


CR 2012/61 - Income tax: Spotless Group Limited Scheme of Arrangement and payment of Special Dividend

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Class Ruling

Income tax: Spotless Group Limited Scheme of Arrangement and payment of Special Dividend

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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;
 - paragraph 128B(3)(ga) of the ITAA 1936;
 - section 128D of the ITAA 1936;
 - former section 160APHN 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 104-10 of the ITAA 1997;
- Division 115-A of the ITAA 1997;
- section 116-20 of the ITAA 1997;
- section 207-20 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;
- section 207-145 of the ITAA 1997; and
- section 855-10 of the ITAA 1997.

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

Class of entities

3. The class of entities to which this Ruling applies are shareholders of Spotless Group Limited (Spotless) who:

- (a) held their shares on capital account;
- (b) participated in the Scheme of Arrangement (the Scheme) under which Pacific Industrial Services Pty Ltd acquired 100% of the shares in Spotless;
- (c) received the Special Dividend and the Scheme Consideration; and
- (d) are not subject to the taxation of financial arrangements rule in Division 230 of the ITAA 1997 in relation to gains and losses on their Spotless shares.

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

Qualifications

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

5. The class of entities defined in this Ruling may rely on its contents provided the scheme actually carried out is carried out in accordance with the scheme described in paragraphs 9 to 22 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 2012 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:

- The application for a Class Ruling received 21 May 2012;
- The Scheme Implementation Agreement (SIA), together with its schedule and annexure, dated 30 April 2012;
- Spotless Scheme Booklet dated 15 June 2012; and
- Other information and documents provided by the applicant.

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

Relevant Entities

Spotless

10. Spotless is an Australian resident company that was listed on the Australian Securities Exchange.

11. Spotless is an international services company which specialised in outsourced facility services on behalf of its clients.

12. The shareholders of Spotless are a mix of individuals, companies, superannuation funds and other institutional investors.

13. On 30 April 2012 Spotless entered into a Scheme Implementation Agreement (SIA) and at that date:

- over 61% of Spotless' registered shareholders were predominantly Australian based investors,
- there were no non-residents, either alone or together with any associates, who beneficially held more than 10% of the shares in Spotless,
- Spotless had 265,746,161 shares and 5,387,890 performance rights on issue, and
- There were 1,533,418 Spotless shares held on trust by the trustee of the Spotless Employee Incentive Plan and Spotless issued additional 966,582 Spotless shares in order to satisfy the vested Performance Rights between the Effective Date of 27 July 2012 and the Special Dividend Record Date of 3 August 2012.

Pacific Industrial Services Group

14. Pacific Industrial Services Bid Co. Pty Ltd (Bid Co) was incorporated in Australia on 3 April 2012 and is a wholly owned subsidiary of Pacific Industrial Services Fin Co Pty Ltd (Fin Co). Fin Co was also incorporated in Australia on 3 April 2012 and is a wholly owned subsidiary of Pacific Industrial Services Pty Ltd (Hold Co), an entity incorporated in Australia on 11 November 2011.

15. Each of Bid Co, Fin Co and Hold Co is a proprietary company limited by shares that was incorporated specifically for the purpose of the acquisition of the Scheme shares pursuant to the SIA.

16. Bid Co is beneficially owned by funds managed or advised by Pacific Equity Partners Pty Ltd (PEP) or its affiliates. PEP is a leading Australasian based private equity advisory firm focusing on buyouts and late stage expansion capital in Australia and New Zealand.

The Scheme of Arrangement

17. On 30 April 2012, Spotless announced that it had entered into the SIA with Bid Co, under which, subject to the satisfaction of a number of conditions, it was proposed that Bid Co would acquire 100% of the ordinary shares in Spotless pursuant to the Scheme.

18. On 20 July 2012, the Board of Directors of Spotless declared a fully franked Special Dividend of \$0.04 to Spotless shareholders for every Spotless share they held on the Special Dividend Record Date of 3 August 2012. The declaration of the Special Dividend was conditional upon the approval of the Scheme by Spotless shareholders. Neither Bid Co nor PEP influenced the decision of Spotless' Board of Directors to declare the Special Dividend.

19. The Scheme was approved by a majority of eligible Spotless shareholders at the Scheme Meeting held on 25 July 2012. Final Court orders under section 411 of the *Corporations Act 2001* were obtained on 27 July 2012.

20. The Special Dividend was funded from Spotless' existing cash reserves and/or existing banking facilities and was debited against Spotless' retained earnings account. No amount of the Special Dividend was debited to Spotless' share capital account. It was not directly or indirectly funded from Bid Co. or PEP. The Special Dividend was paid to Spotless shareholders on the Special Dividend Payment Date of 7 August 2012.

21. Under the Scheme, shareholders who held Spotless shares on the Scheme Record date of 8 August 2012 disposed of their shares to Bid Co on the Scheme Implementation Date of 16 August 2012 and, in exchange, received \$2.62 per share in cash consideration (the Scheme consideration).

22. The Scheme consideration was not reduced by the amount of the Special Dividend.

Ruling**The Special Dividend**

23. The Special Dividend of \$0.04 cash per share paid to Spotless shareholders will constitute a 'dividend' as defined in subsection 6(1) of the ITAA 1936.

24. Spotless shareholders who receive the Special Dividend and are residents of Australia as defined in subsection 6(1) of the ITAA 1936 are required to include the Special Dividend as assessable income under subparagraph 44(1)(a)(i) of the ITAA 1936.

25. Spotless shareholders who receive the Special Dividend and are non-residents (other than those carrying on business in Australia at or through a permanent establishment in Australia) are not required to include the Special Dividend as assessable income under subparagraph 44(1)(b)(i) of the ITAA 1936 (section 128D of the ITAA 1936) and will not be liable for Australian withholding tax (paragraph 128B(3)(ga) of the ITAA 1936).

26. Spotless shareholders who receive the Special Dividend and are non-residents carrying on business in Australia at or through a permanent establishment in Australia, where the Special Dividend is attributable to the permanent establishment, are required to include the Special Dividend as assessable income under subparagraph 44(1)(c)(i) of the ITAA 1936 and are not liable for Australian withholding tax in respect of the dividend (subsection 128B(3E) of the ITAA 1936).

Gross up and tax offset

27. Spotless shareholders who receive the fully franked Special Dividend directly and who satisfy the residency requirements in section 207-75:

- must include the amount of the franking credit attached to the Special 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, subject to being a qualified person.

28. A Spotless shareholder that receives the Special Dividend as the trustee of a trust (not being a complying superannuation entity or a corporate tax entity) or as a partnership (not being a corporate tax entity) is required to include the amount of the franking credit attached to the dividend as a part of the shareholder's assessable income under subsection 207-35(1), subject to the trustee or partnership being a qualified person.

29. The relevant members of a partnership or trust to whom a distribution flows indirectly through the partnership or trust, are entitled to a tax offset under section 207-45, equal to their share of the franking credit attached to the distribution included in the assessable income of the partnership or trust under section 207-35(1).

Refundable tax offset

30. The tax offset equal to the amount of franking credit attached to the Special Dividend is subject to the refundable tax offset rules in Division 67, provided the Spotless shareholder is a qualified person and is not excluded by the operation of section 67-25.

Qualified Persons

31. Having regard to the relevant circumstances of the Scheme, the Spotless Shareholders are considered to have made, or to be likely to make a related payment in respect of the Special Dividend.

32. Accordingly, each participating Spotless Shareholder will need to hold their Spotless 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.

33. Each Spotless shareholder will no longer be considered to hold their Spotless shares 'at risk' for the purposes of former Division 1A of former Part IIIA of the ITAA 1936 (former Division 1A) as of the Scheme Record Date of 8 August 2012.

34. Therefore, a Spotless shareholder will be a qualified person in relation to the Special Dividend if, from 20 June 2012 until 7 August 2012 inclusive, they continued to hold their Spotless shares and did not have 'materially diminished risks of loss or opportunities for gain' (as defined under former section 160APHM of the ITAA 1936) in respect of their Spotless shares for a continuous period of at least 45 days.

Capital Gains Tax (CGT) consequences***CGT event A1***

35. CGT event A1 happened when a participating Spotless shareholder disposed of their Spotless shares to Bid Co. pursuant to the Scheme (subsection 104-10(1) and 104-10(2)).

36. The time of the CGT event was when the change of ownership occurred (paragraph 104-10(3)(b)). This was when the Spotless shares were transferred to Bid Co. on the Scheme Implementation Date of 16 August 2012.

Capital gain or capital loss

37. A Spotless shareholder made a capital gain if the capital proceeds from the disposal of their Spotless shares exceed the cost base of the shares. A Spotless shareholder made a capital loss if the capital proceeds are less than the reduced cost base of their Spotless shares (subsection 104-10(4)).

Capital proceeds

38. The capital proceeds received by a Spotless shareholder will be the money received or entitled to be received in respect of the event happening (subsection 116-20(1)).

39. The capital proceeds for a participating Spotless shareholder will be \$2.62 per share. The capital proceeds will not include the amount of the Special Dividend as it is considered, having regard to all the circumstances of the Scheme, that the Special Dividend was not paid in respect of the CGT event happening.

Discount capital gains

40. A Spotless shareholder who made a capital gain when CGT event A1 happened may be eligible to treat that gain as a 'discount capital gain' provided they satisfy the requirements of Subdivision 115-A.

Foreign resident shareholders

41. A foreign resident Spotless shareholder who participated in the Scheme may disregard any capital gain made when CGT event A1 happened as their shares are not 'taxable Australian property' (section 855-10).

Anti-avoidance provisions

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

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

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 Special Dividend

44. The term 'dividend' is defined in subsection 6(1) of the ITAA 1936 as any distribution made by a company to any of its shareholders, whether in money or other property.

45. The Special Dividend is a distribution of money made by Spotless to its ordinary shareholders.

46. The definition of 'dividend' in paragraph 6(1)(d) of ITAA 1936 excludes from the definition of 'dividend' any:

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

47. The payment of the Special Dividend was debited against Spotless' retained earnings account and not its share capital amount. Therefore, the exclusion in paragraph (d) will not apply and the Special Dividend constituted a dividend for the purposes of subsection 6(1) of the ITAA 1936.

Assessability of the Special Dividend – residents

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

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

49. As the Special Dividend was paid to Spotless shareholders out of profits derived by Spotless, Spotless shareholders who are residents of Australia as defined in subsection 6(1) of the ITAA 1936 are required to include the Special Dividend in their assessable income under paragraph 44(1)(a)(i) of the ITAA 1936.

Assessability of the Special Dividend – non-residents

50. Subparagraph 44(1)(b)(i) of the ITAA 1936 includes in the assessable income of a non-resident shareholder in a company:

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.

51. However, subsection 44(1) of the ITAA 1936 does not apply to a dividend to the extent to which another provision of the ITAA 1936 that expressly deals with dividends excludes some or all of the dividend from assessable income.

52. Subsection 128B(1) of the ITAA 1936 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.

53. However, subparagraph 128B(3)(ga)(i) of the ITAA 1936 excludes from subsection 128B(1) of the ITAA 1936 income derived by a non-resident that consists of the franked part of a dividend. As the Special Dividend was fully franked, it will not be subject to Australian withholding tax when derived by non-resident Spotless shareholders.

54. In addition, section 128D of the ITAA 1936 states that:

Income other than income to which section 128B applies by virtue of subsection (2A), (2C) or 9(C) of that section upon which withholding tax is payable, or upon which withholding tax would, but for paragraph 128(3)(ga) or (jb), section 128F, section 128FA or section 128GB of the ITAA 1936, be payable, is not assessable income and is not exempt income of a person.

55. As the payment of the Special Dividend is income that is subject to withholding tax but for paragraph 128B(3)(ga) of the ITAA 1936, it will not be assessable income, and will not be exempt income of non-resident Spotless shareholders pursuant to section 128D of the ITAA 1936.

56. Accordingly, Spotless shareholders who received the fully franked Special Dividend and are non-residents (other than those carrying on business in Australia at or through a permanent establishment in Australia) are not required to include the dividend as assessable income under subparagraph 44(1)(b)(i) of the ITAA 1936 (section 128D of the ITAA 1936) and will not be liable for Australian withholding tax (paragraph 128B(3)(ga) of the ITAA 1936).

57. Subsection 128B(1) of the ITAA 1936 is subject to subsection 128B(3E) of the ITAA 1936. Subsection 128B(3E) of the ITAA 1936 states that section 128B of the ITAA 1936 does not apply to dividend income that:

- (a) is paid to a person who is a non-resident carrying on business in Australia at or through a permanent establishment of the person in Australia; and
- (b) is attributable to the permanent establishment; and
- (c) is not paid to the person in the person's capacity as a trustee.

58. Subparagraph 44(1)(c)(i) of the ITAA 1936 includes in the assessable income of a non-resident shareholder of a resident company who is carrying on business in Australia at or through a permanent establishment of the shareholder in Australia:

dividends (other than non-share dividends) that are paid to the shareholder by the company and are attributable to the permanent establishment, to the extent to which they are paid out of profits derived by the company from sources outside Australia.

59. Accordingly, non-resident Spotless shareholders carrying on business in Australia at or through a permanent establishment who received a fully franked Special Dividend (to the extent to which the dividend is attributable to the permanent establishment) are required to include the Special Dividend in assessable income under subparagraph 44(1)(c)(i) of the ITAA 1936; and will not be liable for Australian withholding tax in respect of the Special Dividend.

Gross up and tax offset

60. Section 207-20 provides:

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

61. Therefore, subject to satisfying the qualified person rule, where the fully franked Special Dividend is received directly by a Spotless shareholder and the Spotless shareholder satisfies the residency requirement in section 207-75, the Spotless shareholder:

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

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

63. Subsection 207-35(1) provides:

lf:

- (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.

64. Therefore, subject to satisfying the qualified person rule, a Spotless shareholder that is the trustee of a trust or a partnership are required to include the amount of the franking credit attached to the Special Dividend in the assessable income of that trust or partnership under subsection 207-35(1).

65. The relevant members of a partnership or trust to whom a distribution flows indirectly through the partnership or trust, are entitled to gain entitlement to a tax offset under section 207-45, equal to their share of the franking credit attached to the distribution included in the assessable income of the partnership or trust under section 207-35(1).

Refundable tax offset

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

67. Pursuant to section 67-25, certain taxpayers 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));
- a trustee of a trust who is liable to be assessed under section 98 or 99A of the ITAA 1936 (paragraph 67-25(1B)(b));

- corporate tax entities, unless the entity is an exempt institution that is eligible for a refund, or a life insurance company that has received distributions on membership interests which were not held by the company on behalf of its shareholders (subsections 67-25(1C) and 67-25(1D)); and
- foreign resident entities carrying on business in Australia at or through a permanent establishment (subsection 67-25(1DA)).

68. Accordingly, Spotless shareholders (or entities entitled to a tax offset under section 207-45) are subject to the refundable tax offset rules unless they are specifically excluded pursuant to section 67-25.

Qualified persons, related payment rule and holding period rule

Qualified persons

69. Pursuant to paragraph 207-145(1)(a), an entity must be a 'qualified person' in relation to a dividend in order to be entitled to a tax offset for the franking credit attached to the dividend. The qualified person rules are contained in Division 1A of former Part IIIAA of the ITAA 1936 (the former Division 1A) and have effect via the express terms of section 207-145.

70. The former Division 1A contains the holding period rule and the related payment rule. In broad terms, former Division 1A provides the statutory tests that must be satisfied for a taxpayer to be a 'qualified person' in relation to a franked distribution they have received and to be entitled to a tax offset for the franking credit attached to the distribution.

71. The test of what constitutes a 'qualified person' is provided in former subsection 160APHO(1) of the ITAA 1936 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, 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.

72. Former subsection 160APHO(2) of the ITAA 1936 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 is required to satisfy the holding period rule 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 is required to satisfy the holding period requirement within the secondary qualification period.

Related payment rule

73. In order to determine the relevant qualification period, it is necessary to determine whether, under the Scheme, Spotless shareholders are considered to have made, be under an obligation to make, or be likely to make, a related payment in respect of the Special Dividend.

74. Former section 160APHN of the ITAA 1936 provides non-definitive examples of what constitutes the making of a related payment for the purposes of former Division 1A. Former subsection 160APHN(2) of the ITAA 1936 provides:

The taxpayer or associate is taken, for the purposes of this Division, to have made, to be under an obligation to make, or 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.

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

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

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

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

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

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

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

as the case may be:

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

77. In the current circumstances, it is considered that an integral part of the Scheme is the payment of the Special Dividend of \$0.04 per share. Although the payment of the Special Dividend is not specifically provided for in the SIA, the declaration and payment of the Special Dividend was conditional upon the Scheme of Arrangement being approved by Spotless shareholders. Therefore, having regard to the relevant circumstances of the Scheme, it is considered that Spotless shareholders were doing something, were under an obligation to do something, or were likely to do something that had the effect of passing the benefit of the Special Dividend to another person for the purposes of former subsection 160APHN(3) of the ITAA 1936.

78. Therefore, a Spotless shareholder was taken to have made or was likely to make a related payment in respect of the Special Dividend.

Holding period rule

79. The holding period rule requires shareholders to hold their ordinary shares at-risk for a continuous period of not less than 45 days during the relevant qualification period.

80. As a Spotless shareholder is considered to have made or be likely to make a related payment in respect of the Special Dividend, a Spotless shareholder is also required to satisfy the holding period requirement within the secondary qualification period pursuant to former paragraph 160APHO(1)(b) of the ITAA 1936.

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

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

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

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

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

83. The eligibility for the Special Dividend is determined on the Special Dividend Record Date of 3 August 2012. This was the last day on which acquisition by a person of a Spotless share entitled the person to receive the Special Dividend as per former section 160APHE of the ITAA 1936. Accordingly, the ex-dividend date for the purposes of former subsection 160APHE(1) of the ITAA 1936 was 4 August 2012.

84. The secondary qualification period runs from 45 days before the ex-dividend date of 4 August 2012 and ends 45 days after that day. In particular terms, this means that the secondary qualification period runs from 20 June 2012 to 18 September 2012. However, pursuant to former subsection 160APHO(3) of the ITAA 1936, any days during the relevant qualification period in respect of which a Spotless shareholder's exposure to the relevant risks and opportunities associated with the ownership of the shares were materially diminished, are excluded from counting towards the 45 day holding requirement. As of 8 August 2012, the Record Date for Scheme Implementation, the Spotless shareholders had ceased to hold their shares at-risk, as they were committed to dispose of their shares in exchange for the Scheme Consideration. Therefore, for practical purposes a Spotless shareholder must have held the shares at-risk for a continuous period of 45 days during the period 20 June 2012 and 7 August 2012 (inclusive) in order to be considered qualified persons and gain entitlement to the franking credits attached to the Special Dividend. Also excluded when determining the 45 days, is the date of acquisition and the date of disposal of the shares.

Capital gains tax consequences***CGT event A1***

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

86. A takeover or merger effected by a court approved scheme of arrangement does not involve a disposal of shares under a contract (paragraph 9 of Taxation Determination TD 2002/4¹).

87. CGT event A1 happened when a participating Spotless shareholder disposed of their Spotless shares to Bid Co. pursuant to the Scheme. The event occurred on the Scheme Implementation Date of 16 August 2012 (subsections 104-10(1) and (2)) when the shares were disposed of by Spotless shareholders.

88. A Spotless shareholder who participated in the Scheme made a capital gain if the capital proceeds from the disposal of the Spotless shares exceed the cost base of the shares. A Spotless shareholder made a capital loss if the capital proceeds were less than the reduced cost base of the shares (subsection 104-10(4)).

Capital proceeds

89. The capital proceeds from the Scheme is the money received or entitled to be received by a Spotless shareholder who participated in the Scheme in respect of the event happening (subsection 116-20(1)).

90. The term 'in respect of the event happening' in subsection 116-20(1) requires that 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.

91. The Special Dividend was funded by Spotless from existing cash reserves and/or existing facilities enabling Spotless to utilise remaining franking credits prior to implementation of the Scheme. It was not directly or indirectly funded by Bid Co. or PEP.

¹ Taxation Determination TD 2002/4: Income tax: capital gains: what is the first element of the cost base and reduced cost base of a share in a company you acquire in exchange for a share in another company in a takeover or merger?

92. Although the declaration and payment of the Special Dividend of \$0.04 per Spotless share was contingent on the Scheme proceeding, the declaration and payment of the Special Dividend was at the discretion of the Spotless Board without any influence from Bid Co. or PEP. Further, pursuant to the SIA, the Scheme Consideration was not reduced by the amount of the Special Dividend.

93. Therefore, the Special Dividend did not form part of the capital proceeds which a Spotless shareholder received as a result of CGT event A1 happening. The Scheme Consideration of \$2.62 received per share constitutes the capital proceeds.

Discount capital gain

94. The CGT discount applies to a capital gain made by an individual, a complying superannuation entity, a trust, or (in the circumstances set out in paragraph 115-10(d)) a life insurance company, and the other requirements of Subdivision 115-A are satisfied.

95. 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 that made the capital gain at least 12 months before the CGT event happened (subsection 115-25(1)).

96. Consequently, a capital gain made by a Spotless shareholder who participated in the Scheme when they disposed of their Spotless share is entitled to the CGT discount if the shareholder acquired the Spotless share at least 12 months before the date of disposal under the Scheme, being the Scheme Implementation Date of 16 August 2012, and the other requirements in Subdivision 115-A are met.

Foreign resident shareholders

97. Under subsection 855-10(1), 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'.

98. The term 'taxable Australian property' is defined in the table in section 855-15. The table sets out the following 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) (choosing to disregard a gain or loss on ceasing to be an Australian resident).

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

- their shares in Spotless were an indirect Australian real property interests (item 2 of the table in section 855-15); or
- their shares in Spotless 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); or
- their shares in Spotless were covered by subsection 104-165(3) (item 5 of the table in section 855-15).

100. Item 2 of the table in section 855-15 defines taxable Australian property to include an indirect Australian real property interest. An indirect Australian real property interest under section 855-25 is an interest held by an entity in another entity if it passes:

- the non-portfolio interest test under section 960-105; and
- the principal asset test in section 855-30.

101. The non-portfolio interest test under section 960-195 is as follows:

An interest held by an entity (the holding entity) in another entity (the test entity) passes the non-portfolio interest test at a time if the sum of the direct participation interests held by the holding entity and its associates in the test entity at that time is 10% or more.

102. Spotless has advised that, just before the Scheme was implemented, there were no non-residents, either alone or together with any associates, who beneficially hold more than 10% of the shares in Spotless. Accordingly, none of the Spotless shares disposed of as a part of the Scheme pass the non-portfolio interest test. Consequently, Spotless shares held by non-residents do not constitute indirect Australian real property interest.

103. Since the first condition of an indirect Australian real property under section 855-25 is not satisfied, it is not necessary to consider the application of the principal asset test. The Spotless shares did not constitute 'taxable Australian property' of foreign resident shareholders.

Anti-avoidance provisions

Section 204-30

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

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

105. If section 204-30 applies, the Commissioner may make a determination in writing:

- (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)); and/or
- (b) that no imputation benefit is to arise in respect of a distribution that is made to a favoured member and specified in the determination (paragraph 204-30(3)(c)).

106. For section 204-30 to apply, members to whom distributions are streamed must derive a greater benefit from franking credits than other members. The words 'derives a greater benefit from franking credits' are defined in subsection 204-30(8) by reference to the ability of members to fully utilise franking credits.

107. Under the Scheme for the payment of the Special Dividend, all Spotless shareholders received an imputation benefit as a result of the Special Dividend. Subject to being 'qualified persons', Australian resident Spotless shareholders received an imputation benefit in the form of a tax offset (paragraph 204-30(6)(a)). Non-resident Spotless shareholders received an imputation benefit in the form of an exemption from dividend withholding tax (paragraph 204-30(6)(e)). Resident Spotless shareholders would derive a greater benefit from franking credits than non-resident Spotless shareholders (subsection 204-30(8)).

108. However, the Special Dividend was paid to all Spotless shareholders identified at the Special Dividend Record Date and was fully franked. Accordingly, it cannot be concluded that Spotless intended to direct the flow of distributions in such a way as to stream imputation benefits to members that derive a greater benefit from the associated franking credits, while other members receive lesser or no imputation benefits.

109. As the conditions in subsection 204-30(1) are not met in respect of the Special Dividend, the Commissioner will not make a determination under paragraph 204-30(3)(c) to deny the whole, or any part, of the imputation benefit received in respect of the Special Dividend.

Section 177EA

110. Section 177EA of the ITAA 1936 is a general anti-avoidance provision that applies to a wide range of schemes seeking to obtain a tax advantage in relation to trading of franking credits.

111. Subsection 177EA(3) of the ITAA 1936 provides that section 177EA of the ITAA 1936 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.

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

113. Spotless is a corporate tax entity. The disposal of the ordinary shares in Spotless pursuant to the Scheme of Arrangement represents a scheme for the disposition of membership interests in a corporate tax entity. The Special Dividend is a frankable distribution that was fully franked and paid to Spotless shareholders as a part of the Scheme. As the recipients of the franked Special Dividend it would be reasonable to expect that the Spotless shareholders (the relevant taxpayers) will derive imputation benefits.

114. Consequently, the requirements of paragraphs 177EA(3)(a) to 177EA(3)(d) of the ITAA 1936 will be met. Accordingly, the issue is whether having regard to the relevant circumstances of the Scheme, it could be concluded that, as a result of the distribution, on the part of Spotless or its shareholders, there was a purpose, which was more than a merely incidental purpose, of conferring an imputation benefit upon the relevant taxpayer under the Scheme.

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

116. The relevant circumstances of the Scheme indicate that there was no requisite purpose of conferring an imputation benefit under the Scheme. It includes the fact that the disposition of the shares in Spotless occurred pursuant to the proposed Scheme of Arrangement under the *Corporations Act 2001* to be voted upon by Spotless shareholders.

117. The Special Dividend was fully franked, which was a continuation of Spotless' dividend policy. Spotless had only ordinary shares on issue and the Special Dividend was paid per share held by all Spotless shareholders at the Special Dividend Record Date. The Special Dividend was debited to the retained earnings account of Spotless and paid to shareholders of Spotless that were the true economic owners of the company, allowing the shareholders to share in the accumulated profits of Spotless.

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

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Previous draft:

Not previously issued as a draft

Related Rulings/Determinations:

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Subject references:

- arrangement
- CGT asset
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- distributions
- franking credits
- ordinary shares
- qualified person
- related payment rule
- takeovers and mergers

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Income Tax ~~ Tax integrity measures ~~ qualified persons – franking credits