


# ***CR 2014/98 - Income tax: Ardent Leisure Group (ALG) Capital Reallocation***

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## Class Ruling

# Income tax: Ardent Leisure Group (ALG) Capital Reallocation

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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.

## What this Ruling is about

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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 provision(s)

2. The relevant provisions dealt with in this Ruling are:
- Division 6 of Part III of the *Income Tax Assessment Act 1936* (ITAA 1936)
  - section 99B of the ITAA 1936
  - section 6-5 of the *Income Tax Assessment Act 1997* (ITAA 1997)
  - section 104-70 of the ITAA 1997
  - section 110-25 of the ITAA 1997
  - section 110-55 of the ITAA 1997
  - Subdivision 115-A of the ITAA 1997
  - Division 725 of the ITAA 1997
  - Division 727 of the ITAA 1997, and

- section 855-10 of the ITAA 1997.

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

## **Class of entities**

3. The class of entities to which this Ruling applies are the holders of Ardent Leisure Group (ALG) stapled securities (each stapled security consisting of a share in Ardent Leisure Limited (ALL) stapled to a unit in Ardent Leisure Trust (ALT)) who:

- (a) are registered on the Ardent Leisure Trust (ALT) unit register on the Record Date of 1 December 2014 for the return of capital in respect of their units in ALT
- (b) do not hold their units in ALT and shares in ALL as a revenue assets (as defined in section 977-50) nor as trading stock (as defined in subsection 995-1(1)) - that is, they hold their units in ALT and share in ALL on capital account
- (c) participate in the capital reallocation (Capital Reallocation) to be announced on 1 December 2014 and described in the Scheme part of this Ruling, and
- (d) are not subject to the taxation of financial arrangements rules in Division 230 in relation to gains and losses on their ALG securities.

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

In this Ruling, the entity belonging to this class of entities is referred to as a Securityholder.

## **Qualifications**

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

5. The class of entities defined in this Ruling may rely on its contents provided the scheme actually carried out is carried out in accordance with the scheme described in paragraphs 8 to 24 of this Ruling.

6. If the scheme actually carried out is materially different from the scheme that is described in this Ruling, then:

- this Ruling has no binding effect on the Commissioner because the scheme entered into is not the scheme on which the Commissioner has ruled, and
- this Ruling may be withdrawn or modified.

## Date of effect

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7. This Ruling applies from 1 July 2014 to 30 June 2015. The Ruling continues to apply after 30 June 2015 to all entities within the specified class who entered into the specified scheme during the term of the Ruling. However, this Ruling will not apply to taxpayers to the extent that it conflicts with the terms of a settlement of a dispute agreed to before the date of issue of this Ruling (see paragraphs 75 and 76 of Taxation Ruling TR 2006/10).

## Scheme

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

- application for class ruling dated 26 September 2014 including appendices, and
- correspondence from Greenwoods & Herbert Smith Freehills providing further information.

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

### The Ardent Leisure Group

9. ALG is one of Australia's largest specialist operators of leisure and entertainment assets, with activities across Australia, New Zealand, and the United States.

10. ALG consists of ALL and ALT and their controlled entities. Ardent Leisure Management Limited (ALML) is the responsible entity of ALT.

11. An ALG stapled security consists of:

- a share in ALL, and
- a unit in ALT. ALT is a registered managed investment scheme for the purposes of the *Corporations Act 2001*. ALT is a flow-through unit trust taxed under Division 6 of Part III of the ITAA 1936.

12. ALG trades on the Australian Securities Exchange as a stapled security and has been listed since 11 June 1998.

## The Capital Reallocation

13. At the Annual General meeting (the Meeting) of ALG held on 30 October 2014 Securityholders approved, amongst other things, a Capital Reallocation which included:

- A distribution of trust capital by ALT to all Securityholders of \$0.28 per unit (ALT Capital Reduction Amount), and
- The ALT Capital Reduction Amount being compulsorily applied on behalf of each Securityholder as a further capital contribution in respect of existing shares in ALL, as to \$0.28 per share (ALL Contribution Amount).

14. The ALG considers that the Capital Reallocation will result in a balance sheet of the Group that provides a more desirable debt/equity mix for sustainable long term growth and, if any future capital raisings are undertaken, equity will be more appropriately allocated between ALT and ALL.

15. Securityholders did not receive any cash as part of the Capital Reallocation.

16. There were approximately 436.59 million ALT units on issue as at 30 October 2014 (each included in the ALG staple). Consequently, the total ALT Capital Reduction Amounts and the total ALL Contribution Amounts were approximately \$122.25 million each.

17. The ALT Capital Reduction Amount was debited to the contributed equity of ALT.

18. The ALL Contribution Amount was contributed in respect of an existing share in ALL. No new shares were issued by ALL under the Capital Reallocation.

19. The ALL Contribution Amount was credited directly to share capital in ALL's accounts.

20. ALML resolved that the distribution of the ALT capital Reduction Amount was a distribution of trust capital.

21. ALML will distribute the Distributable Income of ALT for the year ended 30 June 2015 to the Securityholders in the usual manner.

22. Following the approval of Securityholders at the Meeting, the constitutions of both ALT and ALL were amended to facilitate the Capital Reallocation as follows:

- The rights attaching to each share in ALL have been amended so that each Securityholder's liability in respect of their share in ALL will be increased by the amount of the ALL contribution Amount (ALL Share Liability), and
- The ALT constitution has been amended to enable ALML to be irrevocably appointed as an agent and attorney for each Securityholder for the purpose of consenting to the ALL Share Liability, and to apply the ALT Capital Reduction Amount, on behalf of each holder, as the ALL Contribution Amount is full satisfaction of the ALL Share Liability.

23. In respect of ALL, no entity or no entity and its associates between them, control ALL or can exercise or can control the exercise of, at least 40% voting power in ALL or has the right to receive at least 40% of any dividends or distribution of capital as shareholders of ALL. Further, no Securityholder has de facto control over ALL.

24. In respect of ALT, no entity or no entity and its associates between them controls or, has the right to receive at least 40% of any distribution of trust income, or trust capital as unitholders of ALT. Further, no Securityholder has de facto control over ALT.

## **Ruling**

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### **Non-assessable payment**

25. The ALT distribution of trust capital (being Corpus) of \$0.28 per unit will not be included in a Securityholder's assessable income under section 6-5 or under Division 6 of Part III of the ITAA 1936.

### **CGT event E4**

26. CGT event E4 happens in respect of each ALT unit when ALT pays \$0.28 per unit to a Securityholder (section 104-70). For the purposes of section 104-70, the entire amount of \$0.28 per ALT unit is a non-assessable part.

27. The time of CGT event E4 is just before the end of the income year in which ALML made the payment (paragraph 104-70(3)(a)).

### **Capital gain**

28. A Securityholder will make a capital gain if the non-assessable amount of \$0.28 per ALT unit exceeds the cost base of the unit (subsection 104-70(4)). The capital gain will be equal to the amount of the excess.

29. If the ALT unit was acquired by an Australian resident unit holder at least 12 months before the time of CGT event E4, a capital gain from CGT event E4 happening to that unit may qualify as a discount capital gain under subsection 115-25(1), provided the other conditions in Subdivision 115-A are satisfied.

30. An individual who is a foreign resident or temporary resident must meet further conditions to be eligible to treat the capital gain as a discount capital gain under Subdivision 115-A of the ITAA 1997.

## **Cost base reduction**

31. Where a Securityholder makes a capital gain when CGT event E4 happens, the cost base and reduced cost base of the ALT unit will be reduced to nil (subsection 104-70(5)).
32. If the non-assessable amount of \$0.28 per ALT unit is less than or equal to the cost base of the ALT unit, the cost base and reduced cost base of the ALT unit are reduced by that amount (subsection 104-70(6)).

## **Foreign resident Securityholders**

33. A foreign resident Securityholder who was paid the non-assessable amount of \$0.28 per ALT unit disregards any capital gain made from CGT event E4 if their ALT unit does not constitute 'taxable Australian property' (section 855-10).

## **Capital contribution and cost base**

34. The variation of the terms of the shares in ALL to increase the liability of a Securityholder to contribute capital will not cause a CGT event to happen to the Securityholder.
35. The fourth element of the cost base and reduced cost base of an ALL share will increase by \$0.28 per share, which is the amount of the further share capital contribution in respect of each existing share in ALL (subsection 110-25(5) and 110-55(2)).

## **Value shifting**

36. There will be no consequences for a Securityholder under Divisions 725 and 727.

## Appendix 1 – Explanation

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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.***

### **Non-assessable payment**

37. Division 6 of Part III of the ITAA 1936 is the primary scheme for including distributions from trusts in the assessable income of beneficiaries. Subsection 99B(1) of the ITAA 1936 provides that an amount, being property of a trust estate, paid to, or applied for the benefit of, a beneficiary of the trust estate who was a resident at any time during the year of income, is the assessable income of the beneficiary, subject to the exceptions in subsection 99B(2) of the ITAA 1936.

38. The exception in paragraph 99B(2)(a) of the ITAA 1936 reduces the amount that would otherwise be included in assessable income by the amount that represents corpus of the trust estate and is not attributable to amounts derived by the trust estate that, if they had been derived directly by a taxpayer being a resident, would have been included in the assessable income of that taxpayer.

39. Subsection 6-5(1) provides that a taxpayer's assessable income includes income according to ordinary concepts (ordinary income).

40. In *Scott v. Federal Commissioner of Taxation* (1966) 117 CLR 514; (1966) 10 AITR 367; (1966) 14 ATD 286, Windeyer J stated at CRR 526, AITR 375; ATD 293 that:

Whether or not a particular receipt is income depends upon its quality in the hands of the recipient.

41. In *GP International Pipecoaters Pty Ltd v. Federal Commissioner of Taxation* (1990) 170 CLR 124; 90 ATC 4413; (1990) 21 ATR 1, the High Court unanimously stated that the following factors were important in determining the nature of a receipt:

To determine whether a receipt is of an income or a capital nature, various factors may be relevant. Sometimes, the character of receipts will be revealed most clearly by their periodicity, regularity or recurrence; sometimes, by the character of a right or thing disposed of in exchange for the receipt; sometimes by the scope of the transaction, venture or business in or by reason of which money is received and by the recipient's purpose in engaging in the transaction, venture or business.

42. The ALT distribution of trust capital of \$0.28 per unit was a distribution of trust capital for the year ended 30 June 2015 (being a payment of corpus) and does not have the quality of income in the hands of the Securityholders. Therefore, it is not ordinary income under subsection 6-5(1).

43. On the basis that ALML has resolved that the distribution of the ALT Capital Reduction Amount was a distribution of trust capital for the year ending 30 June 2015, the receipt of the ALT Capital Reduction Amount did not result in a Securityholder being presently entitled to a share of the income of ALT and no amount will be included in that Securityholder's assessable income pursuant to Division 6 of Part III of the ITAA 1936.

## **CGT event E4**

44. Under section 104-70, CGT event E4 happens if the trustee of a trust makes a payment to a unitholder in respect of their unit in the trust and some or all of the payment is not included in the unitholder's assessable income (non-assessable payment).

45. CGT event E4 happened in respect of each ALT unit when ALT paid \$0.28 per unit to a Securityholder (section 104-70). For the purposes of section 104-70, the entire amount of \$0.28 per ALT unit is a non-assessable part.

## **Capital Gain**

46. If CGT event E4 happens during an income year, a Securityholder will make a capital gain if the total value of the non-assessable payments made by the trustee during the income year in respect of their unit exceeds its cost base (subsection 104-70(4)). A Securityholder cannot make a capital loss when CGT event E4 happens (subsection 104-70(6)).

47. A Securityholder will make a capital gain if the non-assessable amount of \$0.28 exceeded the cost base of the unit (subsection 104-70(4)).

## **Cost base reduction**

48. When a Securityholder makes a capital gain from CGT event E4 happening, the cost base and reduced cost base of the unit are reduced to nil (subsection 104-70(5)).

49. However, if the sum of the non-assessable payments is less than or equal to the cost of the unit, the cost base and reduced cost base of the unit are reduced by that amount (subsection 104-70(6)).

50. Where the Securityholder makes a capital gain, the cost base and reduced cost base of their ALT unit is reduced to nil (subsection 104-70(5)).

51. If the non-assessable amount of \$0.28 per ALT unit was less than or equal to the cost base of the unit, the cost base and reduced cost base of the ALT unit are reduced by that amount (subsection 104-70(6)).

**Foreign resident Securityholders**

52. Under subsection 855-10(1), an entity disregards a capital gain or capital loss made 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 in relation to a CGT asset that is not 'taxable Australian property'.

53. 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).

54. However, a foreign resident, or the trustee of a foreign trust for CGT purposes, just before CGT event E4 happens, cannot disregard under subsection 855-10(1) a capital gain from CGT event E4 happening if:

- their ALT unit was an 'indirect Australian real property interest' (item 2 of the table in section 855-15)
- their ALT unit had been used at any time by the foreign resident in carrying on a business through a permanent establishment in Australia (item 3 of the table in section 855-15), or
- their ALT unit was covered by subsection 104-165(3) (item 5 of the table in section 855-15).

55. A foreign resident Securityholder will have an 'indirect Australian real property interest' if it holds a membership interest in ALT, and the interest passes the 'non-portfolio interest test' (section 960-195) and the 'principal asset test' (section 855-30).

**Capital contribution and cost base**

56. No CGT event happened to a Securityholder as a result of the variation of the terms of each ALL share to increase the Securityholder's liability to contribute capital.

57. The ALT distribution of trust capital of \$0.28 per unit was applied to each ALL share as a contribution of share capital. This contribution of share capital represents capital expenditure incurred by a Securityholder for the purpose of increasing or preserving the value of their ALL share.

58. The fourth element of the cost base and reduced cost base of each ALL share includes the amount of the share capital contribution that is referable to that share (subsections 110-25(5) and 110-55(2)).

## **Value shifting**

59. There is a direct value shift under a scheme involving equity or loan interests in an entity where there is a decrease in the market value of some equity or loan interest and an increase or issue at a discount of other equity or loan interests (section 725-145).

60. There is an indirect value shift where there is an unequal exchange of economic benefits between two entities – the losing entity and gaining entity (subsection 727-150(3)).

61. There can only be consequences for a direct value shift if there is any entity that controls the target entity for value shifting purposes at some time during the scheme period as defined in section 725-55 (paragraph 725-50(b)). Section 727-355 sets out the relevant tests as to when an entity controls a company for value shifting purposes. Section 727-360 sets out the relevant tests for whether an entity controls a fixed trust for value shifting purposes. Section 727-365 sets out the relevant tests for whether an entity controls a non-fixed trust for value shifting purposes.

62. There can only be consequences for an indirect value shift if the entities between which the value is shifted (the losing entity and the gaining entity) satisfy an ultimate controller test and/or a common ownership nexus test at some time during the indirect value shift period defined in subsection 727-150(7) (paragraph 727-100(c) and sections 727-105 and 727-110).

63. On the basis of the information provided, there was no entity that controlled ALL or ALT for value shifting purposes or that satisfied, together with ALL or ALT, the ultimate controller test and/or the common ownership nexus test as described above. As a result, there are no consequences under Divisions 725 and 727 for any direct value shift or indirect value shift that occurs under the Capital Reallocation.

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

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

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## References

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*Previous draft:*

Not previously issued as a draft

*Related Rulings/Determinations:*

TR 2006/10

*Subject references:*

- Capital gains
- Capital gains tax
- CGT assets
- CGT cost base
- CGT events
- CGT events E1-E9 – trusts
- CGT reduced cost base
- Trusts
- value shifting – entity interests
- indirect value shifting rules
- value shifting- entity interests
- direct value shifting rules

*Legislative references:*

- ITAA 1936 Pt III Div 6
- ITAA 1936 99B
- ITAA 1936 99B(1)
- ITAA 1936 99B(2)
- ITAA 1936 99B(2)(a)
- ITAA 1997 6-5
- ITAA 1997 6-5(1)
- ITAA 1997 104-70
- ITAA 1997 104-70(3)(a)
- ITAA 1997 104-70(4)
- ITAA 1997 104-70(5)
- ITAA 1997 104-70(6)
- ITAA 1997 104-165(3)
- ITAA 1997 110-25
- ITAA 1997 110-25(5)

- ITAA 1997 110-55
- ITAA 1997 110-55(2)
- ITAA 1997 Subdiv 115-A
- ITAA 1997 115-25(1)
- ITAA 1997 Div 230
- ITAA 1997 Div 725
- ITAA 1997 725-50(b)
- ITAA 1997 725-55
- ITAA 1997 725-145
- ITAA 1997 Div 727
- ITAA 1997 727-100(c)
- ITAA 1997 727-105
- ITAA 1997 727-110
- ITAA 1997 727-150(3)
- ITAA 1997 727-150(7)
- ITAA 1997 727-355
- ITAA 1997 727-360
- ITAA 1997 727-365
- ITAA 1997 855-10
- ITAA 1997 855-10(1)
- ITAA 1997 855-15
- ITAA 1997 855-30
- ITAA 1997 960-195
- ITAA 1997 977-50
- ITAA 1997 995-1(1)
- TAA 1953
- Corporations Act 2001

*Case references:*

- GP International Pipecoaters Pty Ltd v. Federal Commissioner of Taxation (1990) 170 CLR 124; 90 ATC 4413; (1990) 21 ATR 1
- Scott v. Federal Commissioner of Taxation (1966) 117 CLR 514; (1966) 10 AITR 367; (1966) 14 ATD 286

## ATO references

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cost base

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