IT 2033 - Bearer debentures - application of section 126 of the Income Tax Assessment Act 1936

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TAXATION RULING NO. IT 2033

BEARER DEBENTURES - APPLICATION OF SECTION 126 OF THE INCOME TAX ASSESSMENT ACT 1936

F.O.I. EMBARGO: May be released

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F.O.I. INDEX DETAIL REFERENCE NO:	SUBJECT REFS:	LEGISLAT. REFS:
I 1104213	INTEREST ON BEARER DEBENTURES	DIVISIONS 11, 11A

PREAMBLE The question has arisen recently whether section 126 of the Income Tax Assessment Act operates to impose a liability to Australian income tax on the payment of interest overseas on moneys borrowed overseas by means of widely spread bearer debentures issued by a foreign branch office of an Australian resident company for use wholly in the foreign branch business operations.

RULING 2. Section 126 is a longstanding provision which was enacted to counter the evasion of Australian income tax arising out of payment of interest on bearer securities. Where a company borrower does not supply to the Commissioner of Taxation the names and addresses of security holders to whom the interest is paid there is a liability on the company borrower to withhold tax of 55% of the interest paid on bearer securities. There is provision in section 127 to credit tax paid by a company under section 126 and to refund any excess where a person includes the interest on bearer securities in assessable income.

3. Section 126 extends to overseas issues of bearer securities. However, interest on bearer securities which satisfy the tests set out in section 128F, i.e. interest paid on overseas borrowings made through widely spread bearer debentures for use in, or in connection with a business carried on in Australia by a resident in Australia, is exempt from both withholding tax imposed by Division 11A and also from section 126 tax.

4. In the particular circumstances of this ruling the withholding tax provisions of Division 11A do not apply, i.e. the moneys were not borrowed for use in or in connection with a business carried on in Australia. Consequently, an exemption certificate in terms of section 128F which would effectively free the interest from liability to withholding tax both under Division 11A and section 126 is not available.

5. Having regard to its legislative purpose and history section 126 is not considered to operate where interest is paid overseas on widely spread bearer debentures issued overseas to non-residents of Australia to secure the repayment of moneys

borrowed overseas for use in the business operation of a foreign branch of an Australian taxpayer and where the interest is an outgoing wholly incurred in the carrying on of a business outside Australia at or through the foreign branch.

6. In the event that an Australian resident became the holder of a bearer debenture of this nature any interest received by the Australian resident would be liable to Australian tax.

COMMISSIONER OF TAXATION
2 May 1983