# *CR 2004/78 - Income tax: capital gains: scrip for scrip roll-over: exchange of units in Principal Office Fund for units in Investa Property Trust*

# Class Ruling

## Income tax: capital gains: scrip for scrip roll-over: exchange of units in Principal Office Fund for units in Investa Property Trust

Contents Para



***Preamble***

*The number, subject heading,* ***What this Class Ruling is about*** *(including* ***Tax law(s)***, ***Class of persons*** *and* ***Qualifications*** *sections),* ***Date of effect***, ***Arrangement*** *and* ***Ruling*** *parts of this document are a 'public ruling' in terms of Part IVAAA of the* ***Taxation Administration Act 1953****. CR 2001/1 explains Class Rulings and Taxation Rulings TR 92/1 and TR 97/16 together explain when a Ruling is a 'public ruling' and how it is binding on the Commissioner.*

# What this Class Ruling is about

1. This Ruling sets out the Commissioner's opinion on the way in which the tax law identified below applies to the defined class of persons who take part in the arrangement to which this Ruling relates.

### Tax law

2. The tax law dealt with in this Ruling is Subdivision 124-M of the *Income Tax Assessment Act 1997* (ITAA 1997).

### Class of persons

3. The class of persons to which this Ruling applies is the holders of units in Principal Office Fund (POF) who:

(a) are 'residents of Australia' within the meaning of subsection 6(1) of the *Income Tax Assessment Act 1936* (ITAA 1936);

(b) disposed of their units in POF under the arrangement that is the subject of this ruling; and

(c) are not 'significant stakeholders' or 'common stakeholders' within the meaning of those expressions as used in Subdivision 124-M of the ITAA 1997.

**Qualifications**

4. The Commissioner makes this Ruling based on the precise arrangement identified in this Ruling.

5. The class of persons defined in this Ruling may rely on its contents provided the arrangement actually carried out is in accordance with the arrangement described below at paragraphs 9 to 14.

6. If the arrangement actually carried out is materially different from the arrangement that is described in this Ruling, then:

(a) this Ruling has no binding effect on the Commissioner because the arrangement entered into is not the arrangement on which the Commissioner has ruled; and

(b) this Ruling may be withdrawn or modified.



## Date of effect

8. This Class Ruling applies to the years ended 30 June 2003 and 30 June 2004.

## Arrangement

9. The arrangement that is the subject of this Ruling is described below. This description is based on the documents listed below. These documents, or relevant parts of them, as the case may be, form part of and are to be read with this description. The relevant documents or parts of documents incorporated into this description of the arrangement are:

(a) Class Ruling applications dated 2 April 2004 and 22 April 2004 from Greenwoods & Freehills requesting that the Commissioner make a Class Ruling in relation to the capital gains scrip for scrip roll-over provisions as they apply to the exchange of units in POF for units in Investa Property Trust (IPT);

(b) the following documentation which accompanied the applications:

- copy of the Investa Property Group (IPG) offer document dated 20 June 2003, which describes the manner in which Investa Property Limited (IPL) as responsible entity for IPT proposed to make its formal takeover offer to POF unitholders;
- copies of the Target Statement dated 4 July 2003 and Supplementary Target Statements dated 14, 16, 21, 23 July 2003 and 28 July 2003 and 4, 6 and 12 August 2003;
- copy of the Notices of Variation Extending Offer Period dated 4 and 18 August 2003;
- copy of the Notice of Variation Improving Consideration Offered dated 11 August 2003;
- copy of the Notice of Change of Interests of Substantial Holder dated 2 September 2003;
- Constitutions of POF and IPT;
- Annual Reports for POF and IPT for the year ended 30 June 2003;
- copy of POF's Shareholder register as at 20 June 2003; and
- copy of the Top 20 Investors Report issued by the ASX Perpetual Registrars as at 20 June 2003.

(c) letter from Freehills, solicitors for IPT, dated 28 May 2004, responding to ATO requests for further information;

(d) letters from Greenwoods & Freehills dated 2 and 8 June 2004 responding to ATO requests for further information; and

(e) email from Greenwoods & Freehills dated 7 July 2004 responding to ATO request for further information.

10. The arrangement involves the acquisition of the units in POF by IPL, as responsible entity for IPT. On 20 June 2003 an offer was made to acquire all of the units in POF. After a number of extensions, the offer period closed on 1 September 2003. At that time IPL had acquired over 94% of the units in POF. The remaining units were later compulsorily acquired on the same terms.

11. For every 12 POF units that they owned, an Australian resident unitholder could select either of the following forms of capital proceeds:

(a) 7 IPG stapled securities (comprising one unit in IPT and one share in IPL) plus $5.70 **(the scrip alternative)**; or

(b) cash via a bookbuild facility plus $5.70 **(the cash alternative)**.

12. The cash alternative was mandatory for non-resident POF unitholders.

13. The IPG offer document stated at page 84:

> Because Investa Units are not separately traded on the ASX, there is not a separate market price for them. However, Investa Properties Limited considers that the fair value of Investa Units is 97% of the value of IPG Securities.

14. Under the arrangement to which this Ruling applies:

(a) POF and IPT are Australian resident trust estates as defined in subsection 95(2) of the ITAA 1936 and resident trusts for capital gains tax purposes as defined in subsection 995-1(1) of the ITAA 1997; and

(b) IPL, as responsible entity of IPT, is a resident of Australia as defined in subsection 6(1) of the ITAA 1936.

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

# Ruling

### Scrip alternative

15. Subject to the qualifications in paragraphs 4 to 6 of this Ruling, POF unitholders who selected the scrip alternative can choose, under paragraph 124-781(3)(c) of the ITAA 1997, scrip for scrip roll-over for the disposal of a POF unit to the extent they received a new unit in IPT if:

(a) apart from the roll-over for which Subdivision 124-M of the ITAA 1997 provides, they would make a capital gain from the disposal of the POF unit; and

(b) any capital gain that could be realised on the future sale or other disposal of a replacement unit in IPT would not be disregarded (except because of a roll-over).

16. Roll-over is not available to the extent that a POF unitholder who selected the scrip alternative received cash or an IPL share, as consideration for the disposal of a POF unit (section 124-790 of the ITAA 1997).

### Cash Alternative

17. A POF unitholder who selected the cash alternative cannot choose scrip for scrip roll-over.

### Time of CGT event under both alternatives

18. Any capital gain that is not disregarded or a capital loss that arises will be made in the income year that a POF unitholder accepted the offer to dispose of their units to IPL.

## Explanations

### Availability of scrip for scrip roll-over

19. Scrip for scrip roll-over enables a unitholder to disregard all or part of a capital gain they make from a unit that is disposed of as part of a takeover or merger if they receive a replacement unit. The capital gain is disregarded completely if the only capital proceeds the unitholder receives is a replacement unit. If the unitholder receives some other form of capital proceeds, the capital gain is disregarded in part.

20. Subdivision 124-M contains a number of conditions for, and exceptions to, the eligibility of a unitholder to choose the roll-over. Below is an outline of the main conditions and exceptions that are relevant to the circumstances of the arrangement that is the subject of this Ruling.

**21. Subparagraph 124-781(1)(a)(i) requires an entity (a POF unitholder) to exchange a unit in a trust (POF) for a unit in another trust (IPT).**

22. This requirement is satisfied for POF unitholders who selected the scrip alternative as they exchanged each of their units in POF for a part of a unit in IPT. This requirement is not satisfied for POF unitholders who selected the cash alternative.

**23. Paragraph 124-781(1)(b) requires that entities have fixed entitlements to all of the income and capital of the original entity (POF) and the acquiring entity (IPT).**

24. Having regard to:

(a) all of the documents and any other material referred to in paragraph 9 of this Ruling; and

(b) all the facts comprising the arrangement as described in paragraphs 10 to 14 of this Ruling

it is considered that for the purposes of paragraph 124-781(1)(b) of the ITAA 1997, there are fixed entitlements to all of the income and capital of POF and IPT immediately before, during and immediately after the arrangement that is the subject of this Ruling.

**25. Paragraphs 124-781(1)(c) and 124-781(2)(a) require that the exchange of units is in consequence of an arrangement that results in the acquiring entity (IPT) becoming the owner of 80% or more of the trust voting interests in the original entity (POF).**

26. A trust voting interest is defined in subsection 124-781(6) as an interest that confers rights of the same or a similar kind as the rights conferred by a voting share in a company. 'Voting shares' are defined in subsection 995-1(1) of the ITAA 1997 by reference to the definition in section 9 of the *Corporations Act 2001*.

27. All of the POF units are trust voting interests. This requirement is therefore satisfied on the basis that IPL, as responsible entity of IPT, acquired 100% of the units in POF, as a consequence of the arrangement that is the subject of this ruling.

**28. Paragraphs 124-781(1)(c) and 124-781(2)(b) require that the exchange of units is in consequence of an arrangement in which at least all owners of trust voting interests in the original entity (POF) could participate.**

29. This requirement is satisfied because all POF unitholders (including non-residents) as set out in the Register of Unitholders were entitled to dispose of their units in POF.

**30. Paragraphs 124-781(1)(c) and 124-781(2)(c) require that the exchange of units is in consequence of an arrangement in which participation was available on substantially the same terms for all of the owners of units of a particular type.**

31. The requirement is satisfied as each resident POF unitholder could choose to dispose of their POF units for the consideration available under the scrip or cash alternatives.

32. Although the foreign POF unitholders could only choose to dispose of their units under the cash alternative, the arrangement is still one that was available on substantially the same terms for all owners of POF units.

**33. Paragraphs 124-781(3)(a) and 124-781(3)(b) require that the original interest holder (a POF unitholder) acquired its interest on or after 20 September 1985 and, apart from the roll-over, would make a capital gain from a CGT event happening in relation to its original interest.**

34. These conditions are satisfied as all POF unitholders acquired their interests in POF after 20 September 1985. Further, this Ruling only applies to those unitholders who would otherwise make a capital gain – refer to paragraph 14(a).

35. Whether a POF unitholder would make a capital gain, apart from the roll-over is dependent on the specific circumstances of each unitholder, in particular, the cost base of each POF unit at the time of the disposal and the value of the consideration received.

36. Roll-over is not available if, in respect of a POF unit, a unitholder would make a capital loss.

**37. Paragraph 124-781(3)(c) requires that the original interest holder (a POF unitholder) chooses to obtain roll-over.**

38. This Ruling applies only to those POF unitholders who choose to obtain roll-over - refer to paragraph 15.

**39. Subsection 124-781(4) provides that additional requirements must be satisfied if the original interest holder (a POF unitholder) and the trustee of the acquiring entity (IPT) did not deal with each other at arm's length, and neither the original entity (POF) nor the acquiring entity had at least 300 beneficiaries just before the arrangement started. The additional requirements are:**

**(a) the market value of the original interest holder's capital proceeds for the exchange must be at least substantially the same as the market value of its original interest; and**

**(b) the replacement interest must carry the same kind of rights and obligations as those attached to the original interest.**

40. Subsection 124-781(4) will not apply because POF had more than 300 members just before the arrangement started.
(Section 124-810 will not apply to POF because its ownership was not concentrated in the manner contemplated by that section.)

**41. Roll-over under Subdivision 124-M is not available if any of the exceptions in section 124-795 applies.**

42. Subsection 124-795(1) provides that roll-over is not available for non-resident unitholders if their replacement interests are in an entity that is not a resident trust for CGT purposes. This Ruling only applies to unitholders who are residents of Australia – refer to paragraph 3(a).

43. Paragraph 124-795(2)(a) provides that roll-over is not available if any capital gain that might be made from a replacement interest would be disregarded (except because of a roll-over). This exception may apply if, for example, the replacement IPT units were treated as trading stock. Roll-over can only be chosen by unitholders who satisfy this condition - refer to paragraph 15(b).

44. The other exceptions in section 124-795 are not relevant as they relate to roll-overs that involve companies.

### Partial roll-over

45. Section 124-790 provides that only a partial roll-over is available if a unitholder receives something other than a replacement unit (ineligible proceeds) as capital proceeds for an original unit.

46. POF unitholders who selected the scrip alternative will be entitled only to a partial roll-over as they received ineligible proceeds in the form of $5.70 cash and a share in IPL (valued on the day the CGT event happened to their POF units – see paragraphs 50 to 52 for when this happened).

47. In calculating the capital gain attributable to their ineligible proceeds, a POF unitholder must deduct from those proceeds a reasonable portion of the cost base of their POF unit (just before the disposal to IPL as responsible entity for IPT). The remaining cost base is taken into account in working out the cost base of a replacement IPT unit.

48. The cost base of a POF unit just before its disposal is determined by deducting the amount of any relevant non-assessable payments in the current and earlier income years: section 104-71 of the ITAA 1997.

49. In making a reasonable apportionment of the cost base of the POF units, it would be appropriate for a unitholder to make an apportionment having regard to the value of the ineligible proceeds and the IPT units on the date they accepted the offer.

### *Time of CGT event*

50. The time when CGT event A1 (about the disposal of an asset) happened to each POF unitholder determines the income year in which any capital gain or loss arises and whether the CGT discount applies to any capital gain.

51. As the POF units were disposed of under a contract, CGT event A1 happened to each unitholder on the date that they accepted the offer made by IPL (paragraph 104-10(3)(a)).

52. Most unitholders accepted the offer during the period 1 July 2003 – 1 September 2003. Their capital gain or loss generally will arise in the 2004 income year. However those who accepted the offer prior to 30 June 2003 generally will make a capital gain or loss in the 2003 income year.

### *Cost base of IPT unit*

53. The first element of the cost base and reduced cost base of an IPT unit is worked out having regard to that portion of the cost base of a POF unit that was not taken into account in working out the capital gain in respect of the ineligible proceeds: subsections 124-785(2), (3) and (4).

***Cost base of IPL share***

54. The acquisition cost of an IPL share is calculated having regard to the market value of the property given to acquire it (subsection 110-25(2) of the ITAA 1997), that is, a proportion of the value of a POF unit.

**Example**

*55. This example shows how to calculate a capital gain attributable to the receipt of ineligible proceeds. It also shows how the acquisition cost of an IPL share and an IPT unit is to be calculated.*

56. *Max acquired 2,400 units in POF. On 1 August 2003 he accepted the offer and chose the scrip alternative. At that time the cost base of each of his units in POF, adjusted as required by section 104-71, was $1.40. Cost Base of 2400 POF units is $3,360 (2400 x $1.40).*

57. *Max received:*

- *1,400 IPG stapled securities (each with a market value of $1.95 on the date the offer was accepted); and*
- *$1,140 cash.*

58. *Assume that a unit in IPT represented 97% of the value of an IPG stapled security and that the value of a share in IPL represented 3% of the value of the security.*

*The total amount of capital proceeds received by Max was $3,870 apportioned as follows:*

| | | |
|---|---|---|
| *IPG stapled securities* | *1,400 @ $1.95* | *$2,730* |
| *IPL shares* | *$81.90 =*<br>*$2,730 x 3%* | |
| *IPT units* | *$2,648.10 =*<br>*$2,730 x 97%* | |
| *Cash* | *(2400/12 x $5.70)* | *$1,140* |
| *Total amount of capital proceeds* | | *$3,870* |

### *Capital gain attributable to ineligible proceeds (IPL shares and cash)*

59. *Max chooses roll-over to the extent he is able. However he must work out his capital gain in relation to the ineligible proceeds that he received. He does this as follows:*

*Capital gain = Ineligible capital proceeds – cost base of 'ineligible part'*

*Ineligible capital proceeds = Shares + cash*

*= $81.90 + $1,140*

*= $1,221.90*

*Cost base of ineligible part* $= \dfrac{\text{Ineligible proceeds} \times \text{cost base of POF units}}{\text{Total proceeds}}$

$= \dfrac{\$1,221.90 \times \$3,360}{\$3,870}$

*= $1,060.87*

*Capital gain = $1,221.90 - $1,060.87*

*= $161.03*

### *Acquisition cost of IPT unit*

60. *Max determines the acquisition cost of his IPT units by apportioning, in a reasonable way, the remaining cost base of his POF units. He does this as follows:*

$\dfrac{\text{Cost base of POF units – Cost base taken into account above}}{\text{Number of IPT units}}$

$= \dfrac{\$3,360 - \$1,060.87}{1,400}$

*= $1.64*

### *Acquisition cost of IPL shares*

61. *Max works out the acquisition cost of his IPL shares having regard to the market value of the POF units for which they were exchanged. The market value of a unit in POF on the day he accepted the offer was $1.58. The market value of 1.71 POF units at that time was $2.70.*

62. *Max works out the acquisition cost using the following formula:*

$$\frac{\textit{Value of share} \times \textit{Market value of POF units given}}{\textit{Value of all property received}}$$

*Value of all property received*

| | |
|---|---|
| *IPL shares* | *$0.06* |
| *IPT units* | *$1.89* |
| *Cash* | *$0.81* |
| *Value of all property received* | *$2.76* |

*Acquisition cost of IPL share* $= \frac{\$0.06 \times \$2.70}{\$2.76}$

*= $0.059 per share.*

## Detailed contents list

63. Below is a detailed contents list for this Class Ruling:

**Paragraph**

**Commissioner of Taxation**
28 July 2004

*Previous draft*:
Not previously issued as a draft

*Related Rulings/Determinations*:
CR 2001/1; TR 92/1; TR 97/16

*Subject references*:
- acquiring entity
- arrangement
- capital
- capital gain
- class of persons
- exchange
- fixed entitlement
- income
- interests
- original entity
- original interest
- replacement interest
- resident
- roll-over
- scrip
- scrip for scrip roll-over
- unit
- unitholder
- unit trust

*Legislative references*:
- ITAA 1936 6(1)
- ITAA 1936 95(2)
- ITAA 1997 104-10(3)(a)
- ITAA 1997 104-71
- ITAA 1997 110-25(2)
- ITAA 1997 Subdivision 124-M
- ITAA 1997 124-781(1)(a)(i)
- ITAA 1997 124-781(1)(b)
- ITAA 1997 124-781(1)(c)
- ITAA 1997 124-781(2)(a)
- ITAA 1997 124-781(2)(b)
- ITAA 1997 124-781(2)(c)
- ITAA 1997 124-781(3)(a)
- ITAA 1997 124-781(3)(b)
- ITAA 1997 124-781(3)(c)
- ITAA 1997 124-781(4)
- ITAA 1997 124-781(6)
- ITAA 1997 124-785(2)
- ITAA 1997 124-785(3)
- ITAA 1997 124-785(4)
- ITAA 1997 124-790
- ITAA 1997 124-795
- ITAA 1997 124-795(1)
- ITAA 1997 124-795(2)(a)
- ITAA 1997 124-810
- ITAA 1997 995-1(1)
- TAA 1953 Part IVAAA
- Copyright Act 1968
- Corporations Act 2001 9

ATO references
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