


CR 2018/29 - Income tax: Tox Free Solutions Limited - Scheme of Arrangement and Special Dividend

 This cover sheet is provided for information only. It does not form part of *CR 2018/29 - Income tax: Tox Free Solutions Limited - Scheme of Arrangement and Special Dividend*



Class Ruling

Income tax: Tox Free Solutions Limited – Scheme of Arrangement and Special Dividend

Contents	Para
LEGALLY BINDING SECTION:	
Summary – what this Ruling is about	1
Date of effect	9
Scheme	10
Ruling	29
NOT LEGALLY BINDING SECTION:	
Appendix 1:	
Explanation	49
Appendix 2:	
Detailed contents list	126

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.

Summary – what this Ruling is about

1. This Ruling sets out the Commissioner's opinion on the way in which the relevant provisions identified below apply to the defined class of entities, who take part in the scheme to which this Ruling relates.

Relevant provisions

2. The relevant provisions dealt with in this Ruling are:
- subsection 6(1) of the *Income Tax Assessment Act 1936* (ITAA 1936)
 - subsection 44(1) of the ITAA 1936
 - subparagraph 44(1)(a)(i) of the ITAA 1936
 - subparagraph 128B(3)(ga)(i) of the ITAA 1936
 - section 128D of the ITAA 1936
 - former section 160APHM of the ITAA 1936
 - former section 160APHN of the ITAA 1936
 - section 177E of the ITAA 1936

- paragraph 177EA(5)(b) of the ITAA 1936
- Division 67 of the *Income Tax Assessment Act 1997* (ITAA 1997)
- section 67-25 of the ITAA 1997
- subsection 104-10(1) of the ITAA 1997
- subsection 104-10(2) of the ITAA 1997
- subsection 104-10(4) of the ITAA 1997
- Division 115 of the ITAA 1997
- subsection 116-20(1) of the ITAA 1997
- paragraph 204-30(3)(c) of the ITAA 1997
- Division 207 of the ITAA 1997
- section 207-20 of the ITAA 1997
- subsection 207-35(1) of the ITAA 1997
- section 207-75 of the ITAA 1997
- paragraph 207-145(1)(a) of the ITAA 1997
- paragraph 207-145(1)(d) of the ITAA 1997
- section 855-10 of the ITAA 1997.

All subsequent legislative references in this Ruling are to provisions of the ITAA 1997 unless specified otherwise.

Class of entities

3. The class of entities to which this Ruling applies are the shareholders of Tox Free Solutions Limited (Toxfree) who:

- participated in the scheme of arrangement as described in paragraphs 10 to 28 of this Ruling under which Cleanaway Waste Management Limited (Cleanaway) acquired 100% of the shares in Toxfree (the Scheme of Arrangement)
- held their shares in Toxfree on capital account, that is, the shares were neither held as revenue assets (as defined in section 977-50) nor as trading stock (as defined in subsection 995-1(1))
- are residents or non-residents of Australia (other than non-residents who carry on a business at or through a permanent establishment in Australia) as defined in subsection 6(1) of the ITAA 1936, and
- are not subject to the taxation of financial arrangements rules in Division 230 in relation to gains and losses on their shares.

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

4. In this Ruling, an entity belonging to this class of entities is referred to as a 'Toxfree Shareholder'.

Qualifications

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

6. This Ruling does not consider the taxation consequences in relation to Toxfree shares acquired pursuant to employee incentive plans.

7. 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 10 to 28 of this Ruling.

8. 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

9. This Ruling applies from 1 July 2017 to 30 June 2018. The Ruling continues to apply after 30 June 2018 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 *Public Rulings*).

Scheme

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

- the Scheme Implementation Deed (SID) dated 11 December 2017
- the Scheme Booklet dated 02 March 2018, and

- the Scheme of Arrangement 02 March 2018.

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

Relevant Entities

Toxfree

11. Toxfree is an Australian resident entity company that has been listed on the Australian Securities Exchange (ASX) since 29 September 2000.
12. The Toxfree Group's principal activities are the provision of industrial services and waste management.
13. On 10 May 2018, Toxfree had 195,719,182 ordinary shares on issue.
14. As at 31 January 2018, approximately 99.18% of Toxfree ordinary shares were held by Australian resident entities and approximately 0.82% held by non-resident entities.

Cleanaway

15. Cleanaway is an Australian resident entity company that has been listed on the ASX since 3 May 2005.
16. Cleanaway is a recycling, waste management and industrial services company.
17. Cleanaway (No. 1) Pty Ltd (Cleanaway No. 1) is a wholly owned subsidiary of Cleanaway and was incorporated in Australia for the sole purpose of acquiring 100% of Toxfree.
18. Prior to the Implementation Date of 25 May 2018, neither Cleanaway nor Cleanaway No. 1 held any Toxfree shares directly or indirectly.

Scheme of Arrangement

19. On 11 December 2017, Toxfree announced that it had entered into a SID with Cleanaway, under which a wholly owned subsidiary of Cleanaway (later identified as Cleanaway No. 1) would acquire 100% of the issued capital of Toxfree by way of a Scheme of Arrangement under Part 5.1 of the *Corporations Act 2001* (Corporations Act).
20. The Scheme Resolution was approved by the requisite majority of Toxfree Shareholders at the Scheme Meeting held on 3 May 2018.

21. The Scheme of Arrangement was approved by the Federal Court of Australia at the hearing held on 10 May 2018. The Scheme of Arrangement became effective on 11 May 2018 when Toxfree lodged the court order with the Australian Securities and Investment Commission. Toxfree shares were suspended from trading at the close of trading on 11 May 2018.

22. On the Scheme Record Date of 18 May 2018, a Toxfree Shareholder was entitled to participate in the Scheme of Arrangement.

23. On the Scheme Implementation Date of 25 May 2018, Toxfree shareholders disposed of each share they held in Toxfree to Cleanaway No.1.

24. Toxfree Shareholders received a total cash payment of \$3.425 per share comprising:

- the Scheme Consideration of \$2.845 which was paid on 25 May 2018 (Implementation Date), and
- a fully franked Special Dividend of \$0.58 which was paid on 23 May 2018.

Special Dividend

25. On 2 March 2018, the Board of Directors of Toxfree declared a fully franked Special Dividend of \$0.58 per Toxfree share to Toxfree Shareholders for every share that they held on the Special Dividend Record Date of 16 May 2018. The Special Dividend was paid on 23 May 2018.

26. The declaration of the Special Dividend was conditional on the Scheme of Arrangement becoming effective and was payable at the discretion of the Toxfree Board. Neither Cleanaway nor Cleanaway No.1 influenced the decision of the Toxfree Board to declare the Special Dividend.

27. The Special Dividend was paid entirely from Toxfree's cash reserves and existing debt facilities. It was not debited against Toxfree's share capital account. Neither Cleanaway nor Cleanaway No. 1 financed or facilitated financing for the payment of the Special Dividend.

28. The Special Dividend complied with the requirements of the Corporations Act, including section 254T of that Act.

Ruling

Special Dividend

29. The Special Dividend paid to Toxfree shareholders is a 'dividend' as defined in subsection 6(1) of the ITAA 1936.

Assessability of the Special Dividend and withholding tax

Residents

30. A resident Toxfree Shareholder includes the Special Dividend in their assessable income (subparagraph 44(1)(a)(i) of the ITAA 1936).

Non-residents not carrying on business at or through a permanent establishment

31. A non-resident Toxfree Shareholder (other than those carrying on business in Australia at or through a permanent establishment in Australia) does not include the Special Dividend in their assessable income under subparagraph 44(1)(b)(i) of the ITAA 1936 (section 128D of the ITAA 1936) and will not be liable for withholding tax (subparagraph 128B(3)(ga)(i) of the ITAA 1936).

Gross-up and tax offset

32. The Special Dividend is a frankable distribution under section 202-40.

33. A Toxfree Shareholder, who received the Special Dividend directly and satisfies the residency requirements in section 207-75:

- includes the amount of the franking credit attached to the Special Dividend in their assessable income, and
- is entitled to a tax offset equal to the franking credit

in the income year it is paid (section 207-20), subject to being a 'qualified person' in relation to the Special Dividend.

34. A Toxfree Shareholder (not being a corporate tax entity), who received the Special Dividend as a trustee of a trust (not being a complying superannuation entity) or as a partnership, includes an amount equal to the franking credit attached to the Special Dividend in its assessable income under subsection 207-35(1), subject to the trustee or the partnership being a 'qualified person'.

Qualified persons

35. The payment of the Special Dividend constitutes a 'related payment' for the purposes of former section 160APHN of the ITAA 1936 (paragraph 207-145(1)(a)).

36. A Toxfree shareholder will be a qualified person in relation to the Special Dividend, if from 2 April 2018 to 17 May 2018 (inclusive), they continued to hold their Toxfree shares and did not have 'materially diminished risks of loss or opportunities for gain' (as defined under former section 160APHM of the ITAA 1936) in respect of their Toxfree shares for a continuous period of at least 45 days.

Refundable tax offset

37. The franking credit tax offset a Toxfree Shareholder is entitled to under Division 207 in relation to the Special Dividend is subject to the refundable tax offset rules in Division 67, provided the Toxfree Shareholder is not excluded by the operation of section 67-25.

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

38. CGT event A1 happened on 25 May 2018 (Scheme Implementation Date) when a Toxfree Shareholder disposed of each of their Toxfree shares to Cleanaway No.1 in accordance with the Scheme of Arrangement (subsections 104-10(1) and 104-10(2)).

Capital proceeds

39. The Scheme Consideration of \$2.845 for each Toxfree share is the capital proceeds from CGT event A1 happening to the share (subsection 116-20(1)).

40. The Special Dividend of \$0.58 is not included in the capital proceeds.

Capital gain or capital loss

41. A Toxfree Shareholder will make a capital gain if the capital proceeds from the disposal of a Toxfree share exceed its cost base (subsection 104-10(4)). The capital gain is the amount of the excess.

42. A Toxfree Shareholder will make a capital loss if the capital proceeds are less than the reduced cost base of the Toxfree share (subsection 104-10(4)). The capital loss is the amount of the difference.

Discount capital gain

43. If a Toxfree Shareholder makes a capital gain from the disposal of a Toxfree share they will be eligible to treat the capital gain as a 'discount capital gain' provided they satisfy the requirements of Division 115.

Non-resident shareholders

44. A non-resident Toxfree Shareholder who participated in the Scheme of Arrangement may disregard any capital gain or capital loss made when CGT event A1 happened if the Toxfree share was not 'taxable Australian property' (section 855-10). A Toxfree share does not constitute 'taxable Australian property'.

The anti-avoidance provisions

45. The Scheme of Arrangement is not a scheme, or a scheme having substantially the effect of a scheme, by way of, or in the nature of dividend stripping within the meaning of section 177E of the ITAA 1936.

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

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

48. The Special Dividend was not made as part of a dividend stripping operation for the purposes of paragraph 207-145(1)(d).

Commissioner of Taxation

20 June 2018

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.*

Special Dividend

49. The term 'dividend' is defined in subsection 6(1) of the ITAA 1936 to include 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' excludes a distribution that is debited against an amount standing to the credit of the share capital account of the company.

50. The payment of the Special Dividend is a distribution of money made by Toxfree to its shareholders. Toxfree did not debit the Special Dividend against its share capital account.

51. Therefore, the exclusion in paragraph (d) does not apply and the Special Dividend constitutes a 'dividend' for the purposes of subsection 6(1) of the ITAA 1936.

Assessability and withholding tax

Residents

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

53. As the Special Dividend is paid to Toxfree Shareholders out of profits derived by Toxfree, the assessable income of Toxfree Shareholders who are residents of Australia includes the Special Dividend (paragraph 44(1)(a) of the ITAA 1936).

Non-residents not carrying on business at or through a permanent establishment

54. The assessable income of a non-resident shareholder in a company includes dividends paid to the shareholder by the company to the extent to which they are paid out of profits derived by it from sources in Australia (subparagraph 44(1)(b)(i) of the ITAA 1936).

55. Dividends paid by a resident company to a non-resident are generally subject to withholding tax (section 128B of the ITAA 1936). However, no withholding tax will be imposed to the extent the dividend is franked (subparagraph 128B(3)(ga)(i) of the ITAA 1936).

56. As the Special Dividend is fully franked, it will not be subject to withholding tax when derived by non-resident Toxfree Shareholders.

57. In addition, income upon which withholding tax would, but for paragraph 128B(3)(ga) of the ITAA 1936 be payable, is not assessable income and is not exempt income of a person (section 128D of the ITAA 1936).

58. As the payment of the Special Dividend is income upon which withholding tax would be payable but for paragraph 128B(3)(ga) of the ITAA 1936, the assessable income of non-resident Toxfree Shareholders (other than those carrying on business in Australia at or through a permanent establishment in Australia) will not include the Special Dividend.

Gross-up and tax offset

59. A distribution is a frankable distribution to the extent it is not unfrankable (section 202-40). Section 202-45 sets out the circumstances under which an amount or distribution is taken to be unfrankable.

60. None of the circumstances in section 202-45 apply to the Special Dividend. Accordingly, the Special Dividend is a frankable distribution under section 202-40.

61. Where a shareholder receives a franked distribution directly, satisfies the residency requirement in section 207-75 and is a 'qualified person' in relation to the franked distribution, the assessable income of the shareholder includes the amount of the franking credit (subsection 207-20(1)). The shareholder will also be entitled to a tax offset equal to the franking credit on the distribution (subsection 207-20(2)).

62. Therefore, subject to satisfying the 'qualified person' rule, the assessable income of a Toxfree Shareholder who receives the Special Dividend directly includes the amount of the franking credit attached to the Special Dividend and will be entitled to a tax offset equal to the amount of the franking credit in the income year in which the Scheme of Arrangement happened.

63. Subject to satisfying the 'qualified person' rule, the assessable income of a Toxfree Shareholder (not being an entity taxed as a corporate tax entity) that is a trustee of a trust (not being a complying superannuation fund) or a partnership, includes the amount of the franking credit attached to the Special Dividend (subsection 207-35(1)).

Qualified persons, related payment and holding period rule

Qualified person

64. If a franked distribution is made to an entity that is not a 'qualified person' in relation to a franked distribution, the franking credit on the distribution is not included in assessable income of the entity. The entity is also not entitled to a franking credit because of the distribution (subsection 207-145(1)).

65. The test of what constitutes a 'qualified person' is provided in former subsection 160APHO(1) of the ITAA 1936. Broadly, if a Toxfree Shareholder is not under an obligation to make a related payment in relation to the Special Dividend, they will have to satisfy the holding period requirement within the primary qualification period. If a Toxfree Shareholder is under an obligation to make a related payment in relation to the Special Dividend, they will have to satisfy the holding period requirement within the secondary qualification period.

Related payment rule

66. In order to determine the relevant qualification period, it is necessary to determine whether, under the Scheme of Arrangement, a Toxfree Shareholder has made, or is under an obligation to make, or is likely to make, a related payment in respect of the Special Dividend they receive (former subsection 160APHN(2) of the ITAA 1936).

67. Examples of what constitutes the making of a related payment for the purposes of Division 1A of former Part IIIA of the ITAA 1936 is provided in former section 160APHN of the ITAA 1936. Broadly, a related payment is where a Toxfree Shareholder has done, or is obliged to do, anything having the effect of passing the benefit of the Special Dividend to one or more other persons.

68. Former subsection 160APHN(3) of the ITAA 1936 lists examples of what may have the effect of passing the benefit of the Special Dividend to one or more other persons, for example, causing an amount or amounts to be set off against, or to be otherwise applied in reduction of, a debt or debts owed by the other person or other persons (former paragraph 160APHN(3)(f) of the ITAA 1936).

69. Former subsection 160APHN(4) of the ITAA 1936 lists the circumstances of making a related payment referred in former paragraph 160APHN(3)(f) of the ITAA 1936 being broadly that the amount of the benefit passed on reflects the amount of the Special Dividend.

70. Under the terms of the SID, the Scheme Consideration is reduced by the amount of the Special Dividend paid by Toxfree to Toxfree Shareholders. It is considered that the payment of the Special Dividend is an integral part of the Scheme of Arrangement.

71. The reduction of the Scheme Consideration has the effect of passing the benefit of the dividends from a Toxfree Shareholder to Cleanaway. Therefore, a Toxfree shareholder, or a partner in a partnership or a beneficiary of a trust that has an interest in Toxfree shares, is taken to have made a related payment in respect of the Special Dividend.

Holding period requirement

72. The holding period rule requires shareholders to hold their ordinary shares at-risk for a continuous period of not less than 45 days during the relevant qualification period (former paragraph 160APHO(2)(a) of the ITAA 1936).

73. As Toxfree Shareholders are taken, for the purposes of Division 1A of former Part IIIAA of the ITAA 1936 to have made a related payment in respect of the Special Dividend, the relevant qualification period is the secondary qualification period pursuant to former paragraph 160APHO(1)(b) of the ITAA 1936.

74. Former section 160APHD of the ITAA 1936 defines the 'secondary qualification period' as follows:

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

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

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

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

76. The eligibility for the Special Dividend was determined on the Special Dividend Record Date of 16 May 2018, being the last day on which acquisition by a person of a Toxfree share entitled the person to receive the Special Dividend as per former section 160APHE of the ITAA 1936. Accordingly, the ex-dividend date of a Toxfree share for the purposes of former subsection 160APHE(1) of the ITAA 1936 is 17 May 2018.

77. The secondary qualification period runs from 45 days before and ends on 45 days after the ex-dividend date of 17 May 2018. In practical terms, this means that the secondary qualification period runs from 2 April 2018 to 1 July 2018. However, pursuant to former subsection 160APHO(3) of the ITAA 1936, any days on which a Toxfree Shareholder has materially diminished risks of loss or opportunities for gain in respect of the Toxfree share is to be excluded. This means that the secondary qualification period runs from 2 April 2018 until the date that the Toxfree Shareholders are no longer holding their shares at risk for the purposes of Division 1A of former Part IIIAA of the ITAA 1936.

78. Entitlement to participate in the Scheme will be determined on the Scheme Record Date (18 May 2018). Toxfree Shareholders who dispose of their shares under the SID will no longer be considered to hold their Toxfree shares at risk for the purposes of Division 1A of former Part IIIAA of the ITAA 1936 as of 18 May 2018.

79. Accordingly, for a Toxfree Shareholder who disposes of their shares under the SID, the secondary qualification period will run for a period of 2 April 2018 to 17 May 2018 (being the day prior to the Scheme Record Date). A Toxfree Shareholder who receives the Special Dividend will need to hold its shares at risk for a continuous period of not less than 45 days during this period in order to be a qualified person for the purposes of Division 1A of former Part IIIAA of the ITAA 1936. Further, pursuant to former paragraph 160APHO(2)(a) of the ITAA 1936, neither the date of acquisition nor the date of disposal is included in the relevant 45 day period.

80. The small shareholder exception in former section 160APHT of the ITAA 1936 does not apply as the Special Dividend constitutes a related payment as discussed at paragraph 66-71 of this Ruling. Therefore, a Toxfree Shareholder who is an individual and who has franking credit offsets not exceeding \$5,000 for the year of income ended 30 June 2018 must also satisfy the holding period requirement in relation to the Special Dividend (former section 160APHT(2) of the ITAA 1936).

Refundable tax offset

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

82. Pursuant to section 67-25, certain taxpayers are specifically excluded from the operation of the refundable tax offset rules. The identified entities include:

- non-complying superannuation funds or non-complying approved deposit funds (subsection 67-25(1A))
- a trustee of a trust who is liable to be assessed under section 98 or 99A of the ITAA 1936 (paragraph 67-25(1B)(b))
- corporate tax entities, unless the entity is an exempt institution that is eligible for a refund, or a life insurance company that has received distributions on membership interests which were not held by the company on behalf of its shareholders (subsections 67-25(1C) and 67-25(1D)), and
- foreign resident entities carrying on business in Australia at or through a permanent establishment (subsection 67-25(1DA)).

83. Division 63 sets out the rules on how, and in what order, tax offsets are applied against income tax liability. Where a tax offset that is subject to the refundable tax offset rules in Division 67 exceeds the income tax liability, a Toxfree Shareholder can get a refund of the remaining amount (item 40 of section 63-10).

CGT Consequences

CGT event A1

84. CGT event A1 happens if there is a change in the ownership of an asset (section 104-10). The event happens when a contract to dispose of the asset is entered into or, if there is no contract, when the change of ownership occurs (subsection 104-10(3)).

85. The acquisition of shares under a court approved scheme of arrangement does not involve a disposal of shares under a contract.¹

86. Therefore, CGT event A1 happened when there was a change of ownership in a Toxfree share from a Toxfree Shareholder to Cleanaway No.1 pursuant to the SID (subsections 104-10(1) and 104-10(2)). The change of ownership occurred on the Scheme Implementation Date of 25 May 2018 (paragraph 104-10(3)(b)).

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

88. A Toxfree Shareholder makes a capital gain from CGT event A1 happening if the capital proceeds from the disposal of a Toxfree share is more than the cost base of the Toxfree share. A Toxfree Shareholder makes a capital loss if the capital proceeds are less than the reduced cost base of the Toxfree share (subsection 104-10(4)).

Capital proceeds

89. The capital proceeds received by a Toxfree Shareholder from a CGT event is the money and the market value of any property received or entitled to be received (worked out at the time of the event happening) in respect of the event happening (subsection 116-20(1)).

¹ See paragraph 9 of the Taxation Determination TD 2002/4 *Income tax: capital gains: what is the first element of the cost base and reduced cost base of a share in a company you acquire in exchange for a share in another company in a takeover or merger?*

90. The term 'in respect of the event happening' in subsection 116-20(1) requires the relationship between the event and the receipt of the money, or the entitlement to receive the money, to be more than coincidental. An amount is not capital proceeds received or entitled to be received in respect of a CGT event merely because it is received in association with the CGT event.²

91. In this case, the Special Dividend was not paid in respect of the disposal of Toxfree shares under the Scheme. The determination to pay the Special Dividend was at the discretion of the Toxfree Board. Cleanaway had no control over Toxfree's decision to pay the Special Dividend. Cleanaway had no control over the quantum of the Special Dividend.

92. The payment of the Special Dividend was funded entirely from cash reserves and existing debt facilities with no actual or contingent funding support from Cleanaway.

93. The Commissioner considers that the Special Dividend was not received in respect of the disposal of Toxfree shares under the Scheme of Arrangement. Accordingly, the Special Dividend does not form part of the capital proceeds in respect of CGT event A1 happening.

94. Therefore, the capital proceeds that a Toxfree Shareholder received for the disposal of a Toxfree share is the Scheme Consideration of \$2.845.

Discount capital gain

95. If a Toxfree Shareholder made a capital gain from the disposal of their Toxfree share, the Toxfree Shareholder may be eligible to treat the capital gain as a discount capital gain provided that all relevant requirements of Division 115 are met.

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

97. This means that a capital gain made by a Toxfree Shareholder is a discount capital gain if they acquired the share at least 12 months before the date of disposal under the Scheme, being the Scheme Implementation Date of 25 May 2018, and the other requirements in Division 115 are satisfied.

² Taxation Ruling TR 2010/4 *Income tax: capital gains: when a dividend will be included in the capital proceeds from a disposal of shares that happens under a contract or a scheme of arrangement.*

Non-resident Toxfree shareholders

98. An entity disregards a capital gain or capital loss from a CGT event if they are a foreign resident, or the trustee of a foreign trust for CGT purposes, just before the CGT event happens and the CGT event happens in relation to a CGT asset that is not 'taxable Australian property' (subsection 855-10(1)).

99. The term 'taxable Australian property' is defined in the table in section 855-15. The table sets out these five categories of CGT assets:

Item 1	taxable Australian real property
Item 2	an indirect Australian real property interest not covered by item 5
Item 3	a CGT asset used at any time in carrying on a business through a permanent establishment in Australia and which is not covered by item 1, 2 or 5
Item 4	an option or right to acquire a CGT asset covered by item 1, 2 or 3; and
Item 5	a CGT asset that is covered by subsection 104-165(3) (choosing to disregard a gain or loss on ceasing to be an Australian resident).

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

- the non-portfolio interest test under section 960-195, and
- the principal asset test in section 855-30.

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

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

102. A non-resident, or the trustee of a foreign trust for CGT purposes, just before CGT event A1 happens, cannot disregard under subsection 855-10(1) a capital gain or capital loss from CGT event A1 happening if their shares in Toxfree are indirect Australian real property interests (item 2 of the table in section 855-15).

103. On the basis that there were no non-residents, either alone or together with any associates, who beneficially hold more than 10% of the shares in Toxfree, none of the Toxfree shares disposed of as part of the Scheme of Arrangement passes the non-portfolio interest test. Consequently, Toxfree shares held by non-residents do not constitute indirect Australian real property interests.

104. As the first condition of an indirect Australian real property interest under section 855-25 is not satisfied, it is not necessary to consider the application of the principal asset test. The Toxfree shares do not constitute 'taxable Australian property' of non-resident shareholders.

The anti-avoidance provisions

Section 177E

105. Section 177E of the ITAA 1936 is an anti-avoidance provision that is designed to prevent tax benefits being obtained as part of a dividend stripping scheme or a scheme with substantially the same effect as a dividend stripping scheme.

106. The term 'dividend stripping' has no precise legal meaning. In its traditional form, a dividend stripping operation occurs when shares in a company with substantial retained profits are acquired by shareholders who pay the existing shareholders a capital sum reflecting the value of the retained profits. The new shareholders then liberate those profits through the payment of a dividend post acquisition. Generally, the new shareholders who derive dividend income from the company would not be liable to tax upon those dividends.

107. Therefore, a scheme by way of, or in the nature of, dividend stripping, or one that has substantially the effect of a scheme by way of, or in the nature of, dividend stripping, would be one that has the effect of delivering a shareholder's entitlement to a dividend in a tax advantaged manner.

108. The retained profits of Toxfree that were distributed to its existing shareholders as the Special Dividend prior to the implementation of the Scheme of Arrangement are not provided in a tax advantaged manner. The Special Dividend was paid to Toxfree Shareholders on the Special Dividend Payment Date. The Special Dividend was funded from cash reserves and existing debt facilities. Consequently, section 177E of the ITAA 1936 will not apply.

Section 177EA

109. Section 177EA of the ITAA 1936 is a general anti-avoidance provision that operates to prevent franking credit trading. For section 177EA to apply, the conditions of paragraphs 177EA(3)(a) to (e) must be satisfied.

110. The conditions of paragraphs 177EA(3)(a) to (d) of the ITAA 1936 are satisfied as Toxfree is a corporate tax entity, the Scheme is a scheme involving the disposal of Toxfree shares in which there is a franked distribution and franking credits were received by Toxfree Shareholders (the relevant taxpayers) that participated in the Scheme and who could, therefore, reasonably be expected to receive imputation benefits.

111. Paragraph 177EA(3)(e) of the ITAA 1936, in broad terms, requires that in considering the relevant circumstances of the scheme, it would be concluded that a person, or one of the persons, who entered into or carried out the scheme, did so for a purpose (whether or not the dominant purpose but not including an incidental purpose) of enabling the taxpayer to obtain an imputation benefit.

112. 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 diverse matters which, taken individually or in conjunction with other matters, listed or not, could indicate the requisite purpose, that is, that the delivery of the imputation benefit is more than an incidental purpose of the scheme.

113. The relevant circumstances are that the disposition of the ordinary shares in Toxfree was made pursuant to a takeover by Cleanaway by way of the Scheme of Arrangement under the Corporations Act voted upon by Toxfree Shareholders entitled to vote. The Scheme of Arrangement is a normal commercial transaction under which Toxfree was acquired by Cleanaway.

114. Toxfree Shareholders are a mix of residents and non-residents. The fully franked Special Dividend was paid to all the existing shareholders of Toxfree in proportion to the number of shares that each shareholder held on the Special Dividend Record Date and irrespective of their ability to utilise the relevant franking credits. The Special Dividend allowed Toxfree Shareholders to share in the accumulated profits of Toxfree.

115. In considering the manner, form and substance of the scheme, it is considered that the scheme was not entered into by Toxfree or Toxfree Shareholders for more than an incidental purpose of enabling Toxfree Shareholders to obtain imputation benefits. The provision of imputation benefits to Toxfree Shareholders remains incidental, in the sense of being subservient to, the purpose of transferring their shares in Toxfree to Cleanaway in exchange for the Scheme Consideration.

116. Having regard to the relevant circumstances of the scheme, it cannot be concluded that Toxfree or the Toxfree Shareholders entered into or carried out the scheme for the purpose of enabling the Toxfree Shareholders to obtain an imputation benefit.

117. As the requisite purpose is not present, the Commissioner will not make a determination under paragraph 177EA(5)(b) of the ITAA 1936 to deny the whole, or any part, of the imputation benefit which Scheme Shareholders received in relation to the Special Dividend.

Section 204-30

118. Section 204-30 applies where a corporate tax entity streams the payment of dividends to its members in such a way that certain shareholders, referred to as favoured members, obtain imputation benefits, and other shareholders, referred to as disadvantaged members, obtain lesser or no imputation benefits, whether or not they receive other benefits. The favoured members are those that derive a greater benefit from imputation benefits than disadvantaged members.

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

120. Under the Scheme of Arrangement, Toxfree Shareholders received an imputation benefit when the Special Dividend was paid. The Special Dividend was paid equally to all Toxfree Shareholders and was fully franked regardless of their tax profiles. Accordingly, it cannot be said that Toxfree selectively directed the flow of franked distributions to those members who obtained the most benefit from the franking credits.

121. As the conditions in subsection 204-30(1) have not been met, the Commissioner will not make a determination under paragraph 204-30(3)(c) to deny the whole of, or any part of, the imputation benefit received by a Toxfree Shareholder in relation to the Special Dividend.

Section 207-145(1)(d)

122. Paragraph 207-145(1)(d) applies if a franked distribution is made as part of a dividend stripping operation. A distribution will be taken to be made as part of a dividend stripping operation if the making of the distribution arose out of, or was made in the course of, a scheme that was by way of, or in the nature of, dividend stripping; or had substantially the effect of a scheme by way of, or in the nature of, dividend stripping (section 207-155).

123. As stated in paragraph 106 of this Ruling, a dividend stripping operation occurs when shares in a company with substantial retained profits are acquired by shareholders who pay the existing shareholders a capital sum reflecting the value of the retained profits.

124. Having regard to the circumstances of the Scheme under which Toxfree Shareholders disposed of their shares to Cleanaway, the Commissioner considers that the payment of the Special Dividend to Toxfree Shareholders was not made as part of a dividend stripping operation.

125. Therefore, paragraph 207-145(1)(d) will not apply to the Special Dividend received by the Toxfree's Shareholders.

Appendix 2 – Detailed contents list

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

	Paragraph
Summary – what this Ruling is about	1
Relevant provisions	2
Class of entities	3
Qualifications	5
Date of effect	9
Scheme	10
Relevant Entities	11
<i>Toxfree</i>	11
<i>Cleanaway</i>	15
Scheme of Arrangement	19
Special Dividend	25
Ruling	29
Special Dividend	29
<i>Assessability of the Special Dividend and withholding tax</i>	30
<i>Residents</i>	30
<i>Non-residents not carrying on business at or through a permanent establishment</i>	31
<i>Gross-up and tax offset</i>	32
<i>Qualified persons</i>	35
<i>Refundable tax offset</i>	37
Capital Gains Tax (CGT) consequences.	38
<i>CGT event A1</i>	38
<i>Capital proceeds</i>	39
<i>Capital gain or capital loss</i>	41
<i>Discount capital gain</i>	43
<i>Non-resident shareholders</i>	44
The anti-avoidance provisions	45
Appendix 1 – Explanation	49
Special Dividend	49
<i>Assessability and withholding tax</i>	52
<i>Residents</i>	52

<i>Non-residents not carrying on business at or through a permanent establishment</i>	54
<i>Gross-up and tax offset</i>	59
<i>Qualified persons, related payment and holding period rule</i>	64
<i>Qualified person</i>	64
<i>Related payment rule</i>	66
<i>Holding period requirement</i>	72
<i>Refundable tax offset</i>	81
CGT Consequences	84
CGT event A1	84
<i>Capital proceeds</i>	89
<i>Discount capital gain</i>	95
<i>Non-resident Taxfree shareholders</i>	98
The anti-avoidance provisions	105
<i>Section 177E</i>	105
<i>Section 177EA</i>	109
<i>Section 204-30</i>	118
<i>Section 207-145(1)(d)</i>	122
Appendix 2 – Detailed contents list	126

References

Previous draft:

Not previously issued as a draft

Related Rulings/Determinations:

TD 2002/4; TR 2006/10;

TR 2010/4

Legislative references:

- ITAA 1936
- ITAA 1936 Pt IIIA Div 1A
- ITAA 1936 6(1)
- ITAA 1936 44(1)
- ITAA 1936 44(1)(a)
- ITAA 1936 44(1)(a)(i)
- ITAA 1936 44(1)(b)(i)
- ITAA 1936 98
- ITAA 1936 99A
- ITAA 1936 128B
- ITAA 1936 128B(3)(ga)
- ITAA 1936 128B(3)(ga)(i)
- ITAA 1936 128D
- ITAA 1936 160APHD
- ITAA 1936 160APHE
- ITAA 1936 160APHE(1)
- ITAA 1936 160APHM
- ITAA 1936 160APHN
- ITAA 1936 160APHN(2)
- ITAA 1936 160APHN(3)
- ITAA 1936 160APHN(3)(f)
- ITAA 1936 160APHN(4)
- ITAA 1936 160APHO(1)
- ITAA 1936 160APHO(1)(b)
- ITAA 1936 160APHO(2)
- ITAA 1936 160APHO(2)(a)
- ITAA 1936 160APHO(3)
- ITAA 1936 160APHT
- ITAA 1936 160APHT(2)
- ITAA 1936 160APHU
- ITAA 1936 177E
- ITAA 1936 177EA
- ITAA 1936 177EA(3)
- ITAA 1936 177EA(3)(a)
- ITAA 1936 177EA(3)(b)
- ITAA 1936 177EA(3)(c)
- ITAA 1936 177EA(3)(d)
- ITAA 1936 177EA(3)(e)
- ITAA 1936 177EA(5)
- ITAA 1936 177EA(5)(a)
- ITAA 1936 177EA(5)(b)
- ITAA 1936 177EA(17)
- ITAA 1997
- ITAA 1997 Div 67
- ITAA 1997 67-25
- ITAA 1997 67-25(1A)
- ITAA 1997 67-25(1B)(b)
- ITAA 1997 67-25(1C)
- ITAA 1997 67-25(1D)
- ITAA 1997 67-25(1DA)
- ITAA 1997 104-10(1)
- ITAA 1997 104-10(2)
- ITAA 1997 104-10(3)
- ITAA 1997 104-10(3)(b)
- ITAA 1997 104-10(4)
- ITAA 1997 104-165(3)
- ITAA 1997 Div 115
- ITAA 1997 115-25(1)
- ITAA 1997 116-20(1)
- ITAA 1997 116-20(1)(a)
- ITAA 1997 116-20(1)(b)
- ITAA 1997 202-40
- ITAA 1997 202-45
- ITAA 1997 204-30
- ITAA 1997 204-30(1)
- ITAA 1997 204-30(3)
- ITAA 1997 204-30(3)(c)
- ITAA 1997 204-30(8)
- ITAA 1997 Div 207
- ITAA 1997 207-20
- ITAA 1997 207-20(1)
- ITAA 1997 207-20(2)
- ITAA 1997 207-35(1)
- ITAA 1997 207-45
- ITAA 1997 207-75
- ITAA 1997 207-75(2)
- ITAA 1997 207-145(1)
- ITAA 1997 207-145(1)(a)
- ITAA 1997 207-145(1)(d)
- ITAA 1997 207-155
- ITAA 1997 855-10
- ITAA 1997 855-10(1)
- ITAA 1997 855-15
- ITAA 1997 855-25
- ITAA 1997 855-30
- ITAA 1997 960-195
- ITAA 1997 977-50
- ITAA 1997 995-1(1)
- Corporations Act 2001
- Corporations Act 2001 Part 5.1
- Corporations Act 2001 254T

ATO references

NO: 1-E7UMS3F

ISSN: 2205-5517

BSL: PGI

ATOlaw topic: Income tax ~~ Assessable income ~~ Dividend income ~~
Dividend incomeIncome tax ~~ Capital gains tax ~~ CGT events ~~ CGT
event A1 - disposal of a CGT assetIncome tax ~~ Capital gains tax ~~ Capital proceeds

**© AUSTRALIAN TAXATION OFFICE FOR THE
COMMONWEALTH OF AUSTRALIA**

You are free to copy, adapt, modify, transmit and distribute this material as you wish (but not in any way that suggests the ATO or the Commonwealth endorses you or any of your services or products).