


CR 2010/71 - Income tax: scrip for scrip: merger of Choiseul Investments Limited and Milton Corporation Limited

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Class Ruling

Income tax: scrip for scrip: merger of Choiseul Investments Limited and Milton Corporation Limited

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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 considered in this Ruling are:

- subsection 6(1) of the *Income Tax Assessment Act 1936* (ITAA 1936);
- subsection 44(1) of the ITAA 1936;
- Division 1A of former Part IIIA of the ITAA 1936;
- section 177E of the ITAA 1936;
- section 177EA of the ITAA 1936;
- section 104-10 of the *Income Tax Assessment Act 1997* (ITAA 1997);
- section 109-10 of the ITAA 1997;
- section 110-25 of the ITAA 1997;

- section 110-55 of the ITAA 1997;
- section 112-30 of the ITAA 1997;
- Subdivision 115-A of the ITAA 1997;
- section 116-20 of the ITAA 1997;
- Subdivision 124-M of the ITAA 1997;
- section 204-30 of the ITAA 1997; and
- section 207-20 of the ITAA 1997.

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

Class of entities

3. The class of entities to whom this Ruling applies consists of entities who were ordinary shareholders of Choiseul Investments Limited (Choiseul) at the time of the scheme, and who:

- (a) held their Choiseul ordinary shares (Choiseul Shares) on capital account at that time;
- (b) exchanged their Choiseul Shares for ordinary shares in Milton Corporation Limited (Milton) under the scheme;
- (c) were 'residents of Australia' within the meaning of that expression in subsection 6(1) of the ITAA 1936 at that time; and
- (d) are not subject to the taxation of financial arrangements rules in Division 230 in relation to gains and losses on their Choiseul shares.

(Note: Division 230 will generally not apply to individuals, unless they have made an election for it to apply to them.)

Qualifications

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

5. 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 9 to 25 of this Ruling.

6. 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

8. This Ruling applies from 1 July 2010 to 30 June 2011. The Ruling continues to apply after 30 June 2011 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

9. 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:

- application for a Class Ruling, dated 13 September 2010;
- Merger Implementation Agreement (MIA), together with its annexures, between Milton Corporation Limited and Choiseul Investments Limited, dated 7 September 2010;
- Scheme Booklet issued by Choiseul Investments Limited to its shareholders, dated 22 October 2010; and
- Choiseul Investments Limited Media Releases dated 20 August 2010 and 7 September 2010.

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

Choiseul Investments Limited (Choiseul)

10. Choiseul was established in 1911 and has been listed on the Australian Securities Exchange (ASX) since 1971. It is currently an Australian listed investment company, having a long-term outlook, with a diversified portfolio of Australian shares, units and interest bearing securities. Capital profits are generally reinvested instead of being distributed to shareholders.

11. At 30 June 2010, there were 96,863,646 Choiseul shares on issue. With the majority of shareholders (99.69%), as at 31 July 2010, being Australian residents. All Choiseul shares are a single class of fully paid ordinary shares listed on the ASX, carrying one vote per share, with the right to receive dividends.

12. Choiseul has a financial and tax year ending 30 June.

13. Choiseul does not have a significant stakeholder or common stakeholder for the purposes of Subdivision 124-M.

Milton Corporation Limited

14. Milton was incorporated in 1938 and has investment objectives similar to Choiseul's.

The Scheme of Arrangement

15. On 20 August 2010, Choiseul and Milton announced that they had entered into discussions to merge the two companies by way of a Scheme of Arrangement (the Scheme).

16. On 7 September 2010, Milton and Choiseul announced that they had entered into a Merger Implementation Agreement (MIA) by which Milton proposed to acquire all the issued shares in Choiseul by way of a Scheme of Arrangement under the *Corporations Act 2001*.

17. The Scheme Meeting of Choiseul shareholders was held on 26 November 2010 and at that meeting a resolution was put seeking their agreement to implement the Scheme of Arrangement. The Scheme Implementation date was 16 December 2010.

The Scheme Consideration

18. Under the Scheme, participating Choiseul Shareholders who sold their shares to Milton received consideration for their Choiseul shares in the form of Milton shares only. There was no cash component in the Scheme Consideration.

19. The number of Milton shares issued to participating Choiseul shareholders was determined in accordance with the formula contained in clause 1 of the MIA as follows:

'Scheme Consideration' means the Milton Shares to be issued to the Scheme Participants as consideration for the implementation of the Scheme, which will consist of the number of new Milton Shares to be issued to each Scheme Participant (rounded to the nearest whole share), determined in accordance with the following formula:

$$\text{NMS} = \text{CSH} \times \left(\frac{\text{Choiseul Adjusted NTA}}{\text{Choiseul Shares on issue as at the Calculation Date}} \times \frac{\text{Milton Shares on issue as at the Calculation Date}}{\text{Milton Adjusted NTA}} \right)$$

20. The terms contained in the formula are defined as:

- **NMS** means the number of New Milton Shares to be issued to the Scheme Participant;
- **CSH** means the number of Choiseul Shares held by the Scheme Participant as at the Record Date;
- **Choiseul Adjusted NTA** means the NTA of Choiseul as at the Calculation Date less the Choiseul Special Dividend and Choiseul Interim Dividend plus Choiseul's Share of the Milton Interim Dividend;
- **Milton Adjusted NTA** means the NTA of Milton as at the Calculation Date less the Milton Interim Dividend plus Milton's Share of the Choiseul Special Dividend and Choiseul Interim Dividend;
- **Choiseul's Share of the Milton Interim Dividend** means the amount of the Milton Interim Dividend payable to Choiseul and;
- **Milton's Share of the Choiseul Special Dividend and Choiseul Interim Dividend** means the amount of the Choiseul Special Dividend and Choiseul Interim Dividend payable to Milton and its related Bodies Corporate.
- **NTA** means the aggregate net tangible asset backing before providing for tax on unrealised capital gains and realised capital losses of Milton or Choiseul (as the context requires) calculated in the same manner used for the purpose of that party's market announcements to ASX of its net tangible asset backing per share as at each calendar month end; and

- **Calculation Date** means 7:00pm on the seventh Business Day before the date of the Scheme Meeting or such other date as Milton and Choiseul agree in writing.

The Dividends

21. Choiseul declared an Interim Dividend of 10.5 cents per share on 18 November 2010. The Record Date for this dividend was 9 December 2010. The Interim Dividend represented the ordinary interim dividend payable from profits to all Choiseul shareholders and was not conditional on the Scheme being approved or implemented.

22. Choiseul declared a Special Dividend of 16 cents per share on 2 December 2010. While the Special Dividend was conditional on the Scheme being approved and implemented, both the Interim Dividend and Special Dividend were sourced entirely from Choiseul's retained earnings. The Record Date for the Special Dividend was 9 December 2010. Both dividends were paid on 16 December 2010.

23. Both the Interim and Special Dividends were fully franked and debited against Choiseul's retained profits account. The dividends were funded from Choiseul's existing cash reserves and were not debited to Choiseul's share capital account.

24. Milton was not required to consent to the payment of the dividends or any aspect relating to their funding.

25. Choiseul had a franking account balance at 30 June 2010 of \$12.852 million. The allocation of franking credits to the Interim and Special Dividends will use approximately \$10.99 million of the available franking credits.

Ruling

CGT event A1

26. CGT event A1 happens when a participating Choiseul Shareholder disposes of a Choiseul share to Milton under the Scheme (subsections 104-10(1) and (2)).

Time of CGT event A1

27. The time of the CGT event is when the change of ownership of the Choiseul share occurs (paragraph 104-10(3)(b)).

Capital gain or capital loss

28. A participating Choiseul Shareholder makes a capital gain, from CGT event A1 happening, if the capital proceeds exceed the cost base of the Choiseul share, and makes a capital loss if the capital proceeds are less than the reduced cost base of the share (subsection 104-10(4)).

Capital proceeds

29. The capital proceeds from CGT event A1 are the total of the market value, as at the time of the CGT event, of the Milton share(s), or part thereof, referable to the Choiseul share to which the CGT event happens (paragraph 116-20(1)(b)).

30. The Interim Dividend and the Special Dividend do not form part of the capital proceeds.

Scrip for scrip roll-over

31. A participating Choiseul Shareholder who makes a capital gain from the disposal of their Choiseul shares in return for Milton shares may, subject to paragraph 32 of this Ruling, choose roll-over under Subdivision 124-M (section 124-780).

32. If the capital gain would be disregarded otherwise than by reason of roll-over under Subdivision 124-M, the roll-over cannot be chosen (subsection 124-795(2)).

33. If roll-over under Subdivision 124-M is chosen, the capital gain from CGT event A1 is disregarded (subsections 124-785(1)).

Discount capital gain

34. If a participating Choiseul Shareholder makes a capital gain and roll-over under Subdivision 124-M is not chosen, or cannot be chosen, they may be eligible to treat the gain as a discount capital gain provided that the participating Choiseul Shareholder satisfies the requirements of Subdivision 115-A.

Cost base of Milton shares***Scrip for scrip roll-over is not chosen***

35. Where roll-over under Subdivision 124-M is not chosen, the first element of the cost base and reduced cost base of each Milton share is equal to the market value of the Choiseul shares referable to the acquisition of the Milton share as at the time of that acquisition (subsections 110-25(2), 110-55(2) and 112-30(1)).

Scrip for scrip roll-over is chosen

36. Where roll-over under Subdivision 124-M is chosen, the first element of the cost base and reduced cost base of the replacement Milton share is worked out by reasonably attributing to it the cost base of each Choiseul share referable to its acquisition (subsections 124-785(2) and 124-785(4)).

Acquisition date of Milton shares

37. The acquisition date of the Milton shares is the date when the shares are issued or allotted (Item 2 of the table in section 109-10).

38. For the purpose of determining whether a capital gain made from any later disposal of Milton shares is eligible to be a discount capital gain, participating Choiseul Shareholders who choose scrip for scrip roll-over are taken to have acquired their Milton shares when they acquired the corresponding Choiseul shares (Item 2 of the table in subsection 115-30(1)).

Pre-CGT Choiseul shares

39. Roll-over is not available for Choiseul shares acquired prior to 20 September 1985 (paragraph 124-780(3)(a)) and a capital gain or capital loss on the disposal of such shares is disregarded (paragraph 104-10(5)(a)).

40. For Choiseul shares acquired prior to 20 September 1985, the first element of the cost base and reduced cost base of each Milton share referable to those Choiseul shares is the market value of the Milton share just after its acquisition (subsection 110-25(2) and 110-55(2)).

The Special and Interim Dividends

41. The Special Dividend of 16 cents and Interim Dividend of 10.5 cents per share paid to Choiseul shareholders (the Dividends) will each constitute a 'dividend' as defined in subsection 6(1) of the ITAA 1936.

Assessability of the Dividends

42. Choiseul shareholders who received the fully franked Dividends and are residents of Australia as defined in subsection 6(1) of the ITAA 1936 are required to include the Dividends as assessable income under subparagraph 44(1)(a)(i) of the ITAA 1936.

Gross up and tax offset

43. Choiseul shareholders who received the fully franked Dividends directly will:

- include the amount of the franking credit attached to the Dividends in their assessable income; and
- be entitled to a tax offset equal to the amount of the franking credit

under section 207-20, subject to being a qualified person.

Refundable tax offset

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

Qualified person rule

45. Having regard to the relevant circumstances of the Scheme, the Choiseul Shareholders are considered to have made, or to be likely to make a related payment in respect of the Dividends.

46. Accordingly, each Choiseul Shareholder will need to hold their Choiseul shares at risk for a continuous period of at least 45 days in the secondary qualification period in order to be a qualified person in respect of the Dividends.

47. Each Choiseul Shareholder will be considered to be a qualified person in respect of the secondary qualification period for the purposes of Division 1A of the former Part IIIA of the ITAA 1936 in relation to the Dividends if:

- (a) the Choiseul Shareholder acquired the Choiseul share or interest in the share on or before 26 October 2010; and
- (b) from 26 October 2010 until 9 December 2010, the Choiseul Shareholder continued to hold the Choiseul share and did not have 'materially diminished risks of loss or opportunities for gain' (as defined under former section 160APHM of the ITAA 1936) in respect of the Choiseul share for a continuous period of at least 45 days.

The anti-avoidance provisions

48. The Commissioner will not make a determination under paragraph 204-30(3)(c) to deny the whole, or any part, of the imputation benefit received in relation to either the Interim Dividend or the Special Dividend.

49. The Commissioner will not make a determination under paragraph 177EA(5)(b) of the ITAA 1936 to deny the whole, or any part, of the imputation benefit received in relation to either the Interim Dividend or the Special Dividend.

Commissioner of Taxation

1 December 2010

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.*

Scrip for scrip roll-over

50. The tax consequences and relevant legislative provisions that arise concerning the Scheme are outlined in the Ruling part of this document.

51. The significant tax consequence is availability of scrip for scrip roll-over under Subdivision 124-M. Scrip for scrip roll-over enables a shareholder to disregard a capital gain from a share that is disposed of as part of a corporate takeover or merger if the shareholder receives a replacement share in the exchange. It also provides special rules for calculating the cost base and reduced cost base of the replacement share.

52. Subdivision 124-M contains a number of conditions for, and exceptions to, a shareholder being eligible to choose scrip for scrip roll-over. The main conditions and exceptions that are relevant to the Scheme are:

- (a) shares in a company are exchanged for shares in another company;
- (b) the exchange occurs as part of a single arrangement;
- (c) conditions for roll-over are satisfied;
- (d) further conditions are not applicable or are satisfied; and
- (e) exceptions to obtaining scrip for scrip roll-over are not applicable.

53. Under the Scheme, the conditions for roll-over under Subdivision 124-M are satisfied. The Ruling section provides a detailed explanation of the Commissioner's decision. Therefore, no further explanation is warranted.

The Special and Interim Dividends

54. The term 'dividend' is defined in subsection 6(1) of the ITAA 1936 and includes any distribution made by a company to any of its shareholders.

55. The payment of the Special and Interim Dividends (the Dividends) are distributions of money by Choiseul to its shareholders.

56. However, paragraph (d) of the definition of 'dividend' in subsection 6(1) of the ITAA 1936 excludes from the definition of 'dividend' any:

moneys paid or credited by a company to a shareholder or any other property distributed by a company to shareholders (not being moneys or other property to which this paragraph, by reason of subsection (4), does not apply or moneys paid or credited, or property distributed for the redemption or cancellation of a redeemable preference share), where the amount of the moneys paid or credited, or the amount of the value of the property, is debited against an amount standing to the credit of the share capital account of the company...

57. The Dividends were sourced entirely from Choiseul's retained earnings and Choiseul did not debit the Dividends to its share capital account. Therefore, the exclusions in paragraph (d) will not apply and the Dividends will each constitute a 'dividend' for the purposes of subsection 6(1) of the ITAA 1936.

Assessability of the Dividends

58. Subparagraph 44(1)(a)(i) of the ITAA 1936 includes in the assessable income of an Australian resident shareholder in a company:

dividends (other than non-share dividends) that are paid to the shareholder by the company out of profits derived by it from any source.

59. As the Dividends were paid to Choiseul shareholders out of profits derived by Choiseul, Choiseul shareholders who are residents of Australia as defined in subsection 6(1) of the ITAA 1936 are required to include Dividends as assessable income.

Gross up and tax offset

60. Section 207-20 provides:

(1) If an entity makes a *franked distribution to another entity, the assessable income of the receiving entity, for the income year in which the distribution is made, includes the amount of the *franking credit on the distribution. This is in addition to any other amount included in the receiving entity's assessable income in relation to the distribution under any other provision of this Act.

(2) The receiving entity is entitled to a *tax offset for the income year in which the distribution is made. The tax offset is equal to the *franking credit on the distribution.

61. Therefore, subject to satisfying the qualified person rule, where the fully franked Dividends were received directly by a Choiseul shareholder, the Choiseul shareholder will:

- include the amount of the franking credit attached to the Dividends in their assessable income; and
- be entitled to a tax offset equal to the amount of the franking credit.

62. Where the fully franked Dividends were received by a Choiseul shareholder (not being an entity taxed as a corporate tax entity) that is a trustee of a trust (not being a complying superannuation fund) or a partnership, subsection 207-35(1) applies, subject to the trustee or partnership being a qualified person. Subsection 207-35(1) provides:

If:

- (a) a *franked distribution is made in an income year to an entity that is a partnership or the trustee of a trust; and
- (b) the entity is not a *corporate tax entity when the distribution is made; and
- (c) if the entity is the trustee of a trust – the trust is not a *complying superannuation entity or *FHSA trust when the distribution is made;

the assessable income of the partnership or trust for that income year includes the amount of the *franking credit on the distribution.

63. Therefore, subject to satisfying the qualified person rule, a Choiseul shareholder that is a trust or a partnership is required to include the amount of the franking credit attached to the Dividends in their assessable income under subsection 207-35(1).

Refundable tax offset

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

65. Pursuant to section 67-25, there are a range of taxpayers who are specifically excluded from the operation of the refundable tax offset rules. This range of excluded entities includes:

- non-complying superannuation funds or non-complying approved deposit funds (subsection 67-25(1A));
- a trustee of a trust who is liable to be assessed under section 98 or 99A of the ITAA 1936 (subsection 67-25(1B));
- corporate tax entities, unless the entity is an exempt institution that is eligible for a refund, or a life insurance company that has received distributions on membership interests which were not held by the company on behalf of its shareholders (subsections 67-25(1C) and (1D)); and
- foreign resident entities carrying on business in Australia at or through a permanent establishment (subsection 67-25(1DA)).

66. Accordingly, holders of Choiseul shares are subject to the refundable tax offset rules unless they are listed as specifically excluded entities under section 67-25. Generally, corporate tax entities (including companies, corporate limited partnerships, corporate unit trusts, and public trading trusts) will be excluded from the operation of the refundable tax offset rules.

Qualified persons

67. Former Division 1A¹ of the ITAA 1936 contains the measures known as the holding period rule and the related payment rule. In broad terms, former Division 1A of the ITAA 1936 provides the statutory tests that must be satisfied for a taxpayer to be a 'qualified person' with respect to a franked distribution they have received and thus be entitled to a tax offset for the franking credit attached to the distribution.

68. The test of what constitutes a 'qualified person' is provided in former section 160APHO of the ITAA 1936. Broadly speaking, to be a qualified person in relation to a dividend, a taxpayer must satisfy either the holding period rule or the related payment rule.

69. Former subsection 160APHO(1) of the ITAA 1936 states:

A taxpayer who has held shares or an interest in shares on which a dividend has been paid is a 'qualified person' in relation to the dividend if:

- (a) where neither the taxpayer nor an associate of the taxpayer has made, is under an obligation to make, or is likely to make, a related payment in respect of the dividend – the taxpayer has satisfied subsection (2) in relation to the primary qualification period in relation to the dividend; or
- (b) where the taxpayer or an associate of a taxpayer has made, is under an obligation to make, or is likely to make, a related payment in respect of the dividend – the taxpayer has satisfied subsection (2) in relation to the secondary qualification in relation to the dividend.

70. If a taxpayer is not under an obligation to make a related payment in relation to a dividend or distribution, the taxpayer will have to satisfy the holding period requirement within the primary qualification period. If a taxpayer is under an obligation to make a related payment in relation to a dividend or distribution, the taxpayer will have to satisfy the holding period requirement within the secondary qualification period.

¹ References to Division 1A of former Part IIIA of the ITAA 1936 and the provisions contained within that Division are references to the Division and those provisions as they existed on 30 June 2002.

71. In order to determine which is the relevant qualification period, it is necessary to determine whether, under the present arrangement, the current shareholders of Choiseul are considered to be under an obligation to make a related payment. Former section 160APHN of the ITAA 1936 provides non-definitive examples of what constitutes the making of a related payment for the purposes of former Division 1A of the ITAA 1936. Former subsection 160APHN(2) of the ITAA 1936 provides as follows:

The taxpayer or associate is taken, for the purposes of this Division, to have made, to be under an obligation to make, or to be likely to make, a related payment in respect of the dividend or distribution if, under an arrangement, the taxpayer or associate has done, is under an obligation to do, or may reasonably be expected to do, as the case may be, anything having the effect of passing the benefit of the dividend or distribution to one or more other persons.

72. Former subsection 160APHN(3) of the ITAA 1936 states:

Without limiting subsection (2), the doing of any of the following by the taxpayer or an associate of the taxpayer in the circumstances mentioned in subsection (4) may have the effect of passing the benefit of the dividend or distribution to one or more other persons:

- (a) causing a payment or payments to be made to, or in accordance with the directions of, the other person or other persons; or
- (b) causing an amount or amounts to be credited to, or applied for the benefit of, the other person or the other persons; or
- (c) causing services to be provided to, or in accordance with the directions of, the other person or other persons; or
- (d) causing property to be transferred to, or in accordance with directions of, the other person or other persons; or
- (e) allowing any property or money to be used by the other person or other persons or by someone nominated by the other person or other persons; or
- (f) causing an amount or amounts to be set off against, or to be otherwise applied in reduction of, a debt or debts owed by the other person or other persons to the taxpayer or associate; or
- (g) agreeing to treat an amount or amounts owed to the other person or other persons by the taxpayer or associate as having been increased.

73. Former subsection 160APHN(4) of the ITAA 1936 states:

The circumstances referred to in subsection (3), are where:

- (a) the amount or the sum of the amounts paid, credited or applied; or
- (b) the value or the sum of the values of the services provided, of the property transferred or of the use of the property or money; or
- (c) the amount or the sum of the amounts of the set-offs, reductions or increases;

as the case may be:

- (d) is, or may reasonably be expected to be, equal to; or
- (e) approximates or may reasonably be expected to approximate; or
- (f) is calculated by reference to;
the amount of dividend or distribution.

74. In the current circumstances, an integral part of the arrangement is the payment of the Interim Dividend of 10.5 cents and the Special Dividend of 16 cents per share. Further, it is clearly contemplated in the current arrangement that the Scheme Consideration is to be reduced by the aggregate amount of the interim dividend and the special dividend to be paid. The reduction is specifically calculated by reference to the amount of the interim dividend and special dividend paid.

75. As the Scheme clearly contemplates the reduction in the consideration for the disposal of a Choiseul share to be calculated by reference to the value of the Interim and Special Dividend paid pursuant to the Scheme, the reduction in the consideration is considered to constitute a notional crediting passing on the benefit of the proposed interim and special dividend from a Choiseul shareholder to Milton. As such, it is considered to constitute a related payment for the purposes of former section 160APHN of the ITAA 1936.

76. As the Choiseul shareholders are taken, for the purposes of former Division 1A of the ITAA 1936, to be under an obligation to make a related payment in respect of the interim and special dividend, the relevant holding period is therefore the secondary qualification period pursuant to former paragraph 160APHO(1)(b) of the ITAA 1936.

77. The secondary qualification period is defined in former section 160APHD of the ITAA 1936 as follows:

in relation to a taxpayer in relation to shares or an interest in shares, means:

- (a) if the shares are not preference shares – the period beginning on the 45th day before, and ending on the 45th day after, the day on which the shares or interest become *ex dividend*...

78. The concept of 'ex dividend' is defined by former subsection 160APHE(1) of the ITAA 1936 as follows:

A share in respect of which a dividend is to be paid, or an interest (other than an interest as a beneficiary of a widely held trust) in such a share, becomes *ex dividend* on the day after the last day on which the acquisition by a person of the share will entitle the person to receive the dividend.

79. Pursuant to the Scheme, Choiseul has advised that the record date for the Dividends is 9 December 2010. Accordingly, the ex-dividend date for the purposes of former subsection 160APHE(1) of the ITAA 1936 is 10 December 2010.

80. The secondary qualification period therefore begins 45 days before the ex dividend date of 10 December 2010 and ends 45 days after that day. In practical terms, this means that the secondary qualification period begins on 26 October 2010 and ends on 24 January 2011. However, pursuant to former subsection 160APHO(3) of the ITAA 1936, any days on which a taxpayer has materially diminished risks of loss or opportunities for gain in respect of the Choiseul shares are to be excluded. This would mean that the secondary qualification period would run from 26 October 2010 until the date that Choiseul shareholders are no longer at risk for the purposes of former Division 1A of the ITAA 1936.

81. In this context, entitlement to participate in the Scheme will be determined on the Scheme Record Date on the basis of being a Choiseul shareholder who is registered in the register as the holder of a relevant Scheme Share on 13 December 2010. It is considered that once a Choiseul Shareholder is identified as a participating Choiseul Shareholder, that Choiseul Shareholder would no longer be considered to hold their shares 'at risk' for the purposes of former Division 1A of the ITAA 1936 as at that time the Choiseul Shareholder is committed to disposing of their Choiseul share and receiving the Scheme Consideration.

82. Accordingly, the secondary qualification period would run from 26 October 2010 until 12 December 2010 (inclusive). Choiseul Shareholders who receive the Dividends would need to hold their shares at risk for a continuous period of not less than 45 days during this period in order to be a 'qualified person' for the purposes of former Division 1A of the ITAA 1936. Further, pursuant to former paragraph 160APHO(2)(a) of the ITAA 1936, the date of acquisition or disposal are not included in the relevant 45 day period. This would have the effect in the present circumstances, for example, that the 45 day qualification period could not include 26 October 2010 if this was the date of acquisition of Choiseul shares.

The anti-avoidance provisions

Section 204-30

83. Section 204-30 applies where a corporate tax entity streams the payment of dividends, or the payment of dividends and the giving of other benefits, to its members in such a way that:

- (a) an imputation benefit is, or apart from this section would be, received by a member of the entity as a result of the distribution or distributions (paragraph 204-30(1)(a));
- (b) the member would derive a greater benefit from franking credits than another member of the entity (paragraph 204-30(1)(b)); and

- (c) the other member of the entity will receive lesser imputation benefits, or will not receive any imputation benefits, whether or not the other member receives other benefits (paragraph 204-30(1)(c)).

84. Relevantly, if section 204-30 applies, the Commissioner is vested with a discretion under subsection 204-30(3) to make a determination in writing either:

- (a) that a specified franking debit arises in the franking account of the entity, for a specified distribution or other benefit to a disadvantaged member (paragraph 204-30(3)(a)); or
- (b) that no imputation benefit is to arise in respect of any distributions made to a favoured member and specified in the determination (paragraph 204-30(3)(c)).

85. For section 204-30 to apply, members to whom distributions are streamed must derive a greater benefit from franking credits than the members who consequently do not receive franking credits, or do not receive the same amount of franking credits as they would have had streaming not occurred.

86. Under the current Scheme for the payment of both the Interim Dividend and Special Dividend (the dividends), all Choiseul Shareholders will receive an imputation benefit as a result of the dividends; the resident shareholders in the form of a tax offset (paragraph 204-30(6)(a)) and the non-resident shareholders in the form of an exemption from dividend withholding tax (paragraph 204-30(6)(e)). The resident shareholders will derive a greater benefit from franking credits than the non-resident shareholders.

87. However, the dividends will be paid to all Choiseul Shareholders at the respective Record Dates and will be fully franked with Australian franking credits. Accordingly, it cannot be argued that Choiseul will direct the flow of distributions in such a manner as to stream the imputation benefits such that one class of members will derive a greater benefit from the franking credits attached to the dividends, while the other members will receive lesser or no imputation benefits.

88. As the conditions in subsection 204-30(1) for the provision to apply will not be met, the Commissioner will not make a determination under paragraph 204-30(3)(c) to deny the whole, or any part, of the imputation benefit received in relation to either of the dividends.

Section 177EA

89. Section 177EA of the ITAA 1936 is a general anti-avoidance provision that applies to a wide range of schemes seeking to obtain a tax advantage in relation to imputation benefits. Subsection 177EA(3) of the ITAA 1936 provides that section 177EA applies if:

- (a) there is a scheme for a disposition of membership interests, or an interest in membership interests, in a corporate tax entity; and
- (b) either:
 - (i) a frankable distribution has been paid, or is payable or expected to be payable, to a person in respect of the membership interests; or
 - (ii) a frankable distribution has flowed indirectly, or flows indirectly or is expected to flow indirectly, to a person in respect of the interest in membership interests, as the case may be; and
- (c) the distribution was, or is expected to be, a franked distribution or a distribution franked with an exempting credit; and
- (d) except for this section, a person (the *relevant taxpayer*) would receive, or could reasonably be expected to receive, imputation benefits as a result of the distribution; and
- (e) having regard to the relevant circumstances of the scheme, it would be concluded that the person, or one of the persons, who entered into or carried out the scheme or any part of the scheme did so for a purpose (whether or not the dominant purpose but not including an incidental purpose) of enabling the relevant taxpayer to obtain an imputation benefit.

90. If section 177EA of the ITAA 1936 applies, the Commissioner may make a determination under subsection 177EA(5) of the ITAA 1936 that either a franking debit arises to the company in respect of each distribution paid to the relevant taxpayer (paragraph 177EA(5)(a) of the ITAA 1936) or, in the alternative, that no franking credit benefit arises in respect of a distribution paid to the relevant taxpayer (paragraph 177EA(5)(b) of the ITAA 1936).

91. Choiseul is a corporate tax entity. The disposal of the ordinary shares in Choiseul pursuant to the Scheme is a scheme for the disposition of membership interests. Both the fully franked Interim Dividend and Special Dividend are frankable distributions that will be paid to Choiseul Shareholders as a part of this Scheme who could, therefore, reasonably be expected to receive imputation benefits.

92. In the present case, the conditions of paragraphs 177EA(3)(a) to (d) of the ITAA 1936 are satisfied. Accordingly, the issue is whether having regard to the relevant circumstances of the Scheme, it would be concluded that, on the part of Choiseul or its shareholders, there is a purpose, more than merely an incidental purpose, of conferring an imputation benefit under the Scheme.

93. In arriving at a conclusion the Commissioner must have regard to the relevant circumstances of the Scheme which include, but are not limited to, the circumstances set out in subsection 177EA(17) of the ITAA 1936. The relevant circumstances listed there encompass a range of circumstances which taken individually or collectively could indicate the requisite purpose. Due to the diverse nature of these circumstances, some may not be present at any one time in any one scheme.

94. The relevant circumstances of the Scheme indicate that there is no requisite purpose of conferring an imputation benefit under the Scheme. The dividends have been and will be fully franked, which is a continuation of Choiseul's dividend policy to pay fully franked dividends. Choiseul has only ordinary shares on issue and the dividends have been and will be paid to all Choiseul Shareholders on a pro-rata basis in proportion to the number of shares that each Choiseul shareholder holds on the relevant Record Dates for the dividends. The amount of the Interim Dividend is largely consistent with dividends previously paid out by Choiseul and allowed Choiseul shareholders to share in the current profits of Choiseul for the income half year ended 31 December 2010.

95. In considering the manner, form and substance of the Scheme, it is considered that the Scheme is not being entered into for the purpose of enabling participating members to obtain an imputation benefit. Having regard to the relevant circumstances of the Scheme, the Commissioner has come to the view that the requisite purpose is not present and accordingly the Commissioner will not make a determination under paragraph 177EA(5)(b) of the ITAA 1936 to deny the whole, or any part, of the imputation benefit received in relation to the dividends.

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References

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Related Rulings/Determinations:

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- imputation system
- ordinary shares
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- related payment rule

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