


CR 2011/88 - Income tax: demerger of shares in Cordlife Pte Ltd by Cordlife Limited

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Class Ruling

Income tax: demerger of shares in Cordlife Pte Ltd by Cordlife 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 dealt with in this Ruling are:

- subsection 6(1) of the *Income Tax Assessment Act 1936* (ITAA 1936);
- section 45A of the ITAA 1936;
- section 45B of the ITAA 1936;
- section 45C of the ITAA 1936;
- section 104-25 of the *Income Tax Assessment Act 1997* (ITAA 1997);
- section 104-135 of the ITAA 1997;
- section 109-5 of the ITAA 1997;
- subsection 110-25(2) of the ITAA 1997;
- subsection 110-55(2) of the ITAA 1997; and

- section 855-10 of the ITAA 1997.

All subsequent legislative references in this Ruling are to the ITAA 1936 unless otherwise stated.

Class of entities

3. The class of entities to which this Ruling applies consists of the holders of ordinary shares in Cordlife Limited (CBB) who:

- (a) were listed on the share register of CBB as at the Record Date (28 June 2011) for the distribution of shares in Cordlife Pte Ltd (CPL);
- (b) held their CBB ordinary shares on capital account on the Record Date; and
- (c) are not subject to the taxation of financial arrangements rules in Division 230 of the ITAA 1997 in relation to gains and losses on their CBB shares.

(Note – Division 230 of the ITAA 1997 will generally not apply to individuals, unless they have made an election for it to apply to them.)

In this Ruling, a person belonging to this class of entities is referred to as a 'CBB shareholder'.

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 documents and information provided by the applicant.

Note: where certain information has been provided by the applicant on a commercial-in-confidence basis, it will not be disclosed or released under the Freedom of Information legislation.

CBB

10. CBB is an Australian resident company, incorporated on 19 February 2004, which is listed on the Australian Securities Exchange (ASX). CBB is engaged in the provision of cord blood banking services in the Asia Pacific region.

11. As at 16 May 2011, CBB had not made a profit and had no retained earnings.

12. As at the Record Date, CBB had on issue 150,887,354 fully paid ordinary shares. Approximately 85% of the ordinary shares in CBB were held by foreign residents.

CPL

13. CPL is a wholly owned subsidiary of CBB, incorporated and resident for tax purposes in Singapore.

The distribution of shares in CPL

14. On 16 May 2011, CBB announced its intention to restructure the CBB group by:

- CPL issuing a Class A share to CBB which gives CBB the right (but not an obligation) to repurchase all of the CPL ordinary shares by a specified future date in certain circumstances, in consideration for new CBB ordinary shares;
- distributing all of the ordinary shares in CPL to the shareholders of CBB;
- CBB issuing a bond to an investor to obtain additional funding, as well as granting the investor an option to subscribe for 21.8 million new CBB ordinary shares at an exercise price of \$0.40 per share.

This Ruling only considers the distribution of ordinary shares in CPL.

15. After the restructure:

- CBB will focus on the developing blood bank businesses in India, Indonesia and the Philippines (Developing Businesses); and
- CPL will own the more mature blood bank businesses in Singapore and Hong Kong, and a 10% interest in the operator of the sole cord blood banking licensee in the Guangdong province of China (Mature Businesses).

16. On 16 June 2011, the shareholders of CBB voted at an Extraordinary General Meeting to effect the distribution of CPL shares by approving an ordinary resolution to reduce the share capital of CBB. The amount of the reduction was \$29,473,000 (the capital reduction amount). This equates to 19.53 cents per CBB ordinary share.

17. The capital reduction amount was satisfied by an *in specie* distribution to the shareholders of CBB of all of the ordinary shares in CPL. The shareholders of CBB received one CPL ordinary share for every CBB ordinary share they owned at the Record Date for the distribution (28 June 2011).

18. The distribution of shares happened on 30 June 2011 (the Payment Date).

19. CBB debited the entire amount of the *in specie* distribution against its share capital account.

20. As a result of the *in specie* distribution, there was no change in either the number of CBB shares held by, or the proportionate interest of, each shareholder in CBB.

21. After the distribution of shares in CPL, the shareholders of CBB directly hold shares in two separate companies (CBB and CPL).

22. The Board of Directors of CBB is of the view that greater shareholder value will be realised by separating CPL and CBB, given the different cash flow, growth prospects and risk profiles of the Developing Businesses and the Mature Businesses.

Other matters

23. None of the shareholders of CBB acquired their shares in CBB before 20 September 1985.

24. CBB has never paid a dividend to its shareholders. CBB has not previously issued bonus shares, or made a return of capital or share premium to its shareholders.

25. CBB has confirmed that no amounts have been transferred to its share capital account (as defined in section 975-300 of the ITAA 1997) from any of its other accounts, and accordingly its share capital account is not tainted (within the meaning of Division 197 of the ITAA 1997).

Ruling

Distribution is not a dividend for income tax purposes

26. The *in specie* distribution to CBB shareholders of CPL shares under the scheme is not a dividend as defined in subsection 6(1).

The application of sections 45A, 45B and 45C to the distribution of shares

27. The Commissioner will not make a determination under subsection 45A(2) that section 45C applies to the whole, or any part, of the capital benefit provided to CBB shareholders under the distribution of CPL shares.

28. The Commissioner will not make a determination under paragraph 45B(3)(b) that section 45C applies to the whole, or any part, of the capital benefit provided to CBB shareholders under the distribution of CPL shares.

Capital gains tax

29. CGT event G1 (section 104-135 of the ITAA 1997) will happen when CBB makes the *in specie* distribution of a CPL share to a CBB shareholder in respect of a CBB share that they own at the Record Date and continue to own at the Payment Date.

30. CGT event C2 (section 104-25 of the ITAA 1997) will happen when CBB makes the *in specie* distribution to a CBB shareholder of a CPL share in respect of a CBB share that they owned at the Record Date but which they ceased to own before the Payment Date.

Foreign resident shareholders

31. A foreign resident CBB shareholder who receives the *in specie* distribution of CPL shares disregards any capital gain made when CGT event G1 happens if their CBB shares are not 'taxable Australian property' (section 855-10 of the ITAA 1997).

32. A foreign resident CBB shareholder who receives the *in specie* distribution of CPL shares disregards any capital gain or capital loss made when CGT event C2 happens if their right to receive the distribution is not 'taxable Australian property' (section 855-10 of the ITAA 1997).

Cost base of CPL shares

33. The first element of the cost base and reduced cost base of a CPL ordinary share received by a CBB shareholder pursuant to the *in specie* distribution will equal the money paid (as a result of the capital reduction amount being applied on behalf of each CBB shareholder) to acquire the CPL ordinary share (subsections 110-25(2) and 110-55(2) of the ITAA 1997).

Acquisition time of CPL shares

34. A CBB shareholder will acquire the CPL ordinary shares they receive under the *in specie* distribution, as a result of CGT event G1 or CGT event C2 happening, at the time when they become a shareholder in CPL. This will be on the Payment Date (subsection 109-5(1) of the ITAA 1997).

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.*

Distribution is not a dividend for income tax purposes

35. Subsection 44(1) includes in a shareholder's assessable income any dividends, as defined in subsection 6(1), paid to the shareholders out of profits derived by the company from any source (if the shareholder is a resident of Australia) and from an Australian source (if the shareholder is a non-resident).

36. The term 'dividend' in subsection 6(1) includes any distribution made by a company to any of its shareholders. However, paragraph (d) of the definition of 'dividend' in subsection 6(1) excludes a distribution from being a 'dividend' if the amount of the distribution is debited against an amount standing to the credit of the company's share capital account.

37. The term 'share capital account' is defined in section 975-300 of the ITAA 1997 as an account which the company keeps of its share capital, or any other account created on or after 1 July 1998 where the first amount credited to the account was an amount of share capital.

38. Subsection 975-300(3) of the ITAA 1997 states that an account is generally taken not to be a share capital account if it is tainted. Section 197-50 of the ITAA 1997 states that a company's share capital account becomes tainted when an amount to which Division 197 of the ITAA 1997 applies is transferred to the account, and the account is not already tainted.

39. The capital reduction amount (that was satisfied by the *in specie* distribution) was debited against an amount standing to the credit of CBB's share capital account, which was not tainted within the meaning of Division 197 of the ITAA 1997. Therefore, paragraph (d) of the definition of 'dividend' in subsection 6(1) will apply and the *in specie* distribution will not constitute a dividend under subsection 6(1).

Subsection 6(4)

40. The exclusion in paragraph (d) of the definition of dividend in subsection 6(1) is limited by subsection 6(4) which applies in circumstances where, under an arrangement:

- (a) a company raises share capital, receiving either cash or property from a person or group of persons, crediting the amount of money or the value of the property to its share capital account; and

- (b) returns the money or property to another person or group of persons, debiting the amount of the money or the value of the property to its share capital account.

41. In the scheme that is the subject of this Ruling, there is no arrangement under which CBB raised share capital from certain shareholders and then distributed the capital raised to other shareholders. Accordingly, subsection 6(4) will not apply to the *in specie* distribution.

Anti-avoidance provisions

42. Sections 45A and 45B are two anti-avoidance provisions which, if they apply, allow the Commissioner to make a determination that section 45C applies to treat all or part of the *in specie* distribution received by CBB shareholders as an unfranked dividend.

Section 45A – streaming of dividends and capital benefits

43. Section 45A applies in circumstances where capital benefits are streamed to certain shareholders (the advantaged shareholders) who derive a greater benefit from the receipt of capital and it is reasonable to assume that the other shareholders (the disadvantaged shareholders) have received or will receive dividends.

44. CBB will provide all of its shareholders with a 'capital benefit' (as defined in paragraph 45A(3)(b)) in direct proportion to their individual share holding. As all shareholders benefit equally from the *in specie* distribution, there is no 'streaming' of capital benefits to some shareholders and dividends to other shareholders.

45. Accordingly, section 45A will not apply to the *in specie* distribution. The Commissioner will not make a determination under subsection 45A(2) that section 45C applies to the whole, or any part, of the capital benefit provided to CBB shareholders under the distribution of CPL shares.

Section 45B – schemes to provide capital benefits in substitution for dividends

46. Section 45B applies where certain capital payments are made to shareholders in substitution for dividends.

47. Subsection 45B(2) sets out the conditions under which the Commissioner may make a determination under subsection 45B(3) that section 45C applies. These conditions are that:

- there is a scheme under which a person is provided with a capital benefit by a company (paragraph 45B(2)(a));
- under the scheme, a taxpayer (the 'relevant taxpayer'), who may or may not be the person provided with the

- capital benefit, obtains a tax benefit (paragraph 45B(2)(b)); and
- 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 a tax benefit (paragraph 45B(2)(c)).

Each of these conditions is considered in paragraphs 48 to 61 of this Ruling.

Scheme

48. A 'scheme' for the purposes of section 45B is defined in subsection 177A(1) to include:

- any agreement, arrangement, understanding, promise or undertaking, whether express or implied and whether or not enforceable, or intended to be enforceable, by legal proceedings; and
- any scheme, plan, proposal, action, course of action or course of conduct.

49. The arrangement involving the *in specie* distribution by CBB will constitute a 'scheme' for the purposes of section 45B.

Capital benefit

50. The phrase 'provided with a capital benefit' is defined in subsection 45B(5). It states that a person is provided with a capital benefit if:

- (a) an ownership interest in a company is issued to the person;
- (b) there is a distribution to the person of share capital; or
- (c) the company does something in relation to an ownership interest that has the effect of increasing the value of the ownership interest (which may or may not be the same interest) held by that person.

51. As the *in specie* distribution will be recorded as a debit to the share capital account, its shareholders will receive a distribution of share capital. Therefore, they will be provided with a capital benefit under paragraph 45B(5)(b).

Tax benefit

52. A taxpayer 'obtains a tax benefit', as defined in subsection 45B(9), if:

- the amount of tax payable; or
- any other amount payable under the ITAA 1936 or the ITAA 1997,

would, apart from the operation of section 45B,

- be less than the amount that would have been payable; or
- be payable at a later time than it would have been payable,

if the capital benefit had instead been a dividend.

53. Ordinarily, the *in specie* distribution (which is a capital benefit) would be subject to the CGT provisions of the income tax legislation. Unless the amount of the distribution exceeds the cost base of the shares, there will only be a cost base reduction under CGT event G1 (section 104-135 of the ITAA 1997). It is only to the extent (if any) that the distribution exceeds the cost base of the shares that a capital gain arises. A capital gain may not arise at all for certain foreign resident shareholders under section 855-10 of the ITAA 1997. By contrast, a dividend would generally be included in the assessable income of a resident shareholder or, in the case of a foreign resident, be subject to dividend withholding tax under section 128B. Therefore, CBB shareholders will obtain a tax benefit from the *in specie* distribution.

Relevant circumstances

54. Under paragraph 45B(2)(c) the Commissioner is required to consider the 'relevant circumstances' set out in subsection 45B(8) to determine whether any part of the scheme would be entered into for a purpose, other than an incidental purpose, of enabling a relevant taxpayer to obtain a tax benefit. However, the list of relevant circumstances in subsection 45B(8) is not exhaustive and regard may be had to other circumstances on the basis of their relevance.

55. The test of purpose is an objective one. The question is whether it would be concluded that a person who entered into or carried out the scheme did so for the purpose of obtaining a tax benefit for the relevant taxpayer in respect of the capital benefit. The requisite purpose does not have to be the most influential or prevailing purpose, but it must be more than an incidental purpose.

56. The purpose which causes section 45B to apply may be the purpose of any party to the scheme.

57. The relevant circumstances under subsection 45B(8) cover the circumstances of CBB and the tax profile of the shareholders of CBB. In this instance, because the *in specie* distribution will be made to all of the shareholders of CBB holding ordinary shares, regardless of their individual circumstances, paragraphs 45B(8)(c) to (h) do not incline towards or against a conclusion as to purpose. The circumstances covered by paragraphs 45B(8)(i) and (j), pertaining to the provision of ownership interests and a demerger respectively, are not relevant in this case. The relevant matters are those covered by the circumstances described in paragraphs 45B(8)(a), (b) and (k).

58. Paragraph 45B(8)(a) refers to the extent to which the capital benefit is attributable to capital or profits (realised and unrealised) of the company or an associate (within the meaning of section 318) of the company. In this case, the *in specie* distribution is made entirely out of share capital. No part of the distribution is being made out of profits. In these circumstances, the *in specie* distribution is wholly attributable to capital, and not to any realised or unrealised profits, of CBB.

59. Paragraph 45B(8)(b) refers to the pattern of distributions of dividends, bonus shares and returns of capital or share premium by the company or an associate (within the meaning of section 318) of the company. CBB has never paid a dividend. CBB has not previously issued bonus shares, or made a return of capital or share premium. Accordingly, CBB's pattern of distributions does not suggest that the *in specie* distribution is being made in substitution for dividends.

60. Paragraph 45B(8)(k) refers to the matters in subparagraphs 177D(b)(i) to (viii). These are matters by reference to which a scheme is able to be examined from a practical perspective in order to identify and compare its tax and non-tax objectives. The matters include the manner in which the scheme is carried out, the timing of the scheme, its form and substance, and its financial and other implications for the parties involved.

61. In this case, the practical implications of the scheme for CBB and its shareholders are consistent with it being, in form and substance, a distribution of share capital.

62. Accordingly, section 45B will not apply to the *in specie* distribution. The Commissioner will not make a determination under paragraph 45B(3)(b) that section 45C applies to the whole, or any part, of the capital benefit provided to CBB shareholders under the distribution of CPL shares.

Capital gains tax

CGT event G1 – section 104-135

63. CGT event G1 (section 104-135 of the ITAA 1997) happens when:

- a company makes a payment (which can include giving property) to a shareholder in respect of a share they own in the company;
- some or all of the payment is not a dividend (as defined in subsection 995-1(1) of the ITAA 1997) or an amount that is taken to be a dividend under section 47 of the ITAA 1936; and
- the payment is not included in the shareholder's assessable income.

64. No part of the *in specie* distribution to a CBB shareholder will be a dividend.

65. Accordingly, CGT event G1 will happen when CBB pays the *in specie* distribution to a CBB shareholder in respect of a CBB share that they own at the Record Date and continue to own at the Payment Date.

66. If the amount of the distribution (19.53 cents per CBB share) is equal to or less than the cost base of the CBB share at the Payment Date, the cost base and reduced cost base of the share will be reduced (but not below nil) by the amount of the distribution (subsection 104-135(4) of the ITAA 1997).

67. A CBB shareholder will make a capital gain if the amount of the distribution (19.53 cents per CBB share) is more than the cost base of the CBB share (subsection 104-135(3) of the ITAA 1997). The amount of the capital gain is equal to the excess.

68. If a CBB shareholder makes a capital gain from CGT event G1 happening, the cost base and reduced cost base of the CBB share are reduced to nil. A CBB shareholder cannot make a capital loss from CGT event G1 happening (subsection 104-135(3) of the ITAA 1997).

69. If the CBB share to which the *in specie* distribution relates was acquired by a CBB shareholder at least 12 months before the payment, a capital gain from CGT event G1 happening may qualify as a discount capital gain under subsection 115-25(1) of the ITAA 1997, provided the other conditions in Division 115 of the ITAA 1997 are satisfied.

CGT event C2 – section 104-25

70. The right to receive the payment of the *in specie* distribution is one of the rights inherent in a CBB share at the Record Date. If, after the Record Date but before the Payment Date, a CBB shareholder ceased to own a share in CBB, the right to receive the payment of the *in specie* distribution in respect of that share will be retained by the shareholder and is considered to be a CGT asset separate from the CBB share to which the right relates.

71. In this situation, CGT event C2 (section 104-25 of the ITAA 1997) will happen when the *in specie* distribution is paid on the Payment Date. The right to receive the distribution (being an intangible CGT asset) will end by the right being discharged or satisfied when the distribution is paid.

72. A CBB shareholder will make a capital gain if the capital proceeds from the ending of the right are more than its cost base. The capital gain is equal to the amount of the excess. A CBB shareholder will make a capital loss if the capital proceeds from the ending of the right are less than the reduced cost base of the right. The capital loss is equal to the amount of the difference (subsection 104-25(3) of the ITAA 1997).

73. In working out the capital gain or capital loss made when CGT event C2 happens, the capital proceeds will be the market value of the CPL ordinary shares received under the *in specie* distribution, worked out as at the time of CGT event C2, which is when the distribution is paid (subsection 116-20(1) of the ITAA 1997).

74. The cost base of a CBB shareholder's right to receive the *in specie* distribution is worked out under Division 110 of the ITAA 1997 (modified by Division 112 of the ITAA 1997). The cost base of the right does not include the cost base or reduced cost base of the previously owned CBB share that has already been applied in working out the capital gain or capital loss made when a CGT event happened to that share – for example, when the CBB shareholder disposed of the CBB share after the Record Date but before the Payment Date.

75. Therefore, if the full cost base or reduced cost base of a CBB share has been previously applied in working out a capital gain or capital loss made when a CGT event happened to that share, the right to receive the *in specie* distribution should have a nil cost base.

76. As the right to receive the *in specie* distribution was inherent in the CBB share during the time it was owned, the right is considered to have been acquired at the time when the corresponding share was acquired (section 109-5 of the ITAA 1997).

77. Accordingly, if the CBB share was acquired by the CBB shareholder at least 12 months before the *in specie* distribution was paid, a capital gain from CGT event C2 happening on the ending of the corresponding right may qualify as a discount capital gain under subsection 115-25(1) of the ITAA 1997, provided the other conditions in Division 115 of the ITAA 1997 are satisfied.

Foreign resident shareholders

78. Under subsection 855-10(1) of the ITAA 1997, an entity disregards a capital gain or capital loss from a CGT event if they are a foreign resident, or the trustee of a foreign trust for CGT purposes, just before the CGT event happens, and the CGT event happens in relation to a CGT asset that is not 'taxable Australian property'.

79. The term 'taxable Australian property' is defined in the table in section 855-15 of the ITAA 1997. The table sets out these five categories of CGT assets:

Item 1	taxable Australian real property
Item 2	an indirect Australian real property interest not covered by item 5
Item 3	a CGT asset used at any time in carrying on a business through a permanent establishment in Australia and which is not covered by item 1, 2 or 5
Item 4	an option or right to acquire a CGT asset covered by item 1, 2 or 3
Item 5	a CGT asset that is covered by subsection 104-165(3) of the ITAA 1997 (choosing to disregard a capital gain or capital loss on ceasing to be an Australian resident)

80. A CBB shareholder that is a foreign resident, just before CGT event G1 happens, disregards any capital gain made when CGT event G1 happens if their CBB shares are not 'taxable Australian property' (section 855-10 of the ITAA 1997).

81. A CBB shareholder that is a foreign resident, just before CGT event C2 happens, who has a right to the payment of the *in specie* distribution, disregards any capital gain or capital loss made when CGT event C2 happens if that right is not 'taxable Australian property' (section 855-10 of the ITAA 1997).

Appendix 2 – Detailed contents list

82. 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:

- capital benefit
- capital gains tax
- CGT event G1
- CGT event C2
- dividends
- share capital
- return of capital

Legislative references:

- ITAA 1936
- ITAA 1936 6(1)
- ITAA 1936 6(4)
- ITAA 1936 44(1)
- ITAA 1936 45A
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- ITAA 1936 45A(3)(b)
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ATO references

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Income Tax ~~ Capital Gains Tax ~~ CGT events C1 to
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Income Tax ~~ Capital Gains Tax~~ CGT events G1 to
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