


CR 2010/4 - Income tax: demerger of Lion Selection Group Ltd by Lion Selection Ltd

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Class Ruling

Income tax: demerger of Lion Selection Group Ltd by Lion Selection Ltd

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① This publication provides you with the following level of protection:

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

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

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

What this Ruling is about

1. This Ruling sets out the Commissioner's opinion on the way in which the relevant 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 provision(s) dealt with in this Ruling are:

- subsection 6(1) of the *Income Tax Assessment Act 1936* (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 104-135 of the *Income Tax Assessment Act 1997* (ITAA 1997);
- section 110-25 of the ITAA 1997; and
- section 110-55 of the ITAA 1997.

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

Class of entities

3. The class of entities to which this Ruling applies consists of the ordinary shareholders of Lion Selection Limited (Lion) who:

- (a) were listed on the share register of Lion as at the Record Date (7 December 2009) for the demerger of shares in Lion Selection Group Limited (LSG);
- (b) were residents of Australia as defined in subsection 6(1) of the ITAA 1936 on that date; and
- (c) held their Lion shares on capital account on that date.

In this Ruling, a person belonging to this class of entities is referred to as a 'Lion shareholder'.

Qualifications

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

5. The class of entities defined in this Ruling may rely on its contents provided the Scheme actually carried out is carried out in accordance with the Scheme described in paragraphs 9 to 34 of this Ruling.

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

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

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Date of effect

8. This Ruling applies from 1 July 2009 to 30 June 2010. The Ruling continues to apply after 30 June 2010 to all entities within the specified class who entered into the specified scheme during the term of the Ruling. However, this Ruling will not apply to taxpayers to the extent that it conflicts with the terms of a settlement of a dispute agreed to before the date of issue of this Ruling (see paragraphs 75 and 76 of Taxation Ruling TR 2006/10).

Scheme

9. The following description of the Scheme is based on information provided by the applicant.

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

The restructure of Lion

10. On 24 June 2009, Lion announced a restructure. The key transactions under the restructure are:

- the demerger of 100% of the ordinary shares in LSG to the shareholders of Lion;
- the payment of a cash distribution of 10 cents per share to the shareholders of Lion;
- following the demerger, the acquisition of 100% of the ordinary shares in Lion by Catalpa Resources Ltd (Catalpa) pursuant to a Scheme of Arrangement under Part 5.1 of the *Corporations Act 2001* (the Scheme).

Relevant entities

Lion

11. Lion was, at the time of the restructure, an Australian resident company listed on the Australian Securities Exchange (ASX). Lion was the head company of a consolidated tax group for the purposes of Part 3-90.

12. Lion is a resource company. Before the restructure, it had invested in global mining companies, with operations focussed in Australia, Africa and South East Asia. Lion had a diversified investment portfolio which included interests in companies that undertake exploration and mining for gold, copper, nickel and other base metals.

13. In addition to its investment portfolio, Lion had a 30% interest in the Cracow joint venture, an operational gold mine in Queensland, and an interest of approximately 46.9% in Catalpa.

14. Immediately before the demerger, Lion had 88,029,353 fully paid ordinary shares on issue.

15. There were no other ownership interests in Lion just before the demerger.

LSG

16. At the time of the demerger, LSG was an Australian resident company and a wholly owned subsidiary of Lion. LSG is a growth orientated investment company with exposure to investments made through funds managed by Lion Manager Pty Limited.

17. Immediately before the demerger, LSG had 88,029,353 fully paid ordinary shares on issue, all owned by Lion.

18. There were no other ownership interests in LSG just before the demerger.

19. The ordinary shares in LSG have been listed on the National Stock Exchange, of Australia and began trading on 16 December 2009.

Catalpa

20. Catalpa is an Australian resident company listed on the ASX, which is developing the Edna May gold project at Westonia in Western Australia.

21. As at 16 November 2009, Catalpa had 1,171,852,429 fully paid ordinary shares on issue. Lion indirectly owned approximately 46.9% of Catalpa.

The demerger of LSG

22. The broad outline of the demerger of LSG involved the following key steps:

- the transfer of assets and the allocation of liabilities between Lion, LSG and their respective subsidiaries;
- inter-company loans were forgiven prior to the demerger; and
- LSG demerges from the Lion consolidated group.

23. Lion shareholders voted at a general meeting on 17 November 2009 to approve an ordinary resolution (the demerger resolution) to reduce the share capital of Lion by an amount equal to the value of 88,029,353 ordinary shares in LSG (the capital reduction amount). For the purposes of debiting Lion's share capital account, the value of each ordinary share in LSG was 40 cents.

24. The demerger resolution was not conditional upon a special resolution being passed at the subsequent Scheme meeting of Lion shareholders on the same day, approving the merger of Lion and Catalpa (see below).

25. The capital reduction amount was satisfied by an *in specie* distribution to Lion shareholders of LSG shares. Lion effected the demerger by distributing all of the shares it owned in LSG to the Lion shareholders on 10 December 2009. Lion shareholders received one LSG share for each Lion share they owned at the Record Date for the demerger (7 December 2009). As a result of the demerger, Lion shareholders will own shares in both Lion and LSG.

26. Under a share sale arrangement known as the Matching Facility, Lion shareholders had the choice of selling (through a stockbroker chosen by Lion) some or all of the LSG shares they were entitled to receive under the demerger to third parties. The price at which LSG shares were sold under the Matching Facility was 40 cents per share.

Reasons for the demerger

27. Lion expects that a number of advantages will accrue to its shareholders as a result of the demerger. These advantages are said to include:

- Lion and LSG will focus on their respective core competencies and strategies;
- reducing the discount to net tangible assets of Lion's share price;
- improving the ability of Lion and LSG to pursue investment opportunities, and to grow through acquisitions and mergers;
- enhancing the awareness of investors; and
- improving the investment choice for Lion shareholders who will have the choice of holding an investment in companies with markedly different profiles, that is, Lion (Australian gold mining) and LSG (early stage resource investments).

The merger of Lion and Catalpa

28. Lion shareholders voted at a meeting on 17 November 2009 for a special resolution in favour of the Scheme. Under the Scheme, Catalpa acquired all of the ordinary shares in Lion on 10 December 2009. As consideration, a Lion shareholder received one Catalpa share (after Catalpa had undertaken an 11 for 1 share consolidation) for each Lion share they owned at the Record Date for the Scheme (7 December 2009).

29. The Scheme was conditional upon the demerger resolution being approved, which did in fact happen.

30. As a consequence of the Scheme, the Lion shareholders were issued approximately 88,029,353 new ordinary shares in Catalpa (after Catalpa had undertaken the share consolidation).

Ineligible Overseas Shareholders

31. Shareholders of Lion whose address, as shown on Lion's shareholder register, is outside Australia or New Zealand (and their respective external territories), or who are residents of a jurisdiction other than those places, and in respect of whom LSG and Catalpa are not satisfied that the laws of that shareholder's country of residence permit the issue of LSG shares or Catalpa shares, respectively, to, either unconditionally or after compliance with acceptable and practical terms, are Ineligible Overseas Shareholders.

32. The shares in LSG and Catalpa that these shareholders would otherwise have been entitled to receive were transferred or issued to a nominee, who will sell them on the ASX and pay to each Ineligible Overseas Shareholder their share of the net proceeds of sale of those LSG and Catalpa shares, in accordance with the procedures outlined in the Explanatory Booklet.

Other matters

33. None of the Lion shareholders acquired their shares in Lion before 20 September 1985.

34. Lion has confirmed that no amounts have been transferred to its share capital account (as defined in section 975-300) from any of its other accounts, and accordingly its share capital account is not tainted (within the meaning of Division 197).

Ruling

The demerger of LSG shares

CGT event G1

35. CGT event G1 happened in relation to each of the Lion ordinary shares owned by Lion shareholders at the time Lion made the payment of the capital reduction amount (satisfied by the *in specie* distribution of LSG shares) (section 104-135).

Capital gain

36. Lion shareholders will make a capital gain from CGT event G1 happening if the capital reduction amount exceeds the cost base of the Lion share (subsection 104-135(3)). No capital loss can be made from CGT event G1.

Reducing the cost base and reduced cost base of Lion shares

37. If the capital reduction amount is not more than the cost base of the Lion share, the cost base and the reduced cost base of the Lion share will be reduced (but not below nil) by the capital reduction amount (subsection 104-135(4)).

Cost base of the LSG shares

38. The first element of the cost base and reduced cost base of each share in LSG received by Lion shareholders will equal the capital reduction amount applied on behalf of each Lion shareholder to acquire the LSG share (subsections 110-25(2) and 110-55(2)).

Distribution is not a dividend for income tax purposes

39. The *in specie* distribution to Lion shareholders of LSG shares under the scheme is not a 'dividend' as defined in subsection 6(1) of the ITAA 1936.

The application of sections 45, 45A, 45B and 45C

40. Section 45 of the ITAA 1936 will not apply to the *in specie* distribution received by Lion shareholders.

41. The Commissioner will not make a determination under section 45A of the ITAA 1936 that section 45C of the ITAA 1936 applies to the whole, or any part, of the *in specie* distribution received by Lion shareholders.

42. The Commissioner will not make a determination under section 45B of the ITAA 1936 that section 45C of the ITAA 1936 applies to the whole, or any part, of the *in specie* distribution received by Lion shareholders.

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.*

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

The demerger of LSG shares

44. The capital gains tax consequences of the demerger of LSG shares are described in paragraphs 35 to 38 of this Ruling.

45. This transaction does not qualify for the demerger concessions outlined in Division 125 of the ITAA 1997, and in subsections 44(3) and (4) of the ITAA 1936.

Distribution is not a dividend for income tax purposes

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

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

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

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

50. The *in specie* distribution to Lion shareholders of LSG shares will be recorded as a debit to Lion's share capital account. As the share capital account of Lion is not tainted within the meaning of Division 197 of the ITAA 1997, paragraph (d) of the definition of 'dividend' in subsection 6(1) of the ITAA 1936 applies. Accordingly the *in specie* distribution to Lion shareholders of LSG shares is not a 'dividend' as defined in subsection 6(1) of the ITAA 1936.

The application of sections 45, 45A, 45B and 45C**Section 45**

51. 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 shareholders and minimally franked dividends are received by other shareholders. Minimally franked dividends are dividends which are not franked or are franked to less than 10%.

52. Based on the information provided and having regard to the circumstances of the scheme, section 45 of the ITAA 1936 will not apply to the *in specie* distribution received by Lion shareholders.

Section 45A

53. Section 45A of the ITAA 1936 is an anti-avoidance provision which applies where capital benefits are streamed to certain shareholders (the advantaged shareholders) who derive a greater benefit from the receipt of capital, and it is reasonable to assume that the other shareholders (the disadvantaged shareholders) have received or will receive dividends.

54. Where the Commissioner makes a written determination under subsection 45A(2) of the ITAA 1936 that section 45C of the ITAA 1936 applies in relation to the whole or part of the capital benefits, the capital benefits will be treated as unfranked dividends paid out of the company's profits.

55. Paragraph 45A(3)(b) of the ITAA 1936 provides that one of the means by which a capital benefit is provided to a shareholder is through the distribution of share capital to the shareholder.

56. However, the circumstances of the *in specie* distribution to Lion shareholders of LSG shares do not indicate that there was a streaming of capital benefits to advantaged shareholders at the expense of disadvantaged shareholders.

57. Although Lion provided its shareholders with a 'capital benefit' as defined in paragraph 45A(3)(b) of the ITAA 1936 in the form of LSG shares, the capital benefit was provided to all of the shareholders in the same proportion as their share holdings in Lion. Consequently, there are no 'advantaged' or 'disadvantaged' shareholders as contemplated by subsection 45A(1) of the ITAA 1936.

58. Therefore, section 45A of the ITAA 1936 will not apply to the *in specie* distribution to Lion shareholders of LSG shares and the Commissioner will not make a determination under subsection 45A(2) that section 45C of the ITAA 1936 applies.

Section 45B

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

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

- (a) there is a scheme under which a person is provided with a capital benefit by a company (paragraph 45B(2)(a));
- (b) under the scheme a taxpayer, who may or may not be the person provided with the capital benefit, obtains a tax benefit (paragraph 45B(2)(b)); and
- (c) having regard to the relevant circumstances of the scheme, it would be concluded that the person, or one of the persons, who entered into or carried out the scheme or any part of the scheme did so for a purpose, (other than an incidental purpose) of enabling a taxpayer to obtain a tax benefit (paragraph 45B(2)(c)).

61. The arrangement involving the *in specie* distribution to Lion shareholders of LSG shares constitutes a scheme for the purposes of section 45B of the ITAA 1936.

62. The phrase 'provided with a capital benefit' is defined in subsection 45B(5) of the ITAA 1936 and includes a distribution to a person of share capital. As the *in specie* distribution of LSG shares was recorded by means of a debit to Lion's untainted share capital account, Lion shareholders will be taken to have been provided with a capital benefit as defined in paragraph 45B(5)(b).

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

64. Accordingly, the Commissioner will not make a determination pursuant to subsection 45B(3) of the ITAA 1936 that section 45C of the ITAA 1936 applies to the *in specie* distribution of LSG shares by Lion.

Appendix 2 – Detailed contents list

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References

Previous draft:

Not previously issued as a draft

Related Rulings/Determinations:

TR 2006/10

Subject references:

- capital benefit
- capital gains
- capital proceeds
- CGT event G1-G3 – shares
- cost base adjustments
- demerger
- return of capital on shares

- ITAA 1936 45A(3)(b)
- ITAA 1936 45B
- ITAA 1936 45B(2)(a)
- ITAA 1936 45B(2)(b)
- ITAA 1936 45B(2)(c)
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- ITAA 1936 45B(5)
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- ITAA 1997 Pt 3-90
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- Corporations Act 2001 Pt 5.1
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Legislative references:

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- ITAA 1936 6(1)
- ITAA 1936 44
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- ITAA 1936 45A(1)
- ITAA 1936 45A(2)

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