

Agenda for today

- Introduction and outline of discussion paper
- Stakeholder perspectives
 - Karen Phin
 - Vivian Chang
 - John Paterson
- Open forum and panel discussion

Background

- Treasurer announcement 10 October 2006
- Board of Taxation to conduct review
- Extensive consultation
- Report to Government second half of 2007

Terms of reference

- Focus on taxation arrangements
- Law and administrative practices
- Implications for different types of shareholders
- Listed and unlisted companies

Policy objectives

- Efficiency
- Equity
- Simplicity and low compliance costs

Review process

- Targeted consultation with selected stakeholders earlier this year
- Consultation meetings 26 and 31 July 2007
- Submissions to Board by 24 August 2007
- Recommendations to Government later this year

Structure of Discussion Paper

- Introductory chapters (Ch 1 & 2)
- Current arrangements for OMSBB (Ch 3)
- Implication of current arrangements (Ch 4)
- Assessment of current arrangements (Ch 5)

Benefits of OMSBB

- Capital market efficiencies
- Earnings per share
- Timing and flexibility
- Compared with other mechanisms

Disadvantages of OMSBB

- Implications for non-participating shareholders
- Administrative processes
- Revenue implications

Key issues for discussion

- Ability to participate in OMSBB
- Level of discount
- Capital/dividend split
- Administrative processes
- Unlisted companies
- Possible options for change
- Other issues



Off Market Buy Backs: Tax Practitioner's Perspective

Vivian Chang

Off Market Buy Backs

Tax Practitioner's Perspective

From a tax practitioner's perspective

- 4 Briefly – key tax outcomes and drivers
- 4 Comments on change

Off Market Buy Backs

Tax Practitioner's Perspective

Role of Tax in an Off-Market Buy Back Transaction:

- 4 Share buy backs are driven by commercial considerations, being effective capital management
- 4 Tax is an implementation issue:
 - 4 Minimise impact on shareholders
 - 4 Minimise impact on corporate
 - 4 Risk mitigation

Off Market Buy Backs

Tax Practitioner's Perspective

Tax Treatment of an Off Market Buy Back

- 4 Buy backs involve both a disposal of a share and a distribution to the shareholder
- 4 Hence buyback rules need to apply capital gains tax disposal rules and dividend rules to the one payment

Off Market Buy Backs

Tax Practitioner's Perspective

Tax Treatment – Split between Dividend and Disposal Proceeds

4 Dividend amount:

- 4 Amount of the buy back price not debited to share capital is a dividend for tax purposes
- 4 Does not matter what accounting treatment is for the difference
- 4 Can be franked (subject to anti-avoidance rules)

4 Disposal Amount:

- 4 For non-corporate shareholders:
 - 4 Deemed sale consideration = buy back price less deemed dividend amount
 - 4 Gain included in shareholder's assessable income
 - 4 Loss could also arise

Off Market Buy Backs

Tax Practitioner's Perspective

Tax Treatment – Split between Dividend and Disposal Proceeds

Example

4 Assume

- 4 Share bought back for \$10
- 4 \$10 is market value of share
- 4 \$2 is debited to share capital account
- 4 \$8 is debited to retained earnings
- 4 Dividend component is fully franked

4 Deemed dividend component is:

- 4 $\$10 - \2 (dr share capital account) = \$8

4 Sale proceeds (for non-corporate shareholder) is:

- 4 $\$10 - \8 (deemed dividend amount) = \$2

Off Market Buy Backs

Tax Practitioner's Perspective

Shareholder Impact:

- 4 Low-tax Individuals and Superfunds:
 - 4 Receive franked dividend and (excess) imputation credits
 - 4 Plus capital (or revenue) loss (or reduced gain)
- 4 Corporates:
 - 4 Neutral impact on franked dividend
 - 4 Limited capital (or revenue) loss (or reduced gain)
- 4 High-tax Individuals:
 - 4 Top-up tax on franked dividend
 - 4 Possible capital (or revenue) loss (or reduced gain)
- 4 Non-residents (CGT shareholders)
 - 4 No withholding tax on dividend (if fully franked)
 - 4 No gain or loss on disposal

Off Market Buy Backs

Tax Practitioner's Perspective

Other Key Drivers – Tax Safeguards

- 4 ATO Practice Statement
- 4 Market Value of Shares – substitution rule
 - 4 TD 2004/22
- 4 Allocation between capital and dividend
- 4 45-day holding rule
- 4 Benchmark rule

Off Market Buy Backs

Tax Practitioner's Perspective

Anti-Avoidance Measures

- 4 ATO have two measures on dividend franking side
 - 4 Subdivision 204-D: Streaming of dividends
 - 4 Section 177EA: Franking Credit trading
 - 4 Franking Credit – Anti avoidance measures
 - 4 Where "streaming" or "trading" of franking credits, Commissioner can either (or both)
 - 4 Disallow credits for shareholder; or
 - 4 Specify franking debit to company's franking account – standard approach on tender system
- 4 ATO have measures on the capital side
 - 4 Sections 45A and 45B

Off Market Buy Backs

Tax Practitioner's Perspective

Other Capital Management Methods

4 On-market buy back

- 4 From shareholder perspective - treated entirely as disposal of shares
- 4 From company perspective – if debit to profits, as a dividend and subject to franking debit possibly

4 Special dividends

- 4 Entirely as a dividend and franking applies
- 4 (tax loss on subsequent sale?)

Off Market Buy Backs

Tax Practitioner's Perspective

Summary – Tax Considerations In Undertaking Off Market Buy Back

- 4 Allow time for class ruling form the ATO
 - 4 Negotiated outcomes
 - 4 Time frame
 - 4 Draft versus final class ruling
 - 4 Determine tax implications for shareholders
- 4 Appropriate split between share capital and dividend
- 4 Shareholder mix
- 4 On-going dividend policy
- 4 On-going franking capability
- 4 Commercial reasons for buy back

Off Market Buy Backs

Tax Practitioner's Perspective

4 Changes to off-market Share Buy Back?

- 4 Policy about streaming rules
- 4 Reduce cost associated with tax compliance
- 4 More transparency and certainty
- 4 Safe harbours
- 4 Class Ruling for marginal cases

Open forum and panel discussion



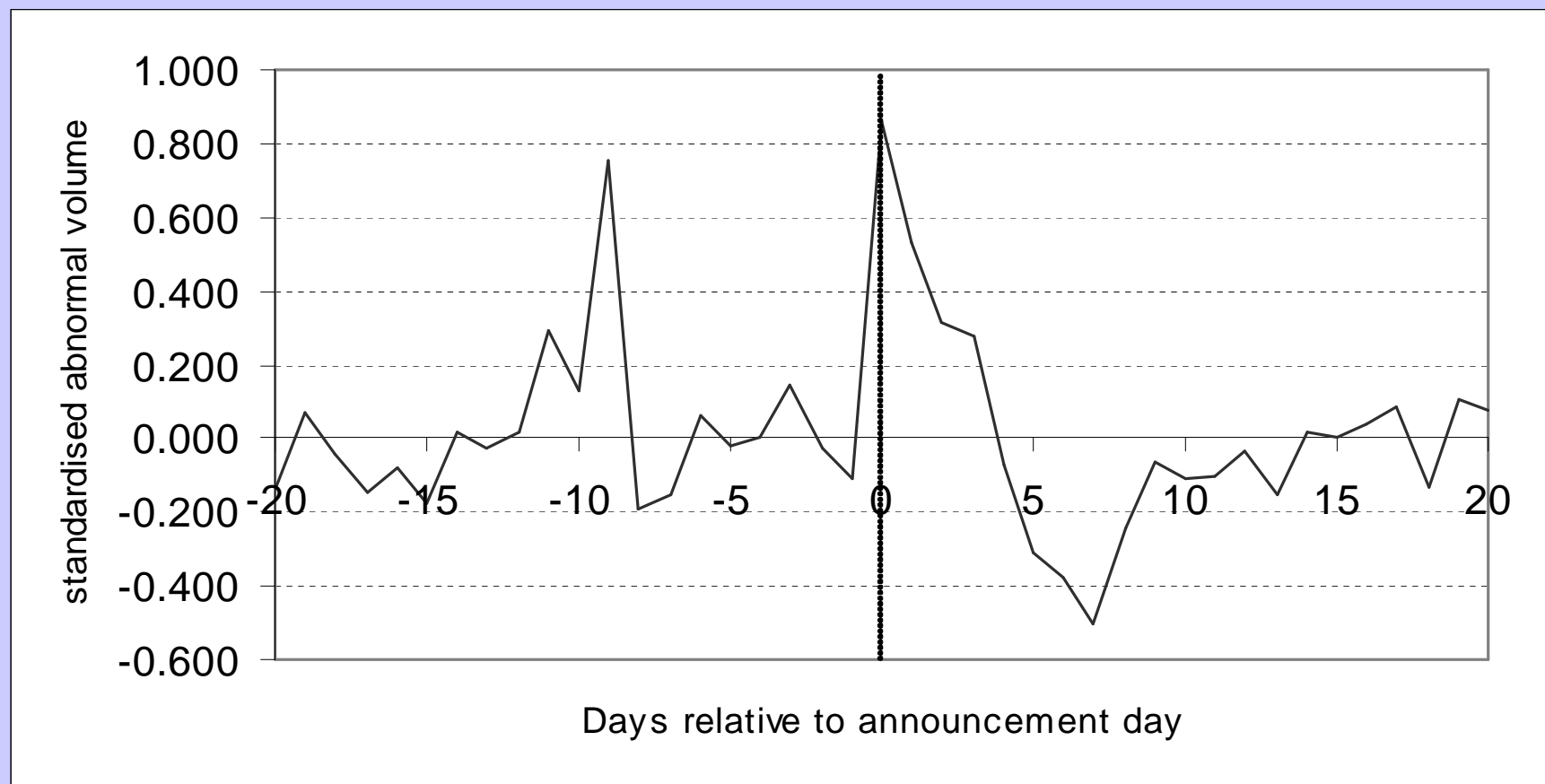
Ground rules

- Name and affiliation
- Brief and to the point
- Who are you addressing
- Keep to the structure of the paper
- General discussion at the end

Key issues for discussion

- Ability to participate in OMSBB
- Level of discount
- Capital/dividend split
- Administrative processes
- Unlisted companies
- Possible options for change
- Other issues

Participation in OMSBB



Participation in OMSBB

- Should investors be able to buy shares following the announcement of a buyback and participate in the buyback?
- If not, how could this be prevented?
- Would there be issues associated with anticipatory trading?

Level of discount

- 14 per cent cap
 - Debit to the franking account of company
 - Imputation benefits not denied to shareholders
- Debit to franking account for non-resident to resident streaming

Level of discount

- Should there be a cap on the level of discount?
- What is the appropriate level of cap?
- Should franking accounts be debited for resident-to-resident streaming?

Capital/dividend split

- Acceptable methodologies
 - Average capital per share
 - Share capital to retained earnings
 - Embedded value
- Generally apply average capital approach
- Capital loss prevents double taxation

Capital/dividend split

- What is the appropriate methodology for determining the split?
- Should the methodology be specified in the law?
- Should shareholders who receive tax free dividends also get the benefits of a capital loss?
- If not, how could this be addressed?

Administrative processes

- Class rulings and private binding rulings
- Practice statement

Administrative processes

- Should current ATO practice be specified in the law?
- Should there be specific provisions for dealing with dividend and/or capital streaming in the context of OMSBB?

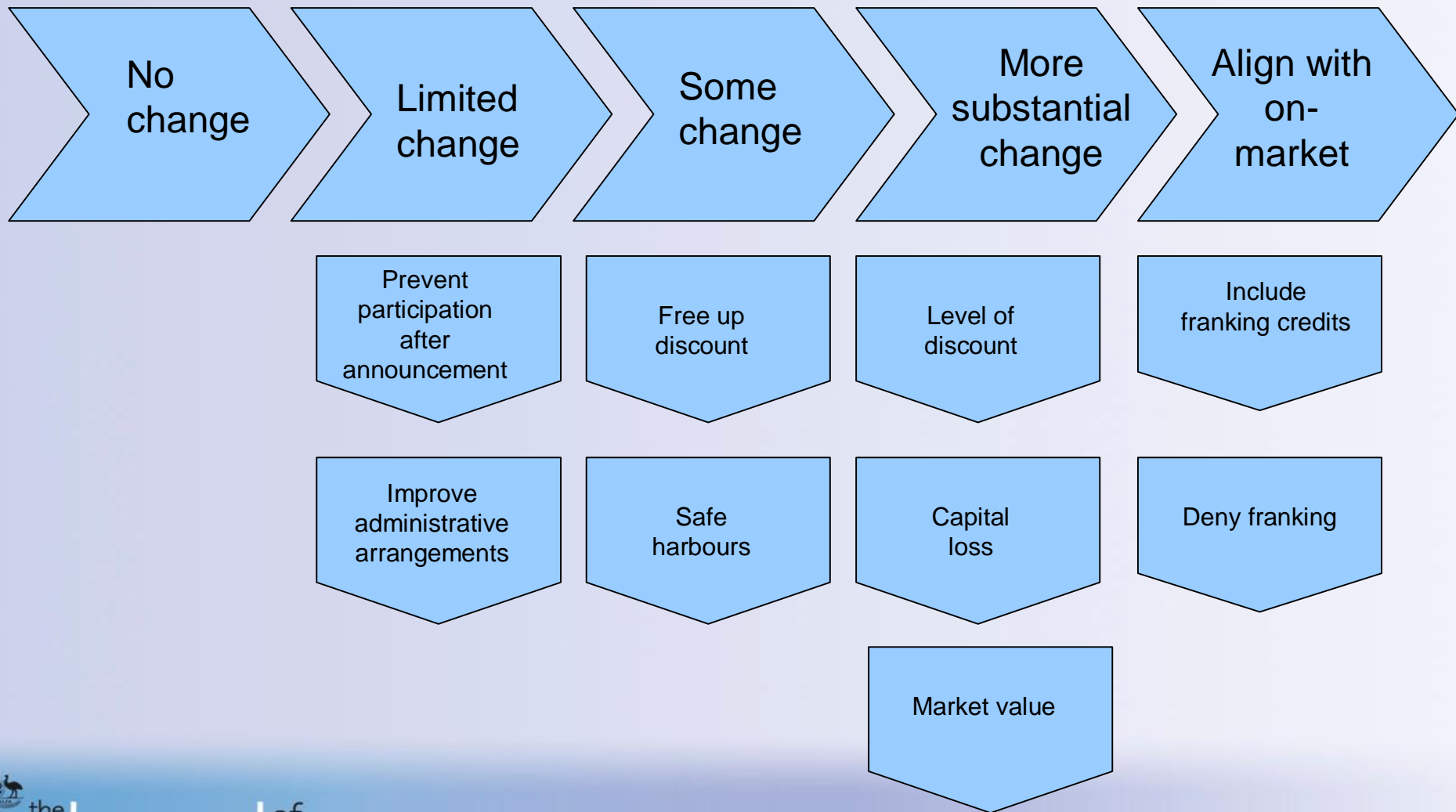
Unlisted companies

- Different objectives in using OMSBB
- Different taxation consequences
- Widely-held unlisted companies

Unlisted companies

- Should there be different taxation arrangements for OMSBB for listed and unlisted companies?
- Should the current arrangements be retained for unlisted companies, with any changes being made for listed companies only?

Options for change



Other issues



Making submissions

- Deadline 24 August 2007
- Email: taxboard@treasury.gov.au
- Post: (see press release)
- Facsimile: (02) 6263 4471