


# ***CR 2014/81 - Income tax: demerger of OMI Holdings Limited by Donaco International Limited***

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## Class Ruling

### Income tax: demerger of OMI Holdings Limited by Donaco International Limited

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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)
  - section 44 of the ITAA 1936
  - section 45B of the ITAA 1936
  - section 45BA of the ITAA 1936
  - section 45C of the ITAA 1936
  - section 104-35 of the *Income Tax Assessment Act 1997* (ITAA 1997)
  - section 115-30 of the ITAA 1997, and
  - Division 125 of the ITAA 1997.

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

## Class of entities

3. The class of entities to which this Ruling applies is the holders of ordinary shares in Donaco International Limited (Donaco) who:

- (a) were listed on the share register of Donaco as at the Record Date (12 September 2014) for the demerger of shares in OMI Holdings Limited (OMI);
- (b) on the Record Date, held their shares in Donaco as neither revenue assets (as defined in section 977-50) nor as trading stock (as defined in subsection 995-1(1)) that is, broadly on capital account;
- (c) were either
  - (i) a 'resident of Australia' as defined in subsection 6(1) of the ITAA 1936 on the Record Date; or
  - (ii) a foreign resident with non-portfolio interests in Donaco as at the Record Date;
- (d) a foreign resident whose shares in Donaco, or right to receive something of value in respect of shares in Donaco, they owned as at the Record Date, are not taxable Australian property (as that term is defined in section 855-15);
- (e) are not subject to the taxation of financial arrangements (TOFA) rules in Division 230 in relation to gains and losses on their Donaco 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 8 to 44 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

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7. This Ruling applies from 1 July 2014 to 30 June 2015. The Ruling continues to apply after 30 June 2015 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).

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## Scheme

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8. The following description of the scheme is based on information provided by William Buck (NSW) Pty Limited, Donaco's advisers, the applicant for this ruling.

9. The following documents, or relevant parts of them form part of and are to be read with the description:

- The application for class ruling dated 3 June 2014,
- The Independent Expert's Report (IER) dated 9 July 2014, and
- All other correspondence from the applicant in relation to this ruling.

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

10. The Scheme that is the subject of this ruling involved the demerger of shares in OMI by Donaco (the Demerger). The Demerger happened on 16 September 2014.

### Relevant Entities

#### ***Donaco***

11. Donaco is an Australian resident company incorporated on 13 June 1990. Its shares are listed on the Australian Securities Exchange (ASX).

12. Donaco was previously known as Two Way Limited and was the subject of an initial public offering in 2004.

13. On 1 February 2013 Donaco acquired 100% of the share capital of Donaco Singapore Pte Limited, a holding company registered in Singapore with an indirect 75% interest in a casino in Vietnam.

14. Donaco operates leisure, entertainment and associated technology businesses across the Asia Pacific region.
15. Immediately before the demerger, Donaco had on issue:
  - 460,951,560 ordinary shares; and
  - listed and unlisted options to acquire shares in Donaco that have been issued under various share schemes.
16. There were no other ownership interests (as defined in subsection 125-60(1)) in Donaco immediately before the demerger.
17. Donaco, as a stand-alone entity, reported the following retained earnings (losses) in 2012 and 2013:
  - negative retained earnings (losses) of \$50,284,130 in the year ended 30 June 2012, and;
  - negative retained earnings (losses) of \$50,298,741 in the year ended 30 June 2013.

## ***iSentric SDN BHD***

18. iSentric SDN BHD (iSentric) is a mobile technology business, incorporated in Malaysia.
19. In April 2013, Donaco acquired 100% of the issued share capital of iSentric for \$8,500,000, in consideration for \$8,500,000 of fully paid shares in Donaco. Since then iSentric personnel have been providing technology services to Donaco's core hotel and casino business in Vietnam.

## ***OMI***

20. OMI is an Australian resident company that is listed on the ASX.
21. For all intents and purposes, OMI is a 'shell company'.
22. Immediately before conducting any transactions to implement the demerger, OMI had 14,134,977 fully paid ordinary shares on issue.

## **Pre-demerger transactions**

23. OMI undertook a share capital consolidation such that it has 3,750,000 fully paid ordinary shares on issue.
24. Prior to the demerger, Donaco shareholders approved the sale of all shares in Donaco's mobile technology business iSentric - to OMI.

25. The market value of the iSentric shares is \$12,000,000, which is also the value of the OMI shares issued to Donaco as consideration for the sale.

26. Pursuant to the terms of the Share Sale Agreement, Donaco transferred to OMI 100% of Donaco's interest in iSentric in consideration for \$12,000,000 of ordinary fully paid shares in OMI, calculated on a post-consolidation basis at \$0.20 per share (OMI transaction shares).

27. To ensure that OMI had the necessary funding to complete the acquisition, OMI issued up to 600 convertible notes. These notes will be convertible to not more than 3,000,000 OMI shares at an exercise price of \$0.20.

28. OMI issued a further 10,000,000 new ordinary shares in OMI to raise an additional \$2,000,000 and comply with ASX listing rules.

29. Therefore, prior to Donaco making the in specie distribution of the OMI transaction shares to the Donaco shareholders, OMI had 76,750,000 fully paid ordinary shares on issue, of which 60,000,000 (that is 78%) are held by Donaco.

### **The demerger of OMI shares**

30. To effect the demerger by Donaco of OMI shares, the shareholders of Donaco voted at a special general meeting on 25 August 2014 to approve an ordinary resolution under section 256C of the *Corporations Act 2001* to reduce the share capital of Donaco by \$8,500,000 (the capital reduction amount). This amount was debited to the share capital account of Donaco. The capital reduction amount equated to \$0.0185 per Donaco ordinary share.

31. The demerger dividend is the difference between the market value of the OMI transaction shares (\$12,000,000) less the capital reduction amount of \$8,500,000. The demerger dividend equated to \$0.0076 per Donaco ordinary share.

32. The market value of the shares in OMI demerged by Donaco exceeded the capital reduction amount.

33. The aggregate of the capital reduction amount and the demerger dividend was satisfied by an in specie distribution to the shareholders of Donaco of 60,000,000 ordinary shares in OMI held by Donaco.

34. Donaco option holders will not be eligible to participate in the demerger and will therefore not receive any shares in OMI.

## **Reasons for the demerger**

35. Donaco have advised the reasons for the demerger are:
- to allow Donaco to focus on its core activities in the entertainment and leisure business,
  - to allow iSentric to focus on its own growth path in areas of mobile commerce, content publishing and location-based services, and
  - to allow iSentric to receive proper attention from investors who have been eager to follow businesses in the mobile commerce space.

## **Share sale facility**

36. A share sales facility was made available to the following categories of shareholders:
- Ineligible overseas shareholders
  - Shareholders entitled to receive a parcel of OMI transaction shares with a value of less than \$500, and
  - Shareholders who elect to use the share sale facility.

37. The share sale facility enables eligible shareholders' OMI transaction shares to be registered in the name of a nominee entity. After a period of time, the shares are sold and the net proceeds from the sale (less costs) are remitted to the relevant shareholder.

## **Accounting for the distribution to effect the demerger**

38. Donaco accounted for the distribution that effected the demerger by debiting its share capital account by the capital reduction amount of \$8,500,000.
39. The difference of \$3,500,000 between the market value (of \$12,000,000) of the distributed shares in OMI at the time of the demerger and the capital reduction amount (of \$8,500,000), was debited to a demerger reserve and was not sourced from Donaco's share capital account.

## **Post-demerger transactions**

40. Following the demerger, the major shareholding group of Donaco is the Lim Family who hold their interests through Jox Holdings Ltd, an entity controlled by Lim Keong Yew. This enables the Lim family to consolidate their share holdings.

**Other matters**

41. The share capital account of Donaco is not tainted within the meaning of Division 197 immediately before the demerger.
42. Donaco will not make an election under subsection 44(2) of the ITAA 1936 that subsections 44(3) and (4) of the ITAA 1936 do not apply to the total demerger dividend for all shareholders.
43. CGT assets owned by OMI representing at least 50% of the market value of all its CGT assets will be used in the business carried on by OMI and its subsidiary iSentric.
44. Donaco was incorporated in 1990 with the initial public offering of shares in Donaco taking place in 2004. Hence, all shares issued in Donaco are post-CGT assets.

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**Ruling****CGT Consequences*****CGT event G1***

45. CGT event G1 happened in relation to each Donaco ordinary share owned by a Donaco shareholder at the time Donaco made the payment of the capital reduction amount (satisfied by the *in specie* distribution of OMI shares) (section 104-135).

***Capital gain***

46. Donaco shareholders who are Australian residents will make a capital gain from CGT event G1 happening if the capital reduction amount (\$0.0185 per Donaco ordinary share) exceeds the cost base of the Donaco ordinary share. The capital gain is equal to the amount of the excess. No capital loss can be made from CGT event G1 (subsection 104-135(3)).

***Demerger roll-over***

47. A demerger, as defined under section 125-70, happened to the Donaco demerger group (which included Donaco and OMI) under the scheme.
48. A Donaco shareholder can choose demerger roll-over under subsection 125-55(1) for their Donaco ordinary shares.

***CGT consequences of choosing a demerger roll-over***

49. A Donaco shareholder who chooses demerger roll-over will disregard any capital gain made when CGT event G1 happened in relation to each of their Donaco ordinary shares under the demerger (subsection 125-80(1)).



50. If an Australian resident Donaco shareholder chooses demerger roll-over, they must also recalculate the cost base and reduced cost base of their Donaco ordinary shares and calculate the cost base and reduced cost base of their new OMI shares.

51. The first element of the cost base and reduced cost base of each Donaco share and corresponding OMI share received under the demerger is worked out as follows:

- total the cost bases of the Donaco ordinary shares (just before the demerger), and
- apportion that sum over the Donaco shares and corresponding new OMI shares received under the demerger.

52. The apportionment of this sum is done on a reasonable basis having regard to the market values (just after the demerger) of the Donaco shares and OMI shares, or a reasonable approximation of those market values (subsections 125-80(2) and 125-80(3)).

53. For the purposes of determining the cost base and reduced cost base of Donaco ordinary shares and OMI ordinary shares under subsections 125-80(2) and (3), the Commissioner accepts that a reasonable approximation of the market values (just after the demerger) will be provided by the volume weighted average price of Donaco and OMI ordinary shares as traded on the ASX over the five trading days after the date of the demerger (being the date on which Donaco distributed the relevant shares it owned in OMI to the Donaco shareholders).

**Note:** Shareholders will be advised of these prices by Donaco and iSentric after the date of the demerger.

### ***CGT consequences of not choosing a demerger roll-over***

54. A Donaco shareholder who does not choose demerger roll-over will not disregard any capital gain made when CGT event G1 happened in relation to a Donaco ordinary share under the demerger.

55. The first element of the cost base and reduced cost base of each Donaco ordinary share and corresponding OMI share is calculated as described in paragraphs 51 to 52 of this Ruling (subsections 125-85(1) and (2)).

### ***Acquisition date of the OMI shares for the purpose of making a discount capital gain***

56. For the purpose of determining eligibility for a discount capital gain, the OMI shares received by Australian resident and foreign resident Donaco shareholders will be taken to have been acquired on the date the shareholder acquired, for CGT purposes, the corresponding Donaco ordinary shares (item 2 of the table in subsection 115-30(1)). This will be the case whether or not the Donaco shareholder chooses, or is eligible for, demerger roll-over relief.

***Foreign resident Donaco shareholders***

57. Donaco shareholders can disregard a capital gain from CGT event G1 that happened to each of their Donaco shares if:

- they were a foreign resident just before the CGT event happened, and
- their Donaco shares were not taxable Australian property (section 855-10).

58. Donaco shareholders who are foreign residents and their Donaco shares were taxable Australian property (under section 855-10) cannot disregard any capital gain made from CGT event G1 that happened to their shares under the demerger.

59. Donaco shareholders who are foreign residents cannot choose demerger roll-over under subsection 125-55(1) for their Donaco shares if the OMI shares they acquired under the demerger are not taxable Australian property just after they acquired them (subsection 125-55(2)).

60. The first element of the cost base and reduced cost base of each Donaco share and new OMI share is calculated in the same manner as if they had chosen demerger roll-over (subsections 125-85(1) and 125-85(2)).

**Dividend Consequences*****Capital Return component***

61. To the extent that the *in specie* distribution to Donaco shareholders of OMI shares under the scheme is debited to the share capital account of Donaco (that is, \$8,500,000), it is not a 'dividend' as defined in subsection 6(1) of the ITAA 1936.

***Demerger Dividend component***

62. To the extent that the balance of the *in specie* distribution (that is, \$3,500,000) to Donaco shareholders of OMI shares is a dividend, it will be a demerger dividend (subsection 6(1) of the ITAA 1936).

63. Donaco shareholders received a demerger dividend consisting of a pro rata share of the excess of the money value of the *in specie* distribution of OMI shares over the amount debited to the share capital account of Donaco (see Taxation Ruling TR 2003/8).

64. The demerger dividend is neither assessable income nor exempt income of Australian resident and foreign resident Donaco shareholders for Australian tax purposes (subsection 44(3) and 44(4) of the ITAA 1936).

***The application of sections 45B, 45BA and 45C***

65. The Commissioner will not make a determination under paragraph 45B(3)(a) of the ITAA 1936 that section 45BA of the ITAA 1936 applies to the whole, or any part, of the demerger benefit provided to Donaco shareholders under the demerger of OMI shares.

66. The Commissioner will not make a determination under paragraph 45B(3)(b) of the ITAA 1936 that section 45C of the ITAA 1936 applies to the whole, or any part, of the capital benefit provided to Donaco shareholders under the demerger of OMI shares.

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**Commissioner of Taxation**

8 October 2014

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## 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.*

67. The tax consequences and relevant legislative provisions that arise concerning the scheme that is the subject of this Ruling are outlined in the Ruling part of this document.

### **Distribution debited to the share capital account is not a dividend for income tax purposes**

68. Subsection 44(1) of the ITAA 1936 includes in a shareholder's assessable income any dividends, as defined in subsection 6(1) of the ITAA 1936, paid to the shareholders out of profits derived by the company from any source (if the shareholder is a resident of Australia) and from an Australian source (if the shareholder is a non-resident).

69. The term 'dividend' in subsection 6(1) of the ITAA 1936 includes any distribution made by a company to any of its shareholders, whether in money or other property. However, paragraph (d) of the definition of 'dividend' in subsection 6(1) excludes a distribution from the meaning of 'dividend' if the amount of a distribution is debited against an amount standing to the credit of the company's share capital account.

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

71. Subsection 975-300(3) states that an account is not a share capital account if it is tainted.

72. The *in specie* distribution to Donaco shareholders of OMI shares has been recorded as a debit to Donaco's share capital account of \$8,500,000. As the share capital account of Donaco is not tainted within the meaning of Division 197, paragraph (d) of the definition of 'dividend' in subsection 6(1) of the ITAA 1936 applies. Accordingly the *in specie* distribution to Donaco shareholders of OMI shares, being debited to the share capital account, is not a 'dividend' as defined in subsection 6(1) of the ITAA 1936. Therefore, it will not be included in the assessable income of Donaco shareholders under subsection 44(1) of the ITAA 1936.

## **Balance of the distribution is a demerger dividend**

73. Donaco shareholders also received a dividend to the extent that the market value of the OMI shares distributed under the demerger exceeded the amount debited against the share capital account (see Taxation Ruling TR 2003/8).

74. This dividend is not assessable income or exempt income (subsections 44(3) and 44(4) of the ITAA 1936) if:

- the dividend is a 'demerger dividend' (as defined in subsection 6(1) of the ITAA 1936)
- Donaco (as the head entity of the demerger group) does not elect that subsections 44(3) and 44(4) of the ITAA 1936 will not apply to the demerger dividend (subsection 44(2) of the ITAA 1936), and
- subsection 44(5) of the ITAA 1936 is satisfied.

75. As each of the conditions in paragraph 74 of this Ruling are satisfied, the demerger dividend received by Donaco shareholders will not be assessable income or exempt income (subsection 44(4) of the ITAA 1936).

## **The demerger of OMI shares**

76. The demerger roll-over provisions in Division 125 contain a number of conditions for eligibility to choose roll-over. The main conditions that are relevant are:

- (a) a person owns a share in a company, or a unit or other interest in a trust (the original interest)
- (b) the company or trust is the head entity of a demerger group
- (c) a demerger happens to the demerger group, and
- (d) under the demerger, a CGT event happens to the original interest and the person acquires a new or replacement interest in the demerged entity and nothing else.

77. Under the scheme, the conditions for choosing demerger roll-over under Division 125 were satisfied in respect of the demerger of OMI shares. As a consequence, the demerger concessions in Division 125, and in subsections 44(3) and (4) of the ITAA 1936, are available to the Donaco shareholders in respect of the demerger of OMI shares.

78. If a Donaco shareholder chooses demerger roll-over, they must recalculate the cost base and reduced cost base of their Donaco ordinary shares and calculate the cost base and reduced cost base of their new OMI shares.

**The application of sections 45B, 45BA and 45C**

79. Section 45B of the ITAA 1936 is an anti-avoidance provision which, if applicable, allows the Commissioner to make a determination that all or part of a demerger allocation or return of capital to be received by shareholders is to be treated as an unfranked dividend.

80. The purpose of section 45B of the ITAA 1936 is to ensure that the relevant amounts distributed to shareholders are treated as dividends for tax purposes if certain payments, allocations and distributions are made in substitution for dividends. Specifically, the provision applies where:

- (a) there is a scheme under which a person is provided with a demerger benefit or a capital benefit by a company (paragraph 45B(2)(a) of the ITAA 1936)
- (b) under the scheme a taxpayer, who may or may not be the person provided with the demerger benefit or the capital benefit, obtains a tax benefit (paragraph 45B(2)(b) of the ITAA 1936), and
- (c) 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, (other than an incidental purpose) of enabling a taxpayer to obtain a tax benefit (paragraph 45B(2)(c) of the ITAA 1936).

81. The arrangement involving the *in specie* distribution to Donaco shareholders of OMI shares constitutes a scheme for the purposes of section 45B of the ITAA 1936.

82. The phrase 'provided with a demerger benefit' is defined in subsection 45B(4) of the ITAA 1936 and includes a company providing a person with ownership interests in that or another company. The phrase 'provided with a capital benefit' is defined in subsection 45B(5) of the ITAA 1936 and includes the provision of ownership interests in a company to a person. The *in specie* distribution of OMI shares means that Donaco shareholders will be taken to have been provided with a demerger benefit, and provided with a capital benefit.

83. For the purposes of paragraph 45B(2)(c) of the ITAA 1936, the Commissioner is required to consider the relevant circumstances (as outlined in subsection 45B(8) of the ITAA 1936) of the scheme to determine whether it could be concluded that entities that entered into or carried out the scheme or any part of the scheme did so for a purpose (other than an incidental purpose) of enabling the relevant taxpayer to obtain a tax benefit (as defined in subsection 45B(9) of the ITAA 1936). On the basis of the information surrounding the *in specie* distribution of OMI shares as described in the Class Ruling application and further information, the Commissioner has formed the view that the demerger benefits and capital benefits provided to the Donaco shareholders have not been made for a more than incidental purpose of enabling a taxpayer to obtain a tax benefit.

84. Accordingly, the Commissioner will not make a determination:

- under paragraph 45B(3)(a) of the ITAA 1936 that section 45BA of the ITAA 1936 applies to the whole, or any part, of the demerger benefit provided to Donaco shareholders under the demerger of OMI shares, or
- under paragraph 45B(3)(b) of the ITAA 1936 that section 45C of the ITAA 1936 applies to the whole, or any part, of the capital benefit provided to Donaco shareholders under the demerger of OMI shares.

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

85. The following is a detailed contents list for this Ruling:

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## References

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<i>Previous draft:</i>	- ITAA 1936 45B(4)
Not previously issued as a draft	- ITAA 1936 45B(5)
	- ITAA 1936 45B(8)
<i>Related Rulings/Determinations:</i>	- ITAA 1936 45B(9)
TR 2003/8; TR 2006/10	- ITAA 1936 45BA
	- ITAA 1936 45C
<i>Subject references:</i>	- ITAA 1997 104-135
- capital benefit	- ITAA 1997 104-135(3)
- capital reduction	- ITAA 1997 115-30(1)
- demerger	- ITAA 1997 Div 125
- demerger benefit	- ITAA 1997 125-55(1)
- demerger dividend	- ITAA 1997 125-55(2)
- demerger group	- ITAA 1997 125-60(1)
	- ITAA 1997 125-70
	- ITAA 1997 125-80(1)
<i>Legislative references:</i>	- ITAA 1997 125-80(2)
- ITAA 1936 6(1)	- ITAA 1997 125-80(3)
- ITAA 1936 44	- ITAA 1997 125-85(1)
- ITAA 1936 44(1)	- ITAA 1997 125-85(2)
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- ITAA 1936 44(4)	- ITAA 1997 855-10
- ITAA 1936 44(5)	- ITAA 1997 855-15
- ITAA 1936 45B	- ITAA 1997 975-300
- ITAA 1936 45B(2)(a)	- ITAA 1997 975-300(3)
- ITAA 1936 45B(2)(b)	- ITAA 1997 977-50
- ITAA 1936 45B(2)(c)	- ITAA 1997 995-1(1)
- ITAA 1936 45B(3)(a)	- TAA 1953
- ITAA 1936 45B(3)(b)	- Corporations Act 2001 256C

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### ATO references

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