(1)).

### ***Section 130-60(2): acquisition of Share***

109. The CGT asset comprising the Securityholder's Share is taken to have been acquired when the exchange of the PTrackERS occurs (subsection 130-60(2)).

### **Capital streaming**

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

110. 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%.

111. Based on the information provided and having regard to the relevant circumstances of the scheme, section 45 of the ITAA 1936 will not apply to treat the value of the Shares provided to Securityholders by Parent Company as an unfrankable dividend in their hands.

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

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

113. 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 the capital benefit is taken to be an unfranked dividend.

114. 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 Shares to Securityholders on Exchange of PTrackERS will constitute the provision of capital benefits by the Parent Company. However the issue of Shares on Exchange will not be considered a streaming of capital benefits to some Securityholders that derive a greater tax benefit compared to other Securityholders. It is notable that the PTrackERS are being offered to Australian resident or domiciled investors (and possibly New Zealand domiciled investors).

115. The Redemption of PTrackERS will involve the provision of a capital benefit by the Company within the meaning of subsection 45A(3) of the ITAA 1936 as it will constitute a non-share capital return (subsection 45A(3A) of the ITAA 1936). The amount paid to Securityholders on Redemption is limited to the amount of the Redemption Price of PTrackERS and any Final Distribution which are at the Company's discretion.

116. However it is not the case that some Securityholders receive a capital benefit in the form of the Redemption Price and other Securityholders (that is, non-redeeming Securityholders) will receive dividends from the Company.

117. Accordingly, it is considered that Securityholders will not derive a greater benefit from capital benefits than other shareholders of the Company. The issue of Shares on Exchange or the Redemption of PTrackERS will not trigger the application of section 45A of the ITAA 1936.

118. Therefore, 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 Exchange or Redemption of PTrackERS as an unfranked dividend in the hands of Securityholders.

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

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

120. The Commissioner may make a determination under paragraph 45B(3)(b) 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.

121. The issue of Shares to Securityholders on Exchange will constitute a scheme under which the Securityholders are provided with a capital benefit by Parent Company (paragraph 45B(5)(a) of the

ITAA 1936). Similarly, Redemption of PTrackERS will also constitute a scheme under which the Securityholders are provided with a capital benefit by Company (paragraph 45B(5)(b) of the ITAA 1936 and subsection 45B(7) of the ITAA 1936).

122. 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.

123. Having regard to the relevant circumstances surrounding the issue of Shares on Conversion or Redemption of PTrackERS, it is not considered that the Company, the Parent Company, the Securityholders or any other person entered into or carried out the Exchange or Redemption of PTrackERS for a purpose other than an incidental purpose of enabling Securityholders to obtain a tax benefit.

124. 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 Exchange or Redemption of PTrackERS as an unfranked dividend in the hands of Securityholders.

## **Part IVA – anti-avoidance**

125. In relation to the anti-avoidance measures, specifically section 177EA of the ITAA 1936, a determination will not be made under paragraph 177EA(5)(b) to deny the whole, or any part, of the imputation benefits received by Securityholders in relation to Distributions paid in respect of the PTrackERS.

126. Further, provided that the scheme ruled on is entered into and carried out as disclosed in this Ruling, it is accepted that the scheme is an ordinary commercial transaction and Part IVA of the ITAA 1936 will not apply in relation to the PTrackERS offered under the Prospectus.

## **Appendix 2 – Detailed contents list**

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