


CR 2012/53 - Income tax: Ludowici Limited Scheme of Arrangement and payment of Final Ordinary Dividend and Special Dividend

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Class Ruling

Income tax: Ludowici Limited Scheme of Arrangement and payment of Final Ordinary Dividend and Special Dividend

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① 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);
- subsection 44(1) of the ITAA 1936;
- section 128B of the ITAA 1936;
- section 128D of the ITAA 1936;
- section 160APHM of the ITAA 1936;
- section 160APHO of the ITAA 1936;
- Division 1A of former Part IIIAA of the ITAA 1936;
- section 177EA of the ITAA 1936;

- Division 67 of the *Income Tax Assessment Act 1997* (ITAA 1997);
- section 67-25 of the ITAA 1997;
- section 104-10 of the ITAA 1997;
- subsection 104-165(3) of the ITAA 1997;
- Subdivision 115-A of the ITAA 1997;
- Subdivision 115-C of the ITAA 1997;
- section 116-20 of the ITAA 1997;
- section 118-20 of the ITAA 1997;
- section 202-40 of the ITAA 1997;
- section 204-30 of the ITAA 1997;
- section 207-20 of the ITAA 1997;
- section 207-35 of the ITAA 1997;
- subsection 855-10(1) of the ITAA 1997; and
- section 855-15 of the ITAA 1997.

All subsequent legislative references are to the ITAA 1936 unless otherwise indicated.

Class of entities

3. The class of entities to which this Ruling applies are the shareholders of Ludowici Limited (Ludowici), referred to as Ludowici shareholders, who:

- (a) held their Ludowici shares on capital account;
- (b) participated in the Scheme of Arrangement under which FLSmith Pty Ltd acquired 100% of the shares in Ludowici;
- (c) received or were entitled to receive any of the following:
 - the Final Ordinary Dividend; or
 - the Special Dividend; or
 - the Final Ordinary Dividend and the Special Dividend; and
- (d) 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 Ludowici shares.

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

Qualifications

4. The Commissioner makes this Ruling based on the precise arrangement 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 8 to 33 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 2011 to 30 June 2013. The Ruling continues to apply after 30 June 2013 to all entities within the specified class who entered into the specified scheme during the term of the Ruling. However, this Ruling will not apply to taxpayers to the extent that it conflicts with the terms of a settlement of a dispute agreed to before the date of issue of this Ruling (see paragraphs 75 and 76 of Taxation Ruling TR 2006/10).

Scheme

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

- application for Class Ruling dated 16 March 2012 from PricewaterhouseCoopers (PwC);

- copy of the Scheme Implementation Agreement (SIA) dated 16 February 2012;
- copy of the Scheme Booklet issued by Ludowici to its shareholders, dated 10 April 2012;
- Australian Securities Exchange (ASX) announcements by Ludowici dated 16 February 2012, 24 February 2012, 28 February 2012, 4 April 2012, 10 April 2012, 1 June 2012, 12 June 2012, 13 June 2012 and 3 July 2012; and
- Correspondence and particulars received from PwC on 29 February 2012, 8 March 2012, 16 March 2012, 23 March 2012, 3 April 2012, 5 April 2012, 10 April 2012 and 4 July 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.

Ludowici Limited

10. Ludowici is an Australian publicly listed company on the ASX, operating in the global mineral processing industry.

11. Ludowici designs, manufactures and markets mineral processing equipment including vibrating screens, reflux classifiers, coal centrifuges, an extensive range of wear resistant products and a variety of other products and services.

Just before the Implementation Date of 3 July 2012, Ludowici had a single class share capital structure consisting of ordinary shares. As at 1 March 2012, Ludowici had 29,473,203 ordinary shares on issue. Of these shares, an analysis of the company's Top 50 shareholders determined that at least 64.84% of the issued capital was held by shareholders whose registered address was within Australia.

FLSmidth & Co. A/S

12. FLSmidth & Co. A/S (FLSmidth) is a Danish company and has been listed on NASDAQ OMX Copenhagen since 1968. It is a market-leading supplier of equipment and services to the global minerals and cement industries.

FLSmidth Pty Ltd

13. FLSmidth Pty Ltd is a wholly owned subsidiary of FLSmidth.

14. Prior to the Effective Date of the Scheme, FLSmidth and FLSmidth Pty Ltd did not own any shares in Ludowici either directly or through wholly owned subsidiaries.

The Scheme of Arrangement

15. On 16 February 2012, Ludowici announced that it had entered into a SIA with FLSmidth and FLSmidth Pty Ltd under which it was proposed that FLSmidth Pty Ltd would acquire all of the issued shares in Ludowici by means of a Scheme of Arrangement under part 5.1 of the *Corporations Act 2001* (the Scheme).

16. The terms of the SIA were subsequently amended by the parties to reflect an increase in the offer price for each Ludowici share and the removal of certain conditions precedent.

17. Under the amended terms of the SIA, a Ludowici shareholder was entitled to receive Scheme Consideration from FLSmidth Pty Ltd of a cash payment of \$11.00 less the amount of the Final Ordinary Dividend and the Special Dividend for each of their Ludowici shares.

18. Accordingly, the Scheme Consideration payable by FLSmidth Pty Ltd was reduced by the fully franked Final Ordinary Dividend that Ludowici declared and paid to shareholders on 9 May 2012.

19. The cash amount payable by FLSmidth Pty Ltd was further reduced by the fully franked Special Dividend that Ludowici declared and paid to shareholders on 25 June 2012.

20. As a result, a Ludowici shareholder who participated in the Scheme received a cash payment of \$10.44 as Scheme Consideration in exchange for each of their Ludowici shares.

21. The Scheme, as amended, was approved by the required majority of eligible Ludowici shareholders at a Scheme Meeting on 31 May 2012. The Effective Date for the Scheme was 12 June 2012 and the shares in Ludowici ceased to trade on the ASX at the close of trading on the ASX on this date.

22. The Record Date for the Scheme was 26 June 2012 and the Scheme Implementation Date was 3 July 2012.

The Final Ordinary Dividend

23. On 24 February 2012, Ludowici declared a fully franked Final Ordinary Dividend of \$0.11 cash per Ludowici share. The Record Date for the Final Ordinary Dividend was 24 April 2012 and the Payment Date was 9 May 2012.

24. The payment of the Final Ordinary Dividend did not exceed an amount that would have caused Ludowici's franking account to have a negative balance. The amount of the Final Ordinary Dividend was consistent with final dividends paid by Ludowici in prior years.

25. The Final Ordinary Dividend was paid out of accounting profits (retained earnings) derived by Ludowici and from existing working capital (including working capital facilities with external finance providers). Neither FLSmidth nor FLSmidth Pty Ltd provided any funds to Ludowici to finance the Final Ordinary Dividend.

26. The Final Ordinary Dividend was not contingent on the Scheme proceeding however the payment of the Final Ordinary Dividend reduced the amount paid to a Ludowici shareholder as Scheme Consideration by FLSmidth Pty Ltd under the Scheme.

27. Neither FLSmidth nor FLSmidth Pty Ltd had any influence or control over the decision by Ludowici to declare the Final Ordinary Dividend. It was paid in the ordinary course of trading and was not conditional upon Ludowici shareholders voting in favour of the Scheme.

The Special Dividend

28. On 12 June 2012, the Board of Directors of Ludowici (in its sole and absolute discretion) declared a fully franked Special Dividend of \$0.45 per Ludowici share. Payment of the Special Dividend was conditional upon the Scheme becoming effective.

29. The Special Dividend Record Date was 19 June 2012. The Special Dividend Payment Date was 25 June 2012.

30. The payment of the Special Dividend did not exceed an amount which would have caused Ludowici's franking account to have a negative balance.

31. The Special Dividend was paid out of accounting profits (retained earnings) derived by Ludowici from trading activities. The Special Dividend was funded via a drawdown of an additional working capital facility from Ludowici's existing credit provider.

32. Under the terms of the SIA, if Ludowici was unable to procure finance from its existing credit provider to ensure payment of the Special Dividend, FLSmidth Pty Ltd was required to extend a loan to Ludowici to fund this payment.

33. The payment of a Special Dividend to a Ludowici shareholder reduced the amount paid to a Ludowici shareholder by FLSmidth Pty Ltd under the Scheme.

Ruling

The Final Ordinary Dividend

34. The Final Ordinary Dividend of \$0.11 per share paid to a Ludowici shareholder is a 'dividend' as defined in subsection 6(1).

The Special Dividend

35. The Special Dividend of \$0.45 per share paid to a Ludowici shareholder is a 'dividend' as defined in subsection 6(1).

Assessability of the Ludowici Dividends

36. A Ludowici shareholder who received the fully franked Final Ordinary Dividend and/or Special Dividend (the Ludowici Dividends), and is a resident of Australia as defined in subsection 6(1), is required to include the Ludowici Dividends as assessable income under subparagraph 44(1)(a)(i).

Gross Up and Tax Offset

37. A Ludowici shareholder who received the Ludowici Dividends directly:

- must include the amount of the franking credit attached to the Ludowici Dividend in their assessable income; and
- will be entitled to a tax offset equal to the amount of the franking credit,

under section 207-20 of the ITAA 1997, subject to being a qualified person.

38. Where the fully franked Ludowici Dividends were received by a Ludowici shareholder (not being an entity taxed as a corporate tax entity) who is a trustee of a trust (not being a complying superannuation fund) or a partnership, the trustee of the trust or the partnership must include an amount equal to the franking credit attached to the Ludowici Dividends as assessable income under subsection 207-35(1) of the ITAA 1997.

Refundable Tax Offset

39. The franking credits allocated to the Ludowici Dividends are subject to the refundable tax offset rules in Division 67 of the ITAA 1997, provided the Ludowici shareholder or entity entitled to the tax offset is not excluded by the operation of section 67-25 of the ITAA 1997.

Non Resident Shareholders

40. In the case of a non-resident Ludowici shareholder who is carrying on business in Australia at or through a permanent establishment, the shareholder is required to include the Ludowici Dividends in their assessable income to the extent they are attributable to that permanent establishment.

41. For a non-resident Ludowici shareholder, the Ludowici Dividends:

- will not be subject to Australian withholding tax; and

- will not be assessable income and will not be exempt income pursuant to section 128D, being income that would be subject to withholding tax but for paragraph 128B(3)(ga).

Qualified Persons

The Final Ordinary Dividend

42. The payment of the Final Ordinary Dividend by Ludowici constitutes a related payment for the purposes of former section 160APHN.

43. Accordingly, a Ludowici shareholder will need to have held their Ludowici shares at risk for a continuous period of at least 45 days in the secondary qualification period in order to be a qualified person in respect of the Final Ordinary Dividend.

44. A Ludowici shareholder will no longer be considered to have held their Ludowici shares 'at risk' for the purposes of former Division 1A of the former Part IIIAA as of 26 June 2012, which is the Scheme Record Date.

45. Each Ludowici shareholder will be considered to be a qualified person in respect of the secondary qualification period for the purposes of Division 1A of the former Part IIIAA in relation to the Final Ordinary Dividend if:

- the Ludowici shareholder acquired the Ludowici share or interest in the share on or before 24 April 2012; and
- from 11 March 2012 until 9 June 2012 the Ludowici shareholder continued to hold the Ludowici share and did not have 'materially diminished risks of loss or opportunities for gain' (as defined under former section 160APHM) in respect of the Ludowici share for a continuous period of at least 45 days.

The Special Dividend

46. The payment of the Special Dividend by Ludowici constitutes a related payment for the purposes of former section 160APHN.

47. Accordingly, a Ludowici shareholder will need to have held their Ludowici shares at risk for a continuous period of at least 45 days in the secondary qualification period in order to be a qualified person in respect of the Special Dividend.

48. A Ludowici shareholder will no longer be considered to have held their Ludowici shares 'at risk' for the purposes of former Division 1A of the former Part IIIAA as of 26 June 2012, which is the Scheme Record Date.

49. Each Ludowici shareholder will be considered to be a qualified person in respect of the secondary qualification period for the purposes of Division 1A of the former Part IIIAA in relation to the Special Dividend if:

- the Ludowici shareholder acquired the Ludowici share or interest in the share on or before 19 June 2012; and
- from 6 May 2012 until 25 June 2012 the Ludowici shareholder continued to hold the Ludowici share and did not have 'materially diminished risks of loss or opportunities for gain' (as defined under former section 160APHM) in respect of the Ludowici share for a continuous period of at least 45 days.

Exempting Entity

50. Ludowici will not be an exempting entity under Division 208 of the ITAA 1997 at the time of the Final Ordinary Dividend and Special Dividend.

Capital Gains Tax

CGT event A1

51. CGT event A1 happened when a Ludowici shareholder disposed of a Ludowici share to FLSmith Pty Ltd pursuant to the Scheme (subsections 104-10(1) and (2) of the ITAA 1997).

52. The time of the CGT event was the Scheme Implementation Date of 3 July 2012 (paragraph 104-10(3)(b) of the ITAA 1997).

53. A Ludowici shareholder made a capital gain when CGT event A1 happened if the capital proceeds in respect of the disposal of their Ludowici share exceeded its cost base. A Ludowici shareholder made a capital loss if the capital proceeds in respect of the disposal of their Ludowici share were less than its reduced cost base (subsection 104-10(4) of the ITAA 1997).

Capital Proceeds

54. The capital proceeds received by a Ludowici shareholder is the money received or entitled to be received in respect of CGT event A1 happening (subsection 116-20(1) of the ITAA 1997).

55. The capital proceeds for each Ludowici share received by a Ludowici shareholder who received or was entitled to receive the Special Dividend was \$10.89 per Ludowici share. This amount includes the Special Dividend of \$0.45 paid by Ludowici in respect of each Ludowici share held by the Ludowici shareholder.

56. The capital proceeds for each Ludowici share received by a Ludowici shareholder who did not receive or was not entitled to receive the Special Dividend was \$10.89 reduced by the amount of the Special Dividend.

57. The Final Ordinary Dividend of \$0.11 per Ludowici share does not form part of capital proceeds for the disposal of the Ludowici share.

Anti-Overlap Provisions

58. Any capital gain made by a Ludowici shareholder when CGT event A1 happened can be reduced by the amount of the Special Dividend that is included in the Ludowici shareholder's assessable income under subsection 44(1) (section 118-20 of the ITAA 1997).

Discount Capital Gain

59. If a Ludowici shareholder made a capital gain from the disposal of their Ludowici share, the Ludowici shareholder may be eligible to treat the capital gain as a discount capital gain provided all relevant requirements of Subdivision 115-A of the ITAA 1997 and, if applicable, 115-C of the ITAA 1997 are satisfied.

Foreign resident shareholders

60. A Ludowici shareholder that was a foreign resident, or was the trustee of a foreign trust for CGT purposes, just before CGT event A1 happened disregards under subsection 855-10(1) of the ITAA 1997 any capital gain or capital loss from CGT event A1 happening to the Ludowici shares if the shares are not taxable Australian property as defined in section 855-15 of the ITAA 1997.

Anti Avoidance Provisions

61. The Commissioner will not make a determination under paragraph 204-30(3)(c) of the ITAA 1997 to deny the whole, or any part, of the imputation benefit received in respect of the Final Ordinary Dividend or the Special Dividend.

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

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.*

The Final Ordinary Dividend and Special Dividend

Dividend as defined in subsection 6(1)

63. The term 'dividend' is defined in subsection 6(1) to include any distribution made by a company to any of its shareholders, whether in money or other property.

64. The payment of the Ludowici Dividends was a distribution of money by Ludowici to its shareholders.

65. The definition of 'dividend' in paragraph 6(1)(d) excludes from the definition of 'dividend' any:

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

66. The Ludowici Dividends were sourced from Ludowici's retained earnings and working capital. Ludowici did not debit the Ludowici Dividends from its share capital account. Therefore, the exclusion in paragraph (d) will not apply and the Ludowici Dividends will constitute dividends for the purposes of subsection 6(1).

Assessability of the Ludowici Dividends

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

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

68. As the Final Ordinary Dividend and Special Dividend were paid to Ludowici shareholders out of the profits derived by Ludowici, Ludowici shareholders who are residents of Australia as defined in subsection 6(1) are required to include the dividends as assessable income.

Gross up and tax offset

69. Section 207-20 of the ITAA 1997 provides:

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

70. Therefore, subject to satisfying the qualified person rule, where the fully franked Final Ordinary Dividend and/or the Special Dividend were received directly by a Ludowici shareholder, the Ludowici shareholder:

- must include the amount of the franking credit attached to the Final Ordinary Dividend and/or Special Dividend in their assessable income; and
- will be entitled to a tax offset equal to the amount of the franking credit.

71. Where the fully franked Final Ordinary Dividend and/or Special Dividend were received by a Ludowici shareholder (not being an entity taxed as a corporate tax entity) that is a trustee of a trust (not being a complying superannuation fund) or a partnership, subsection 207-35(1) of the ITAA 1997 applies, subject to the trustee or partnership being a qualified person. Subsection 207-35(1) of the ITAA 1997 provides:

If:

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

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

72. Therefore, subject to satisfying the qualified persons rule, a Ludowici shareholder that is a trust or a partnership will be required to include the amount of the franking credit attached to the Final Ordinary Dividend and/or Special Dividend in their assessable income under subsection 207-35(1) of the ITAA 1997.

Refundable tax offset

73. Ludowici shareholders who are entitled to a tax offset under subsection 207-20(2) of the ITAA 1997, in respect of the franking credit received (or entities entitled to a tax offset under section 207-45 of the ITAA 1997 equal to their share of the franking credit) will also be subject to the refundable tax offset rules in Division 67 of the ITAA 1997, unless specifically excluded under section 67-25 of the ITAA 1997.

74. Pursuant to section 67-25 of the ITAA 1997, there are a range of taxpayers who are specifically excluded from the operation of the refundable tax offset rules. The identified entities include:

- non-complying superannuation funds or non-complying approved deposit funds (subsection 67-25(1A) of the ITAA 1997);
- a trustee of a trust who is liable to be assessed under subsection 98 or 99A (subsection 67-25(1B) of the ITAA 1997);
- corporate tax entities, unless the entity is an exempt institution that is eligible for a refund, or a life insurance company that has received distributions on membership interests which were not held by the company on behalf of its shareholders (subsection 67-25(1C) and 67-25(1D) of the ITAA 1997); and
- foreign resident entities carrying on a business in Australia at or through a permanent establishment (subsection 67-25(1DA) of the ITAA 1997).

75. Accordingly, a holder of Ludowici shares will be subject to the refundable tax offset rules unless they are listed specifically as one of the excluded entities under section 67-25 of the ITAA 1997.

Non-resident shareholders

76. Subparagraph 44(1)(b)(i) includes in the assessable income of a non-resident shareholder dividends (other than non-share dividends) paid to the shareholder by the company to the extent to which they are paid out of profits derived by it from sources in Australia.

77. Subsection 128B(1) imposes Australian withholding tax on income that:

- (a) is derived, on or after 1 January 1968, by a non-resident; and
- (b) consists of a dividend paid by a company that is a resident.

78. However, subparagraph 128B(3)(ga)(i) excludes from subsection 128B(1) income derived by a non-resident that consists of the franked part of a dividend. As the Final Ordinary Dividend and Special Dividend are both fully franked, they will not be subject to Australian withholding tax when derived by non-resident Ludowici shareholders.

79. In addition, section 128D states that:

Income other than income to which section 128B applies by virtue of subsection (2A), (2C) or (9C) of that section upon which withholding tax is payable, or upon which withholding tax would, but for paragraph 128B(3)(ga) or (jb), section 128F, section 128FA or section 128GB, be payable, is not assessable income and is not exempt income of a person.

80. As the Final Ordinary Dividend and the Special Dividend are income subject to withholding tax, but for paragraph 128B(3)(ga), it will not be assessable income and will not be exempt income of the non-resident Ludowici shareholders pursuant to section 128D.

81. Accordingly, Ludowici shareholders who receive the fully franked Final Ordinary Dividend and/or the Special Dividend and are non-residents (other than those carrying on a business in Australia at or through a permanent establishment in Australia) will not be required to include the dividend as assessable income under subparagraph 44(1)(b)(i) (section 128D) and will not be liable for Australian withholding tax (paragraph 128B(3)(ga)).

Qualified persons

82. Pursuant to paragraph 207-145(1)(a) of the ITAA 1997, an entity must be a 'qualified person' in relation to a dividend in order to be entitled to a tax offset in respect of the franking credit allocated to the dividend.

83. Division 1A of the former Part IIIAA (the former Division 1A) contains the measures known as the holding period rule and the related payments rule. In broad terms, it provides the statutory tests that must be satisfied for a taxpayer to be a 'qualified person' with respect to a franked distribution they have received and thus be entitled to a tax offset for the franking credit attached to the distribution.

84. The test of what constitutes a 'qualified person' is provided in former section 160APHO as follows:

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

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

- (b) where the taxpayer or an associate of the taxpayer has made, is under an obligation to make, or is likely to make, a related payment in respect of the dividend - the taxpayer has satisfied subsection (2) in relation to the secondary qualification period in relation to the dividend.

85. Former subsection 160APHO(2), referred to in the preceding paragraph, sets out the holding period requirement. Broadly, if a taxpayer is not under an obligation to make a related payment in relation to a dividend or distribution, the taxpayer will have to satisfy the holding period requirement within the primary qualification period. If a taxpayer is under an obligation to make a related payment in relation to a dividend or distribution, the taxpayer will have to satisfy the holding period requirement within the secondary qualification period.

Related payment rule

86. In order to determine what the relevant qualification period is, it is necessary to determine whether, under the present arrangement, the shareholders of Ludowici were considered to be under an obligation to make a related payment.

87. Former section 160APHN provides non-definitive examples of what constitutes the making of a related payment for the purposes of former Division 1A. Former subsection 160APHN(2) provides:

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

88. Former subsection 160APHN(3) states:

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

- (a) causing a payment or payments to be made to, or in accordance with the directions of, the other person or other persons; or
- (b) causing an amount or amounts to be credited to, or applied for the benefit of, the other person or the other persons; or
- (c) causing services to be provided to, or in accordance with the directions of, the other person or other persons; or
- (d) causing property to be transferred to, or in accordance with directions of, the other person or other persons; or
- (e) allowing any property or money to be used by the other person or other persons or by someone nominated by the other person or other persons; or

- (f) causing an amount or amounts to be set off against, or to be otherwise applied in reduction of, a debt or debts owed by the other person or other persons; or
- (g) agreeing to treat an amount or amounts owed to the other person or other persons by the taxpayer or associate as having been increased.

89. Former subsection 160APHN(4) states:

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

- (a) the amount or the sum of the amounts paid, credited or applied; or
- (b) the value or the sum of the values of the services provided, of the property transferred or of the use of the property or money; or
- (c) the amount or the sum of the amounts of the set-offs, reductions or increases; as the case may be:
- (d) is, or may reasonably be expected to be, equal to; or
- (e) approximates or may reasonably be expected to approximate; or
- (f) is calculated by reference to; the amount of dividend or distribution.

90. Where a shareholder is not taken to pass the benefit of the dividend to another person in the circumstances set out above, the shareholder will need to satisfy the holding requirement in respect of the primary qualification period in order to be entitled to a tax offset in respect of the franking credit allocated to the dividend. However, where a shareholder is taken to pass the benefit of the dividend to another person in the circumstances set out above, the shareholder will need to satisfy the holding requirement in respect of the secondary qualification period in order to be entitled to a tax offset in respect of the franking credit allocated to the dividend.

91. In the current circumstances, it is considered that the payment of the Final Ordinary Dividend of \$0.11 and the Special Dividend of \$0.45 per Ludowici share is an integral part of the Scheme. Under the terms of the SIA, the Scheme Consideration was adjusted by the Final Ordinary Dividend and Special Dividend paid by Ludowici to its shareholders. Therefore the circumstances as mentioned in paragraphs 160APHN(3)(f) and 160APHN(4)(c) would apply, and a Ludowici shareholder is taken to have made or be likely to make a related payment in respect of the Final Ordinary Dividend and Special Dividend.

Holding period requirement

92. The holding period rule requires a shareholder to hold the shares, or the interest in the shares, on which a dividend is paid, at risk for a continuous period of at least 45 days during the relevant qualification period.

93. As the Ludowici shareholders are taken, for the purposes of former Division 1A, to have made or be likely to make a related payment in respect of the Final Ordinary Dividend and the Special Dividend, the relevant holding period is thus the secondary qualification period pursuant to former paragraph 160APHO(1)(b).

94. The secondary qualification period is defined in former section 160APHD as follows:

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

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

95. The concept of 'ex-dividend' is defined by former subsection 160APHE(1) as follows:

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

The Final Ordinary Dividend

96. Ludowici determined eligibility for the Final Ordinary Dividend on the Final Ordinary Dividend Record Date of 24 April 2012. Accordingly, the ex-dividend date for the purposes of former subsection 160APHE(1) was 25 April 2012.

97. The secondary qualification period ran from 45 days before the ex-dividend date of 25 April 2012 and ended 45 days after that day. This means that the secondary qualification period ran from 11 March 2012 to 9 June 2012. However, pursuant to former subsection 160APHO(3), any days on which a Ludowici shareholder who participated in the Scheme had materially diminished risks of loss or opportunities for gain in respect of their Ludowici shares are excluded from counting towards the 45 day holding requirement.

98. Accordingly during the secondary qualification period, a Ludowici shareholder who participated in the Scheme and received the Final Ordinary Dividend must hold their shares 'at risk' for a continuous period (not counting the day on which the share was acquired) of not less than 45 days during this period in order to be a qualified person for the purposes of former Division 1A.

The Special Dividend

99. Ludowici determined eligibility for the Special Dividend on the Special Dividend Record Date of 19 June 2012. Accordingly, the ex-dividend date for the purposes of former subsection 160APHE(1) was 20 June 2012.

100. The secondary qualification period ran from 45 days before the ex-dividend date of 20 June 2012 and ended 45 days after that day. This means that the secondary qualification period ran from 6 May 2012 to 4 August 2012. However, pursuant to former subsection 160APHO(3), any days on which a Ludowici shareholder who participated in the Scheme had materially diminished risks of loss or opportunities for gain in respect of their Ludowici shares are excluded from counting towards the 45 day holding requirement. Ludowici shares held by Ludowici shareholders who participated in the Scheme were not held 'at risk' on and after the Record Date for the Scheme of 26 June 2012.

101. Accordingly, for a Ludowici shareholder who participated in the Scheme the secondary qualification period ran from 6 May 2012 to 25 June 2012. A Ludowici shareholder who participated in the Scheme and received the Special Dividend must hold their shares 'at risk' for a continuous period (not counting the day on which the share was acquired) of not less than 45 days during this period in order to be a qualified person for the purposes of former Division 1A.

Exempting Entity

102. Section 208-20 of the ITAA 1997 states that a corporate tax entity is an exempting entity at a particular time if it is effectively owned by prescribed persons at that time. Subsection 208-25(1) of the ITAA 1997 provides in broad terms that an entity is effectively owned by prescribed persons if not less than 95% of accountable membership interests or accountable partial interests (broadly direct and indirect ownership interests) are held by or on behalf of prescribed persons.

103. Section 208-40 of the ITAA 1997 provides the definition of a prescribed person in relation to another corporate tax entity. The definition includes companies, trustees, partnerships or individuals that are a foreign resident or if they were to receive a distribution by the corporate tax entity, the distribution would be exempt income or non-assessable non-exempt income of the company, trust estate, partnership or individual.

104. Based on Ludowici's shareholder register as at 1 March 2012 and taking into account the circumstances described by the applicant, the total percentage of non-resident shareholder ownership in the accountable membership interests of Ludowici at the time of the payment of the Final Ordinary Dividend and Special Dividend does not amount to Ludowici being effectively controlled by prescribed persons.

Capital Gains Tax***CGT Event A1***

105. CGT event A1 in section 104-10 of the ITAA 1997 happens if there is a change in the ownership of an asset from one entity to another. This event happens when a contract to dispose of an asset is entered into or, if there is no contract, when the change of ownership occurs (paragraph 104-10(3) of the ITAA 1997).

106. CGT event A1 happened when a Ludowici shareholder disposed of each of their Ludowici shares to FLSmidth Pty Ltd pursuant to the Scheme (subsections 104-10(1) and (2) of the ITAA 1997). The disposal occurred on the Scheme Implementation Date of 3 July 2012 when the shares were disposed of by the Ludowici shareholders (paragraph 104-10(3)(b) of the ITAA 1997).

107. The time when CGT event A1 happens determines the income year in which any capital gain or loss is made and whether the CGT discount applies to any capital gain.

Capital Proceeds

108. The capital proceeds received by each Ludowici shareholder is the money received or entitled to be received in respect of the event happening (subsection 116-20(1) of the ITAA 1997).

109. A Ludowici shareholder who participated in the Scheme received or was entitled to receive a cash payment of \$10.44 per Ludowici share from FLSmidth Pty Ltd in exchange for their Ludowici shares.

110. A Ludowici shareholder may however have also received or have been entitled to receive the Final Ordinary Dividend and/or the Special Dividend.

111. The term 'in respect of the event happening' in subsection 116-20(1) of the ITAA 1997 requires the relationship between the event and the receipt of the money, or entitlement to receive the money, must be more than coincidental. An amount is not 'capital proceeds' of an event merely because it is received in association with the event.

The Final Ordinary Dividend

112. In this case, the payment of the Final Ordinary Dividend was expected in due course irrespective of the scheme. The Final Ordinary Dividend was not paid as a term of the Scheme and neither FLSmidth nor FLSmidth Pty Ltd had influenced the decision to pay the Final Ordinary Dividend.

113. Further, the Final Ordinary Dividend was paid from existing working capital (including existing working capital facilities with external finance providers) without any participation or funding from FLSmidth Pty Ltd. Accordingly, the Final Ordinary Dividend does not form part of the capital proceeds which a Ludowici shareholder received in respect of CGT event A1 happening.

The Special Dividend

114. A dividend declared by a company that is subject to a takeover can form part of the vendor shareholders' capital proceeds from the disposal of the shares. Taxation Ruling TR 2010/4 states in paragraph 9 that:

A dividend declared or paid by the target company to the vendor shareholder will be money or property that the vendor shareholder has received, or is entitled to receive, under the contract or the scheme of arrangement, in respect of the transfer of the shares, if the vendor shareholder has bargained for the receipt of the dividend (whether or not in addition to other consideration) in return for giving up the shares. That is to say, if the dividend forms the whole or part of that sum of money or property in return for which the vendor shareholder is willing, and under the contract has promised or under the scheme of arrangement is bound, to transfer the shares in the target company, it will be capital proceeds in respect of the CGT event A1 happening.

115. In this case, the payment of the Special Dividend of \$0.45 did not occur independently of the Scheme. Evidence of this includes:

- the Scheme Consideration of \$11.00 per Ludowici share payable by FLSmidth Pty Ltd to a Ludowici shareholder in exchange for each Ludowici share was reduced by the Special Dividend;
- the Special Dividend would not have been paid if the Scheme did not become effective; and
- pursuant to the terms of the SIA, FLSmidth Pty Ltd was required to provide finance for payment of the Special Dividend had finance not been obtained from Ludowici's existing credit provider.

116. Accordingly, the Special Dividend is considered to form part of the capital proceeds that a Ludowici shareholder received or was entitled to receive in respect of CGT event A1 happening to their Ludowici shares.

117. The capital proceeds received by a Ludowici shareholder who received or was entitled to receive the Special Dividend is therefore considered to be \$10.89 for each Ludowici share disposed of under the Scheme.

Anti-overlap provisions

118. A capital gain made from a CGT event is reduced if the capital gain includes an amount that is included in assessable income under another provision of the ITAA 1997 or the ITAA 1936 (section 118-20 of the ITAA 1997). This has the effect of reducing (but not below zero) the capital gain by the amount that is assessable under the other provision. A capital loss made from a CGT event will not be increased by the operation of section 118-20 of the ITAA 1997.

119. Where a dividend forms part of the capital proceeds from the disposal of shares and is assessable income under subsection 44(1), section 118-20 of the ITAA 1997 will reduce any capital gain by the amount of the dividend.

120. The Special Dividend will be included in the assessable income of Ludowici shareholders under subsection 44(1). Therefore, section 118-20 of the ITAA 1997 will operate to reduce (but not below zero) any capital gain made by these Ludowici shareholders from CGT event A1 by the amount of the Special Dividend that is included in assessable income under subsection 44(1).

121. However, the capital gain will not be reduced by the amount of the franking credit that is included in the Ludowici shareholder's assessable income (paragraph 118-20(1B)(b) of the ITAA 1997).

122. The amount of any capital loss made by a Ludowici shareholder will not be adjusted under section 118-20 of the ITAA 1997 by the amount of the Special Dividend.

Discount capital gains

123. If a Ludowici shareholder made a capital gain from the disposal of their Ludowici share, the Ludowici shareholder may be eligible to treat the capital gain as a discount capital gain provided that all relevant requirements of Subdivision 115-A of the ITAA 1997 and, if applicable, Subdivision 115-C of the ITAA 1997 are met.

124. One of those requirements is that the capital gain must result from a CGT event happening to a CGT asset that was acquired by the entity making the capital gain at least 12 months before the CGT event (subsection 115-25(1) of the ITAA 1997).

125. This means that a capital gain made by a Ludowici shareholder who disposed of their Ludowici share is a discount capital gain if the shareholder acquired the Ludowici share at least 12 months before the date of disposal under the Scheme, being the Scheme Implementation Date of 3 July 2012, and the other requirements in Subdivision 115-A of the ITAA 1997 and, if applicable, Subdivision 115-C of the ITAA 1997 are satisfied.

Foreign resident shareholders

126. 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'.

127. 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; and
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).

128. A foreign resident, or the trustee of a foreign trust for CGT purposes, just before CGT event A1 happened under the Scheme, can not disregard under subsection 855-10(1) of the ITAA 1997 a capital gain or capital loss from CGT event A1 happening if:

- their share in Ludowici was an indirect Australian real property interest (item 2 of the table in section 855-15 of the ITAA 1997);
- their share in Ludowici had been used at any time by the foreign resident, or the trustee of a foreign trust for CGT purposes, in carrying on a business through a permanent establishment in Australia (item 3 of the table in section 855-15 of the ITAA 1997); or
- their share in Ludowici was covered by subsection 104-165(3) of the ITAA 1997 (item 5 of the table in section 855-15 of the ITAA 1997).

Anti-avoidance provisions***Section 204-30 of the ITAA 1997***

129. Section 204-30 of the ITAA 1997 applies where a corporate tax entity streams the payment of dividends, or the payment of dividends and the giving of other benefits, to its members in such a way that:

- (a) an imputation benefit is, or apart from this section would be, received by a member of the entity as a result of the distribution or distributions (paragraph 204-30(1)(a) of the ITAA 1997);
- (b) the member would derive a greater benefit from franking credits than another member of the entity (paragraph 204-30(1)(b) of the ITAA 1997); and
- (c) the other member of the entity will receive lesser imputation benefits, or will not receive any imputation benefits, whether or not the other member receives other benefits (paragraph 204-30(1)(c) of the ITAA 1997).

130. Relevantly, if section 204-30 of the ITAA 1997 applies, the Commissioner is vested with a discretion under subsection 204-30(3) of the ITAA 1997 to make a determination in writing either:

- (a) that a specified franking debit arises in the franking account of the entity, for a specified distribution or other benefit to a disadvantaged member (paragraph 204-30(3)(a) of the ITAA 1997); or
- (b) that no imputation benefit is to arise in respect of any distributions made to a favoured member and specified in the determination (paragraph 204-30(3)(c) of the ITAA 1997).

131. For section 204-30 of the ITAA 1997 to apply, members to whom distributions are streamed must derive a greater benefit from franking credits than the members who consequently do not receive franking credits, or do not receive the same amount of franking credits as they would have had streaming not occurred.

132. Under the current Scheme, all Ludowici shareholders received an imputation benefit as a result of the Ludowici Dividends; the resident shareholders in the form of a tax offset (paragraph 204-30(6)(a) of the ITAA 1997) and the non-resident shareholders in the form of an exemption from dividend withholding tax (paragraph 204-30(6)(e) of the ITAA 1997). The resident shareholders derived a greater benefit from franking credits than the non-resident shareholders.

133. However, the Ludowici Dividends were paid to all Ludowici shareholders at the respective Payment Dates and were fully franked with Australian franking credits. Accordingly, it cannot be argued that Ludowici directed the flow of distributions in such a manner as to stream the imputation benefits such that one class of members derived a greater benefit from the franking credits attached to the dividends, while the other members received lesser or no imputation benefits.

134. As the conditions in subsection 204-30(1) of the ITAA 1997 for the provision to apply are not met, the Commissioner will not make a determination under paragraph 204-30(3)(c) of the ITAA 1997 to deny the whole, or any part, of the imputation benefit received in relation to either the Final Ordinary Dividend or the Special Dividend.

Section 177EA

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

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

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

137. In the present case, Ludowici is a corporate tax entity. The disposal of the ordinary shares in Ludowici pursuant to the Scheme is a scheme for the disposition of membership interests. Both the Final Ordinary Dividend and the Special Dividend are frankable distributions that were paid to Ludowici shareholders as a part of this Scheme who could, therefore, reasonably be expected to receive imputation benefits.

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

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

140. The relevant circumstances of the Scheme indicate that there is no requisite purpose of conferring an imputation benefit under the Scheme. The Ludowici Dividends were fully franked, which is a continuation of Ludowici's dividend policy to pay fully franked dividends. Ludowici has only ordinary shares on issue and the Ludowici Dividends were paid to all Ludowici shareholders on a pro-rata basis in proportion to the number of shares that each Ludowici shareholder held on the relevant Record Dates. The amount of the Ludowici Dividends allows Ludowici shareholders to share in the accumulated profits of Ludowici.

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

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References

Previous draft:

Not previously issued as a draft

Related Rulings/Determinations:

TR 2006/10; TR 2010/4;
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