

PRODUCT RULING – BR Prd 16/09

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 Smartshares Limited in its capacity as Manager of the NZX 50 Portfolio Index Fund.

Taxation Laws

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

This Ruling applies in respect of ss BG 1, CB 4, CD 8, CX 56C, DB 23, and FC 2.

The Arrangement to which this Ruling applies

The Arrangement is the resettlement of the NZX 50 Portfolio Index Fund (the Existing Fund) onto the NZ Top 50 Fund (the New Fund) by redeeming units held by unitholders (Unitholders) in the Existing Fund, applying the redemption proceeds to acquire units in the New Fund on behalf of Unitholders, and transferring the assets of the Existing Fund to the New Fund.

However, the New Fund will not issue units to Unitholders whose address on the register of Unitholders is outside New Zealand (Offshore Unitholders). The redemption proceeds that Offshore Unitholders will receive from the Existing Fund will be cash only and the resettlement process will not result in them becoming unitholders in the New Fund.

Prior to the resettlement Unitholder's units in the Existing Fund will be subdivided and the Manager of the Existing Fund will resolve that the subdivision of units is a dividend that will be fully imputed.

The New Fund will be established as part of a managed investment scheme as defined in the Financial Markets Conduct Act 2013 (FMCA) in relation to which units are issued that are managed investment products (as defined in the FMCA).

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

The Existing Fund

1. The Existing Fund was established by a trust deed dated 15 October 2004 (the Trust Deed), as subsequently amended by:
 - a) first deed of modification to the Trust Deed dated 9 December 2005;
 - b) second deed of modification to the Trust Deed dated 1 October 2007;
 - c) third deed of modification to the Trust Deed dated 30 March 2010;
 - d) fourth deed of modification to the Trust Deed dated 3 September 2010; and
 - e) deed of amendment to the Trust Deed to be dated 2016 (the Amendment Deed).
2. The Trust Deed established the Existing Fund as a group investment fund in accordance with the Trustee Companies Act 1967.
3. The Existing Fund elected into the portfolio investment entity (PIE) regime and is a **"listed PIE" as defined in s YA 1.**
4. The Manager of the Existing Fund is Smartshares Limited (the Manager), and the trustee of the Existing Fund is The New Zealand Guardian Trust Company Limited.
5. The Existing Fund invests in financial products listed on the NZX Main Board and is **designed to track the S & P / NZX 50 Portfolio Index. The Existing Fund's** investment objective is to provide a return that closely matches the return on the S & P / NZX 50 Portfolio Index. The S & P / NZX 50 Portfolio Index is comprised of the 50 largest financial products listed on the NZX Main Board. The S & P / NZX 50 Portfolio Index is made up of the same financial products as the S & P / NZX 50 Index, but with a 5% cap on the float-adjusted market capitalisation.

The New Fund

6. The New Fund is a fund established as part of a managed investment scheme (as defined in the Financial Markets Conduct Act 2013) in relation to which units will be issued that are managed investment products (as defined in the Financial Markets Conduct Act 2013).
7. The New Fund was established under and by virtue of a trust deed dated 24 June 2014 and amended and restated on 9 September 2016 (the Master Trust Deed), and an Establishment Deed dated 9 September 2016 executed by the Manager and Public Trust.
8. The manager of the New Fund is Smartshares Limited (the Manager) and the supervisor and trustee of the New Fund is Public Trust.
9. **The New Fund will elect into the PIE regime and will become a "listed PIE" (as defined in s YA 1).**
10. The investment policy of the New Fund is and will be similar in all material respects to that of the Existing Fund.

Steps to be undertaken to resettle the Existing Fund

11. The resettlement of the Existing Fund onto the New Fund will be achieved by utilising the resettlement mechanism contained in the Trust Deed.
12. The material provisions in the Trust Deed are as follows:

ARTICLE 19 – TERMINATION OF THE FUND

19.1 Termination

- (a) The Fund shall terminate if it has not previously terminated on the day that is the first of the following days to occur:
 - (i) the day that is one day less than 80 years from the date of this Deed;
 - (ii) the day nominated by Unitholders pursuant to clause 19.2(a) (*Unitholders may terminate Fund*);
 - (iii) the day appointed by the Manager pursuant to clause 19.2(b) (*Manager may terminate Fund*); or
 - (iv) the day on which the Trustee retires under clause 14.9 (*Retirement of Trustee*) or clause 14.10 (*Trustee's retirement of Manager's request*) if on the date of retirement no successor Trustee has been appointed; and
 - (v) if NZX Funds Management Limited (or any related company of that company as defined in section 2(3) of the Companies Act 1993) is the manager of the Fund, within 60 days of Unitholders by Extraordinary Resolution terminating the Manager's authority under clause 16.9 (*Removal of Manager by Extraordinary Resolution of Unitholders*).

19.2 Termination by Unitholder or Manager

- (a) **Unitholders may terminate Fund:** Unitholders may resolve by Extraordinary Resolution to terminate the Fund on a date not earlier than two months after the passage of the resolution, but no such resolution to terminate may be made if during a period of 3 months or more prior to the date of the deposit of the requisition of the meeting setting out the terms of such Extraordinary Resolution:
 - (i) holders of Basket Numbers of Units would have been able, if they so wished, to redeem a Basket or more on at least 20 Business Days during that period, at their Current Unit Value; and
 - (ii) the reported weighted average price for sales of Units in parcels of less than a Basket on at least 20 Business Days during that period has been higher than 1% below Current Unit Value at the time of sale.
- (b) **Manager may terminate Fund:** The Manager may terminate the Fund for any reason whatsoever, including (but without limitation) if in the opinion of the Manager the Fund is not sufficiently profitable for the Manager. The date of termination shall be a day appointed by the Manager by giving not less than two months' written notice to the Unitholders and to the Trustee.
- (c) **No redemption once a termination date is determined:** Upon Unitholders pursuant to clause 19.2(a) (*Unitholders may terminate Fund*), or the Manager pursuant to clause 19.2(b) (*Manager may terminate Fund*) determining a date of termination of the Fund the rights of Unitholders with respect to the redemption of Units shall cease.

19.3 Termination Procedure

- (a) **Distribution of Assets:** Upon the Fund being terminated subject to clause 14.12 (*Successor Trustee*), the Trustee shall discharge the liabilities and Expenses of the Fund (and the provisions of Article 12 (Custodial arrangement for Securities), to the extent, if any, they prohibit the payment of Expenses out of the Fund, shall cease to apply) and distribute to each Unitholder that Unitholder's Share of the net Assets of the Fund proportionately to the Unitholders in such manner and within such period after the termination of the Fund as the Trustee considers advisable.
- (b) **Form of distribution:** Such distribution may be made in cash or in kind or partly in both, all as the Trustee in its sole discretion may determine.
- (c) **Certificates and release:** Any Certificates shall in the case of the final distribution be surrendered to the Trustee and such final distribution shall only be made against delivery to the Trustee of such form of release as the Trustee shall in its sole discretion require.
- (d) **Resettlement:** If Unitholders resolve by Extraordinary Resolution to resettle all or part of the income or capital of the Fund and the Trustee is satisfied that it is not, nor is it likely to become, materially prejudicial to the interests of Unitholders generally, the Trustee shall:
- (i) **Compulsory redemption:** Require Unitholders to accept repayment in respect of all or any of the Unitholder's Units for the purposes of the application of the proceeds referred to in clause 19.3(a) (*Distribution of Assets*); or
 - (ii) **Apply Proceeds toward a New Fund:** Apply the proceeds of repayment towards the issue price for Units in an alternative Fund, being a new fund (the *New Fund*) with an investment policy similar in all material respects to those of the Fund (the *Existing Fund*), as if the Unitholder had redeemed units in the Existing Fund and reinvested the proceeds from those units in the New Fund;
 - (iii) **Transfer of GIF Assets:** Sell or otherwise transfer all or any GIF Assets of the Existing Fund to the New Fund;
 - (iv) **Resettle New Fund:** Resettle by irrevocable deed (without infringing the rule against perpetuities) all or part of the income or capital of the Fund on the trusts and with the powers of any New Fund, or other trust approved by the Trustee;
 - (v) **Lend to New Fund:** Lend any sum to the trustee or trustees of that New Fund, with or without security, at an interest rate (if any) and on such other terms as in each respect the Trustee thinks fit;
 - (vi) **Assume Liabilities:** Assume liabilities of the Existing Fund on behalf of the New Fund;
 - (vii) **New Manager or Trustee:** Arrange any of the foregoing with another manager and/or trustee for the New Fund;
 - (viii) **Terminate Fund:** Terminate the Existing Fund.

13. Other relevant provisions of the Trust Deed are as follows:

ARTICLE 1 - INTERPRETATION

1.1 Definitions

In this Deed, unless the subject matter or context otherwise requires:

...

Fund means The NZX 50 Portfolio Index Fund, which is a group investment fund (GIF) governed by this Deed and as the context requires refers also to the Trustee in its capacity as trustee of that group investment fund;

ARTICLE 4 – REGISTERS, TRANSFERS, CERTIFICATES

4.11 Consolidation and split of Units

- (a) **Notice:** The manager may at any time, by notice in writing to the Trustee, cause Units in existence on a date specified in that notice to be consolidated or subdivided. Each such notice shall:
- (i) specify the date on which such consolidation or subdivision is to take place (the "**Operative Date**"); and
 - (ii) specify the ratio (the "**Ratio**") which the number of Units in existence after the consolidation or subdivision will bear to the number of Units in existence before the consolidation or subdivision.
- (b) **New number of Units:** As from the Operative Date, each Unitholder of the Fund shall be deemed to hold a number of Units of the Fund equivalent to the number held by him before the Operative Date multiplied or divided (as the case may be) by the Ratio. For this purpose, at the option of the Manager in each case, fractions may be disregarded or may be rounded upwards or downwards.
- (c) **Arrangement at Manager's discretion:** The Manager shall make such arrangements (if any) as it deems appropriate, following a consolidation or subdivision, for the cancellation of existing Certificates and the Issue of new Certificates, if Certificates are required by law.

ARTICLE 17 - AMENDMENTS

17.1 Amendments to Deed or Issue Terms

The Trustee may at any time make any alteration, modification, variation or addition to the Trust Deed or any Issue Term (excluding any applicable Rule), with the concurrence of the Manager, in any of the following cases:

...

- (f) If it is authorised by an Extraordinary Resolution of the Unitholders under Clause 18.10 (*Effect of a resolution*).

14. Prior to the resettlement of the Existing Fund, the Trust Deed will be amended by the Amendment Deed as follows:

- a) A new definition will be added to clause 1.1 that reads as follows:

"Resettlement Fund" means a fund (other than the Fund) established as part of a managed investment scheme (as defined in the Financial Markets Conduct Act 2013) in relation to which units are issued that are managed investment products (as defined in the Financial Markets Conduct Act 2013) and that, at the date of any resettlement pursuant to Clause 19.3(d), has or will have Smartshares Limited as its manager.

- b) The second sentence of clause 19.2(b) will be amended to read as follows:
- The date of termination shall be a day appointed by the Manager by giving not less than:
- (i) one week's written notice if all of the income and capital of the Fund is to be resettled in accordance with clause 19.3(d) and an Extraordinary Resolution approving that resettlement has been passed; or
- (ii) **two months' written notice in all other cases,**
- to the Unitholders and the Trustee.
- c) Clause 19.3(d)(ii) will be deleted and the following inserted in its place:
- (ii) **Apply Proceeds towards a Resettlement Fund:** Apply the proceeds of repayment towards the issue price for units in a Resettlement Fund (the **New Fund**) with an investment policy similar in all material respects to those of the Fund (the **Existing Fund**), as if the Unitholder had redeemed units in the Existing Fund and reinvested the proceeds from those units in the New Fund.
15. Prior to the date of resettlement, the Manager will provide written notice to the Trustee (in accordance with clause 4.11 of the Trust Deed) requiring that each unit in the Existing Fund is subdivided so as to become two units (the Subdivision). Unitholders will not be given an option whether to receive a bonus **issue (being the Subdivision) or money or money's worth (other than money's worth that is a bonus issue)**.
16. The Subdivision will occur immediately prior to the Existing Fund being resettled. When it makes the Subdivision, the Manager will resolve:
- a) that it is a "dividend" for purposes of the Act;
- b) the amount to be treated as a dividend (which must be more than zero); and
- c) that imputation credits are attached at the maximum permitted ratio.
17. The Manager of the Existing Fund will give notice to the Commissioner under s 63 of the Tax Administration Act 1994 of the election to treat the Subdivision as a dividend under s CD 8, and the amount to be treated as a dividend.
18. The effect of the Subdivision and related resolutions summarised above is that the Existing Fund is unlikely to have any imputation credits at the time the resettlement occurs.
19. The following steps will be undertaken to achieve the resettlement of the Existing Fund on the New Fund:
- a) A notice of meeting will be issued to Unitholders in the Existing Fund in accordance with the requirements of Article 18 of the Trust Deed. The notice of meeting will advise Unitholders of:
- i) the following proposed amendments to the Trust Deed:
- the amendment contained in the Amendment Deed (such amendment allowing the power of resettlement in clause

19.3(d) to be used to resettle the assets of the Existing Fund onto the New Fund notwithstanding that the New Fund is not a group investment fund); and

- the amendment of the notice period required for the termination of the Existing Fund by the Manager under clause 19.2(b) from two months to one week;
 - ii) the intention to seek authorisation of the resettlement of the Existing Fund on the New Fund (as required by clause 19.3(d) of the Trust Deed).
 - b) At the meeting, the Manager will give notice of the intended termination of the Existing Fund pursuant to clause 19.2(b) of the Trust Deed. Such notice will be conditional on the Unitholders passing extraordinary resolutions approving:
 - i) the amendments to the Trust Deed referred to in [19(a)(i)] above; and
 - ii) the resettlement described in [19(a)(ii)] above.
 - c) Formal written notice will be provided in compliance with the provisions of clause 19.2(b) of the Trust Deed (as amended) immediately following the passage of the extraordinary resolutions referred to in [19(b)] above.
 - d) If the Unitholders approve the amendments to the Trust Deed referred to in [19(a)(i)] above, and approve the resettlement described in [19(a)(ii)] above, the Trustee will:
 - i) discharge the liabilities and expenses of the Existing Fund (clause 19.3(a))
 - ii) redeem the Unitholders' units in the Existing Fund (clause 19.3(d)(i));
 - iii) apply the proceeds of redemption towards the issue price of units in the New Fund on behalf of the Unitholders (clause 19.3(d)(ii));
 - iv) transfer the assets of the Existing Fund to the New Fund (to be held and invested subject to a statement of investment policy and objectives identical in all material respects to the investment policy to which the Existing Fund is subject) (clause 19.3(d)(iii)); and
 - v) wind up the Existing Fund (clause 19.3(d)(viii)).
20. **Accordingly, the Arrangement will comprise a redemption of Unitholders' interests** in the Existing Fund and a resettlement on the New Fund. At conclusion of the resettlement process:
- a) Unitholders will hold interests in the New Fund of the same value and on substantially similar terms as the interests they held in the Existing Fund;

- b) the New Fund will hold the same assets as the Existing Fund and will continue to invest on the same basis and in the same manner in which the Existing Fund invested prior to resettlement.
21. To ensure that the resettlement process does not result in the New Fund inadvertently breaching foreign securities laws, the New Fund will not issue units to any Unitholders in the Existing Fund whose address on the register of Unitholders (established and maintained under clause 4.1 of the Trust Deed) is outside New Zealand (Offshore Unitholders). Accordingly the redemption proceeds that Offshore Unitholders receive from the Existing Fund will be cash only and the resettlement process will not result in them becoming Unitholders in the New Fund.
22. The trustees of the Existing Fund and the New Fund will enter into a Deed of Resettlement and Related Matters pursuant to which the trustee of the New Fund will undertake to issue units to Unitholders (excluding Offshore Unitholders) in proportion to the units that they each held on resettlement in the Existing Fund and to receive funds which are unallocated at the time of resettlement (if any) and to pay such amounts to the persons lawfully entitled to those funds. This ruling is based on a draft of the Deed of Resettlement and Related Matters provided to the Commissioner on 21 October 2016.
23. The Existing Fund will not at the time of its resettlement onto the New Fund be a party to a "returning share transfer" as defined in s YA 1.
24. Immediately prior to its resettlement, the assets of the Existing Fund will include cash held in short term interest bearing bank accounts (the Bank Accounts) by the Existing Fund. Such amounts of the Bank Accounts that form part of the net assets of the Existing Fund at the time of redemption will be distributed to Unitholders on redemption of their units under the Arrangement.
25. An amount equal to the interest derived on the Bank Accounts is paid by the Existing Fund to the Manager as a management fee.

Conditions stipulated by the Commissioner

This Ruling is made subject to the following conditions:

- a) The Existing Fund:
- is not a "designated group investment fund" (as defined in s HR 3(6));
 - results from investments made into it that are not from a "designated source" (as defined in s HR 3(5));
 - does not derive any "category B income" (as defined in s YA 1); and
 - is a "listed PIE" (as defined in s YA 1).

How the Taxation Laws apply to the Arrangement

Subject in all respects to any conditions stated above, the Taxation Laws apply to the Arrangement as follows:

- a) **Any units received by the Unitholders under the Subdivision will be a “taxable bonus issue” that is a dividend under s CD 8.**
- b) The amount derived by Unitholders of the Existing Fund on redemption of their units in the Existing Fund, and any units received by Unitholders under the Subdivision, are excluded income under s CX 56C(1) if they:
 - i) are resident; and
 - ii) are a natural person or a trustee; and
 - iii) do not include the amount as income in a return of income for the income year.
- c) If any one or more of the criteria listed in subparagraphs (i) to (iii) above does not apply to the Unitholder, the amount derived by the Unitholder on redemption of their units in the Existing Fund, and any units received by Unitholders under the Subdivision, are excluded income to the extent to which the redemption proceeds is more than the amount that is fully credited as described in s CD 43(26).
- d) Unitholders (other than Offshore Unitholders or PIEs) will:
 - i) derive income under s CB 4 from the disposal of the redemption proceeds to the New Fund;
 - ii) be entitled to a deduction under s DB 23 (calculated with reference to s FC 2) for an amount at least the same as the amount of any income under s CB 4; and
 - iii) have no overall income tax liability as a result of their disposal of the redemption proceeds to the New Fund.
- e) Unitholders which are PIEs will derive excluded income under s CX 55 from the disposal of the redemption proceeds to the New Fund to the extent that:
 - i) the redemption proceeds consist of shares issued by a company referred to in s CX 55(3)(a);
 - ii) the Unitholders are not assured under an arrangement with another person of having a gain on the disposal; and
 - iii) the shares are not fixed-rate shares within the meaning of paragraphs (a) **to (d) of the definition of “fixed-rate share”.**
- f) To the extent that Unitholders which are PIEs dispose of redemption proceeds that do not satisfy one or more of the criteria listed in subparagraphs (i) to (iii) of paragraph (e), those Unitholders will:
 - i) derive income under section CB 4 from the disposal of the redemption proceeds to the New Fund;
 - ii) be entitled to a deduction under s DB 23 (calculated with reference to s FC 2) for an amount at least the same as the amount of any income under s CB 4; and

- iii) have no overall income tax liability as a result of their disposal of the redemption proceeds to the New Fund.
- g) Section BG 1 does not apply to the Arrangement.

The period or income year for which this Ruling applies

This Ruling will apply for the period beginning on 1 April 2016 and ending on 30 September 2017.

This Ruling is signed by me on the 25th day of October 2016.

Howard Davis

Director (Taxpayer Rulings)