


CR 2019/5 - Income tax: BHP Group Limited - off-market share buy-back

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Class Ruling

Income tax: BHP Group Limited – off-market share buy-back

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

This publication (excluding appendices) 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 44(1) of the *Income Tax Assessment Act 1936* (ITAA 1936)
- section 45A of the ITAA 1936
- section 45B of the ITAA 1936
- section 45C of the ITAA 1936
- section 90 of the ITAA 1936
- subsection 95(1) of the ITAA 1936
- paragraph 128B(3)(ga) of the ITAA 1936
- Division 16K of the ITAA 1936
- section 159GZZZK of the ITAA 1936
- section 159GZZZP of the ITAA 1936

- section 159GZZZQ of the ITAA 1936
- Division 1A of former Part IIIAA of the ITAA 1936
- section 177EA of the ITAA 1936
- section 6-5 of the *Income Tax Assessment Act 1997* (ITAA 1997)
- Division 67 of the ITAA 1997
- section 67-25 of the ITAA 1997
- section 104-10 of the ITAA 1997
- subsection 104-165(3) of the ITAA 1997
- subsection 106-5(2) of the ITAA 1997
- section 116-20 of the ITAA 1997
- section 118-20 of the ITAA 1997
- section 118-25 of the ITAA 1997
- section 202-5 of the ITAA 1997
- section 202-40 of the ITAA 1997
- paragraph 202-45(c) of the ITAA 1997
- section 204-30 of the ITAA 1997
- Division 207 of the ITAA 1997
- Subdivision 207-B of the ITAA 1997
- section 207-20 of the ITAA 1997
- section 207-35 of the ITAA 1997
- section 207-45 of the ITAA 1997
- section 207-145 of the ITAA 1997
- Division 230 of the ITAA 1997
- section 855-10 of the ITAA 1997
- section 855-15 of the ITAA 1997.

All legislative references in this Ruling are to the ITAA 1936 or the ITAA 1997, unless otherwise stated.

Class of entities

3. The class of entities to which this Ruling applies is the ordinary shareholders of BHP Group Limited (BHP) who:

- disposed of their ordinary shares in BHP under the off-market share buy-back (the 'Buy-Back') which was announced by BHP on 1 November 2018 and which is described in paragraphs 8 to 27 of this Ruling, and

- are not subject to the taxation of financial arrangements rules in Division 230 in relation to gains and losses on their BHP shares.

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

In this Ruling, these ordinary shareholders of BHP are referred to as 'Participating Shareholders'.

Qualifications

4. 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 27 of this Ruling.

5. 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.

6. This Ruling does not address the income tax consequences of the Special Dividend.

Date of effect

7. This Ruling applies from 1 July 2018 to 30 June 2019. The Ruling continues to apply after 30 June 2019 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

8. The following description of the scheme is based on information provided by the applicant.

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

9. BHP is a public company listed on the Australian Securities Exchange (ASX). BHP is in a dual listed company arrangement with BHP Group Plc (Plc) (both the 'BHP Group').

10. As at 30 June 2018, BHP's Share Capital comprised of 3,211.6 million fully paid ordinary shares. The financial statements of BHP as at 30 June 2018 show total share capital of US\$898 million, reserves of US\$182 million and retained profits of US\$52,568 million.

11. The shareholders in BHP are a mix of individuals, companies and superannuation funds, some of whom are non-residents.

12. On 1 November 2018 (First Announcement Date), the BHP Group announced its intention to:

- undertake an off-market share buy-back of BHP ordinary shares, and
- subsequently pay a Special Dividend to ordinary shareholders of BHP and Plc.

BHP announced it was targeting the repurchase of US\$5.2 billion of shares. However, BHP reserved the right to buy back any number of shares, or to not buy back any shares.

13. The BHP Group proposed the Buy-Back and Special Dividend following the sale of its Onshore US oil and gas assets. Under the BHP Group's Capital Allocation Framework, the proceeds represented surplus funds to dividend and capital investment requirements having regard to current and foreseeable capital investment requirements and dividend payments.

14. The Buy-Back was conducted through a tender process during a specified tender period and was open to all eligible shareholders, who were registered as such on 7 November 2018 (Record Date) for the Buy-Back, except for:

- shares held under a BHP employee equity program where as at the Record Date, the holder is not entitled to sell those shares into the Buy-Back or where the shares are subject to forfeiture under the terms of that employee equity program
- shareholders whose ordinary shares were acquired on an ex-entitlement basis on or after the Ex-entitlement Date (6 November 2018)
- certain non-residents described as 'Excluded Foreign Persons' which includes US and Canadian resident shareholders that were not able to participate in the Buy-Back, and
- holders of American Depositary Receipts representing BHP shares.

15. Participation in the Buy-Back was voluntary. Any BHP shareholder who did not wish to participate was not required to do anything. Non-Participating Shareholders would not receive any

property, dividends or distributions by way of compensation for not participating in the Buy-Back.

16. The tender period opened on 19 November 2018 (Opening Date) and closed on 14 December 2018 (Closing Date).

17. Under the tender process, eligible shareholders were entitled to offer to sell some or all of their ordinary shares to BHP at specified discount percentages (Tender Discount) to the volume weighted average price (VWAP) of BHP ordinary shares sold on the ASX over the five trading days up to and including the Closing Date. The Tender Discount ranged from 10% to 14%, in 1% intervals. Eligible shareholders also had the option of offering to sell different parcels of shares at different Tender Discounts, or at the Final Price Tender which was the price that would ultimately be determined under the tender process as the Buy-Back Price.

18. In addition, eligible shareholders had the option of making their Tender conditional on the Buy-Back Price being no less than one of the four specified Minimum Prices available to them on their Tender Form.

19. Eligible shareholders who held 165 ordinary shares or less, and who wished to participate in the Buy-Back, were required to submit one Tender only in respect of all of their shares at one of the specified Tender Discounts, or as a Final Price Tender.

20. BHP would not accept:

- Tenders at a Tender Discount percentage less than the discount percentage determined by BHP (Buy-Back Discount), and
- those Tenders where the Minimum Price specified was greater than the Buy-Back Price.

21. BHP would accept:

- Tenders at a Tender Discount equal to or greater than the Buy-Back Discount, or
- at the Final Price Tender (subject to any specified minimum price and scale back).

22. Where the number of shares tendered that satisfied the Buy-Back criteria exceeded the number of shares BHP determined to buy back, shareholders with tenders equal to the accepted discount percentage (including Final Price Tenders) were scaled back on a pro-rata basis. A Priority Allocation of 165 shares was bought back from each successful tendering shareholder before the scale back was applied.

23. Notwithstanding the scale back, any shareholder who tendered all of their shares at or below the Buy-Back Price, or as a Final Price Tender, and would have 65 or fewer shares as a result of the scale back (or such other number as BHP would determine), would have all of the shares they tendered bought back in full.

24. The Buy-Back Price was subject to two overriding limits:
- (a) BHP would not Buy-Back shares at a discount greater than 14% to the VWAP of BHP shares over the five trading days up to and including the closing day of the tender period (14 December 2018), and
 - (b) the Buy-Back Price would not exceed the market value of BHP shares determined in accordance with Taxation Determination TD 2004/22 *Income tax: for Off-Market Share Buy-Backs of listed shares, whether the buy-back price is set by tender process or not, what is the market value of the share for the purposes of subsection 159GZZZQ(2) of the Income Tax Assessment Act 1936?* (TD 2004/22).
25. On 17 December 2018 BHP announced that:
- it had successfully completed the Buy-Back of approximately 265.8 million BHP shares, representing 8.3 per cent of the issued capital of BHP
 - the total amount of the Buy-Back Price for shares repurchased under the Buy-Back was approximately \$7.3 billion.
 - the actual Buy-Back Price was set at \$27.64 per share, representing a discount of 14% to the VWAP of BHP shares of \$32.1387 over the five days up to and including 14 December 2018 (the closing date)
 - tenders at a discount of 14% or as a Final Price Tender were successful, subject to any minimum price condition and scale back
 - tenders at discounts from 10% to 13% were not accepted, and
 - due to the significant oversubscription for the Buy-Back, a 58.7% scale-back of Tenders was required.
26. All shares bought back under the Buy-Back were cancelled.
27. Under the Buy-Back, \$0.38 per share was debited to BHP's untainted share capital account, and the balance of the Buy-Back Price was debited to BHP's retained earnings.

Ruling

Off-market purchase

28. For the purposes of Division 16K, the Buy-Back is an off-market purchase within the meaning given by paragraph 159GZZZK(d).

The Dividend Component

29. Participating Shareholders are taken to have been paid a dividend of \$27.26 (the Dividend Component) on 17 December 2018 for each share bought back under section 159GZZZP.

30. The Dividend Component is a frankable distribution pursuant to section 202-40, and is capable of being franked in accordance with section 202-5.

31. The difference between the Buy-Back Price and the Dividend Component is not a dividend for income tax purposes (subsection 159GZZZP(2)).

Assessability of the Dividend Component and tax offset***Direct distributions***

32. The Dividend Component of \$27.26 per share and, subject to the shareholder being a 'qualified person', the amount of the franking credit on the Dividend Component is included in the assessable income of Australian resident individual and corporate shareholders and trustees of resident complying superannuation funds, who participated in the Buy-Back in the income year in which the Buy-Back occurred (subsection 44(1) and subsection 207-20(1)).

33. Participating Shareholders will be entitled to a tax offset under subsection 207-20(2) equal to the amount of the franking credit attached to the Dividend Component, subject to being a 'qualified person'.

Indirect distributions***Partnerships***

34. The Dividend Component of \$27.26 per share and, subject to being a qualified person, the amount of the franking credit attached to the Dividend Component, is included in the assessable income of a Participating Shareholder that is a partnership for the purposes of calculating the net income of the partnership pursuant to section 90.

Trusts

35. The Dividend Component of \$27.26 per share and, subject to being a qualified person, the amount of the franking credit attached to the Dividend Component is included in the assessable income of a Participating Shareholder that is a trustee of a trust for the purposes of determining the net income of the trust pursuant to subsection 95(1).

Partners and Beneficiaries

36. Subsections 207-35(3) to (6) set out the circumstances in which a partner or beneficiary to whom a franked distribution flows indirectly is required to gross up their assessable income for their share of the franking credit on the franked distribution. Where the franked distribution flows indirectly (within the meaning of Subdivision 207-B) through a trust or partnership to a resident that is an individual, a corporate tax entity (at the time the distribution flows indirectly to it) or a trustee mentioned in paragraphs 207-45(c), (ca) or (d), the entity will, subject to the qualified person rule, be entitled to a tax offset equal to the entity's share of the franking credit on the franked distribution (section 207-45).

Refundable tax offset

37. The tax offsets are subject to the refundable tax offset rules in Division 67. Certain trustees and corporate tax entities are not entitled to the refundable tax offset rules in accordance with subsections 67-25(1A) to (1DA).

Non-resident Participating Shareholders

38. As the Dividend Component is fully franked, non-resident Participating Shareholders are not liable to Australian withholding tax in respect of the Dividend Component (paragraph 128B(3)(ga)).

Sale Consideration

39. A Participating Shareholder is taken to have received \$4.92 per share as consideration in respect of each share bought back under the Buy-Back (Sale Consideration) on 17 December 2018 in accordance with section 159GZZZQ, unless the Participating Shareholder is a corporate tax entity to which subsections 159GZZZQ(8) and (9) apply.

40. If the Buy-Back Price for each share bought back under the Buy-Back was less than what would have been the market value of the share if the Buy-Back did not occur and was never proposed to occur, then the market value rule in subsection 159GZZZQ(2) applies to the Buy-Back. TD 2004/22 outlines the Commissioner's approach for determining what would have been the market value of the share at the time of the Buy-Back if the Buy-Back did not occur and was never proposed to occur for the purposes of subsection 159GZZZQ(2).

41. The effect of the rule is that if the Buy-Back Price is less than the market value, which is determined in accordance with TD 2004/22, the difference is included in the consideration received for the disposal of the share, in addition to the amount of \$0.38 per share debited to BHP's share capital account. Accordingly, the Sale Consideration is \$4.92 per share.

42. The treatment of the Sale Consideration will depend on whether the sale is on capital account or on revenue account.

Shares held on capital account

43. The shares are taken to have been disposed of for CGT purposes on 17 December 2018 pursuant to section 104-10 (CGT event A1).

44. The Sale Consideration of \$4.92 per share represents the capital proceeds for CGT purposes pursuant to section 116-20. A Participating Shareholder (other than a partnership) will make a capital gain on a share if the Sale Consideration per share exceeds the cost base of that share. The capital gain is the amount of the excess. Similarly, a Participating Shareholder (other than a partnership) will make a capital loss on a share if the Sale Consideration per share is less than the reduced cost base of the share (subsection 104-10(4)).

45. Each partner in a partnership has a separate cost base and reduced cost base for the partner's interest in each BHP share sold into the Buy-Back by the partnership (subsection 106-5(2)). Each partner is allocated an appropriate share of the Sale Consideration received by the partnership for the disposal of BHP shares into the Buy-Back.

Shares held on revenue account

46. Where shares were held as trading stock, the Sale Consideration of \$4.92 per share is included in assessable income pursuant to section 6-5. Participating Shareholders (other than partnerships) that held shares as trading stock also made a capital gain or capital loss calculated as discussed at paragraphs 43 and 44 of this Ruling. However, under section 118-25, any capital gain or capital loss the Participating Shareholders made is disregarded if at the time of the CGT event the shares were held as trading stock. There is a similar exemption for partners in partnerships (paragraph 118-25(1)(b)).

47. Where shares were held as revenue assets (as defined in section 977-50), but were not trading stock, the amount by which the Sale Consideration of \$4.92 per share exceeds the cost of each share is included in the Participating Shareholder's assessable income. Correspondingly, if the cost of each share exceeds the Sale Consideration of \$4.92 per share the difference is an allowable deduction. Where the Sale Consideration per share exceeds the cost base of that share, the Participating Shareholders (other than partnerships) will also make a capital gain. However, under section 118-20, any capital gain the Participating Shareholders make will be reduced if, because of the event, an amount is otherwise included in assessable income. The capital gain will be reduced to zero if the capital gain does not exceed the amount otherwise included in assessable income (subsection 118-20(2)). If the capital gain exceeds

the amount otherwise included in assessable income, the capital gain will be reduced by the amount otherwise included in assessable income (subsection 118-20(3)). There is a similar reduction for partners in partnerships (paragraphs 118-20(1)(b) and 118-20(2)(b), and subsection 118-20(3)).

Foreign resident Participating Shareholders: CGT consequences

48. Under section 855-10, Participating Shareholders that are foreign residents will only have CGT consequences if the shares purchased under the Buy-Back are 'taxable Australian property'.

Qualified persons

49. For the purposes of paragraph 207-145(1)(a) which refers to Division 1A of former Part IIIAA, a Participating Shareholder will be considered to satisfy the holding period rule under former section 160APHO, and be a qualified person (as long as the related payments rule is also met) in relation to the Dividend Component received under the Buy-Back, if:

- the shares sold into the Buy-Back were acquired on or before 1 November 2018, and
- during the period when the shares were held, the Participating Shareholder had sufficient risks of loss or opportunities for gain in respect of the shares (as defined in former section 160APHM) for a continuous period of at least 45 days. Neither the announcement of the Buy-Back, the making of an invitation to shareholders to offer to sell their BHP shares nor the making of an offer by a shareholder to BHP in respect of a BHP share will affect whether the shares bought back under the Buy-Back are held 'at risk' for the purposes of Division 1A of former Part IIIAA.

50. The 'last-in first-out' rule in former subsection 160APHI(4):

- applies for the purposes of the Buy-Back in respect of BHP shares acquired during the period 2-5 November 2018 inclusive which conferred an entitlement to participate in the Buy-Back, and
- has no effect for the purposes of the Buy-Back in respect of BHP shares acquired on or after 6 November 2018 (the Ex-entitlement Date) which did not confer an entitlement to participate in the Buy-Back.

The anti-avoidance provisions

51. The Commissioner will not make a determination under subsections 45A(2) or 45B(3) that section 45C applies to the whole,

or any part, of the Capital Component of the Buy-Back Price received by Participating Shareholders.

52. The Commissioner will not make a determination under paragraph 177EA(5)(b) to deny the whole, or any part, of the imputation benefits received in relation to the Dividend Component of the Buy-Back Price by Participating Shareholders.

53. The Commissioner will not make a determination under paragraph 204-30(3)(c) to deny the whole, or any part, of the imputation benefits received in relation to the Dividend Component of the Buy-Back Price by Participating Shareholders.

Commissioner of Taxation

16 January 2019

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.*

Off-market purchase

54. For the purposes of Division 16K, where a company buys a share in itself from a shareholder, the purchase is a ‘buy-back’ (paragraph 159GZZZK(a)).

55. Division 16K categorises a buy-back as either an ‘on-market purchase’ or an ‘off-market purchase’.

56. A buy-back is an on-market purchase if the share bought back is listed for quotation in the official list of a stock exchange in Australia or elsewhere, and the buy-back is made in the ordinary course of trading on that stock exchange (paragraph 159GZZZK(c)). A buy-back that is not an on-market purchase is an off-market purchase (paragraph 159GZZZK(d)).

57. Although BHP’s ordinary shares are listed for quotation in the official list of the ASX, the Buy-Back was not made in the ordinary course of trading on the ASX. As a result, for the purposes of Division 16K, the Buy-Back is an off-market purchase within the meaning given by paragraph 159GZZZK(d).

The Dividend and Capital Components

58. The Buy-Back Price received by Participating Shareholders comprises two components:

- a Dividend Component, and
- a Capital Component.

59. The amount of each of these components is determined in accordance with sections 159GZZZP and 159GZZZQ, and has regard to how BHP accounted for the Buy-Back.

The Dividend Component

60. Section 159GZZZP provides that where the buy-back of a share is an off-market purchase, the difference between the purchase price and the part (if any) of the purchase price which is debited against amounts standing to the credit of the company’s share capital account is taken to be a dividend paid by the company to the seller on the day the buy-back occurred. The Buy-Back occurred on 17 December 2018.

61. The Buy-Back Price was \$27.64 per share, of which \$0.38 (the Capital Component) was debited against the amounts standing

to the credit of BHP's share capital account. As a result, the Dividend Component is taken to be \$27.26 per share.

62. The Dividend Component of \$27.26 per share is frankable, but only to the extent that the Buy-Back Price does not exceed the market value of a BHP share at the time of the Buy-Back if the buy-back did not occur and was never proposed to occur (paragraph 202-45(c)).

63. TD 2004/22 sets out the Commissioner's view as to how to determine what would have been the market value of a BHP share at the time of the Buy-Back if the buy-back did not occur and was never proposed to occur. In respect of the Buy-Back, the Buy-Back Price per share did not exceed the market value determined in accordance with TD 2004/22. As a result, the entire Dividend Component is frankable.

Assessability of the Dividend Component and tax offset

Direct distributions

64. For Participating Shareholders who are Australian residents (other than a partnership or a trust) and who directly received the Dividend Component:

- the Dividend Component is included in the assessable income of each Participating Shareholder under subsection 44(1), and
- subject to the 'qualified person' rule, the amount of the franking credit on the Dividend Component is included in the assessable income of each Participating Shareholder under subsection 207-20(1).

65. Subject to the 'qualified person' rule, these Participating Shareholders are entitled to a tax offset under subsection 207-20(2) equal to the amount of the franking credit on the Dividend Component.

Indirect distributions

Partnerships

66. Pursuant to subsection 44(1), the Dividend Component is included in the assessable income of the partnership for the purposes of computing the net income of the partnership under section 90.

67. Subject to the 'qualified person' rule, pursuant to subsection 207-35(1), the amount of the franking credit on the Dividend Component is included in the assessable income of the partnership for the purposes of calculating the net income of the partnership under section 90.

Trusts

68. Pursuant to subsection 44(1), the Dividend Component is included in the assessable income of the trustee for the purposes of calculating the net income of the trust under subsection 95(1).

69. Subject to the 'qualified person' rule, pursuant to subsection 207-35(1), the amount of the franking credit on the Dividend Component is included in the assessable income of the trustee for the purposes of calculating the net income of the trust under subsection 95(1).

Partners and Beneficiaries

70. Subsections 207-35(3) to (6) set out the circumstances in which a partner or beneficiary to whom a franked distribution flows indirectly is required to gross up their assessable income for their share of the franking credit on the franked distribution. Where the franked distribution flows indirectly (within the meaning of Subdivision 207-B) through a trust or partnership to a resident that is an individual, a corporate tax entity (at the time the distribution flows directly to it) or a trustee mentioned in paragraphs 207-45(c), (ca) or (d), the entity will, subject to the qualified person rule, be entitled to a tax offset equal to the entity's share of the franking credit on the franked distribution (section 207-45).

Refundable tax offset

71. The tax offsets are subject to the refundable tax offset rules in Division 67, provided the offsets are not excluded from the refundable tax offset rules pursuant to subsections 67-25(1A) to (1DA).

Non-resident Participating Shareholders

72. As the Dividend Component of the Buy-Back Price is fully franked, and no determination will be made in respect of the Dividend Component under either paragraph 204-30(3)(c) or paragraph 177EA(5)(b), a non-resident Participating Shareholder is not liable to Australian withholding tax on the Dividend Component (paragraph 128B(3)(ga)).

The Capital Component

Calculation of Sale Consideration

73. For the purposes of determining the amount of a gain or loss (for BHP shares held on capital account or on revenue account), the consideration received by a Participating Shareholder in respect of the disposal of a share (the Sale Consideration) under the Buy-Back is determined in accordance with section 159GZZZQ. The effect of section 159GZZZQ is to adjust the Capital Component in order to

determine the Sale Consideration for CGT or revenue account treatment.

74. Subsection 159GZZZQ(1) provides that a shareholder is taken to have received an amount equal to the purchase price (in this case the Buy-Back Price of \$27.64 received for each BHP share bought back) as consideration in respect of the sale of the share bought back. However, this amount is subject to certain adjustments in order to arrive at the Sale Consideration.

75. Subsection 159GZZZQ(2) is one of the adjusting provisions. It provides that if the purchase price is less than the market value of the share at the time of the buy-back (calculated as if the buy-back did not occur and was never proposed to occur) the shareholder is taken to have received an amount equal to the market value of the share as consideration in respect of the sale of the share bought back.

76. For the purposes of determining the application of subsection 159GZZZQ(2), BHP proposed the following methodology as outlined in TD 2004/22 (which the Commissioner accepted): The relevant market value of a BHP share is the VWAP of a BHP share over the last five trading days before the first announcement of the Buy-Back, adjusted for the percentage change in the London Stock Exchange quoted price of Plc shares from the close of trading on the day prior to the First Announcement Date (31 October 2018) to the opening of trading on the Closing Date of the Buy-Back (14 December 2018).

77. Under this methodology, the market value of a BHP share bought back was calculated as \$32.18. As a result, Participating Shareholders are taken to have instead received consideration of \$32.18 for the sale of each BHP share.

78. Pursuant to subsection 159GZZZQ(3), the deemed consideration of \$32.18 is reduced by a 'Reduction Amount'. The Reduction Amount is an amount calculated pursuant to subsection 159GZZZQ(4). In the circumstances of the Buy-Back, the Reduction Amount is equivalent to the Dividend Component of \$27.26, unless a Participating Shareholder is a corporate tax entity to whom subsection 159GZZZQ(8) applies (see paragraph 79 of the Ruling). As a result, the Sale Consideration for each BHP share disposed of under the Buy-Back is \$4.92 (being \$32.18 less \$27.26).

79. However, where a Participating Shareholder is a corporate tax entity which is entitled to a tax offset under Division 207 in respect of the Dividend Component, a further adjustment may be made to the Sale Consideration. Under subsection 159GZZZQ(8), if such a Participating Shareholder would also make either a capital loss or a deductible loss (or any increase in such a loss) in respect of the sale of a BHP share bought back under the Buy-Back, the Sale Consideration is increased by an off-settable amount determined under subsection 159GZZZQ(9). The Reduction Amount (being the Dividend Component) is itself reduced by so much of the off-settable amount that does not exceed the capital loss or the deductible loss.

80. Participating Shareholders are taken to have disposed of their shares accepted under the Buy-Back on 17 December 2018 (CGT event A1). The disposal may have different taxation implications for Participating Shareholders depending on how the shares were held, for instance:

- an investor who held their shares on capital account will be subject to the CGT provisions, and
- a share trader who held their shares on revenue account will be subject to the ordinary income provisions and the CGT provisions.

Shares held on capital account

81. The Sale Consideration of \$4.92 per share (which may be adjusted for shareholders that are corporate tax entities as discussed in paragraph 79 of this Ruling) represents the capital proceeds for CGT purposes pursuant to section 116-20. A Participating Shareholder (other than a partnership) will make a capital gain in respect of the disposal of a share if the Sale Consideration per share exceeds the cost base of the share. The capital gain is the amount of the excess. Similarly, a Participating Shareholder (other than a partnership) will make a capital loss in respect of the disposal of a share if the Sale Consideration per share is less than the reduced cost base of the share (subsection 104-10(4)).

82. Where the Participating Shareholder is a partnership, any capital gain or loss will be made by the partners individually (subsection 106-5(1)). Each partner in a partnership has a separate cost base and reduced cost base for the partner's interest in each BHP share sold into the Buy-Back by the partnership (subsection 106-5(2)). Each partner is allocated an appropriate share of the Sale Consideration received by the partnership for the disposal of BHP shares into the Buy-Back.

Shares held on revenue account

83. Where shares were held as trading stock, the Sale Consideration of \$4.92 per share (which may be adjusted for shareholders that are corporate tax entities as discussed in paragraph 79 of this Ruling) is included in assessable income under section 6-5. Participating Shareholders (other than partnerships) who disposed of shares held as trading stock will also make a capital gain or capital loss. However, as the shares were held as trading stock, the capital gain or loss is disregarded pursuant to section 118-25. There is a similar exemption for partners in partnerships (paragraph 118-25(1)(b)).

84. Where shares were held as revenue assets (as defined in section 977-50), but were not trading stock, the amount by which the Sale Consideration of \$4.92 per share (which may be adjusted for shareholders that are corporate tax entities as discussed in

paragraph 79 of this Ruling) exceeds the cost of each share is included in assessable income. Correspondingly, if the cost exceeds the Sale Consideration of \$4.92 per share, the difference is an allowable deduction. Where the Sale Consideration per share exceeds the cost base of the share, these Participating Shareholders (other than partnerships) will also make a capital gain. However, Participating Shareholders who held their shares as revenue assets other than as trading stock will have the amount of the capital gain reduced under the CGT anti-overlap rule (section 118-20). There is a similar reduction for partners in partnerships (paragraphs 118-20(1)(b) and 118-20(2)(b), and subsection 118-20(3)).

Foreign resident Participating Shareholders: CGT consequences

85. A foreign resident shareholder who participates in the Buy-Back disregards any capital gain or capital loss made in respect of a share bought back under the Buy-Back if the share is not 'taxable Australian property' under the tests in section 855-10. A BHP share that is disposed of in the Buy-Back will constitute taxable Australian property if the share:

- is an indirect Australian real property interest (item 2 of the table in section 855-15)
- was used 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
- is 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 – item 5 of the table in section 855-15).

Qualified persons

86. Paragraph 207-145(1)(a) provides that in relation to a franked dividend made by an entity, only a 'qualified person' in relation to the distribution for the purposes of Division 1A of former Part IIIAA is required to include the franking credit in its assessable income or is entitled to claim the franking credit as a tax offset. Broadly speaking, to be a qualified person in relation to the Dividend Component paid under the Buy-Back, a Participating Shareholder must satisfy both the 'holding period rule' and the 'related payments rule'.

87. Broadly, a Participating Shareholder will not satisfy the related payments rule if the Participating Shareholder, or an associate of the Participating Shareholder, is under an obligation to make, or makes, a payment in respect of the dividend, which effectively passes on the economic benefit of the dividend to another person.

88. The holding period rule requires a shareholder to hold the shares on which the dividend is paid 'at risk' for a continuous period of at least 45 days during the relevant qualification period. In the

absence of a related payment, the relevant qualification period is the primary qualification period, which commences on the day after the shares are acquired and ends on the 45th day after the day on which the shares became ex-dividend. In determining whether a shareholder has satisfied the holding period rule, any days during which there is a materially diminished risk of loss or opportunity for gain in respect of the relevant shares are not counted. The day of acquisition and the day of disposal of the relevant shares are also not counted.

89. Under former subsection 160APHM(2), a shareholder is taken to have materially diminished the risks of loss and opportunities for gain with respect to shares if the 'net position' in respect of the risks of loss and opportunity for gain of the shareholder results in the shareholder having less than 30% of the risks and opportunities relating to the shares.

90. The Commissioner does not regard the announcement of the Buy-Back as affecting whether BHP shares were held at risk or not.

91. There are 45 clear days between 1 November 2018 and 17 December 2018 (the date tender offers were accepted). As a result, a Participating Shareholder who acquired shares on or before 1 November 2018 that were bought back under the Buy-Back satisfies the holding period rule as long as those shares were held at risk for at least 45 continuous days. A Participating Shareholder who acquired shares after 1 November 2018 that were subsequently bought back under the Buy-Back may not be a qualified person in relation to the dividend paid under the Buy-Back for the purposes of Division 1A of former Part IIIAA except in certain circumstances.

92. Generally, under the holding period rule a shareholder will be deemed to have disposed of their most recently acquired shares first (former subsection 160APHI(4)). The 45 day rule operates on a 'last-in first-out' basis, so that shareholders will be deemed to have disposed of their most recently acquired shares first for the purposes of applying the 45 day rule. Accordingly, Participating Shareholders who, after 1 November 2018, acquired any additional BHP shares, which conferred an entitlement to participate in the Buy-Back (during the period 2-5 November 2018 inclusive), will not qualify for the franking credits attached to the dividends paid on some or all of the shares sold into the Buy-Back (except for individual taxpayers qualified as small shareholders (former subsection 160APHT(1))).

93. If instead a Participating Shareholder acquired ex-entitlement BHP shares (from 6 November 2018) and participated in the Buy-Back with cum-entitlement shares (which conferred an entitlement to participate in the Buy-Back), the shareholder will not be considered for the purposes of the 45 day rules to be subject to the last-in first-out rule in former subsection 160APHI(4), and so will not be considered to have participated with the 'ex-entitlement' shares. Ex-entitlement shares do not constitute 'related securities' for the purposes of former subsection 160APHI(2) in relation to any cum-entitlement shares. BHP shares commenced trading on an

ex-entitlement basis on 6 November 2018. Accordingly, for any additional BHP shares that a Participating Shareholder acquired on or after 6 November 2018 on an ex-entitlement basis, the 'last-in first-out' rule in former subsection 160APHI(4) will not apply in relation to those shares.

The anti-avoidance provisions

Sections 45A and 45B

94. Sections 45A and 45B are two anti-avoidance provisions, which if they apply, allow the Commissioner to make a determination that section 45C applies. The effect of such a determination is that all or part of the distribution of capital received by a Participating Shareholder under the Buy-Back is treated as an unfranked dividend. Accordingly, the application of these two provisions to the Buy-Back must be considered.

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

96. Although a 'capital benefit' (as defined in paragraph 45A(3)(b)) is provided to Participating Shareholders under the Buy-Back, the circumstances of the Buy-Back indicate that there is no streaming of capital benefits to some shareholders and dividends to other shareholders. Under the Buy-Back, all Participating Shareholders received a distribution of share capital as well as a Dividend Component in equal proportion based on the number of shares they sold into the Buy-Back. Accordingly, section 45A has no application to the Buy-Back.

97. Section 45B applies where certain capital payments are paid to shareholders in substitution for dividends. In broad terms, section 45B 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 (the 'relevant 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 (whether or not the dominant purpose but not including an incidental purpose), of enabling the relevant taxpayer to obtain a tax benefit (paragraph 45B(2)(c)).

98. While the conditions of paragraphs 45B(2)(a) and (b) were met in respect of the Buy-Back, the requisite purpose of enabling a person to obtain a tax benefit as a result of the capital distribution was not present.

99. Having regard to the 'relevant circumstances' (as set out in subsection 45B(8)) of the Buy-Back, it is apparent that:

- the distribution of share capital of \$0.38 per share accords with average capital per share and could not be said to be attributable to the profits of BHP
- the pattern of distributions of BHP does not indicate that the distribution of share capital of \$0.38 per share reflects amounts in substitution for a dividend
- the Buy-Back is not expected to alter BHP's dividend policy, and
- as a consequence of the Buy-Back, the distribution of share capital resulted in the cancellation of ordinary shares in BHP held by Participating Shareholders and a corresponding loss of dividend, voting and other rights.

100. Accordingly, the Commissioner will not make a determination under subsection 45B(3) that section 45C applies to treat all or part of the distribution of share capital of \$0.38 per share as an unfranked dividend paid by BHP.

Section 177EA

101. Section 177EA is a general anti-avoidance provision that applies to a wide range of schemes designed to obtain imputation benefits. In essence, it applies to schemes for the disposition of shares or an interest in shares, where a franked distribution is paid or payable in respect of the shares or an interest in shares. This would include a buy-back with a franked dividend component.

102. Specifically, subsection 177EA(3) provides that section 177EA applies if:

- (a) there is a scheme for a disposition of membership interests, or an interest in membership interests, in a corporate tax entity; and
- (b) either:
 - (i) a frankable distribution has been paid, or is payable or expected to be payable, to a person in respect of the membership interests; or
 - (ii) a frankable distribution has flowed indirectly, or flows indirectly or is expected to flow indirectly, to a person in respect of the interest in membership interests, as the case may be; and

- (c) the distribution was, or is expected to be, a franked distribution or a distribution franked with an exempting credit; and
- (d) except for this section, the person (the *relevant taxpayer*) would receive, or could reasonably be expected to receive, imputation benefits as a result of the distribution; and
- (e) having regard to the relevant circumstances of the scheme, it would be concluded that the person, or one of the persons, who entered into or carried out the scheme or any part of the scheme did so for a purpose (whether or not the dominant purpose but not including an incidental purpose) of enabling the relevant taxpayer to obtain an imputation benefit.

103. The conditions of paragraphs 177EA(3)(a) to (d) are satisfied in respect of the Buy-Back. Accordingly, the issue is whether, having regard to the relevant circumstances of the scheme, it would be concluded that, on the part of BHP, its shareholders or any other relevant party, there is a more than incidental purpose of conferring an imputation benefit under the scheme. In respect of the Buy-Back, the relevant taxpayer is the Participating Shareholder and the scheme comprises the circumstances surrounding the Buy-Back.

104. 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). The relevant circumstances listed in subsection 177EA(17) encompass a range of circumstances which, taken individually or collectively, could indicate the requisite purpose. Due to the diverse nature of these circumstances some may not be present at any one time in any one scheme.

105. The Commissioner has come to the view that section 177EA applies to the Buy-Back. In coming to this conclusion, the Commissioner had regard to all the relevant circumstances of the arrangement, as outlined in subsection 177EA(17). Among the circumstances of the Buy-Back reflected in those paragraphs is the greater attraction of the Buy-Back to resident shareholders of the franking credits than for non-resident shareholders.

106. Where section 177EA applies, the Commissioner has a discretion pursuant to subsection 177EA(5) to make a determination to debit BHP's franking account pursuant to paragraph 177EA(5)(a), or deny the imputation benefit to each Participating Shareholder pursuant to paragraph 177EA(5)(b). The Commissioner will exercise his discretion in such a way that he will not make a determination that the imputation benefit obtained by Participating Shareholders will be denied under paragraph 177EA(5)(b).

Section 204-30

107. Section 204-30 applies where a corporate tax entity streams the payment of dividends, or the payment of dividends and the giving of other benefits, to its members in such a way that:

- (a) an imputation benefit is, or apart from the section would be, received by a member of the entity as a result of the distribution or distributions (paragraph 204-30(1)(a))
- (b) the member would derive a greater benefit from franking credits than another member of the entity (paragraph 204-30(1)(b)), and
- (c) the other member of the entity will receive lesser imputation benefits, or will not receive any imputation benefits, whether or not the other member receives other benefits (paragraph 204-30(1)(c)).

108. If section 204-30 applies, the Commissioner may make a determination to debit BHP's franking account pursuant to paragraph 204-30(3)(a), and / or to deny the imputation benefit to each Participating Shareholder pursuant to paragraph 204-30(3)(c).

109. For section 204-30 to apply, Participating Shareholders to whom distributions are streamed must derive a greater benefit from franking credits than ordinary shareholders of BHP who do not participate in the Buy-Back. Some of the cases in which a member of an entity 'derives a greater benefit from franking credits' are listed in subsection 204-30(8) by reference to the ability of a member to fully utilise franking credits.

110. A portion of BHP's ordinary shares are held by non-resident shareholders who do not benefit from franking credits to the same extent as resident shareholders. As a result, the conditions in subsection 204-30(1) for section 204-30 to apply are met. However, the Commissioner will not make a determination under subsection 204-30(3).

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