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TAX UPDATE
TAX RULING ON RENOUNCEABLE ENTITLEMENT OFFERS

MAY 2017

The Tax Office has recently released draft Taxation Ruling TR 2017/D3, dealing with rights and retail premiums under a renounceable rights offer for shares. It complements Taxation Ruling TR 2012/1 released 5 years ago on non-renounceable rights.

WHO IS AFFECTED BY THESE RULINGS?

Although procedural and largely confirming industry practice, the rulings provide certainty of treatment and are helpful for companies considering the different tax impacts for shareholders before deciding to undertake an entitlement offer.

KEY TAX OUTCOMES

The key difference between a renounceable entitlement and a non-renounceable entitlement is that any retail premium paid on a renounceable rights may be eligible for the CGT discount, reducing the effective tax rate for individual resident shareholders holding on capital account to 24.5%.

TAX TREATMENT OF VARIOUS EVENTS

The following table summarises the key tax impacts at various stages of the process for both renounceable and non-renounceable entitlements where the shareholder holds the shares on capital account.

A WORD OF CAUTION

The concepts of renounceable and non-renounceable entitlements are based on sample surveys conducted by the Tax Office of such offers (summarised in the first row of the table below). Therefore, your particular offer may not be the same and the rulings may not apply to your circumstances. For example, in our experience, it is unusual for non-renounceable entitlements to carry a retail premium in the way contemplated by TR 2012/1. However, the comments in this article summarise the rulings to describe how the Tax Office would treat certain aspects that might be included in an entitlement offer.

POINTS	RENOUNCEABLE RIGHTS (TR 2017/D3)	NON-RENOUNCEABLE RIGHTS (TR 2012/1)
What are the key features of the types of offers to which the rulings apply?	Eligible shareholders in a company receive an entitlement to be issued shares in the company for a fixed price per share (offer price). Shareholders may exercise the entitlements, sell them (on-market or off-market, including via a bookbuild, depending on the structure of the raising) or do nothing. The entitlements of shareholders who do nothing and those of ineligible shareholders are sold on their behalf in a retail bookbuild (in our experience, this occurs only in an accelerated entitlement offer). Successful bidders in this process may pay a premium (retail premium) above the offer price. The offer price is paid to the company as consideration for the subscription for shares. The premium (if any and after certain costs are deducted) is remitted to the original shareholders who had received (or were ineligible to receive) those entitlements.	Eligible shareholders in a company receive an entitlement to be issued shares in the company for a fixed price per share (offer price). The entitlements are not assignable and cannot otherwise be dealt with. Under a bookbuild (in our experience, in the context of an accelerated non-renounceable offer) which is customarily conducted at the "clearing price", the company may issue shares equal in number to the entitlements of shareholders who do not exercise their entitlements and those of ineligible shareholders. Entitlements are not being dealt with; instead, the company is issuing shares to make up the shortfall created by ineligible shareholders and entitlements not being exercised. The clearing price is paid to and typically retained by the company. Although not usual in our experience, a company may choose to pay the excess of the clearing price over a pre-determined amount (for example, the offer price) set by the company (the excess being the retail premium) to the original shareholders. If the company does pay the retail premium to the shareholders, this ruling applies.
Sale of entitlements (on-market or off-market, including under the bookbuild) – resident shareholders	Taxable gain to the extent that the retail premium exceeds the cost base of the entitlement (generally nominal). CGT discount may be available provided shareholder acquired original shares at least 12 months before disposal of the entitlement. For individual shareholders, this is an effective tax rate of up to 24.5%.	Not applicable.
Sale of entitlements (on-market or off-market, including under the bookbuild) – non-resident shareholders	Taxable event similar to the sale of entitlements for resident shareholders, but unlikely to be able to fully access the CGT discount and may not be taxable in most cases.	Not applicable.
Shareholder receives retail premium	Retail premiums are not dividends or ordinary income.	If the retail premiums are paid by the company to shareholders (uncommon in our experience), they are unfrankable dividends, paid from the share capital account. For resident shareholders, this means an effective tax rate of up to 49%. When paid to non-residents, withholding tax of up to 30% will likely apply.

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