


# ***CR 2012/112 - Income tax: issue of CPS2 by Suncorp Group Limited***

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## Class Ruling

### Income tax: issue of CPS2 by Suncorp Group 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

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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 6BA of the *Income Tax Assessment Act 1936* (ITAA 1936);
- subsection 44(1) of the ITAA 1936;
- section 45 of the ITAA 1936;
- section 45A of the ITAA 1936;
- section 45B of the ITAA 1936;
- section 177EA of the ITAA 1936;
- former Division 1A of Part IIIAA of the ITAA 1936;
- section 6-5 of the *Income Tax Assessment Act 1997* (ITAA 1997);
- Division 67 of the ITAA 1997;

- Division 104 of the ITAA 1997;
- section 109-5 of the ITAA 1997;
- section 109-10 of the ITAA 1997;
- section 110-25 of the ITAA 1997;
- section 110-55 of the ITAA 1997;
- Subdivision 130-A of the ITAA 1997;
- section 204-30 of the ITAA 1997;
- Division 207 of the ITAA 1997; and
- section 960-120 of the ITAA 1997.

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

## **Class of entities**

3. The class of entities to which this Ruling applies are acquirers (referred to in this Ruling as Holders) of perpetual, convertible, unguaranteed and unsecured preference shares issued by Suncorp Group Limited (SGL) called Suncorp Group Limited Convertible Preference Shares (CPS2) and who:

- are Australian residents (within the meaning of subsection 6(1) of the ITAA 1936);
- hold the allotted CPS2 on capital account; and
- are not subject to the Taxation of Financial Arrangements (TOFA) rules in Division 230 in relation to financial arrangements under the scheme.

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

4. The class of entities to which this Ruling applies does not extend to Holders of CPS2 who acquired their CPS2 otherwise than by initial application under the Suncorp Group Limited CPS2 Prospectus dated 25 September 2012 and subsequently updated on 3 October 2012 (the Prospectus).

## **Qualifications**

5. This Ruling addresses the tax implications for Holders of holding and conversion of CPS2 into ordinary shares in SGL (SGL Ordinary Shares), a non-operating holding company (NOHC).

6. This Ruling does not deal with how the taxation law applies to Holders who hold their CPS2 as trading stock or revenue assets.

7. This Ruling does not consider the tax implications of the Exchange of CPS2 by Redemption or Resale.
8. This Ruling does not consider how the taxation law applies to the Nominated Purchaser who acquired their CPS2 under the Resale facility.
9. This Ruling does not consider how the gross-up and tax offset rules in Division 207 apply to partnership or trustee Holders, or to indirect distributions to partners in a partnership, or beneficiaries or trustees of a trust.
10. This Ruling does not deal with how the taxation law applies to SGL in relation to the issue of the CPS2.
11. 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 15 to 61 of this Ruling.
12. 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**

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14. This Ruling applies from 6 November 2012 to 30 June 2020. The Ruling continues to apply after 30 June 2020 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

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15. 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 Class Ruling dated 3 October 2012 (Application);
- the Prospectus;
- Suncorp CPS2 Terms as included in Appendix A of the Prospectus (the Terms);
- letter from the Australian Prudential Regulatory Authority (APRA) dated 24 September 2012 (APRA Letter);
- Australian Securities Exchange (ASX) Announcement dated 25 September 2012 (ASX Announcement);
- Offer Management Agreement between SGL, ANZ Securities Limited, National Australia Bank Limited, RBS Morgans Limited, UBS AG, Australia Branch and Westpac Institutional Bank (a division of Westpac Banking Corporation) dated 25 September 2012;
- additional information provided in response to the ATO's request for further information dated 30 July 2012;
- Suncorp Group ASX Announcement 'Suncorp closes CPS2 offer raising \$560 million' dated 6 November 2012; and
- various correspondence and additional information provided by Greenwoods & Freehills up to 7 November 2012.

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

16. In this Ruling, unless otherwise defined, capitalised terms take on the same meaning as in the Terms.

### SGL

17. SGL is an Australian resident company.

18. SGL is a NOHC that is the ASX listed parent company of the Suncorp Group. SGL is also authorised in Australia as a NOHC of the Suncorp Group under the *Insurance Act 1973* (Cth) and is subject to prudential regulation by the APRA.

19. The Suncorp Group is comprised of three separate lines of business, being General Insurance, Banking and Life. Each business line has its own NOHC and a corporate shared services group.

20. Each business line NOHC is owned 100% by SGL. Suncorp Metway-Limited (SML), while no longer the Suncorp Group's holding company, remains the group's Authorised Deposit-taking Institution (ADI).

### **Transaction**

21. In the Prospectus, SGL announced its intention to raise approximately \$500 million with the ability to raise more or less, through an offer of CPS2 (the Offer).

22. The CPS2 were issued on 6 November 2012 and raised \$560 million.

23. The capital raised from the Offer will be used for general corporate, funding and capital management purposes of the Suncorp Group, including maintaining the appropriate levels of gearing following the proposed redemption of certain of SML's regulatory capital instruments. SGL will invest all or some of the proceeds of the issue in notes to be issued by SML (SML Notes). The Offer is part of SGL's continuing capital management strategy within the guidelines prescribed by APRA.

24. In the APRA letter, APRA confirmed that the CPS2 will be treated as Residual Tier 1 capital under APRA's current prudential standard *GPS 112 Capital Adequacy: Measurement of Capital (July 2010)* (GPS 112). APRA also confirmed that, subject to SGL obtaining shareholder approval by 31 March 2013 to amend its constitution, with effect from 1 January 2013, CPS2 will qualify as Additional Tier 1 Capital under *Draft GPS 112 Capital Adequacy: Measurement of Capital (May 2012)*. The continued recognition of the CPS2 as Additional Tier 1 capital after their first call date will be subject to their compliance with the final GPS 112 giving effect to the implementation of the Basel III capital reforms in Australia (per the APRA Letter).

25. The classes of applicants for CPS2 and how they applied for the CPS2 are:

- Securityholder Applicant – a holder of either SGL Ordinary Shares, RPS (fully paid reset preference shares issued by SML on or about 30 August 2001 according to the terms of issue set out in the information memorandum dated 16 August 2001 and the placement offer letter dated 3 September 2001), Floating Rate Capital Notes (floating rate capital notes issued by SML in 1998 under a prospectus dated 26 October 1998) or CPS1 (convertible preference share issued by SML in 2008 under a prospectus dated 14 May 2008 which replaced a prospectus dated 6 May 2008) shown on the Register with an address in Australia and who applied through the Securityholder Offer;

- General Applicant – a member of the general public who is an Australian resident and applied under the General Offer;
- Broker Firm Applicant – an Australian resident retail or high net worth client of a Syndicate Broker invited to participate through the Broker Firm Offer; and
- Institutional Investors – an investor to whom offers or invitations in respect of CPS2 could be made without the need for a lodged prospectus (or other formality, other than a formality which SGL is willing to comply with), including in Australia a person to whom offers or invitations could be made without the need for a lodged prospectus under section 708 of the *Corporations Act 2001* (Corporations Act) and who has been invited by the Joint Lead Managers to bid for CPS2 in the Bookbuild, provided that such investor may not be in the United States.

26. The Prospectus states that no action has been taken to register or qualify the CPS2 or the Offer or to otherwise permit a public offering of the CPS2 outside Australia. However, subject to SGL's approval, the CPS2 may be offered in certain permitted jurisdictions outside Australia under the Institutional Offer where such offer is made, and accepted in accordance with the laws of such jurisdictions.

### **Main features of CPS2**

27. CPS2 are perpetual, fully paid, mandatorily convertible non-cumulative preference shares in the capital of SGL.

28. The issue price of each CPS2 was \$100 and was fully paid up to the \$100 value on issue.

29. A Holder does not have voting rights, except in the limited circumstances as set out in clause 12.1 of the Terms.

30. The CPS2 are listed on the ASX and trade under the ASX code 'SUNPC'.

### **Dividend calculation**

31. Subject to the conditions set out in paragraphs 33 to 36 of this Ruling, pursuant to clause 2.1 of the Terms, the Holder of each CPS2 is entitled to receive, on the relevant Dividend Payment Date, a dividend calculated using the following formula (Dividend):

$$\text{Dividend} = \frac{\text{Dividend Rate} \times \$100 \times \text{N}}{365}$$

where:

**Dividend Rate** (expressed as a percentage per annum) is calculated as follows:

$$\text{Dividend Rate} = (\text{Bank Bill Rate} + \text{Margin}) \times (1 - T)$$

where:

**Bank Bill Rate** (expressed as a percentage per annum) means, for a Dividend Period, the average mid-rate for bills of a term of 90 days which average mid-rate is displayed on Reuters page BBSW (or any page which replaces that page) on the first Business Day of the Dividend Period or, if there is a manifest error in the calculation of that average mid-rate or that average mid-rate is not displayed by 10:30am (Sydney time) on that date, the rate specified in good faith by SGL at or around that time on that date having regard, to the extent possible, to:

- (a) the rates otherwise bid and offered for bills of a term of 90 days or for funds of that tenor displayed on Reuters page BBSW (or any page which replaces that page) at that time on that date; or
- (b) if bid and offer rates for bills of a term of 90 days are not otherwise available, the rates otherwise bid and offered for funds of that tenor at or around that time on that date;

**Margin** (expressed as a percentage per annum) means the margin determined under the Bookbuild;

**T** (expressed as a decimal) means the Australian corporate tax rate applicable to the franking account of SGL at the relevant Dividend Payment Date; and

**N** means in respect of:

- (a) the first Dividend Payment Date, the number of days from (and including) the Issue Date until (but not including) the first Dividend Payment Date; and
- (b) each subsequent Dividend Payment Date, the number of days from (and including) the preceding Dividend Payment Date until (but not including) the relevant Dividend Payment Date.

### ***Dividend payment conditions***

32. The Dividend Payment Dates are 17 March, 17 June, 17 September and 17 December, commencing on 17 December 2012 until (but not including) the date on which a Conversion or Redemption occurs in accordance with the Terms.

33. Under clause 2.3 of the Terms, a Dividend is subject to:

- the Directors, at their absolute discretion, resolving to pay the Dividend on the relevant Dividend Payment Date;
- paying the Dividend on the CPS2 on the Dividend Payment Date not resulting in the Eligible Capital of the Suncorp Group not complying with APRA's then-current capital adequacy guidelines as they are applied to the Suncorp Group at that time;
- paying the Dividend not resulting in SGL becoming insolvent for the purposes of the Corporations Act; and
- APRA not otherwise objecting to the Dividend being paid on the Dividend Payment Date.

34. A Dividend is only payable to those persons registered as the Holders on the Record Date for that Dividend.

35. Dividends are non-cumulative, as stated in clause 2.4 of the Terms. If all or part of a Dividend is not paid, SGL has no liability to pay the unpaid amount, and the Holders will have no claim or entitlement in respect of the non-payment, nor will it constitute an event of default.

36. No interest will accrue on any unpaid Dividends and the Holders will have no claim or entitlement in respect of interest on any unpaid Dividends.

### ***Ranking of Dividends***

37. Under clause 10.1 of the Terms, the CPS2 rank, in respect of payment of Dividends:

- (a) in priority to SGL Ordinary Shares and other instruments that rank behind the CPS2;
- (b) equally amongst themselves and with all Equal Ranking Instruments; and
- (c) behind:
  - (i) any securities or instruments that rank in priority to the CPS2; and
  - (ii) all SGL's debt and liabilities to its creditors, both subordinated and unsubordinated, other than indebtedness that by its terms ranks equally or behind the CPS2.

### ***Restrictions in the case of non-payment of Dividends***

38. If a Dividend is not paid in full on a Dividend Payment Date (Relevant Dividend Payment Date), SGL is prevented, without the approval of a Special Resolution, from declaring or determining to pay or paying a dividend, making a distribution on SGL Ordinary Shares, or buying back or reducing capital on any SGL Ordinary Shares, until and including the next Dividend Payment Date, unless the Dividend is paid in full within 3 Business Days of the Relevant Dividend Payment Date (clause 2.8 of the Terms).

39. These restrictions do not apply in certain limited circumstances as described in clause 2.9 of the Terms.

***Mandatory Conversion***

40. Pursuant to clause 3.1 of the Terms, subject to the occurrence of a Non-Viability Trigger Event or an Acquisition Event, SGL must Convert all (but not some) CPS2 on issue on the Mandatory Conversion Date into SGL Ordinary Shares in accordance with clauses 3 and 7 of the Terms. The Mandatory Conversion Date will be the first of the following dates (each a Relevant Date) on which the Mandatory Conversion Conditions set out in clause 3.3 of the Terms are satisfied:

- (a) 17 December 2019 (Scheduled Mandatory Conversion Date); and
- (b) a Dividend Payment Date after the Scheduled Mandatory Conversion Date (Subsequent Mandatory Conversion Date).

41. The Mandatory Conversion Conditions to be satisfied (as set out in clause 3.3 of the Terms), are:

- (a) the VWAP of the SGL Ordinary Shares on the 25<sup>th</sup> Business Day immediately preceding a Relevant Date being greater than 110% of the Relevant Fraction, multiplied by the Issue Date VWAP (First Mandatory Conversion Condition);
- (b) the VWAP of the SGL Ordinary Shares during the period of 20 Business Days on which trading in SGL Ordinary Shares took place immediately preceding the Relevant Date being greater than 101.01% of the Relevant Fraction, multiplied by the Issue Date VWAP (Second Mandatory Conversion Condition); and
- (c) no Delisting Event applies in respect of the Relevant Date (Third Mandatory Conversion Condition).

***Non-Viability Conversion and Write Off***

42. SGL must convert the CPS2 on the Non-Viability Conversion Date, in accordance with clauses 4 and 7 of the Terms, should a Non-Viability Trigger Event occur. Conversion due to a Non-Viability Trigger Event is not subject to the Mandatory Conversion Conditions set out in clause 3.3 of the Terms.

43. A Non-Viability Trigger Event is defined in clause 4.1 of the Terms as an event where APRA provides a written determination to SGL that the conversion or write off of Relevant Tier 1 Capital Instruments is necessary, because:

- without the conversion or write off, APRA considers that SGL would become non-viable; or
- without a public sector injection of capital or equivalent capital support, APRA considers that SGL would become non-viable.

44. Clause 4.2(a) requires SGL to give notice to Holders if a Non-Viability Trigger Event occurs, to determine the number of CPS2 that will Convert, and state in the notice the date when the relevant number of CPS2 will Convert and how many CPS2 will Convert.

45. If an Inability Event (which means that SGL is prevented due to an applicable law, court order, action of a government authority or any other reason from Converting the CPS2) subsists on the Non-Viability Conversion Date such that SGL cannot Convert the CPS2, and Conversion has not been effected within five days after the Non-Viability Conversion Date, then the CPS2 will be Written Off in accordance with clause 7.12 of the Terms.

46. 'Written Off', in respect of CPS2 and a Non-Viability Conversion date, is defined as follows:

- (a) the CPS2 will not be Converted in respect of a Non-Viability Trigger Event and will not be Converted, Redeemed or Resold on any subsequent date; and
- (b) on and from the sixth day after the Non-Viability Conversion Date:
  - (i) if the Shareholder Approval has been obtained, in a winding-up of SGL, the Liquidation Sum is the sum which would have been paid in respect of CPS2 out of the surplus available to shareholders in a winding-up as if the CPS2 were the Conversion Number of SGL Ordinary Shares (and if such approval is not obtained the Liquidation Sum remains as provided in clause 10.2(c));
  - (ii) subject to clauses 2.3, 2.4 and 2.7 of the Terms and to the requirements of APRA applicable to the payment of dividends on SGL Ordinary Shares, a non-cumulative dividend is payable in respect of the CPS2 if and when a dividend is paid on SGL Ordinary Shares, in an amount determined as if the CPS2 were a number of SGL Ordinary Shares equal to the Conversion Number; and
  - (iii) clauses 2.1, 2.2, 2.5, 2.8, 3, 4 (other than clause 4.3(c)), 5, 6, 7 (other than clause 7.12 and any provisions in clause 7 required to give effect to clause 7.12) and 8 will no longer apply.

***Optional Exchange of CPS2 by SGL***

47. Under clause 5.1 of the Terms, SGL, with APRA's prior written approval, can elect to Exchange:

- (a) all or some CPS2 on an Exchange Date following a Tax Event or a Regulatory Event;
- (b) all (but not some only) CPS2 on an Exchange Date following the occurrence of a Potential Acquisition Event; provided that the Exchange Date in respect of the Potential Acquisition Event does not occur in the period between (but not including) the Optional Exchange Date to the Scheduled Mandatory Conversion Date; or
- (c) all or some CPS2 on the Optional Exchange Date.

48. If SGL elects to Exchange CPS2, it must elect which of the following it intends to do, as specified by clause 5.3 of the Terms:

- (a) Convert the CPS2 into SGL Ordinary Shares in accordance with clause 7 of the Terms;
- (b) Redeem the CPS2 in accordance with clause 8 of the Terms; or
- (c) Resell the CPS2 in accordance with clause 9 of the Terms.

***Conversion on Acquisition Event***

49. Upon the occurrence of an Acquisition Event, SGL must, in accordance with clauses 6 and 7 of the Terms, Convert all of the CPS2 on the Acquisition Conversion Date. An Acquisition Event is defined in clause 19.2 of the Terms as:

- (a) a takeover bid being made to acquire all or some SGL Ordinary Shares and the offer is or becomes unconditional and the bidder either has an interest in more than 50% of the SGL Ordinary Shares or the Directors issue a statement recommending acceptance of the offer; or
- (b) a court approves a scheme of arrangement which will result in a person other than SGL having a relevant interest in more than 50% of the SGL Ordinary Shares.

**Conversion mechanics**

50. If SGL Converts the CPS2, then under clause 7 of the Terms:

- (a) each CPS2 that is being Converted will Convert into one SGL Ordinary Share on the relevant date; and
- (b) each Holder will be allotted, for no consideration, an additional number of SGL Ordinary Shares for each CPS2 being Converted on the relevant date equal to one less than the Conversion Number (but no greater than the Maximum Conversion Number), calculated as follows:

$$\text{Conversion Number} = \frac{\text{Issue Price}}{99\% \times \text{VWAP}}$$

where:

**VWAP** (expressed in dollars and cents) means the Volume Weighted Average Price during the VWAP Period;

The Maximum Conversion Number is calculated as follows:

$$\text{Maximum Conversion Number} = \frac{\text{Issue Price}}{(\text{Issue Date VWAP} \times \text{Relevant Fraction})}$$

where:

**Relevant Fraction** means, in the case of a Conversion other than on account of a Non-Viability Trigger event, 0.5, or, in the case of a Conversion on account of a Non-Viability Trigger Event, 0.5 or, once the Australian Basel III Rules are implemented, 0.2 (or the lowest other fraction less than 0.5 as permitted by APRA under the Australian Basel III Rules to apply).

51. Subject to the operation of the limitation caused by the Maximum Conversion Number, the total market value of the SGL Ordinary Shares held by a Holder immediately after the Conversion of CPS2 will be approximately the Issue Price of the CPS2 (\$100).

52. Pursuant to clause 7.1(d), a CPS2, upon Conversion, confers all of the rights attaching to one SGL Ordinary Share, and at the times specified in the clause:

- (a) all other rights conferred or restrictions imposed on that CPS2 under the Terms will no longer have effect (except for rights relating to a Dividend which has been determined to be payable but has not been paid before the Conversion takes place, which rights will continue); and
- (b) the SGL Ordinary Share resulting from the Conversion will rank equally with all other SGL Ordinary Shares.

53. Clause 7.1 of the Terms states that the Conversion does not constitute a redemption, buy-back, cancellation or termination of CPS2 or an issue, allotment or creation of a new SGL Ordinary Share (other than under clause 7.1(b)).

#### ***Redemption mechanics***

54. SGL may Redeem the CPS2 in accordance with the Terms and subject to APRA's prior written approval.

55. For the purposes of clause 8 of the Terms, 'Redeem' means redeem, buy-back (other than an on market buy-back within the meaning of the Corporations Act) or a reduction of capital, or any combination of such activities.

56. Where the CPS2 are Redeemed, SGL will pay the Issue Price plus any amount payable under clause 8.3(a)(iii) of the Terms, pursuant to which the Directors may, in their absolute discretion, determine that the consideration payable for each CPS2 by way of buy-back will include an amount equal to a Dividend calculated in accordance with clause 2 of the Terms for the Dividend Period (together, the Redemption Price).

57. On the Exchange Date the only right the Holders will have with respect to the CPS2 will be to obtain the Redemption Price payable in accordance with the Terms and, upon payment of the Redemption Price all other rights conferred, or restrictions imposed, by the CPS2 will no longer have effect (pursuant to clause 8.3 of the Terms).

#### ***Resale mechanics***

58. SGL can elect to Resell the CPS2 by electing one or more Nominated Purchasers as set out in clause 9.2 of the Terms.

59. Under clause 9.4 of the Terms, if an election to Resell is made, each Holder is taken to irrevocably offer to sell CPS2 the subject of Resale to the Nominated Purchaser for the Resale Price on the Exchange Date. In accordance with clause 9.5 of the Terms, subject to payment by the Nominated Purchaser of the Resale Price to the Holders, all right, title and interest in such CPS2 (excluding the right to any Dividend payable on that date) will be transferred to the Nominated Purchaser free from Encumbrances.

## ***Ranking of CPS2 on Winding-Up***

60. Under clause 10.2 of the Terms, in a winding-up of SGL, a CPS2 confers upon the Holder the right to payment in cash of the Liquidation Sum (equal to \$100 plus the amount of any Dividend resolved to be paid but unpaid) out of the surplus (if any) available for distribution to shareholders. The CPS2 will rank as follows for payment of the Liquidation Sum:

- (a) in priority to SGL Ordinary Shares and other securities that rank equally with SGL Ordinary Shares;
- (b) equally amongst themselves and with all Equal Ranking Instruments; and
- (c) behind:
  - (i) any securities or instruments that rank in priority to the CPS2; and
  - (ii) all SGL's debt and liabilities to its creditors, both subordinated and unsubordinated, other than indebtedness that by its terms ranks equally or behind the CPS2 in a winding-up.

## **Other matters**

61. This Ruling is made on the basis that:

- (a) the documents provided by SGL (refer to paragraph 15 of this Ruling) represent a complete and accurate description of the Transaction, are intended by the parties to have their legal effect and will be implemented according to their terms;
- (b) during the term of the Transaction, SGL will be a resident of Australia under the income tax laws of Australia and no other jurisdiction;
- (c) all parties to the Transaction are dealing with each other on arm's length terms and fair value consideration will be provided by the Holders to acquire the CPS2;
- (d) the CPS2 are 'equity interests' pursuant to Division 974;
- (e) the additional SGL Ordinary Shares issued in the event of a Conversion of CPS2 will be 'equity interests' pursuant to Division 974;
- (f) dividends on the CPS2 will be frankable distributions pursuant to section 202-40;
- (g) the Dividends are expected to be fully franked, however, if any Dividend is not franked or only partially franked, the Dividend will be grossed up to the extent that the franking percentage of the Dividend is less than 100% as calculated in accordance with clause 2.2 of the Terms;

- (h) SGL will frank the distributions on the CPS2 at the same franking percentage as the benchmark for the franking period in which the payments are made;
- (i) the extent to which a Holder receives franked Dividends will be determined solely by each Holder's proportionate ownership of the CPS2 irrespective of the Holder's tax profile and regardless of the extent to which any particular Holder will actually benefit from the franking credits attached to the Dividend;
- (j) the dividends on the CPS2 are expected to be fully franked in the same proportion as dividends paid on SGL Ordinary Shares;
- (k) SGL will not differentially frank distributions payable to different Holders of the CPS2 according to the tax status of the Holder of those instruments or on any other basis;
- (l) SGL will not differentially frank distributions on the CPS2 or any other frankable interest in SGL according to the tax status of the holders of those instruments or on any other basis;
- (m) any CPS2 held by non-residents that acquired the CPS2 under the Institutional Offer will be franked in the same manner as the CPS2 held by residents;
- (n) the share capital of SGL will not become tainted within the meaning of Subdivision 197-A by an issue of the CPS2 or allotment of additional SGL Ordinary Shares on Conversion of the CPS2;
- (o) no dividends paid in respect of the CPS2 will be sourced, directly or indirectly, from SGL's share capital account or its non-share capital account;
- (p) SGL reasonably expects to have sufficient available profits from which to pay Dividends, and have net assets in excess of ordinary share capital, immediately before the payment of any Dividends payable in respect of the CPS2;
- (q) no debit will be made to any SGL reserve in respect of CPS2 dividends;
- (r) dividend payments in respect of the CPS2 will satisfy the requirements of section 254T of the Corporations Act;
- (s) dividend payments in respect of the CPS2 will not be an exercise of powers under Division 1 of Part 2J.1 of the Corporations Act;
- (t) the CPS2 are expected to be treated as a liability for AIFRS purposes;

- (u) for the purposes of determining whether a Holder is a 'qualified person' in relation to a distribution for the purposes of the former Division 1A of Part IIIAA of the ITAA 1936, a Holder has taken no positions (apart from the holding of the CPS2) in relation to their CPS2 and will not be under an obligation or is likely to make a related payment (within the meaning of former section 160APHN of the ITAA 1936) in relation to the Dividends;
- (v) the Holders in receipt of Dividends on the CPS2 will have held their CPS2 at risk for a period of at least 90 days (excluding the day of disposal), within the period beginning on the day after the day on which the Holder acquired the CPS2 and ending on the 90th day after the day on which the CPS2 go ex-dividend;
- (w) it is reasonable to expect that the dividend payout ratios or the franking credits in relation to the ordinary share capital or other preference share capital of SGL will not change as a result of the issue of the CPS2;
- (x) the Constitution of SGL has been amended to facilitate the issue of CPS2;
- (y) on the date of Conversion of the CPS2 into SGL Ordinary Shares, the rights and obligations attached to the SGL Ordinary Shares are the same as those contained in the Constitution of SGL as at the time of issue of the CPS2; and
- (z) the SML Notes would not satisfy the debt test under section 974-20 of the ITAA 1997.

## Ruling

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### **Acquisition time of the CPS2**

62. Pursuant to section 109-10, the Holders acquired the CPS2 on the date of issue of the CPS2, being 6 November 2012.

### **CPS2 cost base and reduced cost base**

63. Pursuant to subsections 110-25(2) and 110-55(2), the first element of the cost base and reduced cost base of each is \$100.

**Inclusion of Dividends and franking credits in assessable income**

64. The Holders must include in their assessable income all Dividends received under paragraph 44(1)(a) of the ITAA 1936, and an amount equal to the franking credit received on those Dividends under Division 207, unless a Holder is an entity whose ordinary or statutory income is exempt income.

**Entitlement to a tax offset**

65. The Holders will generally be entitled to a tax offset equal to the franking credit received on the Dividends under subsection 207-20(2) for the income year in which the distribution is made, unless Subdivision 207-D applies. This entitlement will be subject to the circumstances listed in section 207-145 not arising (see paragraph 70 of this Ruling).

66. The Holders who are entitled to a tax offset under Division 207, in respect of franking credits received, will also be subject to the refundable tax offset rules in Division 67, unless specifically excluded under section 67-25 (and who are not excepted from the exclusion). Such excluded entities include certain trustees and corporate tax entities under subsections 67-25(1A) to (1D).

**Exempt income or non-assessable non-exempt income**

67. If the Dividend (or a part of it) is either exempt income or non-assessable non-exempt income in the hands of the relevant Holder, then the amount of any franking credit on the Dividend is not included in the assessable income of the Holder and the Holder is not entitled to a tax offset under Division 207 (Subdivision 207-D).

**Section 177EA**

68. 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 benefits received in relation to the Dividends received by the Holders in respect of the CPS2.

**Imputation benefits – streaming**

69. The Commissioner will not make a determination under paragraph 204-30(3)(c) to deny the whole, or any part, of the imputation benefits received by a Holder in relation to the Dividends received by the Holders.

## **Gross-up and tax offset rules**

70. Provided an entity is a 'qualified person', section 207-145 will not apply to the whole, or any part, of the Dividends received by a Holder. Accordingly, section 207-145 will not adjust the gross-up of that Holder's assessable income to exclude the franking credit, nor will it deny the tax offset to which that Holder would have otherwise been entitled.

## **Qualified person and the Resale facility**

71. Under the definition of 'qualified person' contained in former Division 1A of Part IIIAA of the ITAA 1936, the Resale facility contained in clause 9 of the Terms, will not of itself affect a Holder's risk of loss or opportunities for gain in respect of the CPS2 on the basis that it does not constitute a separate position for the purposes of that Division.

## **Written Off CPS2**

72. Capital Gains Tax (CGT) event H2 will occur pursuant to section 104-155 when the CPS2 are Written Off.

73. However, a Holder will not make a capital gain or capital loss as a result of CGT event H2 happening as there will be no capital proceeds or incidental costs incurred because of the CPS2 being Written Off.

74. No other CGT event will occur when the CPS2 are Written Off.

## **Conversion of CPS2 and allotment of additional SGL Ordinary Shares – CGT implications**

75. The Conversion of each CPS2 into SGL Ordinary Shares and the allotment of additional SGL Ordinary Shares under the Terms will not result in any CGT event occurring.

## **Cost base of additional SGL Ordinary Shares**

76. Section 6BA of the ITAA 1936 and Subdivision 130-A will apply to apportion the first element of the cost base and reduced cost base of each CPS2 over the SGL Ordinary Shares, including any additional SGL Ordinary Shares, allotted by SGL pursuant to a Conversion.

## **Acquisition time of additional SGL Ordinary Shares**

77. Under subsection 130-20(3), any additional SGL Ordinary Shares received by a Holder as part of a Conversion will be taken to be acquired at the time the CPS2 were originally acquired by the Holders, which was 6 November 2012.

**Allotment of additional SGL Ordinary Shares – dividend**

78. The allotment of any additional SGL Ordinary Shares on Conversion of the CPS2 will not be assessable as dividend income in the hands of the Holders.

**Allotment of additional SGL Ordinary Shares – ordinary income**

79. The value of any additional SGL Ordinary Shares issued on Conversion of the CPS2 will not be assessable as ordinary income in the hands of the Holders under subsection 6-5(1).

**Section 45**

80. Section 45 of the ITAA 1936 will not apply to treat the SGL Ordinary Shares acquired on Conversion of the CPS2 under the Terms, as an unfranked dividend paid by SGL.

**Section 45A**

81. The Commissioner will not make a determination under subsection 45A(2) of the ITAA 1936, such that section 45C applies in relation to the whole, or a part of the capital benefit represented by the SGL Ordinary Shares acquired on Conversion of the CPS2 under the Terms, so as to treat it as an unfranked dividend in the hands of the Holders.

**Section 45B**

82. The Commissioner will not make a determination under subsection 45B(3) of the ITAA 1936, such that section 45C applies in relation to the whole, or a part of the capital benefit represented by the SGL Ordinary Shares acquired on Conversion of the CPS2 under the Terms, so as to treat it as an unfranked dividend in the hands of the Holders.

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**Commissioner of Taxation**5 December 2012

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## Appendix 1 – Explanation

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**❶** *This Appendix is provided as information to help you understand how the Commissioner's view has been reached. It does not form part of the binding public ruling.*

### **Acquisition time of the CPS2**

83. An equity interest that is issued or allotted by a company is acquired when the contract is entered into or, if no contract exists, when the equity interests are issued or allotted (item 2 of the table in section 109-10).

84. The CPS2 were issued on 6 November 2012. Therefore, for the purposes of item 2 in the table contained in section 109-10, the CPS2 were acquired on 6 November 2012.

### **CPS2 cost base and reduced cost base**

85. The first element of the cost base and reduced cost base includes the money paid, or required to be paid, in respect of acquiring a CGT asset (paragraph 110-25(2)(a) and subsection 110-55(2)).

86. The Issue Price of each CPS2 was \$100. Accordingly, the first element of the cost base and reduced cost base of each CPS2 acquired was \$100.

### **Inclusion of Dividends and franking credits in assessable income**

87. Paragraph 44(1)(a) of the ITAA 1936 provides that the assessable income of a resident shareholder includes dividends that are paid to the shareholder by the company out of profits derived by it from any source.

88. Any dividends paid in respect of the CPS2 will be paid out of SGL's profits and will not be sourced, directly or indirectly, from SGL's share capital account. Accordingly, Holders must include any Dividends paid in their assessable income.

89. Dividends are expected to be fully franked.

90. Subsection 207-20(1) provides that if a corporate tax entity makes a franked distribution to a shareholder, then an amount equal to the franking credit is included in the shareholder's assessable income, in addition to any other amount included in the shareholder's assessable income in relation to the distribution. As such, any franking credits attached to a Dividend that are received by a Holder must be included in the Holder's assessable income.

**Entitlement to a tax offset**

91. Subsection 207-20(2) provides that an entity is entitled to a tax offset equal to the amount of the franking credit on a distribution in the income year in which the distribution is made. Provided the Holder satisfies the requirements of former Division 1A of Part IIIAA of the ITAA 1936 in respect of the CPS2 dividend payments, the Holder will also be entitled to a tax offset equal to the amount of the franking credit received by the Holder, in the income year in which the Holder receives the Dividend.

92. The Holders who are entitled to a tax offset under Division 207, in respect of franking credits received, will also be subject to the refundable tax offset rules in Division 67, unless specifically excluded under section 67-25 (and not excepted from the exclusion). Such excluded entities include certain trustees and corporate tax entities under subsections 67-25(1A) to (1D).

**Exempt income or non-assessable non-exempt income**

93. Subdivision 207-D creates the appropriate adjustment to cancel the effect of the gross-up and tax offset rules where the Holder receives a franked distribution, and the franked distribution (or share of it) is, or would be, exempt income or non-assessable non-exempt income in the hands of the relevant Holder.

**Section 177EA**

94. Section 177EA of the ITAA 1936 is a general anti-avoidance provision that applies where one of the purposes (other than an incidental purpose) of the scheme is to obtain an imputation benefit. Where these circumstances arise, subsection 177EA(5) of the ITAA 1936 enables the Commissioner to make a determination with the effect of either:

- imposing a franking debit or an exempting debit on the distributing entity's franking account; or
- denying the imputation benefit on the distribution that flowed directly or indirectly to the relevant taxpayer.

95. Pursuant to subsection 177EA(3) of the ITAA 1936, the provision applies if the following conditions are satisfied:

- (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, the 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.

96. It is considered that the conditions in paragraphs 177EA(3)(a) to (d) of the ITAA 1936 are satisfied because:

- (a) the issue of CPS2 constitutes a scheme for the disposition of a membership interest (paragraph 177EA(3)(a) of the ITAA 1936). Pursuant to paragraph 177EA(14)(a) of the ITAA 1936, a 'scheme for a disposition of membership interests or an interest in membership interests' includes a scheme that involves the issuing of membership interests. The issuance of CPS2 on the terms set out in the Prospectus is a scheme that involves the issuing of membership interests because, once the CPS2 are issued, the Holders are members of SGL and the CPS2 are not debt interests (sections 960-130 and 930-135);
- (b) frankable distributions are expected to be payable to the Holders (paragraph 177EA(3)(b) of the ITAA 1936). The Commissioner accepts that Dividends will be frankable distributions to the extent that the Dividends do not fall within the list of unfrankable distributions in section 202-45;
- (c) franked distributions are expected to be paid to the Holders (paragraph 177EA(3)(c) of the ITAA 1936). Furthermore, SGL advised that it will continue its policy of fully franking all frankable distributions made by it, to the extent of the franking credits available in its franking account; and
- (d) it is reasonable to expect that an imputation benefit will be received by the relevant taxpayers as a result of distributions made to the Holders given that SGL expects to frank the distributions on the CPS2 (paragraph 177EA(3)(d) of ITAA 1936).

97. Accordingly, the issue is whether having regard to the relevant circumstances of the scheme, it would be concluded that a person, or one of the persons who entered into or carried out 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.

98. Circumstances which are relevant in determining whether any person has the requisite purpose include, but are not limited to, the factors listed in subsection 177EA(17) of the ITAA 1936.

99. The relevant circumstances listed 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 or may not be present at any one time in any one scheme.

100. SGL advised that the primary purpose for the issue of the CPS2 is to provide SGL with Tier 1 Capital for regulatory/capital adequacy purposes. The CPS2 were issued on arm's length terms, and the Holders provided fair value consideration for the issue of the CPS2.

101. The Commissioner considers that a number of the relevant circumstances of the present arrangement go some way towards indicating a non-incidental purpose of enabling a relevant taxpayer to obtain an imputation benefit. In particular, the calculation of the Dividend by reference to the corporate tax rate, and the franking adjustment that arises if the Dividend is not fully-franked, would be matters going to paragraph (f) of subsection 177EA(17) and which go some way to the ascertainment of the relevant purpose.

102. However, based on the information provided and the qualifications set out in this Ruling, the Commissioner's consideration of all of the relevant circumstances of the scheme would not, on balance, lead to a conclusion that the purpose of enabling Holders to obtain imputation benefits is more than incidental to SGL's purpose of raising Tier 1 Capital to meet its capital adequacy requirements.

103. Accordingly, the Commissioner will not make a determination under paragraph 177EA(5)(b) of the ITAA 1936 to deny the imputation benefits to the Holders.

#### **Imputation benefits – streaming**

104. Subdivision 204-D broadly enables the Commissioner to make a determination when distributions with attached imputation benefits are streamed to a member of a corporate tax entity in preference to another member.

105. Section 204-30 prescribes the circumstances that are required to exist before the Commissioner may make such a determination, and applies where an entity 'streams' the payment in such a way that:

- an imputation benefit is received by a member of the entity as a result of the distribution (paragraph 204-30(1)(a));
- the member (the favoured member) derives a greater benefit from the franking credits than another member of the entity (paragraph 204-30(1)(b)); and
- the other member (the disadvantaged 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)).

106. 'Streaming' is not defined for the purposes of Subdivision 204-D. However, the Commissioner has understood it to refer to a company 'selectively directing the flow of franked distributions to those members who can most benefit from imputation credits' (paragraph 3.28 of the Explanatory Memorandum to the New Business Tax System (Imputation) Bill 2002).

107. The CPS2 are listed on the ASX and hence are available to investors of differing tax profiles. The Dividends will be paid irrespective of a Holder's tax profile and will be paid in proportion to the Holder's ownership interest in the CPS2. Additionally, the extent to which a Holder receives franked Dividends will be determined solely by each Holder's proportionate ownership of the CPS2 and regardless of the extent to which any particular Holder will actually benefit from the franking credits attached to the Dividend.

108. With respect to the franking of the Dividends, SGL reasonably expects to fully or substantially frank all Dividends in the same proportion as the SGL Ordinary Shares. Furthermore, the CPS2 were offered to certain non-resident investors under the Institutional Offer, and any CPS2 held by non-residents investors will be franked in the same manner as the CPS2 held by residents. These factors suggest that the requisite element of directing the flow franked distributions to those members of the entity that can most benefit from them, at the expense of those that cannot, is not present in respect of the Dividends.

109. Accordingly, the Commissioner will not make a determination under paragraph 204-30(3)(c) to deny imputation benefits to the Holders of the CPS2.

## **Gross-up and tax offset rules**

110. Subdivision 207-F creates the appropriate adjustment to cancel the effect of the gross-up and tax offset rules where the entity concerned has manipulated the imputation system in a manner that is not permitted under the income tax law.

111. Section 207-145 provides the circumstances that must exist before this adjustment can occur. Pursuant to subsection 207-145(1), a 'manipulation of the imputation system' may occur where:

- the entity is not a 'qualified person' in relation to the distribution (paragraph 207-145(1)(a));
- the Commissioner has made a determination under paragraph 177EA(5)(b) of the ITAA 1936 that no imputation benefit is to arise in relation to the dividend (paragraph 207-145(1)(b));
- the Commissioner has made a determination under paragraph 204-30(3)(c) that no imputation benefit is to arise in relation to the distribution (paragraph 207-145(1)(c)); or
- the dividend is made as part of a dividend stripping operation (paragraph 207-145(1)(d)).

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

113. The holding period rule applies where neither the taxpayer nor an associate has made, is under an obligation to make, or is likely to make, a related payment in respect of the dividend, and requires the shares to have been continuously held at risk throughout the primary qualification period (former paragraph 160APHO(1)(a) of the ITAA 1936).

114. The related payments rule applies where the taxpayer or an associate, has made, is under an obligation to make, or is likely to make, a related payment in respect of the dividend and requires the shares to have been continuously held at risk throughout the secondary qualification period (former subsection 160APHO(1) of the ITAA 1936 and former section 160APHN of the ITAA 1936).

115. The Holders will be 'qualified persons', if:

- the Holders will have held their CPS2 at risk for a period of at least 90 days (excluding the day of acquisition and the day of disposal, and any days on which the Holder has materially diminished risks of loss or opportunities for gain in respect of the shares or interest), in the period, beginning on the day after the day on which the Holders acquired the CPS2 and ending on the 90th day after the day on which the CPS2 become ex-dividend (former subsections 160APHO(2) and 160APHO(3) of the ITAA 1936 and former sections 160APHM and 160APHJ of the ITAA 1936); and
- neither the Holders, nor associates of the Holders, have made, are under an obligation to make, or are likely to make a related payment in relation to the Dividends on CPS2 (former paragraph 160APHO(1)(a) of the ITAA 1936 and former section 160APHN of the ITAA 1936).

116. If either or both of the above two considerations are not met, the Holders will not be a 'qualified person' for the purposes of former Division 1A of Part IIIA of the ITAA 1936. Under these circumstances, Subdivision 207-F will create the appropriate adjustment to cancel the effect of the gross-up and tax offset rules for the Holders in relation to payments of Dividends.

117. The Commissioner has confirmed that he will not make a determination under paragraph 177EA(5)(b) of the ITAA 1936 or paragraph 204-30(3)(c) to deny the imputation benefits attached to Dividends paid by SGL to the Holders (see paragraphs 68 and 69 of this Ruling).

118. A distribution to a member of a corporate tax entity will be taken to be made as part of a dividend stripping operation, pursuant to section 207-155, where the distribution arose out of, or was made in the course of, a scheme that was by way of or in the same nature of dividend stripping, or had substantially the effect of a scheme by way of or in the nature of dividend stripping.

119. The documents provided by SGL provide no indication that the offering of the CPS2 and the associated payment of franked Dividends to the Holders in any way constitute a scheme by way of or in the nature of dividend stripping or a scheme having substantially the effect of a scheme by way of or in the nature of dividend stripping. As such, the dividend stripping provision will have no application to the Holders.

120. Therefore, in the absence of any evidence of the manipulation of the imputation system, section 207-145 will not apply to deny Holders a gross-up or tax offset in respect of the whole or any part of the franked Dividends received by them.

## **Qualified person and the Resale facility**

121. In determining whether a Holder is a 'qualified person', all of the Holder's 'positions' in respect of the CPS2 are taken into account in determining if there has been a material diminution in the risks of loss or opportunities for gain (see former section 160APHJ and subsection 160APHM(3) of the ITAA 1936)). A position relating to a share is anything that has a 'delta' in relation to the shares (former subsection 160APHJ(2) of the ITAA 1936).

122. An embedded share option is a position in relation to a share if it is exercisable by or against a party other than the issuer of the share (Taxation Determination TD 2007/29).

123. Under the Resale facility (clause 9 of the Terms), SGL can elect to require all the Holders to sell their CPS2 to a Nominated Purchaser. A Nominated Purchaser (a third party) will not have the right or ability to trigger redemption of the CPS2, and, until nominated by SGL, will not have the right or ability to acquire the CPS2 from the Holders.

124. SGL is also not required to exercise the Resale facility and has not appointed any Nominated Purchaser. The Resale facility is an option that is held by SGL, the issuer of the share, and not by a third party. The Resale facility therefore does not represent a separate position in relation to the CPS2 for the purposes of former Division 1A of Part IIIAA of the ITAA 1936.

125. Therefore, it is considered that the Resale facility does not affect a Holder's risk of loss or opportunity for gain in respect of the CPS2.

### **Written Off CPS2**

126. Each CPS2 is a bundle of rights, however, those rights are not separate pieces of property capable of being divided out and held separately. Accordingly, the rights attaching to the CPS2 do not constitute individual assets as defined by section 108-5, but rather combine to make up the ultimate asset, being the share (Taxation Ruling TR 94/30 (TR 94/30)).

127. Under section 104-25, CGT event C2 happens if, among other things, the ownership of an intangible asset, such as a preference share, ends by the share:

- being redeemed or cancelled (paragraph 104-25(1)(a)); or
- if the share is a convertible interest – being converted (paragraph 104-25(1)(f)).

128. The mere variation of rights attaching to a share is not a 'redemption' or 'cancellation' of the share for the purposes of paragraph 104-25(1)(a). Further, it does not result in the ownership of a CGT asset coming to an end under paragraph 104-25(f).

129. Under the Terms, when CPS2 are Written Off, a mere variation of rights attaching to the CPS2 will occur. Consequently CGT event C2 will not occur when the CPS2 are Written Off.

130. Under section 104-155, CGT event H2 happens if:

- (a) an act, transaction or event occurs in relation to a CGT asset that you own; and
- (b) the act, transaction or event does not result in an adjustment being made to the asset's cost base or reduced cost base.

131. Although CGT event C2 will not occur when the CPS2 are Written Off, the variation of rights under the Terms is an act, transaction or event that happens in relation to the CPS2. As the variation of rights will not result in any adjustment to the cost base or reduced cost base of the CPS2, CGT event H2 will occur when the CPS2 are Written Off.

132. A capital gain is made if the capital proceeds from CGT event H2 are more than the incidental costs incurred in relation to the event. A capital loss is made if the capital proceeds are less than the incidental costs (subsection 104-155(3)).

133. Subsection 116-20(2) provides that the capital proceeds from CGT event H2 will be the money or other consideration you received, or are entitled to receive, because of the act, transaction or event.

134. There will be no capital proceeds and no incidental costs will be incurred as a result of the CPS2 being Written Off under the Terms. Accordingly, when the CPS2 are Written Off, Holders will make no capital gain or capital loss because of CGT event H2 happening.

135. No other CGT event will happen when the CPS2 are Written Off under the Terms.

### **Conversion of CPS2 and allotment of additional SGL Ordinary Shares – CGT implications**

136. Under the Transaction, each CPS2 will convert into one SGL Ordinary Share through a variation of the rights attaching to each CPS2. The Holders will also receive an allotment of additional SGL Ordinary Shares in accordance with the Terms.

137. As stated at paragraphs 126 to 128 of this Ruling, each CPS2 is a bundle of rights, however, those rights are not separate pieces of property capable of being divided out and held separately, and do not constitute individual assets as defined by section 108-5. Rather, the rights combine to make up the ultimate asset, being the share (TR 94/30).

138. The mere variation of rights attaching to the CPS2 and the allotment of an additional number of SGL Ordinary Shares for no consideration under the Terms will not result in the ownership of an intangible CGT asset coming to an end by the share being 'redeemed' or 'cancelled' under paragraph 104-25(1)(a).

139. Further, the Conversion of the CPS2 into SGL Ordinary Shares by the variation of the rights attaching to the CPS2 under the Terms will not result in the ownership of an intangible CGT asset coming to an end by the CPS2 being converted under paragraph 104-25(1)(f).

140. The relinquishment by the Holders of some of the rights attaching to the CPS2 under the Terms is not a CGT event that happens to part of the CGT asset comprised by each CPS2 under section 112-30 (paragraph 40 of TR 94/30).

141. Consequently, CGT event C2 will not occur on Conversion of the CPS2 into SGL Ordinary Shares under the Terms and, as a result, Subdivision 130-C will not have any application.

142. Further, the Conversion of the CPS2 involving the allotment of additional SGL Ordinary Shares under the Terms will result in an adjustment to the cost base and reduced cost base of the CPS2 under section 6BA of the ITAA 1936 and Subdivision 130-A.

143. Accordingly, CGT event H2 will not happen upon the Conversion of the CPS2 involving the allotment of additional Ordinary Shares under the Terms.

144. No other CGT event in Division 104 will occur as a result of the Conversion of the CPS2 under the Terms.

#### **Cost base of additional SGL Ordinary Shares**

145. Section 6BA of the ITAA 1936 and Subdivision 130-A will apply to apportion the first element of the cost base and reduced cost base of CPS2 over the SGL Ordinary Shares and any additional ordinary shares allocated by SGL.

146. Section 6BA of the ITAA 1936 applies if a shareholder holds shares in a company (the original shares) and the company issues other shares (the bonus shares) in respect of the original shares.

147. Pursuant to subsection 6BA(3) of the ITAA 1936, as the additional SGL Ordinary Shares will be issued to Holders for no consideration and will not be a dividend nor taken to be a dividend (see paragraphs 152 to 156 of this Ruling), the issue price of CPS2 will be apportioned over the Converted CPS2 and any additional SGL Ordinary Shares allotted.

148. Subdivision 130-A applies in a similar manner. It provides special rules relating to the time of acquisition and the cost base of bonus equities for CGT purposes.

149. Section 130-20 sets out what happens if an entity owns shares in a company (the original equities) and the company issues other shares (the bonus equities) in relation to the original equities.

150. Under item 1 of the table in subsection 130-20(3), as the additional SGL Ordinary Shares will not be a dividend nor will they be taken to be a dividend, the first element of the cost base and reduced cost base of each CPS2 will be apportioned over both the Converted CPS2 and any additional SGL Ordinary Shares issued to the Holders by SGL.

#### **Acquisition time of additional SGL Ordinary Shares**

151. The Holders will be taken to have acquired the additional SGL Ordinary Shares at the time when the CPS2 were originally acquired by the Holders (subsection 130-20(3)) on 6 November 2012.

#### **Allotment of additional SGL Ordinary Shares – dividend**

152. Subsection 6(1) of the ITAA 1936 defines a 'dividend' to include any distribution made by a company to any of its shareholders, whether in money or other property, and any amount credited by a company to any of its shareholders as shareholders.

153. Although the additional SGL Ordinary Shares to be issued on Conversion of the CPS2 will constitute 'property' in the hands of the Holders, the allotment will not be a disposition of property in the ordinary meaning of that expression (*Ord Forrest Pty Ltd v. FC of T* (1974) 130 CLR 124; 74 ATC 4034; (1974) 4 ATR 230, per Barwick CJ and McTiernan J). As there is no disposition there cannot be a distribution of property by SGL.

154. The allotment of additional SGL Ordinary Shares will not constitute a dividend under subsection 6BA(5) of the ITAA 1936 as the Terms do not provide Holders with a choice of being paid a dividend or being issued shares.

155. Furthermore, no amount will be credited to the Holders, nor will an amount be paid out of profits.

156. Accordingly, the allotment of additional SGL Ordinary Shares will not constitute a dividend within the meaning of subsection 6(1) of the ITAA 1936.

## **Allotment of additional SGL Ordinary Shares – ordinary income**

157. The allotment of additional SGL Ordinary Shares will be a bonus issue within the meaning of paragraph 254A(1)(a) of the Corporations Act, that is, an issue of shares for which consideration is not payable to SGL. The issue of additional SGL Ordinary Shares will result in a re-expression of the Holder's interest in the share capital of SGL.

158. Accordingly, the value of any additional SGL Ordinary Shares issued on Conversion of the CPS2 will not be assessable as ordinary income under subsection 6-5(2) (*Commissioner of Taxation v. McNeil* (2007) 229 CLR 656; 2007 ATC 4223; (2007) 64 ATR 431).

## **Section 45**

159. Section 45 of the ITAA 1936 applies where a company streams the provision of shares and the payment of minimally franked dividends to its shareholders in such a way that the shares are received by some shareholders and minimally franked dividends are received by other shareholders. Minimally franked dividends are dividends which are not franked or are franked to less than 10%.

160. SGL has consistently paid fully franked dividends and stated it will pay fully franked dividends to all its shareholders, including the Holders, to the extent of the franking credits in its franking account. Furthermore, the Terms do not allow SGL to issue SGL Ordinary Shares to all or some of the Holders in satisfaction of their dividend entitlements in relation to the CPS2.

161. Upon Conversion of the CPS2 under the Terms, Holders may receive additional SGL Ordinary Shares. The issue of additional SGL Ordinary Shares in these circumstances will not be an alternative to the receipt of any dividends payable by SGL, nor will there be any link between the issue of the additional SGL Ordinary Shares and the timing of the declaration or payment of any dividends by SGL.

162. Therefore, section 45 of the ITAA 1936 will not apply to any of the SGL Ordinary Shares that will be acquired on Conversion of the CPS2.

#### **Section 45A**

163. Section 45A of the ITAA 1936 applies in circumstances where capital benefits are streamed to certain shareholders (the advantaged shareholders) who, in the year of income in which the capital benefit is provided, derive a greater benefit from the receipt of capital benefits and it is reasonable to assume that the other shareholders (the disadvantaged shareholders) have received or will receive dividends.

164. The receipt of SGL Ordinary Shares by the Holders will be a provision of capital benefits pursuant to paragraph 45A(3)(a) of the ITAA 1936.

165. Upon Conversion of the CPS2 under the Terms, each CPS2 will Convert to one SGL Ordinary Share. Furthermore, in accordance with the Terms, Holders may be allotted additional SGL Ordinary Shares. However, a Holder's entitlement to SGL Ordinary Shares under the Terms will not be determined based upon their preference for the receipt of capital benefits in lieu of dividends. In the absence of other additional factors that would contribute to an alternative conclusion, the allotment of SGL Ordinary Shares upon Conversion will not constitute the streaming of capital benefits.

166. Therefore, the receipt of SGL Ordinary Shares by all Holders upon Conversion under the Terms will not trigger the application of section 45A of the ITAA 1936. The Commissioner will not make a determination under subsection 45A(2) of the ITAA 1936 such that section 45C of the ITAA 1936 will apply to treat all or part of the capital benefit as an unfranked dividend in the hands of the Holders.

#### **Section 45B**

167. Section 45B of the ITAA 1936 applies where certain capital benefits are provided to shareholders in substitution for dividends.

168. Upon Conversion of the CPS2 under the Terms, each CPS2 will Convert to one SGL Ordinary Share. Furthermore, in accordance with the Terms, Holders may be allotted additional SGL Ordinary Shares. This would constitute a scheme under which a capital benefit, as defined in paragraph 45B(5)(a) of the ITAA 1936, is provided to the Holders. A CPS2 represents a fully paid preference share in the capital of SGL. Consequently, its Conversion under the Terms represents a re-expression of a Holder's interest in SGL's share capital, rather than a distribution of profit disguised as capital.

169. For the provision to apply paragraph 45B(2)(c) requires that, having regard to the relevant circumstances of the scheme, it would be concluded that the person, or one of the persons, who entered into the scheme or carried out the scheme or any part of the scheme did so for a purpose, other than an incidental purpose, of enabling a taxpayer (the relevant taxpayer) to obtain a tax benefit. The relevant circumstances of the scheme are listed in subsection 45B(8) of the ITAA 1936.

170. Therefore, having regard to the relevant circumstances of the scheme, it cannot be concluded that any of the parties to the scheme entered into or carried out the scheme for a more than incidental purpose of enabling the Holders to obtain a tax benefit. Consequently, section 45B of the ITAA 1936 will not apply to treat any of the SGL Ordinary Shares acquired upon Conversion under the Terms as an unfranked dividend in the hands of the Holders.

171. Accordingly the Commissioner will not make a determination under subsection 45B(3) of the ITAA 1936.

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

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## References

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### *Previous draft:*

Not previously issued as a draft

### *Related Rulings/Determinations:*

TR 94/30; TR 2006/10;  
TD 2007/29

### *Subject references:*

- acquisition of CGT assets
- allotment & issue of securities
- banking, finance & securities
- capital gains tax
- CGT assets
- CGT cost base
- CGT events
- CGT events C1-C3 – end of a CGT asset
- CGT events H1-H2 – special capital receipts
- company tax
- conversion of securities
- financial instruments
- frankable dividends
- franked dividends
- franking accounts
- franking credits
- imputation system
- preference shares
- redeemable preference shares
- securities
- securities transactions
- shares

### *Legislative references:*

- ITAA 1936 6
- ITAA 1936 44(1)
- ITAA 1936 45
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ATOLaw topic: Income Tax ~~ Assessable income ~~ dividend, interest and royalty income  
Income Tax ~~ Capital Gains Tax ~~ cost base and reduced cost base  
Income Tax ~~ Capital Gains Tax ~~ CGT events H1-H2  
Income Tax ~~ Tax offsets, credits and benefits ~~ franking tax offset