

CR 2018/26 - Income tax: Macquarie Group Limited - Macquarie Group Capital Notes 3

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Class Ruling

Income tax: Macquarie Group Limited – Macquarie Group Capital Notes 3

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📌 This publication provides you with the following level of protection:

This publication (excluding appendixes) is a public ruling for the purposes of the *Taxation Administration Act 1953*.

A public ruling is an expression of the Commissioner's opinion about the way in which a relevant provision applies, or would apply, to entities generally or to a class of entities in relation to a particular scheme or a class of schemes.

If you rely on this Ruling, the Commissioner must apply the law to you in the way set out in the ruling (unless the Commissioner is satisfied that the ruling is incorrect and disadvantages you, in which case the law may be applied to you in a way that is more favourable for you – provided the Commissioner is not prevented from doing so by a time limit imposed by the law). You will be protected from having to pay any underpaid tax, penalty or interest in respect of the matters covered by this Ruling if it turns out that it does not correctly state how the relevant provision applies to you.

Summary – 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 26BB of the ITAA 1936
 - section 43B of the ITAA 1936
 - subsection 44(1) of the ITAA 1936
 - section 45 of the ITAA 1936
 - section 45A of the ITAA 1936
 - section 45B of the ITAA 1936
 - section 45C of the ITAA 1936
 - section 70B of the ITAA 1936
 - section 159GP 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
- section 104-25 of the ITAA 1997
- section 109-10 of the ITAA 1997
- subsection 110-25(2) of the ITAA 1997
- subsection 110-55(2) of the ITAA 1997
- section 130-60 of the ITAA 1997
- section 204-30 of the ITAA 1997
- section 207-20 of the ITAA 1997
- Subdivision 207-D of the ITAA 1997
- section 207-145 of the ITAA 1997
- section 207-155 of the ITAA 1997
- Division 974 of the ITAA 1997
- subsection 995-1(1) of the ITAA 1997.

Class of entities

3. The class of entities to which this Ruling applies is investors (referred to in this Ruling as Holders) who acquired fully paid, unsecured, subordinated, mandatorily convertible notes issued by Macquarie Group Limited (MGL) called Macquarie Group Capital Notes 3 (MCN3), and who:

- are residents of Australia (within the meaning of subsection 6(1) of the ITAA 1936) during the period in which they hold MCN3
- do not hold their MCN3 as revenue assets (as defined in section 977-50 of the ITAA 1997) or as trading stock (as defined in subsection 995-1(1) of the ITAA 1997) – that is, they hold their MCN3 on capital account
- will not make, be under an obligation to make, or be likely to make (nor will an associate of the investor make, be under an obligation to make, or be likely to make) a ‘related payment’ (as defined in former section 160APHN of the ITAA 1936) in respect of any of the distributions on their MCN3
- will hold their MCN3 for a continuous period of at least 90 days (excluding the day they acquired the MCN3 and, if relevant, the day they disposed of their MCN3)

beginning on the day after the day on which they acquired the MCN3

- will not take any 'positions' (as defined in former section 160APHJ of the ITAA 1936) at any time in relation to their MCN3, apart from holding their MCN3
- will not (and their connected entities will not) engage in distribution washing (within the meaning of section 207-157 of the ITAA 1997) in relation to Distributions on the MCN3 (unless the exception in subsection 207-157(4) applies), and
- are not subject to the taxation of financial arrangements (TOFA) rules in Division 230 of the ITAA 1997 in relation to gains and losses on their MCN3.

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

4. The class of entities to which this Ruling applies does not extend to the Holders of MCN3 who did not acquire their MCN3 by initial application under the Replacement Prospectus for the issue of MCN3 dated 15 May 2018 (the Prospectus).

Qualifications

5. This Ruling does not consider the tax implications of the Exchange of the MCN3 on the occurrence of a Non-Viability Event, Acquisition Event, Regulatory Event or Tax Event.

6. This Ruling does not consider the tax implications of the Resale of the MCN3 under a Resale Notice.

7. This Ruling does not consider how the tax law applies to a Nominated Party who acquires their MCN3 under a Resale Notice.

8. This Ruling does not consider how the gross-up and tax offset rules in Division 207 of the ITAA 1997 apply to a Holder that is a partnership or the trustee of a trust, or to indirect distributions to partners in a partnership, or beneficiaries or trustees of a trust.

9. The Commissioner makes this Ruling based on the precise scheme identified in this Ruling.

10. 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 13 to 63 of this Ruling.

11. 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.

Date of effect

12. This Ruling applies from 1 July 2017 to 30 June 2028. The Ruling continues to apply after 31 March 2028 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

13. The following description of the scheme is based on information provided by the applicant, including:

- the Terms and Conditions of the MCN3 per the Prospectus (Terms)
- the Prospectus, and
- the MCN3 Trust Deed dated 7 May 2018 (Trust Deed).

14. In this Class Ruling, unless otherwise defined, capitalised terms take the meaning that they have in the Terms.

Background

15. MGL is an Australian resident company with shares listed on the Australian Securities Exchange (ASX). The only shares that MGL has issued are ordinary shares (Ordinary Shares).

16. MGL is regulated by APRA as the NOHC of Macquarie Bank Limited (MBL), which is an authorised deposit taking institution (ADI) under the *Banking Act 1959*.

17. For Australian income tax purposes, MGL is the head company of the MGL income tax consolidated group (MGL TCG).

18. In the Prospectus, MGL announced its intention to undertake a capital raising by the issue of the MCN3 to raise A\$900 million, with the ability to raise up to A\$1 billion (the Offer).

19. MCN3 will qualify for inclusion as Eligible capital of MGL, for the purposes of APRA's prudential standards governing MGL as an authorised NOHC.

20. The Offer is part of MGL's ongoing capital management strategy, including the redemption of the Macquarie Group Capital Notes (MCN), and the net proceeds of the Offer will be used for general corporate purposes.

21. The Prospectus states that persons wishing to acquire the MCN3 may apply under one or more of the following offers:

- an institutional offer to institutional investors
- a broker firm offer made to Australian resident retail and high net worth clients of syndicate brokers or New Zealand resident high net wealth clients of syndicate brokers who are invited to apply under the broker firm offer
- a reinvestment offer made to eligible MCN holders, and
- a security-holder offer made to eligible security holders.

22. The MCN3 may also be offered (as part of any Offer category) in certain permitted jurisdictions outside Australia where such Offer is made, and accepted, in accordance with the laws of such jurisdictions.

23. The MCN3 were issued on 7 June 2018. The MCN3 are listed on the ASX and trade under the ASX code MQGPC.

Main features of the MCN3

24. MCN3 are fully paid, perpetual, unsecured, subordinated, mandatorily convertible notes issued by MGL.

25. The obligations of MGL under the MCN3 are constituted by, and specified in, the terms and conditions of the MCN3, the Trust Deed and other applicable constituent documents of MGL including its constitution.

26. Each MCN3 is issued fully paid for an issue price of \$100 (Issue Price).

27. With the prior written consent of APRA (where required), each MCN3 may be Redeemed or Resold by MGL, or Exchanged for fully paid Ordinary Shares, in accordance with the Terms.

28. Exchange is defined as the allotment and issue of Ordinary Shares in respect of the MCN3 in accordance with and subject to the Terms.

29. The MCN3 cannot be Redeemed, Resold or Exchanged at the option of a Holder.

30. There is no certainty that the MCN3 will be Exchanged, Redeemed or Resold as APRA approval for Redemption or Resale may not be granted. In any event, MGL may be unwilling to Exchange, Redeem or Resell the MCN3 on a Scheduled Optional Exchange Date. Accordingly, the MCN3 may remain on issue after the Scheduled Optional Exchange Dates, and may still be on issue on the Mandatory Exchange Date (at which time they must be Exchanged, subject to satisfaction of the Exchange conditions).

Distributions

31. The MCN3 are scheduled to pay floating rate cash distributions commencing on 17 September 2018, thereafter quarterly, in arrears until all MCN3 are Exchanged, Redeemed or Written-Off.

32. Subject to the Terms, the Holder will receive on each Distribution Payment Date a cash distribution for the Distribution Period ending on that Distribution Payment Date calculated as follows:

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

33. The **Distribution Payment Date** in respect of an MCN3 is:

- each 15 March, 15 June, 15 September and 15 December commencing on 17 September 2018 until (but not including) the date on which that MCN3 has been Redeemed or Exchanged, and
- the Redemption Date, Resale Date or an Exchange Date, except where the Exchange is on account of a Non-Viability Event.

34. The **Distribution Rate** is expressed as a percentage per annum and is calculated as:

$$(\text{Reference Rate} + \text{Margin}) \times \text{Franking Adjustment Factor}$$

35. The **Reference Rate** means the rate (expressed as a percentage per annum):

- designated BBSW in respect of prime bank eligible securities having a tenor closest to the Distribution Period which the ASX (or its successor as administrator of that rate) publishes through information vendors at approximately 10:15am (or such other time at which such rate is accustomed to be so published) (Publication Time) on the first day of that Distribution Period, or

- if such rate is not so published by 10:30am (or such other time that is 15 minutes after the then prevailing Publication Time) on that day, or if it does appear but MGL determines that there is an obvious error in that rate, Reference Rate means the rate determined by MGL having regard to comparable indices then available and provided that where an MCN3 is Resold on a day which is not a scheduled quarterly Distribution Payment Date, the Reference Rate for the Distribution Period commencing on the Resale Date is the Reference Rate for the Distribution Period preceding the Resale Date.

36. The **Margin**, as determined under the Bookbuild, is 4.00%.

37. **Franking Adjustment Factor** means:

$$\frac{(1 - T)}{1 - [T \times (1 - F)]}$$

where:

F means the Franking Rate – the franking percentage, as defined under Part 3-6 of the ITAA 1997, for a Distribution as at the relevant Distribution Payment Date (expressed as a decimal) multiplied by the proportion of the relevant Distribution that is frankable.

T means the Tax Rate – the Australian corporate tax rate applicable to the franking account of MGL on the relevant Distribution Payment Date (expressed as a decimal).

N is the number of days in the Distribution Period.

38. The Franking Adjustment Factor operates such that, the higher the Franking Rate of the distribution, the lower the Distribution Rate (and the lower the cash Distribution).

39. The payment of any Distribution will be made where:

- MGL in its absolute discretion determines that the Distribution is payable to Holders
- the payment of the Distribution would not result in MGL breaching APRA's capital adequacy requirements applicable to it
- the payment of the Distribution would not result in MGL becoming, or being likely to become, insolvent for the purposes of the *Corporations Act 2001*, or
- APRA does not otherwise object to the payment of the Distribution.

40. Distributions are non-cumulative. If all or any part of any distribution is not paid, MGL has no liability to pay the unpaid amount of the Distribution and Holders have no claim or entitlement in respect of any person in respect of such non-payment. Such non-payment does not constitute an event of default.

41. No interest accrues on any unpaid Distributions and the Holders have no claim or entitlement in respect of interest on any unpaid Distributions.

42. A Dividend Restriction applies if MGL fails to pay a Distribution in full within 10 Business Days of the relevant Distribution Payment Date. Subject to certain exceptions, the Dividend Restriction operates to restrict MGL (without the prior approval of a Special Resolution of Holders) from determining, declaring or paying a dividend on Ordinary Shares, or undertaking any Buy-Back or Capital Reduction in relation to Ordinary Shares until the next Distribution Payment Date.

Scheduled Mandatory Exchange

43. MGL must Exchange all of the MCN3 for Ordinary Shares on the Mandatory Exchange Date, which is the earlier of:

- 15 December 2027 (the Scheduled Mandatory Exchange Date), or
- any Distribution Payment Date after the Scheduled Mandatory Exchange Date (a Deferred Mandatory Exchange Date).

on which the Exchange Conditions relevant to those dates are satisfied, unless the MCN3 have been or will be Redeemed or Exchanged before that date.

44. The Exchange Conditions in respect of a Mandatory Exchange Date are satisfied where:

- (a) the Daily Volume Weighted Average Price (VWAP) of Ordinary Shares sold on the ASX on the 25th Business Day immediately preceding (but not including) the Mandatory Exchange Date (or, if that day is not an ASX Trading Day, the last ASX Trading Day prior to that day) is greater than 56% of the Issue Date VWAP
- (b) the VWAP of Ordinary Shares sold on the ASX during the period of 20 ASX Trading Days immediately preceding (but not including) the Mandatory Exchange Date is such that the number of Ordinary Shares to be issued is less than or equal to the Maximum Exchange Number applicable to the mandatory exchange date
- (c) no Suspension Event applies in respect of the Mandatory Exchange Date, and

- (d) MGL is not Delisted as at the Mandatory Exchange Date.

Non-Viability Event Exchange

45. If a Non-Viability Event occurs, MGL must Exchange such number of the MCN3 as complies with an APRA notice.

Acquisition Event Exchange

46. If an Acquisition Event occurs, MGL must Exchange all of the MCN3, subject to the conditions in the Terms.

Optional Exchange

47. MGL may, in its sole discretion, elect to:

- Exchange all or some of the MCN3 on any Scheduled Optional Exchange Date, and
- Exchange all or some of the MCN3 following the occurrence of a Tax Event or a Regulatory Event.

48. The Scheduled Optional Exchange Dates are the Distribution Payment Dates falling on or about:

- 16 December 2024
- 16 June 2025, and
- 15 December 2025.

49. The Exchange Date will be deferred if certain additional conditions are not satisfied.

Exchange Mechanics (general rules)

50. On an Exchange Date, MGL will allot and issue the Exchange Number of Ordinary Shares to the Holders (or as they may direct) for each MCN3 held by the Holder.

51. The Exchange Number will be calculated by MGL in accordance with the formula set out in the Terms, subject to the Exchange Number being no greater than the Maximum Exchange Number.

52. On Exchange, each Holder's rights (including to payment of Distributions other than the Distribution, if any, payable on the Exchange Date) in relation to each MCN3 that is being Exchanged will be immediately and irrevocably terminated for an amount equal to the Issue Price of that MCN3 and MGL will apply that Issue Price by way of payment for the subscription for the Ordinary Shares. Each Holder is taken to have irrevocably directed that any amount payable is to be applied as provided for in the Terms and no Holder has any right to payment in any other way.

53. If the total number of Ordinary Shares to be allotted to a Holder in respect of their aggregate holding of MCN3 upon Exchange includes a fraction of an Ordinary Share, that fraction of an Ordinary Share will be disregarded.

54. The Ordinary Shares issued or arising from an Exchange will rank equally with all other fully paid Ordinary Shares.

55. When an Exchange of an MCN3 occurs, all other rights conferred or restrictions imposed on that MCN3 under the Terms will no longer have effect (except for rights relating to a Distribution which is payable but has not been paid on or before the Exchange Date) and the MCN3 is cancelled.

Optional Redemption

56. MGL may, in its sole discretion, but with APRA's prior written approval, elect to:

- Redeem all or some of the MCN3 on a Scheduled Optional Exchange Date, or
- Redeem all or some of the MCN3 following the occurrence of a Tax Event or a Regulatory Event.

57. On the Redemption Date:

- each MCN3 being Redeemed will be Redeemed by payment of the Issue Price of that MCN3 (the Redemption Price) to the relevant Holder recorded on the Register, and
- Distributions from (and including) the immediately preceding Distribution Payment Date and up to (but excluding) the Redemption Date will be paid in respect of the MCN3 being Redeemed on such date, to the extent the conditions for the payment of Distributions are met.

58. Upon payment of the Redemption Price and any Distribution payable on the Redemption Date, all other rights conferred, or restrictions imposed, by each MCN3 being Redeemed on that date will no longer have effect and that MCN3 will be cancelled.

Resale

59. On any date on which it may issue a Redemption Notice, in lieu of such Redemption Notice, MGL may, in its sole discretion, but with APRA's prior written approval, issue to each Holder a notice (a Resale Notice) specifying that all or some of each Holder's holding of the MCN3 will be transferred to one or more Nominated Parties (that is, Resold).

60. Each Holder on the Resale Date is taken to irrevocably offer to sell the MCN3 that are the subject of the Resale Notice to the Nominated Party or Nominated Parties on the Resale Date for a purchase price per MCN3 equal to the Issue Price of that MCN3 (the Resale Price).

Sale Agent

61. Under the Terms, each Holder agrees to provide to MGL, (and, where necessary, the Sale Agent) any information necessary or desirable to give effect to an Exchange.

62. If any MCN3 of a Holder are required to be Exchanged and the Holder has notified MGL that it does not wish to receive Ordinary Shares as a result of the Exchange (whether partly or entirely), then MGL will use reasonable endeavours to appoint a Sale Agent (which is not MGL or any Related Body Corporate of MGL) to sell the Ordinary Shares, and pay to the relevant Holder a cash amount equal to the Attributable Proceeds of the relevant Holder or, where a Foreign Account Tax Compliance Act (FATCA) Withholding is required, the Sale Agent will deal with the Ordinary Shares in accordance with the FATCA rules.

Other Matters

63. The Ruling is made on the basis that:

- (a) each MCN3 is an 'equity interest' in MGL under Division 974 of the ITAA 1997 and a 'non-share equity interest' in MGL as defined in subsection 995-1(1) of the ITAA 1997
- (b) each Ordinary Share obtained by a Holder on the Exchange of the MCN3 will be an 'equity interest' in MGL under Division 974 of the ITAA 1997
- (c) each Distribution paid in respect of the MCN3 will be a 'frankable distribution' under section 202-40 of the ITAA 1997
- (d) MGL is expected to frank each Distribution in respect of the MCN3 in accordance with its franking policy that applies to Ordinary Shares (at such a time as Distributions are made), and at the same franking

- percentage as the benchmark for the franking period in which the Distribution is made
- (e) MGL will not differentially frank Distributions to different Holders in respect of the MCN3 according to the tax status of Holders or on any other basis
 - (f) Distributions in respect of the MCN3 will not be debited to any extent to MGL's share capital account (within the meaning of section 975-300 of the ITAA 1997) or non-share capital account (within the meaning of section 164-10 of the ITAA 1997)
 - (g) Distributions on the MCN3 will not be sourced, directly or indirectly, from MGL's share capital account or its non-share capital account
 - (h) immediately before payment of a Distribution on the MCN3, MGL will have sufficient available frankable profits (worked out under section 215-20 of the ITAA 1997) to pay the Distribution
 - (i) the share capital account of MGL will not become tainted (within the meaning of Division 197 of the ITAA 1997) upon the issue of the MCN3 or the issue of Ordinary Shares on Exchange
 - (j) currently, the MGL TCG partially franks (at 45%) dividends on Ordinary Shares and distributions on frankable non-share equity interests. MGL's policy in relation to franking dividends on Ordinary Shares is not expected to change as a result of the issuance of the MCN3
 - (k) on Exchange or Redemption of the MCN3, MGL will debit the Issue Price of the MCN3 to its non-share capital account (within the meaning of sections 164-10 and 164-20 of the ITAA 1997), and
 - (l) all parties to the transaction are dealing with each other on arm's length terms and fair value consideration will be provided by the Holders to acquire MCN3.

Ruling

Capital Gains Tax (CGT) implications

Acquisition time for each MCN3

64. Each Holder will be taken to have acquired their MCN3 on 7 June 2018, being the date on which the contract for the allotment of the MCN3 is entered into (item 2 of the table in section 109-10 of the ITAA 1997).

Cost base and reduced cost base of each MCN3

65. The first element of the cost base and reduced cost base of each MCN3 will be A\$100 (paragraph 110-25(2)(a) and subsection 110-55(2) of the ITAA 1997).

Exchange of MCN3 for Ordinary Shares

66. Each MCN3 is a convertible interest in MGL (as defined in subsection 995-1(1) of the ITAA 1997 and item 4 of the table in subsection 974-75(1) of the ITAA 1997).

67. CGT event C2 will happen for Holders on Exchange of the MCN3 for Ordinary Shares as the Exchange will be the conversion of a convertible interest (paragraph 104-25(1)(f) of the ITAA 1997).

68. Any capital gain or capital loss made by a Holder from CGT event C2 happening on Exchange of the MCN3 will be disregarded (subsection 130-60(3) of the ITAA 1997).

Acquisition time of Ordinary Shares on Exchange

69. Each Ordinary Share acquired by the Holders on Exchange of the MCN3 will be taken to have been acquired when the Exchange happens on the relevant Exchange Date (subsection 130-60(2) of the ITAA 1997).

Cost base and reduced cost base of Ordinary Shares acquired on Exchange

70. The first element of the cost base and the reduced cost base of each Ordinary Share acquired under the Exchange of the MCN3 will be equal to the cost base and reduced cost base of the relevant MCN3 at the time of the Exchange (item 2 of the table in subsection 130-60(1) of the ITAA 1997).

CGT event A1 happens on the disposal of Ordinary Shares by a Sale Agent on behalf of a Holder

71. CGT event A1 will happen to a Holder where, on Exchange of the MCN3, a Holder elects for a Sale Agent to (on the behalf of the Holder) dispose of their allocation of Ordinary Shares and remit the proceeds to the Holder (section 104-10 of the ITAA 1997)

72. The time of CGT event A1 will be when the Sale Agent, on behalf of the Holder, enters into the contract for the sale of the Ordinary Shares (paragraph 104-10(3)(a) of the ITAA 1997).

73. The first element of the cost base and reduced cost base of the Ordinary Shares acquired by the Holder under the Exchange of the MCN3, and sold by the Sale Agent on behalf of the Holder, will be determined by item 2 of the table in subsection 130-60(1) of the ITAA 1997 (see paragraph 70 of this Ruling).

74. The Ordinary Shares acquired by a Holder under the Exchange of the MCN3, and sold by the Sale Agent on behalf of the Holder, will be taken to have been acquired on the date determined by subsection 130-60(2) of the ITAA 1997 (see paragraph 69 of this Ruling).

Income tax consequences of receiving Distributions

Inclusion of Distributions and franking credits in assessable income

75. The Holders must include in their assessable income all Distributions received in respect of their MCN3 (subparagraph 44(1)(a)(ii) of the ITAA 1936).

76. Holders are also required to include the amount of the franking credit attached to a Distribution in their assessable income for the income year in which the Distribution is made (subsection 207-20(1) of the ITAA 1997), unless Subdivision 207-D of the ITAA 1997 applies.

Entitlement to a tax offset for franking credits

77. Holders will be entitled to a tax offset equal to the amount of the franking credit attached to a Distribution (subsection 207-20(2) of the ITAA 1997), unless Subdivision 207-D of the ITAA 1997 applies.

Exception for exempt income or non-assessable non-exempt income

78. If a Distribution is either wholly exempt income or wholly non-assessable non-exempt income in the hands of a Holder, the amount of the franking credit attached to the Distribution is not included in the assessable income of the Holder and the Holder is not entitled to a tax offset under subsection 207-20(2) of the ITAA 1997 in respect of the franking credit attached to the Distribution (Subdivision 207-D of the ITAA 1997), unless any of the exceptions in Subdivision 207-E of the ITAA 1997 apply.

79. If only part of a Distribution is either exempt income or non-assessable non-exempt income in the hands of a Holder, the amount of the franking credit on the Distribution is worked out under the formula in subsection 207-90(2) of the ITAA 1997. This has the effect of reducing the amount of the franking credit attached to the Distribution that is included in the Holder's assessable income and reducing the amount of the tax offset the Holder is entitled to, unless any of the exceptions in Subdivision 207-E of the ITAA 1997 apply.

Refundable tax offset rules

80. Where a Holder is entitled to a tax offset under subsection 207-20(2) of the ITAA 1997 in respect of the franking credit attached to a Distribution, the tax offset will be subject to the refundable tax offset rules in Division 67 of the ITAA 1997, unless the tax offset is specifically excluded under section 67-25.

Integrity provisions relating to gross-up and tax offset

81. Section 207-145 of the ITAA 1997 will not apply to adjust the Holders' assessable income to exclude the amount of the franking credit on the Distributions, nor will it deny the tax offset to which the Holders would otherwise be entitled.

Qualified persons

82. Based on the description of the scheme and the class of entities to which this Ruling applies (in particular, paragraphs 3(c) to (e)), Holders will be qualified persons in relation to a Distribution under former section 160APHO of the ITAA 1936.

83. For the purpose of determining whether a Holder is a 'qualified person', the Resale mechanism (of itself) and the Exchange mechanism (of itself) will not affect a Holder's risks of loss or opportunities for gain in respect of the MCN3. This is because neither the Resale mechanism nor the Exchange mechanism constitutes a separate position (former sections 160APHJ and 160APHM of the ITAA 1936).

Determination under paragraph 177EA(5)(b) of the ITAA 1936

84. The Commissioner will not make a determination under paragraph 177EA(5)(b) of the ITAA 1936 to deny the whole, or any part, of the imputation benefits received by Holders in relation to a Distribution.

Determination under paragraph 204-30(3)(c) of the ITAA 1997

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

Dividend stripping operation

86. Distributions will not be made as part of a dividend stripping operation as defined in section 207-155 of the ITAA 1997.

Integrity provisions relevant to Exchange or Redemption

Section 45 of the ITAA 1936

87. Section 45 of the ITAA 1936 will not apply to treat the value of Ordinary Shares issued to Holders on Exchange of the MCN3 as an unfrankable dividend paid by MGL to Holders.

Section 45A of the ITAA 1936

88. The Commissioner will not make a determination under subsection 45A(2) of the ITAA 1936 that section 45C of the ITAA 1936 applies to treat the whole, or any part, of the capital benefit provided to the Holders on the Exchange or Redemption of the MCN3 as an unfranked dividend paid by MGL to the Holders.

Section 45B of the ITAA 1936

89. 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 treat the whole, or any part, of the capital benefit provided to the Holders on the Exchange or Redemption of the MCN3 as an unfranked dividend paid by MGL to the Holders.

Acquisition of Ordinary Shares on Exchange not included in assessable income

90. The value of the Ordinary Shares will not be included in the assessable income of the Holders under subsection 44(1) of the ITAA 1936.

MCN3 are not traditional securities

91. Each MCN3 is not a 'traditional security' as defined in subsection 26BB(1) of the ITAA 1936.

92. Accordingly, a gain on the disposal or Redemption of the MCN3 will not give rise to assessable income of a Holder under subsection 26BB(2) of the ITAA 1936.

93. Similarly, a loss on the disposal or Redemption of the MCN3 will not give rise to an allowable deduction to the Holder under subsection 70B(2) of the ITAA 1936.

MCN3 are not qualifying securities

94. Each MCN3 is not a 'qualifying security' as defined in subsection 159GP(1) of the ITAA 1936. Therefore, Division 16E of Part III of the ITAA 1936 will not apply to the MCN3.

Commissioner of Taxation

13 June 2018

CR 2018/26

Appendix 1 – Explanation

ⓘ *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.*

CGT implications

Acquisition time for each MCN3

95. Item 2 of the table in section 109-10 of the ITAA 1997 provides that where a company issues or allots equity interests or non-equity shares to you, you acquire the equity interests or non-equity shares when the contract is entered into, or, if there is no contract, when they are issued or allotted.

96. Each MCN3 is an equity interest in MGL pursuant to Division 974 of the ITAA 1997. When an investor's application for a certain number of MCN3 is accepted by MGL, this leads to the formation of a contract for the allotment of the MCN3 to the investor (who will become a Holder).

97. Consequently, for CGT purposes, each Holder will be taken to have acquired their MCN3 on 7 June 2018, being the date on which the contract for the allotment of the MCN3 is entered into.

Cost base and reduced cost base of each MCN3

98. The first element of the cost base and the reduced cost base of a CGT asset includes the money paid, or required to be paid, in respect of acquiring the CGT asset (paragraph 110-25(2)(a) and subsection 110-55(2) of the ITAA 1997).

99. The Issue Price of each MCN3 is A\$100. Accordingly, the first element of a Holder's cost base and reduced cost base of each MCN3 is A\$100.

Exchange of MCN3 for Ordinary Shares

100. Under paragraph 104-25(1)(f) of the ITAA 1997, CGT event C2 happens if your ownership of an intangible CGT asset that is a 'convertible interest' ends as a result of the asset being converted.

Convertible interests

101. A 'convertible interest' in a company is defined in subsection 995-1(1) of the ITAA 1997 as an interest of the kind referred to in item 4 of the table in subsection 974-75(1) of the ITAA 1997.

102. Paragraph (b) of item 4 of the table in subsection 974-75(1) of the ITAA 1997 refers to an interest issued by the company that is an 'interest that will, or may, convert into an equity interest in the company or a connected entity of the company'.

103. Section 974-165 of the ITAA 1997 states that an interest (the first interest) is an interest that will or may convert into another interest (the second interest) if one of a number of scenarios occurs. One such scenario is that the first interest must be or may be satisfied by the issue of the second interest (whether to the holder of the first interest or to some other person) (subparagraph 974-165(b)(i) of the ITAA 1997).

104. The MCN3 must be or may be satisfied by the issue of the Ordinary Shares by MGL upon Exchange to the Holders.

105. Accordingly, the MCN3 are convertible interests in MGL.

CGT event C2

106. The Exchange of the MCN3 for Ordinary Shares will be the conversion of a convertible interest. Accordingly, CGT event C2 will happen for Holders as a result of an Exchange (paragraph 104-25(1)(f) of the ITAA 1997).

107. Subdivision 130-C of the ITAA 1997 governs the CGT consequences of the conversion of a convertible interest such as the MCN3.

108. Under subsection 130-60(3) of the ITAA 1997, any capital gain or capital loss made from converting a convertible interest is disregarded. Accordingly, any capital gain or capital loss made by a Holder as a result of CGT event C2 happening on Exchange will be disregarded.

Acquisition time of Ordinary Shares on Exchange

109. Subsection 130-60(2) of the ITAA 1997 states that you are taken to have acquired the shares (acquired by converting a convertible interest) when the conversion of the convertible interest happened.

110. Therefore, each Ordinary Share acquired by the Holders on Exchange of the MCN3 will be taken to have been acquired on the relevant Exchange Date.

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Cost base and reduced cost base of Ordinary Shares acquired on Exchange

111. On Exchange of the MCN3, the first element of the cost base and reduced cost base of the Ordinary Shares acquired under the Exchange will be equal to the cost base and reduced cost base of the relevant MCN3 at the time of the Exchange (item 2 of the table in subsection 130-60(1) of the ITAA 1997).

CGT event A1 happens on the disposal of Ordinary Shares by a Sale Agent on behalf of a Holder

112. CGT event A1 happens when you dispose of a CGT asset (subsection 104-10(1) of the ITAA 1997). You dispose of a CGT asset if a change of ownership occurs from you to another entity; however, a change of ownership does not occur if you stop being the legal owner of the asset but continue to be the beneficial owner (subsection 104-10(2) of the ITAA 1997).

113. On Exchange of the MCN3, a Holder can elect for a Sale Agent to (on behalf of the Holder) dispose of their allocation of Ordinary Shares and remit the net sale proceeds to the Holder. CGT event A1 will happen when the Sale Agent (on behalf of the Holder) enters into the contract for the sale of those Ordinary Shares (paragraph 104-10(3)(a) of the ITAA 1997).

114. A Holder will make a capital gain from CGT event A1 happening if the capital proceeds from the sale of the Ordinary Shares exceed the cost base of the shares. A Holder will make a capital loss if those capital proceeds are less than the reduced cost base of the shares (subsection 104-10(4) of the ITAA 1997).

115. The first element of the cost base and the reduced cost base of the Ordinary Shares acquired by a Holder under the Exchange of the MCN3, and sold on behalf of the Holder by the Sale Agent, will be determined by item 2 of the table in subsection 130-60(1) of the ITAA 1997 (see paragraph 111 of this Ruling).

116. The Ordinary Shares acquired by a Holder under the Exchange of the MCN3, and sold by the Sale Agent on behalf of the Holder, will be taken to have been acquired on the date determined by subsection 130-60(2) of the ITAA 1997 (see paragraphs 109 to 110 of this Ruling).

Income Tax consequences of receiving Distributions

Inclusion of Distributions and franking credits in assessable income

117. Paragraph 44(1)(a) of the ITAA 1936 provides that the assessable income of a resident shareholder in a company includes:

- (a) dividends that are paid to the shareholder by the company out of profits derived by it from any source, and

- (b) all non-share dividends paid to the shareholder by the company.

118. The effect of paragraph 43B(1)(b) of the ITAA 1936 is that section 44 of the ITAA 1936 applies to equity holders in the same way as it applies to shareholders.

119. The MCN3 are 'non-share equity interests' and the Holders are 'equity holders' as defined in subsection 995-1(1) of the ITAA 1997. Distributions will not be debited to any extent to MGL's share capital account or non-share capital account. Accordingly, the Distributions paid in respect of the MCN3 will be 'non-share dividends' as defined in section 974-120 of the ITAA 1997.

120. The Holders must include the Distributions paid in respect of the MCN3 in their assessable income under subparagraph 44(1)(a)(ii) of the ITAA 1936.

121. Under the Australian imputation system, where an Australian resident company makes a franked distribution to another entity, subsection 207-20(1) of the ITAA 1997 requires that the assessable income of the receiving entity include the amount of the franking credit on the distribution. The inclusion of both the distribution and the attached franking credit in a receiving entity's assessable income is known as 'grossing-up' the distribution.

122. In accordance with subsection 207-20(1) of the ITAA 1997, the Holders must include any franking credit attached to a Distribution in their assessable income for the income year in which the Distribution is made.

Entitlement to a tax offset for franking credits

123. Holders will be entitled to a tax offset equal to the amount of the franking credit attached to a Distribution in accordance with subsection 207-20(2) of the ITAA 1997, unless Subdivision 207- D of the ITAA 1997 applies.

Exception for exempt income or non-assessable non-exempt income

124. Under Subdivision 207-D of the ITAA 1997, if a Distribution is either wholly exempt income or wholly non-assessable non-exempt income in the hands of a Holder, the amount of the franking credit attached to the Distribution is not included in the assessable income of the Holder and the Holder is not entitled to a tax offset in respect of the franking credit attached to the Distribution.

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125. Subdivision 207-D of the ITAA 1997 also provides that, if only part of a Distribution is either exempt income or non-assessable non-exempt income in the hands of a Holder, the amount of the franking credit on the Distribution is worked out under the formula in subsection 207-90(2). This has the effect of reducing the amount of the franking credit attached to the Distribution that is included in the Holder's assessable income and reducing the amount of the tax offset the Holder is entitled to.

126. However, Subdivision 207-E of the ITAA 1997 provides a number of exceptions to the rules in Subdivision 207-D of the ITAA 1997 for certain exempt institutions, trusts and life insurance companies.

Refundable tax offset rules

127. The Holders who are entitled to a tax offset under subsection 207-20(2) of the ITAA 1997 will be subject to the refundable tax offset rules in Division 67 of the ITAA 1997, unless they are a type of entity that is specifically excluded (subsection 67-25(1)). The refundable tax offset rules ensure that certain taxpayers are entitled to a refund once their available tax offsets have been utilised to reduce any basic income tax liability to nil.

128. Entities excluded under section 67-25 of the ITAA 1997 include corporate tax entities (such as companies, corporate limited partnerships and public trading trusts), unless they satisfy the conditions in subsections 67-25(1C) or 67-25(1D) of the ITAA 1997.

Integrity provisions relating to gross-up and tax offset

129. Subdivision 207-F of the ITAA 1997 creates the appropriate adjustment to cancel the effect of the gross-up and tax offset rules where there has been a manipulation of the imputation system in a manner that is not permitted under the income tax law.

130. Pursuant to subsection 207-145(1) of the ITAA 1997, this adjustment will occur where a franked distribution is made to an entity in one or more of the following circumstances:

- the entity that receives the franked distribution is not a 'qualified person' in relation to the distribution for the purposes of Division 1A of former Part IIIA of the ITAA 1936 (paragraph 207-145(1)(a))
- the Commissioner has made a determination under paragraph 177EA(5)(b) of the ITAA 1936 that no imputation benefit is to arise in respect of the distribution for the entity (paragraph 207-145(1)(b))
- the Commissioner has made a determination under paragraph 204-30(3)(c) of the ITAA 1997 that no

imputation benefit is to arise in respect of the distribution for the entity (paragraph 207-145(1)(c))

- the distribution is made as part of a dividend stripping operation (paragraph 207-145(1)(d)), or
- the distribution is one to which section 207-157 (about distribution washing) applies (paragraph 207-145(1)(da)).

131. This Ruling is made on the assumption that the distribution washing provisions do not apply (see paragraph 3(f) of this Ruling). The remaining circumstances are discussed below.

Qualified persons

132. The main test of what constitutes a 'qualified person' in relation to a franked distribution for the purposes of Division 1A of former Part IIIAA of the ITAA 1936 is known as the holding period rule.

133. By virtue of former section 160AOA of the ITAA 1936, the holding period rule applies to non-share equity interests, equity holders and non-share dividends in the same way as it applies to shares, shareholders and dividends respectively.

134. As this Ruling is made on the basis that a Holder or an associate of a Holder has not made, is not under an obligation to make, or is not likely to make, a related payment in respect of any of the Distributions (see paragraph 3(c) of this Ruling), the holding period rule, as partly set out in former subsection 160APHO(1) of the ITAA 1936, provides that:

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) ...the taxpayer has satisfied subsection (2) in relation to the primary qualification period in relation to the dividend...

135. Former section 160APHD of the ITAA 1936 defines the 'primary qualification period' in relation to a taxpayer in relation to shares as the period beginning on the day after the day on which the taxpayer acquired the shares, and ending:

- (a) for preference shares – on the 90th day after the day on which the shares became ex dividend, or
- (b) for shares that are not preference shares – on the 45th day after the day on which the shares became ex dividend.

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136. The holding period rule, as further enunciated in former subsection 160APHO(2) of the ITAA 1936, requires a person to hold shares 'at risk' for a continuous period (excluding the day of acquisition and the day of disposal of the share) of at least 45 days (if the shares are not preference shares) or at least 90 days (if the shares are preference shares) during either the primary qualification period in relation to the dividend.

137. A Dividend Restriction applies if MGL fails to pay a Distribution in full within 10 Business Days of the relevant Distribution Payment Date. Subject to certain exceptions, the Dividend Restriction restricts MGL (without the prior approval of a Special Resolution of Holders) from paying a dividend on Ordinary Shares, or undertaking any Buy-Back or Capital Reduction in relation to Ordinary Shares until the next Distribution Payment Date. That is, Distributions on the MCN3 are in preference to distributions on Ordinary Shares. Further, each MCN3 ranks for payment, and ranks in a Winding Up of MGL, senior to Ordinary Shares. As such, the MCN3 are less risky than Ordinary Shares in MGL and are 'preference shares' for the purposes of former sections 160APHD and 160APHO of the ITAA 1936.

138. As the MCN3 are treated as 'preference shares', a Holder is required to hold the shares on which a dividend has been paid for a continuous period of at least 90 days during the primary qualification period.

139. In establishing whether a Holder held their MCN3 'at risk' for the required period, any days on which the shareholder had materially diminished risks of loss or opportunities for gain in respect of the shares are to be excluded. The exclusion of those days is not taken to break the continuity of the period for which the shareholder held the shares (former subsection 160APHO(3) of the ITAA 1936).

140. A Holder will be taken to have materially diminished risks of loss or opportunities for gain on a particular day in respect of their MCN3 if their 'net position' (as defined in former subsection 160APHJ(5) of the ITAA 1936) on that day in respect of their MCN3 has less than 30% of those risks and opportunities (former subsection 160APHM(2) of the ITAA 1936).

141. A Holder's 'net position' is worked out based on all 'positions' in respect of their MCN3 and using the financial concept known as 'delta' (former section 160APHJ of the ITAA 1936).

142. Former subsection 160APHJ(4) of the ITAA 1936 provides:

To avoid doubt, shares...are to be treated as a long position (with a delta of +1) in relation to themselves.

143. It is relevant to consider the effect, if any, that the Resale and Exchange mechanisms of the MCN3 may have on a Holder's risks of loss or opportunities for gain in respect of their MCN3.

144. Embedded share options, such as the Resale and Exchange mechanisms, are separate positions in relation to a share if the options are exercisable by or against a party other than the issuer of the shares (paragraph 1 of Taxation Determination TD 2007/29 *Income tax: holding period rule: is an embedded share option a position in relation to the share if it is exercisable by or against a party other than the issuer of the share?*).

145. Under the Resale mechanism, MGL can (subject to certain conditions) require the Holders to sell all or some of their MCN3 to one or more Nominated Parties. Until selected by MGL and approved by APRA, a Nominated Party has no right or ability to call for the MCN3 from the Holders. MGL is not required to exercise the Resale mechanism and no MCN3 can, or will, be Resold at the option of a Holder. As the Resale mechanism is an option that is held by MGL and not by a third party, the Resale mechanism does not constitute a separate 'position' in relation to the MCN3 under former subsection 160APHJ(2) of the ITAA 1936 because, of itself, it will not affect a Holder's risks of loss or opportunities for gain in respect of the MCN3.

146. Similarly, the MCN3 cannot, and will not, be Exchanged at the option of a Holder. Except in the case of Scheduled Mandatory Exchange, Acquisition Event Exchange or Exchange on the occurrence of a Non-Viability Event (whereby, in each case, MGL must Exchange all or some of the MCN3 into Ordinary Shares), it is MGL, as the Issuer, that has the option to Exchange the MCN3 for Ordinary Shares. Consequently, the Exchange mechanism will not represent a separate position in relation to the MCN3 because, of itself, it will not affect a Holder's risks of loss or opportunities for gain in respect of the MCN3.

147. Accordingly, each of the Holders will be a 'qualified person' in relation to a Distribution under former paragraph 160APHO(1)(a) of the ITAA 1936 because:

- the Resale and Exchange mechanisms do not constitute separate positions in respect of the MCN3, and therefore will not, of themselves, affect the 'net position' of a Holder. Consequently, they will not affect a Holder's risks of loss or opportunities for gain in respect of their MCN3
- Holders will not take any position (apart from holding the MCN3) in relation to their MCN3 (see paragraph 3(e) of this Ruling), and
- Holders in receipt of Distributions on the MCN3 will hold their MCN3 for a continuous period of at least 90 days (excluding the day of acquisition and disposal, if applicable) beginning on the day after the day on which they acquired the MCN3 (see paragraph 3(d) of this Ruling).

Determination under paragraph 177EA(5)(b) of the ITAA 1936

148. Section 177EA of the ITAA 1936 is a general anti-avoidance provision that applies to a wide range of schemes designed to obtain imputation benefits.

149. Under subsection 177EA(3) of the ITAA 1936, section 177EA applies if the following conditions are satisfied:

- a) there is a scheme for a disposition of membership interests, or an interest in membership interests, in a corporate tax entity; and
- b) either:
 - (i) a frankable distribution has been paid, or is payable or expected to be payable, to a person in respect of the membership interests; or
 - (ii) a frankable distribution has flowed indirectly, or flows indirectly or is expected to flow indirectly, to a person in respect of the interest in membership interests, as the case may be; and
- c) the distribution was, or is expected to be, a franked distribution...; and
- d) except for [section 177EA], the person (the relevant taxpayer) would receive, or could reasonably be expected to receive, imputation benefits as a result of the distribution; and
- e) having regard to the relevant circumstances of the scheme, it would be concluded that the person, or one of the persons, who entered into or carried out the scheme or any part of the scheme did so for a purpose (whether or not the dominant purpose but not including an incidental purpose) of enabling the relevant taxpayer to obtain an imputation benefit.

150. Where section 177EA of the ITAA 1936 applies, subsection 177EA(5) allows the Commissioner to make a determination that:

- if the corporate tax entity is a party to the scheme, a franking debit arises in the entity's franking account in respect of each distribution made to the relevant taxpayer or that flows indirectly to the relevant taxpayer (paragraph 177EA(5)(a)), or
- no imputation benefit is to arise in respect of a distribution or a specified part of a distribution that is made, or that flows indirectly, to the relevant taxpayer (paragraph 177EA(5)(b)).

151. Pursuant to subsection 177EA(12) of the ITAA 1936, section 177EA applies to:

- a non-share equity interest in the same way as it applies to a membership interest

- an equity holder in the same way as it applies to a member, and
- a non-share dividend in the same way as it applies to a distribution.

152. The MCN3 will be non-share equity interests in MGL paying non-share dividends and MCN3 Holders will be equity holders.

153. The conditions in paragraphs 177EA(3)(a) to (d) of the ITAA 1936 are satisfied because:

- (a) The issue of the MCN3 constitutes a scheme for the disposition of membership interests (paragraph 177EA(3)(a)). Under paragraph 177EA(14)(a) of the ITAA 1936, a scheme for a disposition of membership interests or an interest in membership interests includes a scheme that involves issuing the membership interests.
- (b) Frankable distributions are expected to be payable to the Holders of the MCN3 in respect of their non-share equity interests (paragraph 177EA(3)(b)).
- (c) The Distributions on the MCN3 are expected to be franked (paragraph 177EA(3)(c)). The MGL TCG currently franks distributions on frankable non-share equity interests at 45%. MGL's franking policy is not expected to change as a result of the MCN3 issuance.
- (d) Except for section 177EA, the Holders of the MCN3 could reasonably be expected to receive imputation benefits as a result of the Distributions (paragraph 177EA(3)(d) of the ITAA 1936).

154. Accordingly, the issue is whether, 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 a relevant taxpayer (a Holder) to obtain an imputation benefit (paragraph 177EA(3)(e) of the ITAA 1936).

155. 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.

156. Having regard to all the relevant circumstances of the scheme and the qualifications set out in this Ruling, the Commissioner has concluded that the purpose of enabling the Holders to obtain imputation benefits is not more than incidental to the purpose of issuing the MCN3 to raise regulatory capital.

157. 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 benefits that are to be received by the Holders in respect of the Distributions paid on the MCN3.

Determination under paragraph 204-30(3)(c) of the ITAA 1997

158. Subdivision 204-D of the ITAA 1997 enables the Commissioner to make certain determinations where distributions with attached imputation benefits are streamed to a member of a corporate tax entity in preference to another member.

159. The term 'streams' is not defined for the purposes of Subdivision 204-D of the ITAA 1997, however, the Explanatory Memorandum to the New Business Tax System (Imputation) Bill 2002, which introduced subdivision 204-D into the ITAA 1997, explains that:

3.28 Streaming is selectively directing the flow of franked distributions to those members who can most benefit from imputation credits.

...

3.32 In the simplest case of streaming, the members who can benefit from imputation credits receive a franked distribution, while members who cannot benefit to the same degree (e.g. non-residents) or who receive no benefit (e.g. tax-exempt organisations) simultaneously receive an unfranked distribution (normally adjusted in amount for the lack of franking).

160. Section 204-30 of the ITAA 1997 prescribes the circumstances that must exist before the Commissioner may make such a determination. Section 204-30 applies where an entity streams distributions (or distributions and the giving of other benefits) to its members, whether in a single franking period or in a number of franking periods, 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 (favoured 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 (disadvantaged member) of the entity will receive lesser imputation benefits, or will not receive any imputation benefits, whether or not the disadvantaged member receives other benefits (paragraph 204-30(1)(c)).

161. If section 204-30 of the ITAA 1997 applies, the Commissioner has a discretion under subsection 204-30(3) to make a written determination that no imputation benefit is to arise in respect of a distribution made to a favoured member and specified in the determination (paragraph 204-30(3)(c)).

162. An MCN3 Holder will receive an imputation benefit as a result of a Distribution where, for example, the Holder is entitled to a tax offset under Division 207 of the ITAA 1997 (paragraph 204-30(6)(a) of the ITAA 1997).

163. For section 204-30 of the ITAA 1997 to apply, a member to whom distributions are streamed must derive a greater benefit from franking credits than another member of the entity. The words 'derive a greater benefit from franking credits' are defined in subsection 204-30(8) of the ITAA 1997 by reference to the ability of the members to fully utilise imputation benefits.

164. A member of an entity derives a 'greater benefit from franking credits' than another member of the entity if, for example, the other member is a foreign resident (paragraph 204-30(8)(a) of the ITAA 1997) or the other member would not be entitled to a tax offset under Division 207 of the ITAA (paragraph 204-30(8)(b)). Broadly, an individual or corporate tax entity that receives a franked distribution is not entitled to a tax offset unless they are an Australian resident at the time the distribution is made (Subdivision 207-C). Accordingly, the MCN3 Holders receiving the imputation benefits would derive a greater benefit from franking credits than other members of MGL if those other members are foreign residents.

165. Based on the information provided, the Commissioner has concluded that the requisite element of streaming does not exist in relation to the franked Distributions to be paid by MGL to Holders.

166. Accordingly, 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 benefits that are to be received by the Holders in respect of the Distributions paid on the MCN3.

Dividend stripping operation

167. Section 207-155 provides that a distribution will be taken to be made as part of a dividend stripping operation if, and only if, the making of the distribution arose out of or was made in the course of, a scheme that was in the nature of dividend stripping or had substantially the same effect of a dividend stripping scheme.

168. Based on the MCN3 Terms and Prospectus, there is no indication that the offering of the MCN3 and the associated payment of franked Distributions to the Holders constitute a dividend stripping arrangement.

Integrity provisions relevant to Exchange or Redemption

169. The effect of subsection 43B(1) of the ITAA 1936 is that sections 45, 45A and 45B of the ITAA 1936 apply to non-share equity interests, equity holders and non-share dividends in the same way as they apply to shares, shareholders and dividends, respectively.

170. As stated previously, the MCN3 are non-share equity interests and each of the Holders is an equity holder as defined in subsection 995-1(1) of the ITAA 1997. In addition, the Distributions paid in respect of the MCN3 will be non-share dividends as defined in section 974-120 of the ITAA 1997.

Section 45 of the ITAA 1936

171. Section 45 of the ITAA 1936 applies where a company streams the provision of shares and the payment of minimally franked dividends to its shareholders in such a way that:

- the shares are received by some (but not all) shareholders, and
- some or all of the shareholders who do not receive the shares receive or will receive minimally franked dividends.

172. Minimally franked dividends are dividends that are not franked, or franked to less than 10% (subsection 45(3) of the ITAA 1936).

173. If section 45 of the ITAA 1936 applies, the value of the share at the time the shareholder is provided with the share is taken to be an unfrankable dividend that is paid by the company out of its profits to the shareholder (subsection 45(2) of the ITAA 1936).

174. Distributions paid on the MCN3 are expected to be franked at the same percentage that applies to MGL's Ordinary Shares. As MGL's franking policy is not expected to change as a result of the MCN3 issuance, minimally franked dividends will not be received by any MGL shareholders.

175. Further, the issue of Ordinary Shares upon Exchange of the MCN3 merely reflects a change in the type of equity interest the Holders will hold in MGL – it does not reflect the satisfaction of any distribution due to Holders.

176. Based on the information provided and having regard to the circumstances of the scheme, section 45 of the ITAA 1936 will not apply to treat the value of the Ordinary Shares issued to the Holders on Exchange of the MCN3 as an unfrankable dividend paid by MGL to the Holders.

Section 45A of the ITAA 1936

177. Section 45A of the ITAA 1936 applies where a company streams the provision of capital benefits to certain shareholders who derive a greater benefit from the capital benefits (the advantaged shareholders) than other shareholders, and it is reasonable to assume that the other shareholders (the disadvantaged shareholders) have received or will receive dividends.

178. Where section 45A of the ITAA 1936 applies, the Commissioner may make a determination that section 45C of the ITAA 1936 applies in relation to the whole, or a part, of the capital benefits (subsection 45A(2)). The effect of such a determination is that the capital benefit, or part of the capital benefit, is taken to be an unfranked dividend paid by the company to the shareholder at the time the capital benefit is provided (subsection 45C(1)).

179. The provision of a capital benefit includes the provision to the shareholder of shares in the company (paragraph 45A(3)(a) of the ITAA 1936). The issue of the Ordinary Shares to the Holders on Exchange of the MCN3 will therefore constitute the provision of a capital benefit.

180. However, the issue of the Ordinary Shares on Exchange of the MCN3 is a restatement of a Holder's interest in the capital of MGL. Therefore, in the absence of any other factors, and based on the circumstances of the scheme, the issue of Ordinary Shares on Exchange will not be considered a streaming of capital benefits.

181. The provision of a capital benefit also includes the distribution to the shareholder of share capital or share premium (paragraph 45A(3)(b) of the ITAA 1936). Relevantly, a non-share distribution to an equity holder is taken to be a distribution to the equity holder of share capital to the extent to which it is a non-share capital return (subsection 45A(3A)). A non-share capital return is defined in section 974-125 of the ITAA 1997 as a non-share distribution to the extent to which it is not a non-share dividend. As MGL will debit the Issue Price of the MCN3 to its non-share capital account on Redemption of the MCN3, an Optional Redemption will involve a non-share capital return (sections 974-120 and 974-125). Accordingly, an Optional Redemption will also involve the provision of capital benefits.

182. On Optional Redemption, the amount paid to the Holders is limited to the amount of the Issue Price of the MCN3 being Redeemed and is not paid to Holders to satisfy a Holder's Distribution entitlements. Absent other relevant factors, it cannot be said that Holders would derive a greater benefit from capital benefits than other MGL shareholders.

183. Accordingly, the Commissioner will not make a determination under subsection 45A(2) of the ITAA 1936 that section 45C of the ITAA 1936 applies to treat the whole, or any part, of the capital benefit provided to the Holders on the Exchange or Redemption of the MCN3 as an unfranked dividend paid by MGL to the Holders.

Section 45B of the ITAA 1936

184. Pursuant to subsection 45B(2) of the ITAA 1936, section 45B of the ITAA 1936 applies if:

- (a) there is a scheme under which a person is provided with... a capital benefit by a company; and
- (b) under the scheme, a taxpayer (the relevant taxpayer), who may or may not be the person provided with... the capital benefit, obtains a tax benefit; 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 (whether or not the dominant purpose but not including an incidental purpose) of enabling a taxpayer (the relevant taxpayer) to obtain a tax benefit.

185. Where section 45B of the ITAA 1936 applies, the Commissioner may make a determination under paragraph 45B(3)(b) that section 45C of the ITAA 1936 applies to the whole or a part of the capital benefit. Such a determination would have the effect of treating all or a part of the amount of the capital benefit as an unfranked dividend paid by the company to the shareholder at the time the capital benefit is provided (subsection 45C(1)).

186. Subsection 45B(10) of the ITAA 1936 provides that the term 'scheme' in section 45B has the same meaning as provided in subsection 995-1(1) of the ITAA 1997. That definition is wide and includes any arrangement, scheme, plan, proposal, action, course of action or course of conduct, whether unilateral or otherwise.

187. The arrangement involving the issue of the MCN3 according to the MCN3 Terms, including the issue of Ordinary Shares to the Holders on Exchange of the MCN3, will constitute a scheme under which the Holders are provided with a capital benefit by MGL (paragraph 45B(5)(a) of the ITAA 1936).

188. Similarly, an Optional Redemption under the MCN3 Terms will also constitute a scheme under which the Holders are provided with a capital benefit by MGL (paragraph 45B(5)(b) of the ITAA 1936 by virtue of subsection 45B(7)).

189. In both situations, paragraph 45B(2)(a) of the ITAA 1936 is satisfied.

190. A relevant taxpayer obtains a tax benefit under the scheme if an amount of tax payable (or any other amount payable under the ITAA 1997 or ITAA 1936) by the relevant taxpayer would, apart from the operation of section 45B of the ITAA 1936, be less than the amount that would have been payable, or would be payable at a later time than it would have been payable, if the capital benefit had been an assessable dividend (subsection 45B(9) of the ITAA 1936).

191. The relevant taxpayers are the Holders (who, in this case, are also the persons provided with the capital benefit). The issue of the Ordinary Shares to the Holders on Exchange of the MCN3 will not lead to the Holders deriving assessable income or making a capital gain.

192. An Optional Redemption will generally not lead to the Holders deriving assessable income. In addition, the Holders will only receive the Issue Price of each MCN3 being Redeemed, meaning that the Holders will not make a capital gain (having paid the Issue Price on initial application under the Prospectus).

193. Therefore, in both situations, the Holders will generally obtain a tax benefit from the scheme and paragraph 45B(2)(b) of the ITAA 1936 is satisfied.

194. Whether section 45B of the ITAA 1936 will apply to an Exchange or Redemption turns on whether paragraph 45B(2)(c) will be satisfied. This involves a consideration of the relevant circumstances, including, but not limited to, those listed in subsection 45B(8).

195. Having regard to the relevant circumstances of the scheme, and on the basis of the information surrounding the issue of the MCN3, it could not be concluded that the Exchange or Redemption of the MCN3 will be entered into or carried out for a more than incidental purpose of enabling the Holders to obtain a tax benefit.

196. Accordingly, 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 treat the whole, or any part, of the capital benefit provided to the Holders on the Exchange or Redemption of the MCN3 as an unfranked dividend paid by MGL to the Holders.

Acquisition of Ordinary Shares on Exchange not included in assessable income

197. The issue of Ordinary Shares to the Holders of the MCN3 on Exchange is a distribution of property to holders of a non-share equity interest. This means that it is a 'non-share distribution' under section 974-115 of the ITAA 1997. Subsection 974-120(1) of the ITAA 1997 states that, subject to 974-120(2), all non-share distributions are non-share dividends.

198. Subsection 974-120(2) of the ITAA 1997 provides that a non-share distribution is not a non-share dividend to the extent to which the company debits the distribution against the company's non-share capital account or share capital account.

199. On Exchange of the MCN3, MGL will debit the Issue Price of the MCN3 to its non-share capital account. Accordingly, the issue of Ordinary Shares to the Holders of the MCN3 on Exchange is not a non-share dividend, and will not be included in the assessable income of the Holders under subparagraph 44(1)(a)(ii) of the ITAA 1936.

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200. Furthermore, the Ordinary Shares will not be issued to the Holders of the MCN3 as shareholders of MGL. Therefore, the issue of the Ordinary Shares would not satisfy paragraphs (a) or (b) of the definition of 'dividend' in subsection 6(1) of the ITAA 1936. This means that the value of the Ordinary Shares will not be included in the assessable income of the Holders under subparagraph 44(1)(a)(i) of the ITAA 1936.

MCN3 are not traditional securities

201. Subsection 26BB(1) of the ITAA 1936 defines a 'traditional security' to be a 'security' held by the taxpayer that, relevantly:

- is not trading stock of the taxpayer, and
- either does not have an eligible return or has an eligible return that satisfies the conditions in subparagraph 26BB(1)(b)(ii) of the ITAA 1936.

202. The term 'security' is defined in subsection 26BB(1) of the ITAA 1936 by reference to its meaning in Division 16E of the ITAA 1936. Pursuant to subsection 159GP(1), 'security' means:

- (a) stock, a bond, debenture, certificate of entitlement, bill of exchange, promissory note or other security;
- (b) a deposit with a bank or other financial institution;
- (c) a secured or unsecured loan; or
- (d) any other contract, whether or not in writing, under which a person is liable to pay an amount or amounts, whether or not the liability is secured.

203. The MCN3 are not stock, a bond, debenture, certificate of entitlement, bill of exchange, or promissory note.

204. The term 'or other security' in paragraph (a) of the definition of 'security' in section 159GP(1)(a) of the ITAA 1936 encompasses instruments that evidence an obligation on the part of the issuer or drawer to pay an amount to the holder or acceptor, whether during the term of the instrument or at its maturity. The types of securities referred to in paragraph (a) will generally be recognised as debt instruments (Taxation Ruling TR 96/14 *Income Tax: traditional securities*).

205. Accordingly, the MCN3 will not meet the definition of 'security' paragraph (a) of the definition of 'security' in section 159GP(1) of the ITAA 1936.

206. The MCN3 are not deposits with MGL, nor are they a loan. As such, they will not be securities under paragraphs (b) or (c) of the definition of 'security' in section 159GP(1) of the ITAA 1936.

207. Paragraph (d) of the definition of 'security' in section 159GP(1) of the ITAA 1936 applies to those contracts that have debt like obligations (TR 96/14).

208. The MCN3 Terms do not evidence a liability by MGL to pay an amount or amounts to the Holders of the MCN3 during the term of the instrument or at maturity.

209. The MCN3 are perpetual and the Holders do not have a right to require Exchange, Resale or Redemption.

210. The payment by MGL of Distributions is discretionary and non-cumulative. If a Distribution is not paid, MGL has no liability to pay the Distribution, Holders have no claim in respect of non-payment, and such non-payment does not constitute an event of default.

211. Furthermore, the Terms provide for the Exchange of the MCN3 in return for MGL allotting and issuing the Exchange Number of Ordinary Shares based on the Issue Price of the MCN3 and a formula set out in the Terms. Redemption of the MCN3 is also possible at the option of MGL and requires the prior written approval of APRA. This does not establish a liability on MGL to pay an amount to the Holders.

212. MGL is not expected to become liable to pay an amount in respect of the MCN3 upon winding up as it would be expected that, before winding up commences, the MCN3 would either be Exchanged into Ordinary Shares pursuant to a Non-Viability Event, or the Holders' rights would be terminated (as a result of Write-Off) if MGL is not able to allot and issue Ordinary Shares within the time stated in the Terms.

213. Accordingly, the Terms do not establish any liability to pay for MGL that exhibits the debt like obligation contemplated by paragraph (d) of the definition of 'security'.

214. As the MCN3 are not securities within the meaning of subsection 159GP(1) of the ITAA 1936, they cannot be traditional securities under subsection 26BB(1) of the ITAA 1936

215. Accordingly, a gain on the disposal or Redemption of the MCN3 will not give rise to assessable income under subsection 26BB(2) of the ITAA 1936 and a loss on the disposal or Redemption of the MCN3 will not give rise to an allowable deduction under subsection 70B(2) of the ITAA 1936.

MCN3 are not qualifying securities

216. Under Division 16E of Part III of the ITAA 1936, the income and deductions from a 'qualifying security' are spread over the term of the security on an accruals basis which reflects the economic gains and losses which have accrued at any point in time (section 159GQ of the ITAA 1936).

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217. A 'qualifying security' is defined in subsection 159GP(1) of the ITAA 1936 and must, among other things, be a 'security'. As each MCN3 is not a 'security' under subsection 159GP(1), each MCN3 is not a 'qualifying security' for the purposes of Division 16E of the ITAA 1936.

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