



PR 1999/12A - Addendum - Income tax: deductibility of interest incurred on borrowings under the Macquarie Sharemarket Lending Facility for the purchase of units in the Macquarie Enhanced Index Trust

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Addendum

Income tax: deductibility of interest incurred on borrowings under the Macquarie Sharemarket Lending Facility for the purchase of units in the Macquarie Enhanced Index Trust

This Addendum sets out the Commissioner's opinion as to the way in which the rules in Subdivision H of Division 3 of Part III of the *Income Tax Assessment Act 1936* ('ITAA 1936'), which affect the timing of deductions for certain prepaid expenditure, apply to the unchanged arrangement currently described in the *Arrangement* part of Product Ruling PR 1999/12. Investors are reminded of the important statements made under the *Class of persons* and *Qualifications* sections of the *What this Product Ruling is about* part of PR 1999/12.

This Addendum amends PR 1999/12 as follows:

Paragraph 2, omit the dot point relating to 'section 82KZM of the 1936 Act; and' and substitute with:

- section 82KL of the 1936 Act;
- section 82KZM of the 1936 Act;
- sections 82KZMA, 82KZMB and 82KZMC of the 1936 Act;
- sections 82KZME and 82KZMF of the 1936 Act; and

Subparagraph 15(c), omit the words 'sections 82KJ and 82KK' and substitute with:

'sections 82KJ, 82KK and 82KL'

Subparagraph 15(d), omit the subparagraph and substitute with:

- (d) section 82KZM of Subdivision H of Division 3 of Part III of the 1936 Act will not apply to deny immediate deductibility for prepaid interest expenditure incurred

in respect of borrowings under the Facility used to fund the purchase of units in the Enhanced Index Trust where the expenditure is incurred:

- (i) at or before 11.45 a.m. (by legal time in the Australian Capital Territory) on 21 September 1999; or
- (ii) after 11.45 a.m. (by legal time in the Australian Capital Territory) on 21 September 1999 and during an income year commencing before 1 July 2001 and at least one of the following applies: the expenditure is (A) incurred by a small business taxpayer for the year of income; (B) incurred in meeting a pre-RBT obligation; (C) not incurred in carrying on a business; or
- (iii) during an income year commencing after 30 June 2001 and at least one of the following applies: the expenditure is (A) incurred by an STS taxpayer for the year of income; (B) incurred in meeting a pre-RBT obligation; (C) incurred by an individual but not in carrying on a business.

Further, to obtain the deduction in full in the year of the prepaid interest being incurred the interest must be in respect of the making available or continued making available of the loan principal to which the interest relates for no longer than a period of 12 months after the day on which it is incurred and where (d)(iii) applies, the period ends no later than the last day of the income year following the income year in which the interest was incurred.

Subparagraph 15(d), omit the word ‘and’.

Subparagraph 15(e), omit the subparagraph and substitute with:

- (e) sections 82KZMA, 82KZMB and 82KZMC of the 1936 Act will apply to determine the amount and timing of deductions for prepaid interest expenditure incurred in respect of borrowings under the Facility used to fund the purchase of units in the Enhanced Index Trust where the expenditure is incurred:
 - (i) after 11.45 a.m. (by legal time in the Australian Capital Territory) on 21 September 1999 and during an income year commencing before

- 1 July 2001 by an investor (other than a small business taxpayer for the year of income) in carrying on a business; or
- (ii) during an income year commencing after 30 June 2001 by an investor (other than an STS taxpayer for the year of income) who either carries on a business or is not an individual and does not carry on a business.

After subparagraph 15(e), insert:

- (f) section 82KZMF of the 1936 Act will not apply to prepaid interest expenditure incurred by an investor in respect of borrowings under the Facility used to fund the purchase of units in the Enhanced Index Trust; and
- (g) the anti-avoidance provisions in Part IVA of the 1936 Act will not be applied to deny deductibility of any interest incurred by an investor in respect of borrowings used to fund the purchase of units in the Enhanced Index Trust.

Subparagraph 16(e), omit the subparagraph and substitute with:

- (e) any interest prepaid under the Facility of the loan principal by the Bank will not be for a period greater than 12 months;

Paragraph 22, omit the paragraph and the heading and substitute with:**‘Subdivision H of Division 3 of Part III of the 1936 Act**

22.1 Subdivision H of Division 3 of Part III of the 1936 Act deals with the timing of deductions for certain prepaid expenditure. Separate rules apply depending on whether the expenditure is incurred in carrying on a business, whether the taxpayer is a 'STS taxpayer' and whether the expenditure qualifies for transitional treatment. The expenditure must be otherwise deductible under subsection 51(1) of the 1936 Act or section 8-1 of the *Income Tax Assessment Act 1997* ('ITAA 1997') and must not be 'excluded expenditure'. The rules in sections 82KZME-82KZMF do not apply to prepaid expenditure under an obligation which existed under an agreement before 1 p.m. (by legal time in the Australian Capital Territory) on 11 November 1999 which could not be avoided unilaterally by the taxpayer. The rules in sections 82KZMA-82KZMD do not apply to prepaid expenditure incurred in meeting a pre RBT obligation.

‘Excluded expenditure’ and ‘pre-RBT obligation’ are defined in subsection 82KZL(1) of the 1936 Act.

Sections 82KZM to 82KZMD: prepaid expenditure before and after Business Tax Reform

22.2 Before the amendments (‘the stage 1 amendments’) inserted by the *New Business Tax System (Integrity and Other Measures) Act 1999*, expenditure made under an agreement entered into after 25 May 1988 was deductible in the year in which it was incurred (‘the expenditure year’) if it was for the doing of a thing that was to be done wholly within 13 months of the date of payment (‘the 13-month rule’). Where section 82KZM applies, the deduction for the expenditure is spread over the lesser of the period during which the thing is to be done and 10 years (‘the eligible service period’ - see subsection 82KZL(1)).

22.3 The stage 1 amendments removed the 13-month rule after 11.45 a.m. (by legal time in the Australian Capital Territory) on 21 September 1999 for prepaid expenditure that does not meet a pre-RBT obligation and is incurred in carrying on a business by a taxpayer who is not a small business taxpayer (as defined in section 960-335 of the 1997 Act). Sections 82KZMA-KZMD, which set the amount and timing of relevant prepaid expenditure, include transitional rules to phase-in the initial impact of these amendments.

22.4 The rules in sections 82KZME and 82KZMF (‘the stage 2 amendments’) inserted by the *New Business Tax System (Integrity Measures) Act 2000* removed the 13-month rule for all taxpayers incurring prepaid expenditure after 1 p.m. (by legal time in the Australian Capital Territory) on 11 November 1999 in respect of certain investment schemes (‘the ‘tax shelter’ type arrangements’).

22.5 Further amendments (‘the stage 3 amendments’) brought about by the *New Business Tax System (Simplified Tax System) Act 2001* replaced the 13-month rule with a 12-month rule for certain classes of taxpayers. This new rule will apply to assessments for the first year of income commencing after 30 June 2001 and for later income years.

22.6 The 12-month rule allows an immediate deduction for prepaid expenditure where the expenditure is not excluded expenditure and is incurred for a period of service not exceeding 12 months and the period ends by the last day of the income year following the expenditure year. This 12-month rule applies only to taxpayers that are in the Simplified Tax System (‘STS taxpayers’); or are individual taxpayers incurring deductible non-business expenditure; or are taxpayers incurring expenditure that meets a pre-RBT obligation.

22.7 An eligible taxpayer, who meets the criteria in section 328-365 of the 1997 Act for an income year, can notify the Commissioner of

the choice to become a STS taxpayer. There are rules for entering and leaving the Simplified Tax System ('the STS'). Refer Subdivisions 328-F and 328-G of the 1997 Act.

Sections 82KZME and 82KZMF: prepaid expenditure and 'tax shelter' type arrangements

22.8 The rules in sections 82KZME and 82KZMF apply, subject to the exceptions in section 82KZME, where expenditure is incurred under a 'tax shelter' type arrangement for the doing of a thing that is not wholly done within the expenditure year.

22.9 Exception 5, as contained in subsections 82KZME(9) and (10), applies to exclude expenditure from the operation of section 82KZMF where the expenditure is under an agreement to which a product ruling (as defined in subsection 82KZME(11)) stating the expenditure as being allowable as a deduction applies. The product ruling must be made on or before 1 p.m. (by legal time in the Australian Capital Territory) on 11 November 1999, or in response to a product ruling application lodged with, and acknowledged by, the Commissioner on or before that time.

22.10 Given PR 1999/12 was made on 14 April 1999, prepaid interest expenditure incurred under the agreement covered by PR 1999/12 but incurred by the investor after 1 p.m. (by legal time in the Australian Capital Territory) on 11 November 1999 will be within Exception 5. The expenditure must then be considered under the other prepayment rules outlined above.'

After paragraph 25, insert:

Section 82KL

25.1 The operation of section 82KL depends, among other things, on the identification of a certain quantum of 'additional benefits(s)'. 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.

Paragraph 27 (Detailed contents list), omit:

Section 82KZM

22

and substitute with:

Subdivision H of Division 3 of Part III of the 1936 Act

22.1

PR 1999/12

Sections 82KZM to 82KZMD: prepaid expenditure before and
after Business Tax Reform 22.2

Sections 82KZME and 82KZMF: prepaid expenditure and
'tax shelter' type arrangements 22.8

and insert after 'Section 82KK':

Section 82KL 25.1

Legislative References, insert after 'ITAA 1936 82KK':

- ITAA 1936 82KL
- ITAA 1936 82KZMA
- ITAA 1936 82KZMB
- ITAA 1936 82KZMC
- ITAA 1936 82KZME
- ITAA 1936 82KZMF

Related Rulings, insert:

PR 1999/12

Commissioner of Taxation

5 December 2001

ATO references:

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