

PRODUCT RULING – BR PRD 16/02

This is a product ruling made under s 91F of the Tax Administration Act 1994.

Name of the Person who applied for the Ruling

This Ruling has been applied for by SKYCITY Entertainment Group Limited (SKYCITY) (IRD No: 62-854-472).

Taxation Laws

All legislative references are to the Income Tax Act 2007 unless otherwise stated.

This Ruling applies in respect of ss BG 1, CA 1(2), CE 1, CX 2, GA 1, HC 6, HC 7 and subpart CE.

This Ruling does not rule on or consider whether particular Participants hold their Plan Shares on capital account.

The Arrangement to which this Ruling applies

The Arrangement is the Executive Long-Term Incentive Plan 2009 (the Incentive Plan), which applies to executives (referred to as the Participants) of the SKYCITY Group, a group of companies wholly owned by SKYCITY. In summary, under the Incentive Plan, SKYCITY Auckland Holdings Limited (SKYCITY Auckland) advances to the trustee of the SKYCITY Executive Share Trust (the Trustee), as agent for the Participants, funds that are used to purchase SKYCITY shares (the Plan Shares). The Plan Shares are then held on trust for a restrictive period (usually three years). At the end of the restrictive period, if the Participant has met various performance hurdles, SKYCITY will pay to the Participant a cash bonus equal to the original Loan grossed up for tax, which will be used to repay the Loan, and the legal title in the Plan Shares will be transferred to the Participant. If the performance hurdles are not met, call or put options will be exercised so that the Trustee will be required to purchase the Plan Shares from the Participant for an amount equal to the amount of the outstanding Loan, settled by way of novation of the Loan to the Trustee.

Further details of the Arrangement are set out in the paragraphs below.

Relevant documents

1. The documents relevant to the Arrangement are:
 - Pro Forma Offer Letter from SKYCITY to employees of SKYCITY Group (Offer Letter);
 - SKYCITY Executive Long-Term Incentive Plan Application Form (Application Form);
 - Executive Long-Term Incentive Plan Terms 2009 (versions dated 25 January 2011 and 17 October 2014) (Terms);
 - SKYCITY Simplified Disclosure Prospectus (versions dated 24 January 2011 and 14 August 2013) (Prospectus), which includes the Performance Hurdle Memorandum as a schedule (Hurdle Memo);
 - Deed of Trust relating to the SKYCITY long-term incentive plans dated 3 November 2009 (Trust Deed) entered into between SKYCITY and Public Trust (acting as the Trustee).
2. The documents, including those relating to future grants under the Arrangement, will be materially the same as those provided to Inland Revenue on 23 November 2015 and 11 December 2015.

Objectives of the Incentive Plans

3. The primary objective of the Incentive Plan is to encourage executives to become shareholders in SKYCITY, thus aligning their interests with those of other shareholders. The Incentive Plan:
 - aims to reward and retain key employees;
 - drives long-term performance and alignment of incentives of participants with the interests of SKYCITY's shareholders; and
 - encourages long-term decision-making.

The Arrangement

Invitation

4. Potential participants in the Incentive Plan are provided with an Offer Letter and the Application Form. These documents provide details of the number of Plan Shares offered, the price of the Plan Shares, and the terms of the grant, including terms surrounding the Loan (discussed further below). Potential participants also receive details of the performance hurdles, which are attached as a schedule to the Prospectus.
5. The Participant may accept the grant by signing and returning the Application Form within a prescribed timeframe. In accepting the grant, the Participant acknowledges that they are bound by the Terms.
6. To date, there have been seven grant dates for the Incentive Plan, as follows:
 - 2 September 2009

- 31 August 2010
 - 2 March 2011
 - 31 August 2011
 - 29 August 2012
 - 28 August 2013
 - 27 August 2014
7. All New Zealand Participants are employed by SKYCITY Management Limited, which is associated with SKYCITY for the purposes of the Act. The Participants are not associated with SKYCITY or any of its subsidiaries for the purposes of the Act.

Terms of loan

8. On acceptance of the grant, SKYCITY Auckland advances an interest-free loan (the Loan) to the Trustee on behalf of, and at the request of, the Participant, solely for the purpose of purchasing the Plan Shares (cl 9(vii) of the Application Form and cl 4.4 of the Terms).
9. The Loan is only repayable by the application of a bonus payment if the performance hurdles are met or, if the performance hurdles are not met, by way of the novation arrangements that are triggered by the exercise of the put or call options (discussed further below) (cl 9(i) of the Application Form and cl 4.4 of the Terms). The Loan is repayable at the end of the restrictive period and otherwise in accordance with the Terms (cl 4.5 of the Terms).
10. The restrictive period is the period commencing when a beneficial interest is acquired by the Participant and ending when the performance hurdle has first been met (definition of Restrictive Period in the Terms). The restrictive period usually runs for three years. However, if the performance hurdles are not met at the initial performance testing date, there is a second and third testing date (being six and 12 months respectively after the initial performance testing date) that extend the restrictive period (explained in the Hurdle Memo).
11. **Any dividends received in respect of a Participant's Plan Shares during the restrictive period** (after the deduction of any tax) must be applied to partially repay the relevant Participant's Loan amount (cl 9(ii) of the Application Form and cl 4.8 of the Terms).

Acquisition and holding of Plan Shares

12. The Trustee uses the Loan proceeds to acquire Plan Shares on behalf of a Participant. The Trustee either acquires the shares on-market, is issued shares (either new or Treasury Stock) by SKYCITY, or transfers Plan Shares from the Unallocated Pool of Plan Shares that the Trustee already holds (cl 3.2 of the Terms and rules 1.1 and 5.5 of sch 1 to the Trust Deed).
13. The amount a Participant must pay for the Plan Shares is the volume weighted average sales price on the NZX Main Board over the ten business days commencing on the first business day **following the company's Preliminary Full**

Year or Half Year Announcement, whichever is applicable (cl 4.1, and the definition of Offer Price in the Terms).

14. In respect of the Plan Shares, each Participant has the right to:
 - all cash dividends, capital returns or other cash distributions (cl 4.6 of the Terms) (SKYCITY will maintain a dividend-paying policy throughout the term of the Incentive Plans); and
 - exercise voting rights, either directly or by way of instructing the Trustee (cl 9.1 of the Terms).
15. During the restrictive period, a Participant cannot sell, transfer, mortgage, charge or otherwise encumber or dispose of the Plan Shares (cl 3 of the Application Form and cl 5.2 of the Terms).
16. Clause 2.11 of the Prospectus provides that, if a Participant requests to withdraw from the Incentive Plan prior to the end of the restrictive period, that Participant must transfer the beneficial interest in the Shares back to the Trustee under the terms of the Put and Call Options. However, the Applicant has confirmed that, despite this clause, Participants are required to obtain approval from the Board of SKYCITY to withdraw from the Incentive Plan. The Applicant has confirmed that approval will only be considered in situations provided for in cl 2.13 of the Prospectus, which applies in situations of **"serious hardship"**. **For the avoidance of doubt, a situation where the value of the Plan Shares falls below the original purchase price paid by the Participant for those Plan Shares will not amount to "serious hardship"**. This Ruling will cease to apply if the Participants do withdraw **from the Incentive Plan other than for reasons of "serious hardship", or as a result of ceasing to be employed with the SKYCITY Group, as discussed at [35] to [36]**. Clause 10 of the Terms provides for corporate actions that may occur during the restrictive period. This includes consolidation or subdivision of shares, bonus issues, rights offers and share buy-backs. In these situations, cl 10 provides for any changes in the number of Plan Shares held on behalf of a Participant. Clause 10 also provides for what will happen if there is a takeover offer or amalgamation. In particular, cl 10 states when a Participant may be entitled to bring forward the performance testing date to determine whether Plan Shares will vest or be forfeited. The process for determining whether Plan Shares will vest or be forfeited is discussed further below.
17. The Trustee holds the Plan Shares as trustee on behalf of the Participant pursuant to the Terms and the Trust Deed. The Trustee is required to act in the interests of the Participants (cl 9.2 of the Terms). The Trustee must maintain an account for each Participant detailing the number of Plan Shares allocated and the Loan balance (rule 10.1 of sch 1 of the Trust Deed).
18. The Applicant considers that the SKYCITY Executive Share Trust is a "complying trust", as defined in s HC 10.

[Performance hurdles and vesting](#)

19. **Under the Incentive Plan, each Participant's right to retain the Plan Shares** allocated to them is dependent on the Total Shareholder Return (TSR) achieved by

SKYCITY relative to comparable companies and other companies on the New Zealand and Australian share markets.

20. Plan Shares will be transferred to the Participants if SKYCITY achieves a TSR greater than or equal to the average of the:
 - Peer Median TSR – the TSR representing the 50th percentile of the TSRs of members of the Peer Comparative Group. The Peer Comparative Group is generally a group of 16 entities the Board of SKYCITY (Board) considers to be appropriate peers of SKYCITY.
 - Index Median TSR – the TSR representing the 50th percentile TSR of NZX50 companies at the date the Participant first acquires a beneficial interest in the Plan Shares.
21. If this hurdle is met, legal title in the Plan Shares is transferred to Participants on a straight-line basis from a 50% transfer if the SKYCITY TSR equals the 50th percentile, to a 100% transfer if the SKYCITY TSR is equal to the 75th percentile. In addition, the Board has discretion to determine that up to 25% of the Plan Shares can be **transferred to the Participants if SKYCITY’s TSR for the relevant assessment period does not exceed the average of the Peer Median TSR and Index Median TSR, but exceeds one or other of the Peer Median TSR or Index Median TSR.**
22. All grants for the Incentive Plan have the same performance hurdles as those set out above, apart from the 27 August 2014 grant. For this grant, 50% of the Plan Shares were allocated to the Peer Median TSR Tranche and 50% of the Plan Shares were allocated to the Index Median TSR Tranche. Vesting of the Plan Shares in each Tranche is not interdependent. Therefore, the Board does not have discretion to determine that up to 25% of the Plan Shares can be transferred to the Participant if both hurdles are not met.

If the performance hurdles are achieved

23. **To the extent that the performance hurdles are met, the Participant’s employer or SKYCITY pays a cash bonus equal to the value of the original Loan to the Participant, grossed up based on the top marginal tax rate at the time the beneficial interest in the Plan Shares was acquired (cl 7.1 of the Terms). The after-tax amount of the bonus is paid to the Trustee and applied to repay the Loan balance (cl 7.2 of the Terms).**
24. If dividends or other distributions have been received in relation to the Plan Shares during the restrictive period and applied in part payment of the Loan, the outstanding Loan balance is less than the after-tax amount of the bonus. In this situation, the balance of the bonus payment is paid to the Participant (cl 7.3 of the Terms).
25. In the 28 August 2013 and 27 August 2014 grants, cl 7.2 also stipulates that third-party source deductions (eg KiwiSaver, student loan or child support payments) should be deducted from the bonus payment. This may result in situations where the bonus does not fully cover the amount of the Loan balance. In that situation, the Participant is liable to pay the outstanding Loan balance (para 2.10 of the Prospectus).

26. The Trustee is required to transfer the legal title in the Plan Shares that vest as a result of meeting the performance hurdles within one month of the relevant performance testing date (cl 6.2 of the Terms). However, with the exception of the circumstances discussed at [34] to [35] below, the Plan Shares only vest if the Participant remains employed with the SKYCITY Group, and the Loan is repaid in full (cl 6.3 of the Terms).

If the performance hurdles are not met

27. To the extent performance hurdles are not met, no cash bonus is paid (cl 7.1 of the Terms).
28. In addition, to the extent performance hurdles are not met, the Participant is required to forfeit their Plan Shares (cl 8 of the Terms). This occurs either by the Trustee exercising a call option requiring the Participant to sell their beneficial interest in the Plan Shares to the Trustee or, failing that, by the Participant **exercising a put option requiring the Trustee to purchase the Participant's** beneficial interest in the Plan Shares (cl 8.4 of the Terms).
29. The consideration payable for the forfeited Plan Shares is the outstanding Loan balance relating to those shares. This is satisfied by the Participant novating all their rights and obligations under the Plan Shares and the Loan to the Trustee. After the novation, the Loan is owed by the Trustee to SKYCITY Auckland (cl 9(iv) of the Application Form and cl 8.5 of the Terms).
30. The Participant is not required to reimburse the Trustee for any loss in value of the forfeited Plan Shares compared to the outstanding Loan balance. Conversely, if the forfeited Plan Shares have increased in value, the Participant is not entitled to receive a benefit from the gain (cl 8.6 of the Terms).
31. If a call or demand is made by any person for repayment of the Loan other than in the circumstances expressly permitted (and summarised in this Arrangement Description), the put option will become immediately exercisable by the Participant (cl 9(vi) of the Application Form).
32. **Where the Trustee purchases the beneficial interest in a Participant's Plan Shares,** SKYCITY provides the Trustee with a Trustee Loan that the Trustee uses to repay the novated Loan originally granted to the Participant (rule 5.4 of sch 1 of the Trust Deed). The Trustee then holds the Plan Shares in the Unallocated Pool to be allocated to a future Participant at a later date (rule 5.3 of sch 1 of the Trust Deed).
33. Where Plan Shares from the Unallocated Pool are subsequently sold by the Trustee to a future Participant, the amount of the Loan granted to that future Participant, which is used to pay for those Plan Shares, is used by the Trustee to repay any outstanding Trustee Loans (rule 5.5(d)(i) of sch 1 of the Trust Deed). Any surplus, arising from a difference between the purchase price payable by the future Participant for the Plan Shares and the price the Trustee paid to purchase forfeited Plan Shares, is distributed to SKYCITY as beneficiary income (rule 5.5(d)(iii) of sch 1 of the Trust Deed).

Cessation of employment

34. If, in the period of 12 months preceding the initial performance testing date, the Participant:
- gives notice terminating their employment as a result of a material change to the terms and conditions of employment resulting in a diminution of the **Participant's status and responsibility without consent (definition of Fundamental Change in the Terms)**; or
 - has their employment terminated without cause;

the Participant's Plan Shares continue to be held by the Trustee for the Participant until the first performance testing date. If the Plan Shares do not vest in the Participant at that date, the Plan Shares are forfeited as discussed above (cl 11.2 of the Terms).

35. If the Participant ceases to be employed as a result of an involuntary event (eg death, redundancy or medical incapacity), and the cessation date is on or after the date half way through the period from acquisition of the Plan Shares to the initial performance testing date, the Board may determine that some or all of the Plan Shares be transferred to the Participant at its discretion (cl 11.3 of the Terms). However, for Participants involved in the 27 August 2014 grant, where employment ceases due to medical incapacity or permanent disability, then the Plan Shares vest on a straight-line basis depending on the time elapsed from the acquisition date to the cessation date, and such vesting is not subject to the performance hurdles.
36. If the Participant ceases to be employed for any other reason, the Plan Shares are forfeited (cl 11.1 if the Terms).
37. For the avoidance of any doubt, this Ruling only applies to the extent that any of the events described in the Arrangement Description above occur during the period of this Ruling.

How the Taxation Laws apply to the Arrangement

The Taxation Laws apply to the Arrangement as follows:

- a) **The Trustee's purchase of the Plan Shares on behalf of a Participant does not give** rise to any income to that Participant under subpart CE, provided the value of the Plan Shares on the date they are acquired by the Trustee on behalf of the Participant is equal to the price payable by the Participant for those Plan Shares.
- b) Cash bonuses paid by SKYCITY or SKYCITY Management Limited to eligible Participants are income of the Participant under s CE 1(1)(a).
- c) The transfer of legal title in the Plan Shares to a Participant does not result in the Participant deriving income under ss CA 1(2), CE 1(1) or HC 6.
- d) Where the Trustee derives dividends on Plan Shares that are held on behalf of the Participants, **such distributions constitute "beneficiary income" of the relevant Participant in accordance with s HC 6 and not "trustee income" under s HC 7.**

- e) When a Participant transfers their beneficial interest in the Plan Shares to the Trustee following the exercise of the call or put option:
- the Participant will not derive income under s CE 1; and
 - no fringe benefit tax will arise under s CX 2.
- f) Sections BG 1 and GA 1 do not apply to the Arrangement.

The period or income year for which this Ruling applies

This Ruling will apply for the period beginning on 7 April 2016 and ending on 6 April 2019.

This Ruling is signed by me on the 7th day of April 2016.

Howard Davis

Director (Taxpayer Rulings)