



## Product Ruling

### Income tax: tax consequences of investing in ANZ Cobalt

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#### **❶ This publication provides you with the following level of protection:**

This publication (excluding appendixes) 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.

### **No guarantee of commercial success**

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The Commissioner **does not** sanction or guarantee this product. Further, the Commissioner gives no assurance that the product is commercially viable, that charges are reasonable, appropriate or represent industry norms, or that projected returns will be achieved or are reasonably based.

Potential participants must form their own view about the commercial and financial viability of the product. The Commissioner recommends a financial (or other) adviser be consulted for such information.

This Product Ruling provides certainty for potential participants by confirming that the tax benefits set out in the **Ruling** part of this document are available, **provided that** the scheme is carried out in accordance with the information we have been given, and have described below in the **Scheme** part of this document. If the scheme is not carried out as described, participants lose the protection of this Product Ruling.

### **Terms of use of this Product Ruling**

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This Product Ruling has been given on the basis that the entity(s) who applied for the Product Ruling, and their associates, will abide by strict terms of use. Any failure to comply with the terms of use may lead to the withdrawal of this Product Ruling.

## What this Ruling is about

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1. This Product Ruling sets out the Commissioner's opinion on the way in which the relevant provisions identified in the Ruling section apply to the defined class of entities who take part in the scheme to which this Ruling relates. All legislative references in this Ruling are to the *Income Tax Assessment Act 1997* (ITAA 1997) unless otherwise indicated.
2. In this Product Ruling the scheme is referred to as ANZ Cobalt offered by Australia and New Zealand Banking Group Limited (ANZ) and issued under the ANZ Cobalt Product Disclosure Statement (PDS).
3. This Product Ruling does not address:
  - (a) the taxation consequences of:
    - Early Termination of the Loan;
    - an investor's Default;
    - using the Loan to finance the exercise price of Vested Employee Options;
    - making an Adviser Option Payment;
    - entering into an additional Loan during the Term of the Loan where the investor's Protection Level is greater than the Amount Outstanding in respect of a Loan;
    - buying or selling Options (other than the Purchase Put Option or the Capped Purchase Put Option bought under the Loan);
    - buying a Purchase Put Option over an Index;
    - acquiring a Loan in respect of a Parcel (or Parcels) of Securities that an investor already holds;
    - income derived from the Securities (except where specifically addressed in the context of the Dividend Give-Up Facility as per paragraphs 16(q)(i) and 51 of this Product Ruling);
    - a Loan over International Securities (except where specifically addressed in the context of an investor's entitlement to a foreign income tax offset as per paragraphs 16(r), 53 and 54 of this Product Ruling), including a Loan over ASX-listed CHESS Depository Interests (CDIs) over International Securities;

- electing to use the Dividend Give-Up Facility (except where specifically addressed in paragraphs 16(q), 51 and 52 of this Product Ruling); and
  - an Adjustment Event;
- (b) an investor's entitlement to franking credits (except where specifically addressed in the context of the Dividend Give-Up Facility as per paragraphs 16(q)(ii) and 52 of this Product Ruling);
- (c) the taxation consequences for SMSF Investors; and
- (d) whether this scheme constitutes a financial arrangement for the purposes of Division 230 (Taxation of financial arrangements).

### **Class of entities**

4. This part of the Product Ruling specifies which entities can rely on the Ruling section of this Product Ruling and which entities cannot rely on the Ruling section. In this Product Ruling, those entities that can rely on the Ruling section are referred to as the investor.

5. The class of entities who can rely on the Ruling section of this Product Ruling consists of those entities that are accepted to participate in the scheme specified below on or after 8 April 2013 and on or before 30 June 2016. They must have a purpose of remaining in the scheme until it is completed (that is, being a party to the relevant agreements until their term expires), and deriving assessable income from this investment.

6. The class of entities who can rely on this Product Ruling does **not** include entities who:

- are non-residents for Australian taxation purposes;
- intend to terminate their investment in the scheme prior to its completion, or who do not intend to derive assessable income from it;
- are accepted to participate in the scheme described below before 8 April 2013 or after 30 June 2016;
- acquire a Loan in respect of a Parcel (or Parcels) of Securities that an investor already holds, or use the Loan to finance the exercise price of Vested Employee Options;
- are SMSF Investors;

- participate in the scheme through offers made other than through the PDS, or who enter into an undisclosed arrangement with the promoter or a promoter associate, or an independent adviser that is interdependent with scheme obligations and/or scheme benefits (which may include tax benefits) in any way;
- trade in Securities and are treated for taxation purposes as trading in Securities, carrying on a business of investing in the Securities, or holding the Securities as trading stock or as revenue assets;
- trade in Options and are treated for taxation purposes as trading in the Purchase Put Option or Capped Purchase Put Option, carrying on a business of investing in the Purchase Put Option or Capped Purchase Put Option, or holding the Purchase Put Option or Capped Purchase Put Option as trading stock or as a revenue asset; or
- are subject to Division 230 in respect of this scheme. Division 230 will generally not apply to individuals, unless they have made an election for it to apply to them.

## ***Superannuation Industry (Supervision) Act 1993***

7. This Product Ruling does not address the provisions of the *Superannuation Industry (Supervision) Act 1993* (SISA). The Commissioner gives no assurance that the scheme is an appropriate investment for a superannuation fund. The trustees of superannuation funds are advised that no consideration has been given in this Product Ruling as to whether investment in this scheme may contravene the provisions of SISA.

## **Qualifications**

8. The class of entities defined in this Product Ruling may rely on it provided the scheme actually carried out is carried out in accordance with the scheme described in paragraphs 17 to 21 of this Ruling.

9. If the scheme actually carried out is materially different from the scheme that is described in this Product Ruling, then:

- this Product 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 Product Ruling may be withdrawn or modified.

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## **Date of effect**

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11. This Product Ruling applies prospectively from 8 April 2013. It therefore applies only to the specified class of entities that enter into the scheme from 8 April 2013 until 30 June 2016 being its period of application. This Product Ruling will continue to apply to those entities even after its period of application has ended for the scheme entered into during the period of application.

12. However the Product Ruling only applies to the extent that there is no change in the scheme or in the entity's involvement in the scheme.

### **Changes in the law**

13. Although this Product Ruling deals with the income tax laws enacted at the time it was issued, later amendments may impact on this Product Ruling. Any such changes will take precedence over the application of this Product Ruling and, to that extent, this Product Ruling will have no effect.

14. Entities who are considering participating in the scheme are advised to confirm with their taxation adviser that changes in the law have not affected this Product Ruling since it was issued.

### **Note to promoters and advisers**

15. Product Rulings were introduced for the purpose of providing certainty about tax consequences for entities in schemes such as this. In keeping with that intention the Commissioner suggests that promoters and advisers ensure that participants are fully informed of any legislative changes after the Product Ruling has issued.

## Ruling

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16. Subject to paragraph 3 of this Ruling and the assumptions in paragraph 21 of this Ruling:

- (a) Where the cost of the Purchase Put Option is factored into the interest rate charged on the Loan (and the investor does not pay a Protection Level Increase Fee in the circumstances discussed at paragraph 20(m) of this Product Ruling):
  - (i) the interest incurred under the Loan, reduced by an amount reasonably attributable to the cost of capital protection worked out under step 3 of the method statement in subsection 247-20(3), will be deductible under section 8-1;
  - (ii) under subsection 247-20(3), the amount reasonably attributable to the cost of capital protection in an income year is the amount by which the interest incurred under the Loan for the income year exceeds:
    - where interest is charged on the Loan from ANZ at a fixed rate for all or part of the term of the Loan and that fixed rate is applicable to the Loan for all or part of the income year, the amount of the Loan multiplied by the sum of the Reserve Bank of Australia's Indicator Lending Rate for Standard Variable Housing Loans and 100 basis points (the 'adjusted loan rate') at the time when the interest charge is first incurred during the term of the Loan, or the relevant part of the term (subsections 247-20(4) and (5)); and
    - where interest is charged on the Loan from ANZ at a variable rate for all or part of the term of the Loan and a variable rate is applicable to the Loan for all or part of the income year, the amount of the Loan multiplied by the average of the adjusted loan rates applicable during those parts of the income year when the Loan is at a variable rate (subsections 247-20(5) and (5A)); and

- (iii) the amount reasonably attributable to the cost of capital protection as worked out under paragraph 16(a)(ii) of this Product Ruling, is treated as the cost of the Purchase Put Option under subsection 247-20(6). This amount is not deductible under section 8-1.
- (b) Where the cost of the Purchase Put Option is factored into the interest rate charged on the Loan and the investor pays the Protection Level Increase Fee in the circumstances discussed at paragraph 20(m) of this Product Ruling:
  - (i) under subsection 247-20(3), the amount reasonably attributable to the cost of capital protection in an income year is the amount by which the total of the Protection Level Increase Fee and the interest incurred under the Loan for the income year exceeds:
    - where interest is charged on the Loan from ANZ at a fixed rate for all or part of the term of the Loan and that fixed rate is applicable to the Loan for all or part of the income year, the amount of the Loan multiplied by the adjusted loan rate at the time when the interest charge is first incurred during the term of the Loan, or the relevant part of the term (subsections 247-20(4) and (5)); and
    - where interest is charged on the Loan from ANZ at a variable rate for all or part of the term of the Loan and a variable rate is applicable to the Loan for all or part of the income year, the amount of the Loan multiplied by the average of the adjusted loan rates applicable during those parts of the income year when the Loan is at a variable rate (subsections 247-20(5) and (5A));
  - (ii) the amount reasonably attributable to the cost of capital protection as worked out under paragraph 16(b)(i) of this Product Ruling, reduced by the Protection Level Increase Fee, is treated as a further cost of the Purchase Put Option under subsection 247-20(6). For the purposes of this Product Ruling, this further cost of the Purchase Put Option is referred to as the 'additional amount';
  - (iii) the additional amount (if any) and the Protection Level Increase Fee are not deductible under section 8-1; and

- (iv) an amount equal to the interest incurred under the Loan, reduced by the additional amount (if any), will be deductible under section 8-1.
- (c) Where the cost of the Purchase Put Option (the Initial Option Fee) is paid as an upfront lump sum:
  - (i) under subsection 247-20(3), the amount reasonably attributable to the cost of capital protection in an income year is the amount by which the total of the Initial Option Fee, any Protection Level Increase Fee paid and the interest incurred under the Loan for the income year exceeds:
    - where interest is charged on the Loan from ANZ at a fixed rate for all or part of the term of the Loan and that fixed rate is applicable to the Loan for all or part of the income year, the amount of the Loan multiplied by the adjusted loan rate at the time when the interest charge is first incurred during the term of the Loan, or the relevant part of the term (subsections 247-20(4) and (5)); and
    - where interest is charged on the Loan from ANZ at a variable rate for all or part of the term of the Loan and a variable rate is applicable to the Loan for all or part of the income year, the amount of the Loan multiplied by the average of the adjusted loan rates applicable during those parts of the income year when the Loan is at a variable rate (subsections 247-20(5) and (5A));
  - (ii) the amount reasonably attributable to the cost of capital protection as worked out under paragraph 16(c)(i) of this Product Ruling, reduced by the Initial Option Fee and any Protection Level Increase Fee paid, is treated as a further cost of the Purchase Put Option under subsection 247-20(6) (the additional amount);
  - (iii) the additional amount (if any), the Initial Option Fee and any Protection Level Increase Fee paid are not deductible under section 8-1; and
  - (iv) an amount equal to the interest incurred under the Loan, reduced by the additional amount (if any), will be deductible under section 8-1.

- (d) Section 51AAA of the *Income Tax Assessment Act 1936* (ITAA 1936) will not apply to deny deductibility of the interest allowable as a deduction under section 8-1 of the ITAA 1997.
- (e) Section 82KL of the ITAA 1936 will not apply to deny deductibility of the interest allowable as a deduction under section 8-1 of the ITAA 1997.
- (f) Section 82KZMF of the ITAA 1936 will not apply to set the amount and timing of deductions for prepaid interest allowable as a deduction under section 8-1 of the ITAA 1997.
- (g) Section 82KZM of the ITAA 1936 will not apply to deny the investor immediate deductibility of any part of the prepaid interest allowable as a deduction under section 8-1 of the ITAA 1997, where at least one of the following applies for the year of income:
- the investor is a small business entity (as defined in subsection 328-110(1) of the ITAA 1997) that has not chosen to apply section 82KZMD of the ITAA 1936 to the expenditure; or
  - the investor is an individual who does not incur the interest in carrying on a business.
- (h) Sections 82KZMA and 82KZMD of the ITAA 1936 will apply to set the amount and timing of deductions for the prepaid interest allowable as a deduction under section 8-1 of the ITAA 1997 to an investor (other than a small business entity for the year of income that has not chosen to apply section 82KZMD of the ITAA 1936 to the expenditure) who is a taxpayer that is not an individual and does not carry on a business.
- (i) The cost base and reduced cost base that an investor has in the Securities will include the amount of the Loan used to finance the acquisition of the Securities, the investor's Contribution (if any) towards the acquisition of the Securities, and incidental costs of acquisition and disposal of the Securities (sections 110-25 and 110-55).
- (j) If the Closing Price of the Securities at Maturity is below the Protection Level and the investor's Purchase Put Option is exercised, under a Physical Settlement:
- (i) CGT event A1 under section 104-10 will happen in relation to the Securities for the investor;
  - (ii) the cost of capital protection, including the amount reasonably attributable to the cost of capital protection (as calculated under Division

- 247) and, where applicable, the Protection Level Increase Fee and the Initial Option Fee will be added to the cost base and reduced cost base of the Securities under subsection 134-1(1); and
- (iii) any capital gain or capital loss made by the investor on exercise of the Purchase Put Option will be disregarded under subsection 134-1(4).
- (k) If the Closing Price of the Securities at Maturity is below the Protection Level and the investor's Purchase Put Option is exercised, under a Cash Settlement:
- (i) CGT event C2 under paragraph 104-25(1)(e) will happen in relation to the Purchase Put Option for the investor; and
- (ii) pursuant to sections 110-25 and 110-55, the cost base and the reduced cost base of the Purchase Put Option will include the amount reasonably attributable to the cost of capital protection (as calculated under Division 247) and, where applicable, the Protection Level Increase Fee and the Initial Option Fee.
- (l) If the Closing Price of the Securities at Maturity is above or equal to the Protection Level and the investor's Purchase Put Option expires unexercised:
- (i) CGT event C2 under paragraph 104-25(1)(c) will happen in relation to the Purchase Put Option for the investor, resulting in a capital loss equal to the reduced cost base of the Purchase Put Option under subsection 104-25(3);
- (ii) pursuant to section 110-55, the reduced cost base of the Purchase Put Option will include the amount reasonably attributable to the cost of capital protection (as calculated under Division 247) and, where applicable, the Protection Level Increase Fee and the Initial Option Fee; and
- (iii) under a Physical Settlement, CGT event A1 under section 104-10 will happen in relation to the Securities for the investor.
- (m) If the Closing Price of the Securities at Maturity is above the Cap Level and the investor's Capped Purchase Put Option expires unexercised:

- (i) CGT event C2 under paragraph 104-25(1)(c) will happen in relation to the Capped Purchase Put Option for the investor, resulting in a capital loss equal to the reduced cost base of the Capped Purchase Put Option under subsection 104-25(3);
  - (ii) pursuant to section 110-55, the reduced cost base of the Capped Purchase Put Option will include the amount reasonably attributable to the cost of capital protection (as calculated under Division 247) and, where applicable the Protection Level Increase Fee, the Initial Option Fee and any Variable Premium Amount; and
  - (iii) under a Physical Settlement, CGT event A1 under section 104-10 will happen in relation to the Securities for the investor.
- (n) For CGT purposes, the investor's date of acquisition of Securities is the Commencement Date pursuant to section 109-5.
- (o) Any capital gain realised by an investor on the sale of Securities or exercise of the Purchase Put Option under a Cash Settlement will be treated as a discount capital gain under section 115-5 where the investor is an individual or a trust and the sale or exercise occurs more than 12 months after the Commencement Date.
- (p) Division 230 will not apply to any gains or losses with respect to ANZ Cobalt where the investor is excepted from the Division pursuant to section 230-455.
- (q) Where the investor elects to use the Dividend Give-up Facility in respect of their Securities:
  - (i) any dividends or distributions paid on those Securities will be assessable to the investor under paragraph 97(1)(a) of the ITAA 1936; and
  - (ii) the application of any dividends paid on those Securities by ANZ Equities Pty Ltd (the Nominee) to pay the Dividend Interest Amount will not constitute a related payment for the purposes of former Division 1A of Part IIIAA of the ITAA 1936.
- (r) Subject to the foreign income tax offset limit in section 770-75, the investor will be entitled to a foreign income tax offset under Division 770 in an income year for foreign income tax paid by the investor (or the Nominee) on an amount received by the investor under ANZ Cobalt that is included, in part or whole, in the assessable income of the investor for that income year.

- (s) The anti-avoidance provisions contained in Part IVA of the ITAA 1936 will not apply to deny deductibility of the interest incurred by the investor in respect of the Loan.
- (t) Paragraphs 16(a), (b), (c), (j), (k), (l) and (o) of this Product Ruling apply to a Capped Purchase Put Option acquired by the investor as they do to the Purchase Put Option.

## Scheme

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17. The scheme that is the subject of this Ruling is identified and described in the following documents:

- application for a Product Ruling as constituted by documents and information received on 22 February 2013, 6 March 2013, 14 March 2013, 15 March 2013, 2 April 2013, 3 April 2013 and 4 April 2013;
- ANZ Cobalt Product Disclosure Statement dated 3 April 2013, including the ANZ Cobalt Terms; and
- Deed Poll – Declaration of Trust (Trust Deed) dated 3 April 2013.

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

18. For the purposes of describing the scheme to which this Ruling applies, there are no other agreements, whether formal or informal, and whether or not legally enforceable, which an investor, or any associate of an investor, will be a party to, which are a part of the scheme. Unless otherwise defined, capitalised terms in this Product Ruling take their meaning as per the draft PDS and draft Trust Deed. Any use of the singular also includes the plural unless otherwise specified.

19. All Australian Securities and Investments Commission (ASIC) requirements are, or will be, complied with for the term of the agreements.

20. Following is a summary of the scheme:

- (a) ANZ Cobalt consists of a loan from ANZ (the Loan), used by the investor to finance up to 100% of the purchase price of a Parcel of Securities on the Commencement Date. Where the Loan finances less than 100% of the purchase price of a Parcel, the investor is required to make a Contribution towards the purchase price of the Parcel for an amount being the difference between the total cost of purchasing the Parcel on the Commencement Date and the amount of the Loan in respect of that Parcel.
- (b) The investor must complete and sign the Application Form. Upon acceptance by ANZ of an investor's Application Form, the investor is bound by the Terms and may request a Quote Sheet from ANZ. The Quote Sheet is prepared on the basis of the investor's specified parameters including the amount of the Loan, the Securities they propose to acquire with the Loan, the proposed Protection Level, the proposed Cap Level (if applicable), the proposed Term of the Loan (maximum 5 years) and whether the Loan is at a fixed or floating rate (reset annually). Where the investor wishes to proceed with the Loan on the terms set out in the Quote Sheet, the investor must provide a Transaction Request under which they irrevocably offer to enter into the Loan on those terms.
- (c) Unless an investor who purchases multiple Parcels of Securities applies for a Basket investment structure (where offered by ANZ), the investor will apply for a separate Loan for each Parcel of Securities. A Basket investment structure consists of only one Loan for the entire Basket. The Purchase Put Option (or Capped Purchase Put Option) in respect of that Loan and the set Protection Level (and Cap Level where applicable) will apply across all the Parcels of Securities that constitute the Basket on an aggregate basis.
- (d) The minimum Loan Limit is \$500,000 (or less at ANZ's discretion), subject to a minimum for each Parcel or Basket of Securities of \$100,000 (or less at ANZ's discretion). ANZ may at any time specify a Facility Limit, being the maximum total of all Amounts Outstanding under every Loan acquired by the investor.

- (e) For all investors (other than SMSF Investors), the Loan will be full recourse. To that end, investors (other than SMSF Investors) grant a Security Interest to ANZ over the Secured Property, including the Securities constituting each Parcel or Basket, as security for the Loan. In the case of a SMSF Investor, the Loan will be limited in recourse both at and before Maturity and ANZ will generally also require the provision of a Guarantee, which will be full recourse such that if there is any Amount Outstanding to ANZ after it has exercised its rights as the secured party in relation to the Parcel and any other Secured Property to which the Loan relates (as part of the Nominee Security Interest granted to ANZ by the Nominee), ANZ will be entitled to recover that amount from the Guarantor.
- (f) The investor selects from a range of Securities that ANZ have approved for inclusion in ANZ Cobalt. The Securities (other than those Securities acquired by or on behalf of SMSF Investors, International Securities or Securities that are the subject of the Dividend Give-Up Facility) are held by the Sponsoring Participant for the purposes of CHESS. Investors (with the exception of SMSF Investors, and those investors who acquire International Securities or elect to use the Dividend Give-Up Facility) hold the legal and (unless they are trustees) beneficial interest in the Securities.
- (g) The Securities acquired by or on behalf of a SMSF Investor, International Securities acquired by any investor and Securities that are the subject of the Dividend Give-Up Facility are held by the Nominee (or a sub-custodian of the Nominee) as trustee for the investor on the terms of the Trust Deed. SMSF Investors and those investors who acquire International Securities or elect to use the Dividend Give-Up Facility will hold a beneficial interest in the relevant Securities whilst those Securities are held by the Nominee or a sub-custodian of the Nominee;
- (h) Interest on the Loan is payable in advance on each Interest Payment Date as specified in the relevant Confirmation Letter (unless agreed otherwise with ANZ and subject to an investor's participation in the Dividend Give-Up Facility).

- (i) An investor that enters into a Loan must also acquire a Purchase Put Option in respect of a Parcel or Basket of Securities, under which the investor will have the right to sell the corresponding Parcel or Basket of Securities to ANZ at the Protection Level on the Maturity Date. The cost of the Purchase Put Option (being the Initial Option Fee) may be paid either as an upfront lump sum or as a component of the interest rate payable on the Loan.
- (j) There may be a different interest rate applicable to each Parcel of Securities or Basket. However, where an investor has acquired multiple Parcels of Securities and applied the Basket investment structure, ANZ will apply a single blended interest rate across all the Parcels of Securities held by that investor in the Basket. The interest rate will be determined prior to the Loans being made available and will be reflective of the type and size of the Parcels of Securities chosen, the Protection Level (and Cap Level, if relevant) chosen and the Maturity Date chosen.
- (k) A Purchase Put Option includes a Capped Purchase Put Option. A Capped Purchase Put Option involves both a Protection Level and a Cap Level, the latter being the level at which the investor elects to cap the capital growth in relation to a Parcel or Basket of Securities. As per the Purchase Put Option, the Initial Option Fee in respect of a Capped Purchase Put Option may be paid by the investor as either an upfront lump sum or as a component of the interest rate payable on the Loan. If the Closing Price of the Securities on the Maturity Date is above the Cap Level, the investor will be required to pay to ANZ a Variable Premium Amount equal to the difference.
- (l) The investor can also request, prior to the Commencement Date and subject to ANZ's consent to use the Automatic Lock-In Facility, to automatically increase the Protection Level for their Purchase Put Option to an Increased Protection Level if the aggregate last trade price of the Securities in their Parcel or Basket on any day during the Term equals or exceeds the nominated Trigger Price. This feature may have the effect of increasing the cost of the Purchase Put Option.
- (m) Where, during the Term of a Loan, the Closing Price of a Parcel or Basket (as applicable) increases in value by at least \$50,000 since the Commencement Date, an investor can, subject to approval from ANZ and the payment to ANZ of the Protection Level Increase Fee, increase their Protection Level.

- (n) Under the Dividend Give-Up Facility the investor elects to have any cash dividends and other distributions paid on the Securities held by the Nominee on behalf of the investor applied on behalf of the investor towards the payment of the interest on the Loan (the Dividend Interest Amount) to ANZ.
- (o) At the Maturity Date, the Purchase Put Option (or Capped Purchase Put Option) may either automatically exercise (where the Closing Price of the Parcel or Basket, as applicable, is less than the Protection Level for that Parcel or Basket) or exercise by delivery of an Exercise Notice by the investor to ANZ, and the investor may specify whether it elects to have a Physical Settlement or Cash Settlement.
- (p) Where the Purchase Put Option (or Capped Purchase Put Option) is exercised and Physical Settlement is chosen, or the Purchase Put Option (or Capped Purchase Put Option) is automatically exercised without the investor having nominated Physical or Cash Settlement, the Securities constituting each Parcel or Basket will be transferred (sold) to ANZ for an amount equal to the Protection Level. Where the Closing Price of the Parcel or Basket (as applicable) on the Maturity Date is less than the Protection Level for that Parcel or Basket, ANZ will pay to the investor an amount equal to the Protection Level for that Parcel or Basket, less any costs incurred in connection with the transfer.
- (q) Where the Purchase Put Option (or Capped Purchase Put Option) is exercised and Cash Settlement is chosen, the investor will keep the Securities constituting each Parcel or Basket and will be required to pay to ANZ the Amount Outstanding. On the Settlement Date ANZ will be required to pay to the investor the amount by which the Protection Level for the relevant Parcel or Basket (as applicable) exceeds the Closing Price of that Parcel or Basket on the Maturity Date (if at all).

- (r) At the Maturity Date, the Purchase Put Option (or Capped Purchase Put Option) may instead expire unexercised and automatically lapse. In this instance the investor may request (where the Closing Price of the relevant Parcel or Basket, as applicable, is equal to or greater than the Protection Level the investor is deemed to have requested) that ANZ facilitate a sale of the relevant Parcel or Basket on the investor's behalf. Upon acceptance of that request by ANZ, it will acquire or arrange for the sale of the investor's Parcel or Basket (as applicable) on the Maturity Date and pay the proceeds of the sale (net of transaction costs) in reduction of the Amount Outstanding by the investor in respect of the Loan and Purchase Put Option (including the Variable Premium Amount for a Capped Purchase Put Option), before paying any excess to the investor. In the absence of such a settlement, the investor may keep the Securities constituting each Parcel or Basket and pay the Amount Outstanding to ANZ (including the Variable Premium Amount for a Capped Purchase Put Option).
- (s) For Capped Purchase Put Options, if the Closing Price of the Parcel or Basket (as applicable) on the Maturity Date is greater than the Cap Level for that Parcel or Basket,
  - (i) if the investor requests that ANZ facilitate a sale of that Parcel or Basket (and ANZ accepts this request), the investor's Parcel or Basket will be sold on the investor's behalf and the proceeds from that sale will be applied to pay ANZ the Variable Premium Amount and any Amount Outstanding in respect of the Loan to which the Capped Purchase Put Option relates; and
  - (ii) if the investor does not request a sale of that Parcel or Basket, the applicable Variable Premium Amount is automatically due and payable by the investor to ANZ in addition to any other Amount Outstanding.

**Assumptions**

21. This Ruling is made on the basis of the following necessary assumptions:

- (a) all investors are Australian residents for taxation purposes;
- (b) the Securities consist solely of ordinary shares in an ASX-listed company, units in an ASX-listed unit trust, ASX-listed CDIs or International Securities;

- (c) at all times during the scheme, where the Securities consist of units in a trust, the trust satisfies the requirements of subparagraph 82KZME(5)(b)(iii) of the ITAA 1936;
- (d) at all times during the scheme, where the underlying securities in the CDIs are shares in a company, the shares will satisfy the requirements of subparagraph 82KZME(5)(b)(ii) of the ITAA 1936;
- (e) at all times during the scheme, where the underlying securities in the CDIs are units in a unit trust, the trust will satisfy the requirements of subparagraph 82KZME(5)(b)(iii) of the ITAA 1936;
- (f) the investors will hold their interests in the Securities on capital account, are not traders in the Securities and are not treated for taxation purposes as trading in the Securities, carrying on a business of investing in the Securities, or holding the Securities as trading stock or a revenue asset;
- (g) the investors will hold the Purchase Put Option or Capped Purchase Put Option on capital account, are not treated for taxation purposes as trading in the Purchase Put Option or Capped Purchase Put Option, carrying on a business of investing in the Purchase Put Option or Capped Purchase Put Option, or holding the Purchase Put Option or Capped Purchase Put Option as trading stock or a revenue asset;
- (h) in respect of any interest to be paid in advance under the Loan, these may be prepaid only in relation to a loan interest payment period of 12 months or less, and which ends on or before the last day of the income year following the expenditure year;
- (i) the dominant purpose of an investor in entering into the arrangement is to derive an amount of assessable income from the Securities that exceeds the total expenses incurred;
- (j) the investors have not made an election under subsection 230-455(7) to have Division 230 apply;
- (k) the investors or any other entity will not become entitled to either a refund of any foreign income tax paid by the investor (or the Nominee), or any other benefit worked out by reference to the amount of the foreign income tax (other than a reduction in the amount of the foreign income tax);
- (l) the investors will not be under any legal disability and will be presently entitled to 100% of the income of the trust estate created under the Dividend Give-Up Facility;

- (m) the scheme will be executed in the manner described in the Scheme section of this Ruling and the scheme documentation referred to in paragraph 17 of this Ruling; and
- (n) all dealings by the investors, ANZ and the Nominee under the scheme will be at arm's length.

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**Commissioner of Taxation**

17 April 2013

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## 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.*

### **Section 8-1 and Division 247 – capital protected borrowings and deductibility of interest**

22. The interest paid on a borrowing used to acquire income producing assets such as Securities is generally treated as deductible under section 8-1 where it is expected that dividends, trust distributions or other assessable income would be derived from the investment (see Taxation Ruling TR 95/33). However, the ability to claim interest deductions may be subject to Division 247.

23. Division 247 limits the allowable deductions for expenditure incurred under a 'capital protected borrowing'. Broadly, a capital protected borrowing arises where an amount is borrowed under an arrangement where the borrower is protected against the fall in value of some specified securities, and where that borrowing is made for the purpose of investing in those securities.

24. Division 247 applies to the Loan where the investor uses the Loan to acquire Securities and the investor is protected against the fall in the market value of those Securities.

25. Division 247 sets out a methodology for reasonably attributing the cost of capital protection incurred by a borrower under a capital protected borrowing (section 247-20). Division 247 ignores any amount which is not in substance for capital protection or interest in calculating the cost of capital protection, pursuant to subsection 247-20(3).

26. Where the cost of the Purchase Put Option is factored into the interest rate charged on the Loan and there is no separate charge payable by an investor for the Purchase Put Option:

- (a) the cost of capital protection is the amount worked out under the method statement in subsection 247-20(3), as set out in paragraph 16(a)(ii) of this Product Ruling;
- (b) under step 1 of the method statement, the total amount incurred by the investor under or in respect of the Loan for the income year is the interest incurred on the Loan for the income year;
- (c) where the total amount incurred by the investor worked out under step 1 of the method statement is less than the total interest that would have been incurred by the investor worked out under step 2 of the method statement, there is no amount reasonably attributable to the cost of capital protection. In these circumstances, the interest on the Loan will be fully deductible under section 8-1;

- (d) where the total amount incurred by the investor worked out under step 1 of the method statement is greater than the total interest that would have been incurred by the investor worked out under step 2 of the method statement, the balance is reasonably attributable to the cost of capital protection and is treated as if it were incurred for the Purchase Put Option (subsection 247-20(6)); and
- (e) the investor's Purchase Put Option is a capital asset. Therefore, the amount reasonably attributable to the cost of capital protection is capital in nature and not deductible under section 8-1.

27. Where either the cost of the Purchase Put Option is factored into the interest rate charged on the Loan and the investor pays a Protection Level Increase Fee in the circumstances discussed at paragraph 20(m) of this Product Ruling; or the investor elects to pay the Initial Option Fee for the Purchase Put Option as an upfront lump sum:

- (a) the cost of capital protection is the amount worked out under the method statement in subsection 247-20(3), as set out in paragraph 16(b)(i) or 16(c)(i) of this Product Ruling, as applicable;
- (b) under step 1 of the method statement, the total amount incurred by the investor under or in respect of the Loan for the income year includes the interest incurred on the Loan and any amounts that are in substance for capital protection (such as the Initial Option Fee and/or the Protection Level Increase Fee) for the income year;
- (c) where the total amount incurred by the investor worked out under step 1 of the method statement is less than the total interest that would have been incurred by the investor worked out under step 2 of the method statement, there is no amount reasonably attributable to the cost of capital protection. In these circumstances, the interest on the Loan will be fully deductible under section 8-1;

- (d) where the total amount incurred by the investor worked out under step 1 of the method statement is greater than the total interest that would have been incurred by the investor worked out under step 2 of the method statement, the balance is reasonably attributable to the cost of capital protection. In calculating the additional amount (as per paragraph 16(b)(ii) or 16(c)(ii) of this Product Ruling, as applicable), the amount reasonably attributable to the cost of capital protection will be reduced by the actual payment for a Purchase Put Option (the Initial Option Fee and any Protection Level Increase Fee paid) in accordance with subsection 247-20(6). The additional amount, to the extent that it is greater than zero, constitutes a further cost of capital protection in addition to the Initial Option Fee for the Purchase Put Option or any Protection Level Increase Fee paid; and
- (e) the investor's Purchase Put Option is a capital asset. Therefore, the Initial Option Fee, any Protection Level Increase Fee paid and the additional amount (if any) is capital in nature and not deductible under section 8-1.

28. Where an investor has acquired multiple Parcels of Securities (and applied the Basket investment structure) and ANZ has applied a single blended interest rate across all the Parcels of Securities held by the investor in the Basket, the investment will be treated as one arrangement for the purposes of Division 247.

## Section 51AAA

29. By acquiring the Securities, it is contemplated that an investor will derive assessable income by way of the receipt of dividend income or trust distributions and capital gains. As interest would have been deductible under section 8-1 of the ITAA 1997 notwithstanding the inclusion of a net capital gain in assessable income, section 51AAA of the ITAA 1936 has no application to an investor who enters into ANZ Cobalt.

## Section 82KL

30. The operation of section 82KL of the ITAA 1936 depends, among other things, on the identification of a certain quantum of 'additional benefits'. Insufficient additional benefits will be provided to trigger the application of section 82KL. Section 82KL will not apply to deny the deductions otherwise allowable under section 8-1 of the ITAA 1997.

**Subdivision H of Division 3 of Part III**

31. Subdivision H of Division 3 of Part III (Subdivision H) of the ITAA 1936 deals with the timing of deductions for certain advance expenditure incurred under an agreement in return for the doing of a thing under that agreement that will not be wholly done within the same year of income. Separate rules apply depending on whether the expenditure is incurred in the carrying on of a business, whether the investor is a small business entity, whether the investor is an individual and whether the investor is not an individual and incurs the expenditure otherwise than in carrying on a business. This Subdivision does not apply to 'excluded expenditure' which is defined in subsection 82KZL(1) of the ITAA 1936 to include amounts of less than \$1,000 or amounts that are of a capital nature.

**Subdivision 328-C – small business entities**

32. Under section 328-110, an investor carrying on a business in an income year will be a small business entity for that year (the current year) if:

- (a) the investor carried on a business in the previous income year and the aggregated turnover for that year was less than \$2 million;
- (b) the aggregated turnover for the current year is likely to be less than \$2 million and, where the investor carried on a business in each of the two previous income years, the aggregated turnover for each of those income years was less than \$2 million; or
- (c) the aggregated turnover for the current year, worked out as at the end of the year is less than \$2 million.

**The eligible service period for the purposes of Subdivision H**

33. The interest charged on the Loan that is deductible under section 8-1 of the ITAA 1997 is in relation to a prepayment of loan interest for a period that is 12 months or less. Paragraph 82KZL(2)(a) of the ITAA 1936 provides that a payment of interest that is made in return for the making available of a loan principal is to be taken, for the purposes of Subdivision H, to be expenditure incurred under an agreement in return for the doing of a thing under the agreement for the period to which the interest payment relates. The eligible service period in relation to a payment of loan interest is determined by reference to the period to which the interest relates, and not to the period of the Loan.

## **Sections 82KZME and 82KZMF – prepaid expenditure and ‘tax shelter’ style arrangements**

34. The rules in sections 82KZME and 82KZMF of the ITAA 1936 apply, subject to the exceptions in section 82KZME, where expenditure is incurred in relation to a ‘tax shelter’ style arrangement for the doing of a thing that is not to be wholly done within the expenditure year.

35. For the purposes of section 82KZME of the ITAA 1936, ‘agreements’ are broadly defined to include an entire scheme of which a contract may form part. Under subsection 82KZME(4) of the ITAA 1936, the relevant agreement is all the contractual arrangements and activities associated with the participation in ANZ Cobalt, including the financing, Securities acquisition and Securities disposal arrangements.

36. Exception 1, as contained in subsection 82KZME(5) of the ITAA 1936, applies to exclude the Loan from the operation of section 82KZMF of the ITAA 1936 where:

- (a) the prepaid interest expenditure under the Loan is incurred in respect of money borrowed to acquire Securities that are as described in subparagraphs 82KZME(5)(b)(ii) and (iii) of the ITAA 1936;
- (b) the investor can reasonably be expected to obtain dividends or trust distributions from the investment;
- (c) the investor will not obtain any other kind of assessable income from the investment except for capital gains; and
- (d) all aspects of ANZ Cobalt are conducted at arm’s length.

37. Deductibility of the prepaid interest must therefore be considered under the prepayment rules contained in paragraphs 38 to 43 of this Product Ruling.

## **Section 82KZM – prepaid expenditure incurred by certain small business entities and individuals incurring non-business expenditure**

38. Section 82KZM of the ITAA 1936 operates to spread over more than one income year a deduction for prepaid expenditure incurred by a taxpayer that is either:

- (a) a small business entity for the year of income that has not chosen to apply section 82KZMD of the ITAA 1936 to the expenditure; or
- (b) a taxpayer that is an individual and the expenditure is not incurred in carrying on a business.

39. The expenditure must not be excluded expenditure and must be incurred otherwise than in carrying on a business. Section 82KZM of the ITAA 1936 applies if the eligible service period for the expenditure is longer than 12 months, or the eligible service period for the expenditure is 12 months or shorter but ends after the last day of the year of income after the one in which the expenditure was incurred and the expenditure would otherwise be immediately deductible under section 8-1 of the ITAA 1997.

40. As the eligible service period in relation to the deductible interest payment under the Loan is not more than 12 months and does not end after the last day of the year of income after the one in which the expenditure was incurred, section 82KZM of the ITAA 1936 will have no application to investors who are a small business entity for the year of income that have not chosen to apply section 82KZMD of the ITAA 1936 to the expenditure, or to investors who are individuals where the expenditure is not incurred in carrying on a business. Investors who satisfy these tests will be able to claim an immediate deduction for the interest allowable under section 8-1 of the ITAA 1997 incurred under the Loan.

**Sections 82KZMA and 82KZMD – prepaid non-business expenditure incurred by non-individual and non-small business entities**

41. Sections 82KZMA and 82KZMD of the ITAA 1936 set the amount and timing of deductions for expenditure for an investor (other than a small business entity for the year of income that has not chosen to apply section 82KZMD to the expenditure) that is not an individual and does not incur the expenditure in carrying on a business.

42. The expenditure must not be excluded expenditure and must be incurred in return for the doing of a thing under an agreement that is not to be wholly done within the expenditure year.

43. For these investors, the amount of prepaid interest incurred under the Loan which is allowable as a deduction under section 8-1 will be apportioned over the relevant interest payment period.

**Parts 3-1 and 3-3 – application of CGT provisions to the Purchase Put Option, Capped Purchase Put Option and Securities**

44. If an investor's Purchase Put Option is exercised and the investor elects a Physical Settlement, the investor will dispose of the Securities and CGT event A1 will arise for the investor in respect of the disposal (section 104-10). Under item 2 of the table in subsection 134-1(1), the investor's cost base and reduced cost base in the Securities for these purposes will include the cost of capital protection as worked out under Division 247 plus the Protection Level Increase Fee and the Initial Option Fee (where applicable). Any capital gain or capital loss on exercise of the Purchase Put Option will be disregarded (subsection 134-1(4)).

45. If an investor's Purchase Put Option is exercised and the investor elects a Cash Settlement, CGT event C2 will arise for the investor in respect of the exercise of the Purchase Put Option (section 104-25). The cost base and reduced cost base of the Purchase Put Option will include the cost of capital protection as worked out under Division 247 plus the Protection Level Increase Fee and the Initial Option Fee (where applicable) – sections 110-25 and 110-55. No CGT event will occur in relation to the Securities.

46. Where the Purchase Put Option expires unexercised, CGT event C2 will arise for the investor in relation to the Purchase Put Option at that time (section 104-25). As the investor will not receive any capital proceeds in respect of the expiry of the Purchase Put Option, a capital loss will be made by the investor in this regard, equal to the investor's reduced cost base in the Purchase Put Option. Under section 110-55, the reduced cost base of the Purchase Put Option will include:

- (a) the cost of capital protection as worked out under Division 247 plus the Protection Level Increase Fee and the Initial Option Fee (where applicable); and
- (b) any Variable Premium Amount paid by the investor.

47. If an investor's Purchase Put Option or Capped Purchase Put Option expires unexercised and the investor elects a Physical Settlement, the investor will sell the Securities and CGT event A1 will arise for the investor in respect of the disposal (section 104-10).

48. Under section 110-25 and 110-55 respectively, the investor's cost base and reduced cost base in the Securities will include the amount of the Loan used to finance the acquisition of the Securities, their Contribution (if any) and incidental costs incurred by the investor in acquiring and disposing of the Securities (this includes stamp duty and costs of transfer). As per paragraph 44 of this Product Ruling, where the investor's Purchase Put Option is exercised and the investor elects a Physical Settlement, the investor's cost base and reduced cost base in the Securities also include the cost base or reduced cost base of the Purchase Put Option.

49. Division 115 allows a taxpayer a discount on capital gains in certain circumstances. In accordance with section 115-5, any capital gain realised by an investor on the sale of the Securities or exercise of the Purchase Put Option under a Cash Settlement will be treated as a discount capital gain where the investor is an individual or a trust and has held the Securities or Purchase Put Option for more than 12 months (excluding the days of acquisition and disposal).

### **Division 230 – taxation of financial arrangements**

50. Division 230 of the ITAA 1997 sets out the tax treatment of gains or losses from a 'financial arrangement'. Where an arrangement is not a qualifying security for the purposes of Division 16E of the ITAA 1936 and an election under section 230-455 to have Division 230 of the ITAA 1997 apply to financial arrangements has not been made, then pursuant to section 230-455 of the ITAA 1997, Division 230 of the ITAA 1997 does not apply in relation to gains or losses from a financial arrangement held by:

- (a) an individual; or
- (b) a superannuation entity, a managed investment scheme or an entity substantially similar to a managed investment scheme under foreign law with assets of less than \$100 million; or
- (c) an ADI, a securitisation vehicle or other financial sector entity with an aggregated turnover of less than \$20 million; or
- (d) another entity with an aggregated turnover of less than \$100 million, financial assets of less than \$100 million and assets of less than \$300 million.

### **Dividend Give-Up Facility**

51. Pursuant to the assumption at paragraph 21(l) of this Product Ruling, an investor who elects to use the Dividend Give-Up Facility in respect of their Securities will be assessable under section 97 of the ITAA 1936 on any dividends and distributions received by the Nominee on those Securities.

52. The payment by the Nominee of any dividends received by the Nominee under the Dividend Give-Up Facility in respect of the Dividend Interest Amount owing by the investor to ANZ does not have the effect of 'passing the benefit' of those dividends to ANZ, and therefore will not constitute a related payment for the purposes of former section 160APHN under Division 1A of Part IIIAA of the ITAA 1936.

## **Division 770 – foreign income tax offsets**

53. Division 770 allows a non-refundable tax offset for an income year for foreign income tax paid where that amount of foreign income tax is paid in respect of an amount that is included in your assessable income for the year.

54. To the extent that the investor has paid, or is deemed to have paid, foreign income tax (such as withholding tax at source):

- (a) the foreign taxes paid by the investor will be regarded as foreign income tax for the purposes of section 770-15;
- (b) where those foreign taxes are paid by the Nominee (or a sub-custodian of the Nominee), the foreign income tax will be deemed, under section 770-130, to have been paid by the investor; and
- (c) subject to the foreign income tax offset limit in section 770-75 the investor will be entitled to a non-refundable foreign income tax offset in an income year for the foreign income tax the investor paid, or is deemed to have paid, on amounts that are included in the investor's assessable income that year.

## **Part IVA – anti-avoidance**

55. Provided that the scheme ruled on is entered into and carried out as described in this Ruling, it is accepted that the scheme is an ordinary commercial transaction and Part IVA of the ITAA 1936 will not apply.

## **Appendix 2 – Detailed contents list**

56. The following is a detailed contents list for this Ruling:

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*Previous draft:*

Not previously issued as a draft

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TR 95/33

*Subject references:*

- capital protected borrowings
- financial products
- interest expenses
- prepaid expenses
- product rulings
- public rulings
- taxation administration

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- ITAA 1997 8-1
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