


CR 2014/42 - Income tax: scrip for scrip: exchange of shares in Envestra for APA stapled securities

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Class Ruling

Income tax: scrip for scrip: exchange of shares in Envestra for APA stapled securities

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

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

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

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

What this Ruling is about

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

Relevant provision(s)

2. The relevant provisions dealt with in this Ruling are:

- section 102-5 of the ITAA 1997
- section 102-10 of the ITAA 1997
- section 104-10 of the ITAA 1997
- section 115-30 of the ITAA 1997
- section 116-20 of the ITAA 1997
- Subdivision 124-M of the ITAA 1997
- section 124-785 of the ITAA 1997
- section 124-790 of the ITAA 1997, and
- section 124-795 of the ITAA 1997.

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

Class of entities

3. The class of entities to which this Ruling applies is the ordinary shareholders of Envestra who:

- (a) participate in the Scheme that is the subject of this Ruling
- (b) acquired their ordinary shares in Envestra (Envestra shares) on or after 20 September 1985
- (c) hold their Envestra shares on capital account at the time of their participation in the Scheme
- (d) are residents of Australia for the purposes of subsection 6(1) of the *Income Tax Assessment Act 1936* (ITAA 1936) at all relevant times and are not considered temporary residents for tax purposes
- (e) are not 'significant stakeholders' or 'common stakeholders' within the meaning of those expressions as used in Subdivision 124-M at the time of the Scheme, and
- (f) are not subject to the taxation of financial arrangements rules in Division 230 in relation to gains and losses on their Envestra shares.

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

In this Ruling, a person belonging to this class of entities is referred to as an Envestra 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 8 to 29 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

7. This Ruling applies from 1 July 2013 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

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:

- Class Ruling application dated 1 April 2014
- Scheme Implementation Agreement dated 4 March 2014
- Scheme Booklet for the scheme of arrangement, and
- additional information received in relation to the Class Ruling application.

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

APA Group

9. APA Group is Australia's largest natural gas infrastructure business. APA is the stapled entity comprising Australian Pipeline Trust (APT) and APT Investment Trust (APTIT), acting through Australian Pipeline Limited (APL) in its capacity as responsible entity and trustee of APT and APTIT.

10. A stapled security held in APA (APA Security) comprises one unit in APT and one unit in APTIT, stapled together such that they must only be transferred together.

11. APT is a managed investment scheme regulated by the Corporations Act. It is a public trading trust as defined in Division 6C of the ITAA 1936 and has elected to be the head company of a tax consolidated group.

12. APTIT is a managed investment scheme regulated by the Corporations Act. It is not a public trading trust.

13. Both APT and APTIT have only one class of units on issue and both are Australian residents for tax purposes.

14. APT will have more than 300 members at the time of the Scheme.

15. APA was listed on the Australian Securities Exchange (ASX) on 13 June 2000. As at 31 December 2013, the net tangible asset (NTA) split, as published by the APA Group, between APT and APTIT was 75.8% and 24.2% respectively.

Envestra Limited

16. Envestra Limited (Envestra) is one of Australia's largest natural gas distribution companies. Envestra is the head company of a tax consolidated group and listed on the ASX on 29 August 1997. It has only one class of share on issue. Envestra is an Australian resident for income tax purposes.

17. Envestra will have more than 300 members at the time of the scheme.

18. APA (through APT) owns 33.05% of the shares in Envestra and operates and maintains its assets under long term operating and management agreements.

Scheme of Arrangement

19. APA and Envestra have agreed that Envestra will enter into a Scheme of Arrangement (the Scheme) under Part 5.1 of the *Corporations Act 2001*, which will be approved by order of a Court made for the purposes of paragraph 411(4)(b) of the *Corporations Act 2001*, between Envestra and its shareholders (other than members of the APA Group) (eligible Envestra Shareholders), pursuant to which APL as responsible entity and trustee of APT (APL as RE of APT) will acquire all of the ordinary shares in Envestra which it does not already own.

20. The Scheme is subject to approval by eligible Envestra Shareholders at a Scheme Meeting to be held on 13 May 2014 and subsequent Court approval.

21. Under the proposed Scheme, all eligible Envestra shareholders who hold their Envestra shares on the Record Date (five business days after the Scheme becomes effective), will be entitled to elect to receive either:

- (a) 'All Scrip Consideration' comprising .1919 APA Securities for each Envestra share held, or
- (b) 'Maximum Cash Consideration' of \$1.17 per Envestra share, subject to an aggregate cap of \$241 million.

22. Those Envestra shareholders who elect the Maximum Cash Consideration will have their entitlements scaled back proportionately to the extent that the \$241 million aggregate cap would otherwise be exceeded, with the balance of their consideration comprising an entitlement to APA Securities.

23. The APA Securities offered as consideration will rank equally with all other APA Securities on issue.

24. Subject to the Scheme's approval, the Scheme Implementation Date is expected to occur within the financial year ending 30 June 2014.

25. Should the Scheme Implementation Date be delayed past 30 June 2014, the Scrip Consideration per Envestra Share and the Cash Consideration per Envestra share may be adjusted under the terms of the Scheme in the event that Envestra's 2014 year final dividend is greater or lesser than 0.1919 of APA Group's 2014 year final distribution.

Other matters

26. Envestra shareholders as at 21 March 2014 were entitled to receive the Envestra 2014 year interim dividend of 3.2 cents per share paid on 30 April 2014, whether the Scheme is implemented or not.

27. The Constitutions of APT and APTIT require that APA Securities be issued at the 'Market Price', being the market value determined as the weighted average traded price for ten business days prior to the issue.

28. Envestra, the Envestra shareholders and APT have dealt with each other at arm's length at all times in respect of the Scheme of Arrangement.

29. Just prior to entering into the Scheme of Arrangement, neither APA nor Envestra had a concentrated ownership of the nature described in section 124-810.

Ruling

CGT event A1 will happen on the disposal of Envestra Shares

30. CGT event A1 will happen when the Envestra shareholders dispose of their Envestra shares to APT on the Scheme Implementation Date (the fifth business day after the Record Date) (subsections 104-10(1) and 104-10(2) and paragraph 104-10(3)(b)).

Capital gain or capital loss

31. An Envestra shareholder will make a capital gain when CGT event A1 happens if the capital proceeds from the disposal of an Envestra share exceed its cost base. The capital gain is the amount of the excess. An Envestra shareholder will make a capital loss if those capital proceeds are less than the reduced cost base of the Envestra share. The capital loss is the amount of the difference (subsection 104-10(4)).

Capital proceeds

32. For an Envestra shareholder, the capital proceeds for each Envestra share will be the market value of the APA Securities received, worked out as at the time that CGT event A1 happens (subsection 116-20(1), and, if relevant, the amount of any cash consideration received.

33. The market value of an APA Security will be determined based on the 10 day weighted average traded price of APA Securities (10 day VWAP) immediately prior to the issue date.

Interim distribution

34. The Envestra 2014 year interim dividend of 3.2 cents per share received by Envestra shareholders on 30 April 2014 will not be capital proceeds from the disposal of an Envestra share to APT, as it is considered, having regard to all the circumstances of the arrangement, that it was not paid in respect of a CGT event happening.

If a capital gain is made

Availability of partial scrip for scrip roll-over

35. Each APA Security comprises two separate CGT assets: a unit in APT and a unit in APTIT (section 108-5). For the purposes of section 124-790:

- (a) The APT unit component of each APA Security is eligible proceeds, and
- (b) The APTIT unit component of each APA Security is ineligible proceeds.

36. Subject to the qualification in paragraph 37, an Envestra shareholder who makes a capital gain from the disposal of an Envestra share may choose partial scrip for scrip roll-over under subsection 124-790(1).

37. Scrip for scrip roll-over cannot be chosen if any capital gain the Envestra shareholder makes from the replacement APT units would be disregarded, except because of a roll-over (subsection 124-795(2)).

If scrip for scrip roll-over is chosen

38. If an Envestra shareholder chooses scrip for scrip roll-over, the capital gain made from the disposal of an Envestra share is disregarded to the extent the Envestra shareholder received replacement APT units for the disposal of the Envestra share (eligible proceeds) (subsection 124-785(1)).

39. The capital gain is not disregarded to the extent that the Envestra shareholder received APTIT units or cash for the disposal of the Envestra share (ineligible proceeds) (124-790(1)).

If scrip for scrip roll-over is not chosen, or cannot be chosen

40. An Envestra shareholder who does not, or cannot, choose scrip for scrip roll-over must take any capital gain or capital loss from the disposal of their shares into account in working out their net capital gain or net capital loss for the income year (sections 102-5 and 102-10).

Cost base of APT units

If scrip for scrip roll-over is chosen

41. Where scrip for scrip roll-over is chosen, the first element of the cost base and reduced cost base of each APT unit received is equal to that part of the cost base of the Envestra shares reasonably attributable to the APT units received (subsection 124-785(2) or (4)).

42. In order to calculate the cost base of an APT unit, the Envestra shareholders must reduce the cost base of their Envestra shares by so much of the cost base as is reasonably attributable to an ineligible part (subsection 124-785(3)), being the market value of the APTIT units, and cash. A reasonable apportionment of the cost base may be made by reference to the NTA split for the APT and APTIT units most recently published by the APA Group before the Scheme Implementation Date.

If scrip for scrip roll-over is not chosen

43. Where scrip for scrip is not chosen, the first element of the cost base and reduced cost base of each APT unit received is equal to that part of the market value of the Envestra shares reasonably attributable to the APT units at the time of their acquisition (paragraph 110-25(2)(b) and subsections 110-55(2) and 112-30(1)). The amount reasonably attributable to the APT units may be determined based upon the most recently published NTA split prior to the Scheme Implementation Date.

Acquisition date of APA securities

44. The Envestra shareholders who choose scrip for scrip roll-over are taken to have acquired the APT units when they originally acquired their Envestra shares that were exchanged for the relevant APT units (Item 2 of the table in subsection 115-30(1)).

45. Envestra shareholders who do not, or are unable, to choose scrip for scrip roll-over are deemed to acquire the APT units when they dispose of their Envestra shares on the Scheme Implementation Date.

Commissioner of Taxation

7 May 2014

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.*

Availability of scrip for scrip roll-over

46. The significant tax consequence that is the subject of this Ruling is the availability of scrip for scrip roll-over under Subdivision 124-M. It enables a shareholder to disregard a capital gain from a share that is disposed of as part of a takeover or merger if the shareholder receives a replacement share in the exchange. It also provides special rules for calculating the cost base and reduced cost base of the replacement share.

47. Subdivision 124-M contains a number of conditions for, and exceptions to, a shareholder being eligible to choose partial scrip for scrip roll-over. One of the conditions relevant to the present Scheme is that shares in a company are exchanged for shares in another company.

48. In the present case, APT is a public trading trust under Division 6C of the ITAA 1936 and has made a choice under section 703-50 to form an income tax consolidated group. The effect of the choice by APT is that, generally, 'this Act', as defined in subsection 995-1(1), applies to APT in a way corresponding to the way in which the Act applies to a company. One application of the Act in this way is to treat the units in APT as analogous to shares in a company (see Note 2 to subsection 713-135(1)). On this basis, the APT units will be the replacement interest.

49. Accordingly, this condition is satisfied to the extent that the Envestra shareholders receive APT units in exchange for their Envestra shares. Scrip for scrip roll-over will not be available to the extent that the Envestra shareholders receive APTIT units or cash consideration in exchange for their Envestra shares.

50. The other main conditions for, and exceptions to, that are relevant to the present scheme are:

- the exchange occurs as part of a single arrangement
- conditions for roll-over are satisfied
- further conditions are not applicable or are satisfied, and
- exceptions to the availability of scrip for scrip roll-over are not applicable.

51. Under the Scheme that is the subject of this Ruling, the conditions for partial roll-over under Subdivision 124-M are satisfied.

APA Security

52. Although the APA Security is a stapled security, it comprises two separate and distinct CGT assets for Australian income tax purposes (section 108-5). It consists of a unit in APT and a unit in APTIT.

53. The respective cost bases and reduced cost bases of these CGT assets need to be worked out separately. The first element of the cost base and reduced cost base of each CGT asset is that part of the expenditure that is reasonably attributable to the acquisition of the asset (subsection 112-30(1)).

54. The Commissioner accepts that a reasonable method of apportionment of the first element of the cost base and reduced cost base of the respective APT and APTIT units should be based on the relative NTA of each entity, given it is an entity whose principle operating activity is infrastructure based.

55. Provided the Scheme Implementation Date is before 30 June 2014, the most recent NTA split will date from 31 December 2013. Based on historical NTA splits for the preceding five years, the Commissioner considers the NTA split to be non-volatile and appropriate to use despite the amount of time between its determination and the Scheme Implementation Date. Should the Scheme Implementation Date not occur before 30 June 2014, then the Commissioner will accept the most recently published NTA split as appropriate to use in the circumstances.

Examples**Example 1: Shareholder chooses the All Scrip Consideration**

56. A shareholder acquired ordinary class Envestra shares in February 2010. At the Scheme Implementation Date, the shareholder received all scrip consideration of APA Securities. As the shareholder would (in the absence of scrip for scrip roll-over) make a capital gain, they can choose for scrip for scrip roll-over to apply.

57. The APTIT units are ineligible proceeds.

Calculation of capital gain attributable to the ineligible proceeds

The capital gain from the APTIT units component of the consideration is determined as follows:

$$\begin{aligned} \text{Ineligible proceeds} &= \text{total proceeds} \times \text{NTA split of APTIT units} \\ &= (\text{number of APA Securities} \times 10 \text{ day VWAP of APA Securities}) \times \text{NTA split of APTIT units} \end{aligned}$$

$$\begin{aligned} \text{Cost base of} \\ \text{ineligible proceeds} &= \text{cost base of Envestra shares} \times \text{NTA split of APTIT units} \end{aligned}$$

Capital gain = *ineligible proceeds - cost base of ineligible proceeds*

Calculation of capital gain subject to scrip for scrip roll-over

Eligible proceeds = *Total proceeds x NTA split of APT units*
 = *(number of APA Securities x 10 day VWAP of APA Securities) x NTA split of APT units*

Cost base of eligible proceeds = *cost base of Envestra shares x NTA split of APT units*

Capital gain (roll-over) = *eligible proceeds - cost base of eligible proceeds*

Calculation of cost base of APT units

The first element of the cost base of each of the shareholder's APT units is determined as follows:

First element of cost base of each APT unit =
$$\frac{\text{cost base of Envestra shares} - \text{cost base of ineligible proceeds}}{\text{number of APT units}}$$

Example 2: Shareholder chooses the Maximum Cash Consideration

58. A shareholder acquires ordinary class Envestra shares in February 2010. The shareholder elected to receive the Maximum Cash Consideration. At the Scheme Implementation Date, as the aggregate cap would otherwise be exceeded, the shareholder received consideration of cash and APA Securities. As the shareholder would (in the absence of scrip for scrip roll-over) make a capital gain, they can choose for scrip for scrip roll-over to apply.

59. The cash component and the APTIT units are ineligible proceeds.

Calculation of capital gain attributable to the ineligible proceeds

The capital gain from the APTIT units component of the consideration is determined as follows:

Scrip proceeds = *number of APA Securities x 10 day VWAP*

Ineligible scrip proceeds = *scrip proceeds x NTA split of APTIT units*

Total ineligible proceeds = *ineligible scrip proceeds + cash*

$$\text{Total proceeds} = \text{scrip proceeds} + \text{cash}$$

$$\text{Cost base of ineligible proceeds} = \text{cost base of Envestra shares} \times \frac{\text{ineligible proceeds}}{\text{total proceeds}}$$

$$\text{Capital gain (no roll-over)} = \text{Total ineligible proceeds} - \text{cost base of ineligible proceeds}$$

Calculation of capital gain subject to scrip for scrip roll-over

$$\text{Eligible proceeds} = \text{scrip proceeds} \times \text{NTA split of APT units}$$

$$\text{Cost base of eligible proceeds} = \text{cost base of Envestra shares} - \text{cost base of ineligible proceeds}$$

$$\text{Capital gain (roll-over)} = \text{eligible proceeds} - \text{cost base of eligible proceeds}$$

Calculation of cost base of APT units

The first element of the cost base of each of the shareholder's APT units is determined as follows:

$$\text{First element of cost base of each APT unit} = \frac{\text{Cost base of Envestra shares} - \text{cost base of ineligible proceeds}}{\text{Number of APT units}}$$

Appendix 2 – Detailed contents list

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

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References

Previous draft:

Not previously issued as a draft

Related Rulings/Determinations:

TR 2006/10

Subject references:

- arrangement
- capital gain
- CGT event A1 – disposal of a CGT asset
- disposal of assets
- partial scrip for scrip roll-over
- scrip for scrip roll-over
- stapled security
- unit trust

Legislative references:

- ITAA 1936
- ITAA 1936 6(1)
- ITAA 1936 Div 6C
- ITAA 1997
- ITAA 1997 102-5
- ITAA 1997 102-10
- ITAA 1997 104-10(1)
- ITAA 1997 104-10(2)
- ITAA 1997 104-10(3)(b)
- ITAA 1997 104-10(4)
- ITAA 1997 108-5
- ITAA 1997 115-30
- ITAA 1997 112-30(1)
- ITAA 1997 115-30(1)
- ITAA 1997 116-20(1)
- ITAA 1997 124-785
- ITAA 1997 124-785(1)
- ITAA 1997 124-785(2)
- ITAA 1997 124-785(3)
- ITAA 1997 124-785(4)
- ITAA 1997 124-790(1)
- ITAA 1997 124-795(2)
- ITAA 1997 703-50
- ITAA 1997 713-135(1)
- ITAA 1997 995-1
- TAA 1953
- Copyright Act 1968
- Corporations Act 2001 Pt 5.1

ATO references

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