

CR 2009/48 - Income tax: Orchard Industrial Property Fund Restructure: Orchard Management Limited and Orchard Industrial Property Fund stapling arrangement

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Class Ruling

Income tax: Orchard Industrial Property Fund Restructure: Orchard Management Limited and Orchard Industrial Property Fund stapling arrangement

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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.

What this Ruling is about

1. This Ruling sets out the Commissioner's opinion on the way in which the relevant provision(s) identified below apply to the defined class of entities, who take part in the scheme to which this Ruling relates.

Relevant provision(s)

2. The relevant provisions dealt with in this Ruling are:

- section 99B of the *Income Tax Assessment Act 1936* (ITAA 1936);
- section 6-5 of the *Income Tax Assessment Act 1997* (ITAA 1997);
- Division 104 of the ITAA 1997;
- section 109-5 of the ITAA 1997;
- section 110-25 of the ITAA 1997;
- section 110-55 of the ITAA 1997; and
- section 112-25 of the ITAA 1997.

All legislative references in this Ruling are to the ITAA 1997 unless otherwise indicated.

Class of entities

3. The class of entities to which this Ruling applies are those unitholders in the Orchard Industrial Property Fund (OIF) who:

- participated in the scheme that is the subject of this Ruling;
- are Australian residents within the meaning of subsection 6(1) of the ITAA 1936; and
- hold their units in OIF on capital account.

Qualifications

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

5. It should be noted that this Ruling is limited to those questions set out in the Ruling section. There may be other taxation issues relating to the overall arrangement. However, the Commissioner has not been asked to form a view, and has not formed a view, on any such issues.

6. The class of entities defined in this Ruling may rely on its contents provided the scheme actually carried out is carried out in accordance with the scheme described in paragraphs 10 to 15 of this Ruling.

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

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- this Ruling may be withdrawn or modified.

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Date of effect

9. This Ruling applies from 1 July 2009 to 30 June 2010. The Ruling continues to apply after 30 June 2010 to all entities within the specified class who entered into the specified scheme during the term of the Ruling. However, this Ruling will 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 this Ruling (see paragraphs 75 and 76 of Taxation Ruling TR 2006/10).

Scheme

10. The following description of the scheme is based on information provided by the applicant. The following documents, or relevant parts of them, form part of and are to be read with the description:

- Class Ruling application from PricewaterhouseCoopers dated 24 June 2009;
- additional information supplied at the meeting held on 23 June 2009;
- the Australian Securities Exchange (ASX) announcement dated 18 May 2009;
- the Implementation Agreement dated 18 May 2009;
- the Meeting Booklet for OIF dated 23 June 2009;
- the OIF Constitution dated 10 May 2007;
- the Supplemental Deed to the OIF Constitution approved by the unitholders on 28 July 2009;
- the Orchard Management Limited (OML) Constitution;
- the 2008 Annual Report for OIF; and
- further information provided by the applicant on 22 July 2009.

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

11. Orchard Property Limited (OPL) and OML are wholly-owned subsidiaries of Orchard Funds Limited (OFL) and members of the OFL income tax consolidated group.

12. On 18 May 2009, OPL as Responsible Entity (RE) for OIF announced that it had entered into an implementation agreement with Growthpoint Properties Limited (Growthpoint) to recapitalise and restructure OIF. Part of this proposed restructure involved establishing a stapled security that would comprise of a share in OML and a unit in OIF. This is referred to as 'the stapling arrangement' and is the subject of this Ruling.

13. Immediately prior to the stapling arrangement, OIF raised \$55.6 million via a placement of 347,563,813 new OIF units to Growthpoint at an issue price of 16 cents per unit. The new units issued via the placement ranked pari passu with the existing OIF units. The placement resulted in Growthpoint owning 50.1% of the units in OIF.

14. The stapling arrangement involved the following steps:

- Each holding of original OML shares was split so that the number of shares on issue was equal to the number of OIF units on issue.
- OIF made a capital distribution of 0.89 cents per OIF unit to each OIF unitholder. This capital distribution was attributable to its contributed capital in corpus and was recorded by OIF as a reduction in its contributed equity account which was permissible under OIF's constitution.
- OPL, on behalf of each OIF unitholder, applied the capital distribution to acquire OIF's shareholding in OML for market value consideration. Each OIF unitholder received one OML share for each OIF unit held.
- The shares in OML and the units in OIF were then stapled on a one for one basis, to form the OIF stapled securities.
- OIF and OML undertook a consolidation of the units and shares respectively such that:
 - for every 10 OIF units held, each OIF stapled security holder now held 1 OIF unit; and
 - for every 10 OML shares held, each OIF stapled security holder now held 1 OML share.

The total number of consolidated OIF units and OML shares held by each OIF stapled security holder was rounded up to the nearest whole number.

- The OIF stapled security then began trading on the ASX.

15. Following the stapling arrangement, the OIF Stapled Group intends to undertake a fully underwritten renounceable rights issue to raise an additional \$144.4 million at 16 cents per OIF stapled security. This rights issue is separate from the stapling arrangement and is not considered in this Ruling.

Ruling

Non-assessable payments

16. Section 99B of the ITAA 1936 does not apply to the capital distribution to OIF unitholders.

17. The capital distribution to OIF unitholders is not otherwise assessable under subsection 6-5(1) as ordinary income of the unitholder.

Capital distribution

18. The capital distribution of 0.89 cents per unit to an OIF unitholder resulted in CGT event E4 happening in respect of each of their OIF units (section 104-70).

Transfer of OML shares

19. The first element of the cost base and reduced cost base of each OML share acquired by an OIF unitholder under the scheme is 0.89 cents (sections 110-25 and 110-55).

20. Each OML share was acquired by an OIF unitholder on the implementation date of 5 August 2009 (subsection 109-5(2)).

Stapling of securities

21. No CGT event in Division 104 happened as a result of the stapling of each OML share to each OIF unit.

Consolidation of OIF units

22. The consolidation of OIF units did not result in a CGT event happening. Each element of the cost base and reduced cost base of each consolidated OIF unit is the sum of the corresponding elements of each original OIF unit (subsection 112-25(4)).

23. Each OIF stapled security holder is taken to have acquired their consolidated OIF unit at the time that they acquired their original OIF units (subsection 109-5(1)).

Consolidation of OML shares

24. No CGT event in Division 104 happened as a result of the consolidation of the OML shares (subsection 112-25(4)).

Appendix 1 – Explanation

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.***

Non-assessable payments

25. Division 6 of Part III of the ITAA 1936 is the primary scheme for including distributions from trust funds in the assessable income of unitholders. Subsection 99B(1) of the ITAA 1936 provides that an amount, being property of a trust estate, paid to, or applied for the benefit of, a beneficiary of the trust estate who was a resident at any time during the year of income, is the assessable income of the beneficiary, subject to the exceptions in subsection 99B(2) of the ITAA 1936.

26. The exception in paragraph 99B(2)(a) of the ITAA 1936 is to the extent it represents corpus of the trust estate and is not attributable to amounts derived by the trust estate that, if they had been derived directly by a taxpayer being a resident, would have been included in the assessable income of that taxpayer.

27. Subsection 6-5(1) provides that a taxpayer's assessable income includes income according to ordinary concepts (ordinary income).

28. In *Scott v. Federal Commissioner of Taxation* (1966) 117 CLR 514; (1966) 10 AITR 367; (1966) 14 ATD 286 Windeyer J stated that:

Whether or not a particular receipt is income depends upon its quality in the hands of the recipient.

29. In *GP International Pipecoaters Pty Ltd v. Federal Commissioner of Taxation* [1990] HCA 25; (1990) 170 CLR 124; 90 ATC 4413; (1990) 21 ATR 1 the Full High Court considered the following factors were important in determining the nature of a receipt:

To determine whether a receipt is of an income or a capital nature, various factors may be relevant. Sometimes, the character of receipts will be revealed most clearly by their periodicity, regularity or recurrence; sometimes, by the character of a right or thing disposed of in exchange for the receipt; sometimes by the scope of the transaction, venture or business in or by reason of which money is received and by the recipient's purpose in engaging in the transaction, venture or business.

30. The capital distributed to the unitholders was corpus and was attributable to the contributed equity capital of OIF. The contributions were received solely to establish the fund and as such are of a capital nature and not ordinary income.

31. Accordingly, the capital distributed is not included in assessable income of the unitholders under subsection 99B(1) of the ITAA 1936 as it represents corpus of the fund that is attributable to amounts derived by the fund that, if they had been derived by a taxpayer being a resident, would not have been included in the assessable income of that taxpayer.

32. On similar analysis, the payment of corpus is not assessable under subsection 6-5(1) as ordinary income of the unitholder.

Capital distribution

33. Under section 104-70, CGT event E4 happens if the trustee of a trust makes a payment to a unitholder in respect of their unit in the trust and some or all of the payment is not included in the unitholder's assessable income (non-assessable payment).

34. The consequences of CGT event E4 happening are determined on an annual basis, that is, having regard to all such CGT events that happen to a unit during an income year (subsection 104-70(3)).

35. If CGT event E4 happens during an income year, a unitholder will make a capital gain if the total value of the non-assessable payments made by the trustee during the income year in respect of a unit exceeds the cost base of the unit (subsection 104-70(4)).

36. Where a unitholder makes a capital gain when CGT event E4 happens, the cost base and reduced cost base of the unit are reduced to nil (subsection 104-70(5)).

37. However, if the sum of the non-assessable payments is not more than the cost base of the unit, the cost base and reduced cost base are reduced by that amount (subsection 104-70(6)).

38. The distribution of 0.89 cents per OIF unit paid by OIF on the implementation date was not included in the assessable income of OIF unitholders. Therefore, the distribution by OIF under the stapling arrangement resulted in CGT event E4 happening to each OIF unit.

39. Accordingly, the cost base and reduced cost base of each OIF unit, which may have been adjusted by previous tax deferred distributions, will be reduced (but not below nil) by 0.89 cents. A unitholder whose cost base for the OIF unit is less than 0.89 cents will make a capital gain to the extent of the difference.

Transfer of OML shares

40. Sections 110-25 and 110-55 provide that the first element of the cost base and reduced cost base of a CGT asset is the money paid or the property given in respect of its acquisition.

41. Owners of OIF units are taken to have paid 0.89 cents for each OML share acquired (as a result of the capital distribution being applied by OPL as the RE of OIF on behalf of each unitholder).

42. Accordingly, the first element of the cost base and reduced cost base of each OML share acquired by an OIF unitholder under the scheme is 0.89 cents.

43. Where an entity disposes of a CGT asset to you (except where you compulsorily acquire it), you acquire the CGT asset at the time when the disposal contract is entered into or, if no contract is entered into, when the entity stops being the asset's owner (item 1 of the table in subsection 109-5(2)).

44. Under this scheme, the disposal of the OML shares by OFL to an OIF unitholder resulted in CGT event A1 happening to OFL. That event happened on the implementation date, being the date when the OML Deed became effective. Accordingly, under the scheme, an OIF unitholder is taken to have acquired each OML share on 5 August 2009.

Stapling of securities

45. The effect of the stapling is to apply restrictions to the transferability of the individual units that together make up each OIF stapled security. Each individual security (that is, an OML share and an OIF unit) retains its legal character without any change in beneficial ownership. There was no variation to the rights or obligation attaching to, or to the beneficial ownership of, the individual securities that make up the OIF stapled security as a consequence of the stapling.

46. Therefore, no CGT event in Division 104 happened as a consequence of the stapling of each OML share to each OIF unit.

Consolidation of OIF units

47. Subsection 112-25(4) provides that, if two or more CGT assets are merged into a single asset and the beneficial ownership of the old and new assets remains the same, the merger does not result in the happening of a CGT event. It also provides that each element of the cost base and reduced cost base of the new asset (at the time of merging) is the sum of the corresponding elements of each original asset.

48. Accordingly, the consolidation of the OIF units did not result in a CGT event happening to the holder of the OIF stapled security.

49. Each element of the OIF stapled security holder's cost base and reduced cost base for their consolidated OIF units will be the sum of the corresponding elements of their original OIF units in accordance with the merger ratio of ten securities into one.

50. Subsection 109-5(1) generally provides that a CGT asset is acquired when it commences to be owned by someone.

51. If one or more consolidated OIF units can be formed from a parcel of OIF units that all have the same acquisition date, an OIF stapled security holder is taken to have acquired those consolidated OIF units on the date of acquisition of the original OIF units. Where there are parcels of original OIF units which have different acquisition dates, the consolidated OIF units can be apportioned to the different acquisition dates on a reasonable basis.

Consolidation of OML shares

52. No ordinary shares in OML were cancelled as a result of the consolidation of OML shares. OIF stapled security holders did not receive any capital proceeds for the reduction in the number of shares on issue.

53. The consolidation of OML shares did not result in any change to OML's share capital. Further, there was no change to the proportionate interests held by each shareholder.

54. Accordingly, no CGT event happened as a result of the share consolidation (subsection 112-25(4)).

Appendix 2 – Detailed contents list

55. The following is a detailed contents list for this Ruling:

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References

Previous draft:

Not previously issued as a draft

Related Rulings/Determinations:

TR 2006/10

Subject references:

- acquisition dates
- allotment & issue of securities
- capital gains
- capital reductions
- CGT cost base
- CGT events
- CGT reduced cost base
- return of capital on shares
- stapled structure

Legislative references:

- ITAA 1936 6(1)
- ITAA 1936 Pt III Div 6
- ITAA 1936 99B
- ITAA 1936 99B(1)
- ITAA 1936 99B(2)
- ITAA 1936 99B(2)(a)
- ITAA 1997
- ITAA 1997 6-5
- ITAA 1997 6-5(1)
- ITAA 1997 Div 104

- ITAA 1997 104-70
- ITAA 1997 104-70(3)
- ITAA 1997 104-70(4)
- ITAA 1997 104-70(5)
- ITAA 1997 104-70(6)
- ITAA 1997 109-5
- ITAA 1997 109-5(1)
- ITAA 1997 109-5(2)
- ITAA 1997 110-25
- ITAA 1997 110-55
- ITAA 1997 112-25
- ITAA 1997 112-25(4)
- Copyright Act 1968
- TAA 1953

Case references:

- GP International Pipecoaters Pty Ltd v. Federal Commissioner of Taxation [1990] HCA 25; (1990) 170 CLR 124; 90 ATC 4413; (1990) 21 ATR 1
- Scott v. Federal Commissioner of Taxation (1966) 117 CLR 514; (1966) 10 AITR 367; (1966) 14 ATD 286

ATO references

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