IT 2238 - Income tax : interest withholding tax - exemption of interest where moneys raised by widely distributed debentures - use of loan funds outside of Australia

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TAXATION RULING NO. IT 2238

INCOME TAX : INTEREST WITHHOLDING TAX - EXEMPTION OF INTEREST WHERE MONEYS RAISED BY WIDELY DISTRIBUTED DEBENTURES - USE OF LOAN FUNDS OUTSIDE OF AUSTRALIA

F.O.I. EMBARGO: May be released

REF H.O. REF: 82/3705-1
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DATE OF EFFECT: Immediate

B.O. REF:

DATE ORIG. MEMO ISSUED: 8 July 1982
24 Aug 1984
10 Oct 1984

F.O.I. INDEX DETAIL

REFERENCE NO:	SUBJECT REFS:	LEGISLAT. REFS:
I 1205596	EXEMPTION FROM INTEREST WITHHOLDING TAX	128F 128F(4)(a) 128F(4)(b)
	WIDELY DISTRIBUTED DEBENTURE ISSUE	128F(7)
	USE OF MONEYS IN AN AUSTRALIAN BUSINESS OVERSEAS SUBSIDIARIES	

PREAMBLE Advice was sought from this office whether a certificate of exemption from withholding tax would be forthcoming under section 128F of the Income Tax Assessment Act 1936 on interest payable on loans raised by way of promissory note issues. The notes were to be issued overseas in bearer form under borrowing facilities involving the use of tender panels for marketing purposes. Moneys raised by the issues were to be used by the borrower for business purposes, to some extent outside Australia.

FACTS 2. Each of the borrowing facilities provided for notes with an aggregate face value of $A100m to be issued in denominations of $US 100,000 or /stg 50,000, with a minimum issue of $US10m. or /stg 5m. The notes would have varying periods to maturity. In some cases notes would be issued at a discount maturing at periods of 1-12 months. In other cases the period was in excess of 8 years with an option exercisable by the noteholders at the end of each six monthly interest period requiring repurchase by the tender panel members.

3. The notes were to be issued through a tender panel of approximately 30 international banks and financial institutions, including the managers and the underwriters. Members of the panel would be selected for their access to and capacity to place securities with a broad range of investors. The members would be able, but not obliged, to bid for notes upon issue in minimum amounts of $US1M or /stg. 500,000 for onsale to investors. The bids would be on the basis that the notes would be purchased at prices not less than the stipulated

minimum purchase price and the price would be expressed as a yield in relation to the London Inter Bank Offer Rate (LIBOR) for notes of the kind, up to a maximum of 1/4% above LIBOR. The lowest bids would be accepted progressively until the total amount of the issue was fully placed.

4. In the unlikely event that a note issue was not fully purchased by members of the tender panel the managers and underwriters would be required to purchase the shortfall. It would be unlikely however for any of the parties i.e., managers, underwriters or tender panelists, to retain the notes themselves for any period in the ordinary course of their businesses whether acquired upon original issue or under the 6 monthly option referred to above.

5. In one instance tender panelists were to receive a placement fee of 1/16% p.a. of their allotment for the period of the issue while in another members were to take a margin of much the same proportions by buying the notes and reselling them to their clients. The managers were formally required to use their best endeavours to maintain a secondary market in the notes while tender panel members similarly had an obligation to distribute any notes allotted to them on a basis which is as wide as practicable.

6. Some of the loan moneys raised by the issue of notes in the manner described were to be used to take up additional capital in, or to be on-lent to, a subsidiary company or companies resident in countries outside Australia and which did not carry on business wholly or partly in Australia. It was claimed that the borrowing company would be using the relevant loan moneys outside Australia for purposes connected with the operations in Australia of a business carried on by the borrower wholly or partly in Australia, i.e., the integrated worldwide business of the borrower group. The borrower, being a resident of Australia, use of the loan moneys in that way would constitute "use of moneys in the Australian business" in terms of sub-section 128F(7).

7. Confirmation was sought that the arrangements satisfied the wide distribution requirements of paragraph 128F(4)(a) and that the use of the loan moneys described in paragraph 6 would be satisfactory in terms of paragraph 128F(4)(b).

RULING

8. It was accepted that notes issued in accordance with the proposed arrangements would be issued with a view to public subscription or purchase or other wide distribution among investors as required by paragraph 128F(4)(a) of the Assessment Act. The size of the note issue, the denominations of the notes and the marketing arrangements under which the tender panel members would bid for notes against firm orders received by them from customers in advance of the issue were taken into account in reaching that decision. However, a review of the arrangements would be necessary should there be evidence of any of the parties consistently retaining the notes.

9. The issue of a certificate under section 128F of

exemption from withholding tax is also dependent on the borrower or ultimate end user of the loan moneys using those moneys in an Australian business or businesses - paragraph 128F(4)(b) of the Assessment Act. Such use is stated in sub-section 128F(7) to be, broadly, a use of the loan moneys by a resident for the purposes of a business carried on by the resident wholly or partly in Australia, or a use of the loan moneys by the resident outside of Australia for purposes connected with the operations in Australia of a business carried on by the resident wholly or partly in Australia.

10. The use in Australia test applies to the end user of the loan moneys. None of the subsidiary companies who were to be the end users of the loan money carried on business wholly or partly in Australia. When the legislation was being drafted it was to be on the basis that exemption should not extend to loans raised by means of bearer debentures for on-lending to a non-resident subsidiary company operating only outside Australia because it could result in Australia being used as a tax haven. For these reasons it was not accepted that interest payable on the loan moneys would be exempt from withholding tax.

COMMISSIONER OF TAXATION
30 December 1985