



# ***PR 2004/15 - Income tax: tax consequences of investing in the Westpac Protected Equity Loan Plus***

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 This document has changed over time. This is a consolidated version of the ruling which was published on *18 February 2004*



## Product Ruling

### Income tax: tax consequences of investing in the Westpac Protected Equity Loan Plus

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Contents	Para
What this Product Ruling is about	1
Date of effect	10
Withdrawal	12
Arrangement	13
Ruling	17
Assumptions	18
Explanations	19
Detailed contents list	48

Participants may wish to refer to the ATO's Internet site at <http://www.ato.gov.au> or contact the ATO directly to confirm the currency of this Product Ruling or any other Product Ruling that the ATO has issued.

#### **Preamble**

*The number, subject heading, and the **What this Product Ruling is about** (including **Tax law(s)**, **Class of persons** and **Qualifications** sections), **Date of effect**, **Withdrawal**, **Arrangement** and **Ruling** parts of this document are a 'public ruling' in terms of Part IVAAA of the **Taxation Administration Act 1953**. Product Ruling PR 1999/95 explains Product Rulings and Taxation Rulings TR 92/1 and TR 97/16 together explain when a Ruling is a public ruling and how it is binding on the Commissioner.*

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

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The Australian Taxation Office (ATO) **does not** sanction or guarantee this product. Further, we give 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.

Participants must form their own view about the commercial and financial viability of the product. This will involve a consideration of important issues such as whether projected returns are realistic, the 'track record' of the management, the level of fees in comparison to similar products, how the investment fits an existing portfolio, etc. We recommend a financial (or other) adviser be consulted for such information.

This Product Ruling provides certainty for participants by confirming that the tax benefits set out below in the **Ruling** part of this document are available, **provided that** the arrangement is carried out in accordance with the information we have been given, and have described below in the **Arrangement** part of this document.

If the arrangement is not carried out as described below, participants lose the protection of this Product Ruling. Participants may wish to seek assurances from the promoter that the arrangement will be carried out as described in this Product Ruling.

Participants should be aware that the ATO will be undertaking review activities to confirm the arrangement has been implemented as described below and to ensure that the participants in the arrangement include in their income tax returns income derived in those future years.

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

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This Product Ruling has been given on the basis that the person(s) who applied for the 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 Ruling.

## What this Product Ruling is about

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1. This Ruling sets out the Commissioner's opinion on the way in which the 'tax law(s)' identified below apply to the defined class of persons, who take part in the arrangement to which this Ruling relates. In this Ruling, the arrangement is the grant of a put option and the borrowing of moneys, on the terms of a fully protected lending product named the Protected Equity Loan Plus ('PEL Plus'), from Westpac Banking Corporation ('Westpac'). The borrowings are used to acquire shares and/or units listed on the Australian Stock Exchange ('ASX').

2. This Ruling does not address the tax consequences of:

- early repayment or termination of the PEL Plus;
- repaying the PEL Plus using the limited recourse provisions;
- using the Top-up Loan;
- using the Portfolio Adjustment Facility; and
- extending or re-financing the PEL Plus at maturity.

These additional features are available under the terms of the PEL Plus and are described and disclosed in the Product Disclosure Statement.

3. This Ruling does not address an Investor's entitlement to franking credits.

### Tax law(s)

4. The tax laws dealt with in this Ruling are:

- section 8-1 of the *Income Tax Assessment Act 1997* ('ITAA 1997');
- section 104-10 (ITAA 1997);
- section 104-25 (ITAA 1997);
- section 110-25 (ITAA 1997);
- section 115-5 (ITAA 1997);
- Division 134 (ITAA 1997);
- section 51AAA of the *Income Tax Assessment Act 1936* (ITAA 1936);
- section 82KL (ITAA 1936);
- section 82KZM (ITAA 1936);

- section 82KZMA (ITAA 1936);
- section 82KZMD (ITAA 1936);
- section 82KZME (ITAA 1936);
- section 82KZMF (ITAA 1936); and
- Part IVA (ITAA 1936).

**Class of persons**

5. The class of persons to whom this Ruling applies is those who enter into the arrangement described below as cash applicants on or after the date this Ruling is made with the purpose of staying in the arrangement until it is completed and of deriving assessable income from their involvement as set out in the description of the arrangement. In this Ruling these persons are referred to as 'Investors'.

6. This Ruling does not apply to Securityholder Applicants.

**Qualifications**

7. The Commissioner rules on the precise arrangement identified in the Ruling.

8. If the arrangement described in the Ruling is materially different from the arrangement that is actually carried out:

- the Ruling has no binding effect on the Commissioner as the arrangement entered into is not the arrangement ruled upon; and
- the Ruling will be withdrawn or modified.

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## Date of effect

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10. This Ruling applies from 18 February 2004, the date this Ruling is made. However, the Ruling does not apply to taxpayers to the extent that it conflicts with the terms of settlement of a dispute agreed to before the date of issue of the Ruling (see paragraphs 21 and 22 of Taxation Ruling TR 92/20).

11. If a taxpayer has a more favourable private ruling (which is legally binding), the taxpayer can rely on the private ruling if the income year to which the private ruling relates has ended, or has commenced but not yet ended. However, if the arrangement covered by the private ruling has not begun to be carried out, and the income year to which it relates has not yet commenced, this Product Ruling applies to the taxpayer to the extent of the inconsistency only (see Taxation Determination TD 93/34).

## Withdrawal

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12. This Product Ruling is withdrawn and ceases to have effect after 30 June 2007. The Ruling continues to apply, in respect of the tax laws ruled upon, to all persons within the specified class who enter into the specified arrangement during the term of the Ruling. Thus, the Ruling continues to apply to those persons, even following its withdrawal, who entered into the specified arrangement prior to withdrawal of the Ruling. This is subject to there being no material difference in the arrangement or in the persons' involvement in the arrangement.

## Arrangement

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13. The arrangement that is the subject of this Ruling is described below. This description incorporates the following documents:

- the application for a Product Ruling, dated 12 December 2003, lodged by Allens Arthur Robinson on behalf of Westpac;
- the amendment to the application for a Product Ruling dated 2 February 2004, lodged by Allens Arthur Robinson on behalf of Westpac;
- the draft Product Disclosure Statement received 3 February 2004 from Allens Arthur Robinson on behalf of Westpac, incorporating the Terms and Conditions of the PEL Plus; and

- indicative Term Sheets for the PEL Plus received 3 February 2004 from Allens Arthur Robinson on behalf of Westpac.

Capitalised terms in this product ruling have the same meaning as in the Terms and Conditions in Part B of the Product Disclosure Statement.

14. The details and aspects of the arrangement subject to this Ruling are summarised as follows:

- (a) the PEL Plus is a limited recourse loan product by which Investors borrow funds from Westpac to finance the acquisition of shares and/or units listed on the ASX ('Securities') in the Investor's name. Where the Securities include a stapled security, the stapled security comprises share/s and unit/s that are jointly listed for quotation on the ASX. The Securities are selected by an Investor from a range of CHESS Securities listed in the Term Sheet, or otherwise approved by Westpac;
- (b) the term of a PEL Plus is 1, 3 or 5 years (2 or 4 year terms are also available on request). The minimum investment amount is \$50,000 with additional increments of \$25,000;
- (c) under the terms of the PEL Plus, Westpac advances the Investor funds to acquire a Parcel of Securities (the 'Loan'). There is a separate Loan for each Parcel of Securities acquired by an Investor;
- (d) the Interest Rate on the funds borrowed is either fixed for the term of the Loan with different Interest Rates for individual Securities or a variable rate (reset annually);
- (e) Interest is payable annually in advance or monthly in arrears and is calculated by applying the applicable Interest Rate to the relevant Loan balance at the beginning of each period. Westpac may allow an Investor to change their interest payment method from monthly in arrears to annually in advance and vice versa. The election to change interest payments from annually in advance to monthly in arrears can only be made after the expiry of the relevant prepayment period;
- (f) Investors may repay the Loan prior to maturity. If this occurs, the Investor may be required to pay break costs;

- (g) the Loan is secured by a Mortgage in favour of Westpac over the Secured Property;
- (h) in the event of Default, where an Investor fails to repay the Loan, Westpac's recourse under each Loan is limited to the relevant Parcel of Securities and the Deposit Account. Westpac's recourse is not limited in respect of any other Default by an Investor;
- (i) Investors are granted a Put Option under which the Investor may sell the Securities for the outstanding amount of the Loan at the Maturity Date;
- (j) Westpac may allow Investors to utilise a Reduced Rate Facility in relation to a Parcel of Securities under which:
  - (i) the Investor grants Westpac a right entitling Westpac to acquire the Parcel of Securities if, at the Maturity Date of the Loan relating to that Parcel, the Market Value of the Securities equals or exceeds the Cap Price chosen by the Investor (which will be greater than the outstanding Loan amount) for an exercise price equal to the Cap Price plus the excess of the Market Value of the relevant Parcel of Securities over the Cap Price multiplied by the Participation Rate chosen by the Investor (a 'Right');
  - (ii) no amount is payable by Westpac to an Investor for the Right, instead the Investor will be charged a lower rate of interest in respect of the Loan relating to that Parcel of Securities than would apply if no Right was granted;
  - (iii) if Westpac exercises its Right at the Maturity Date:
    - (A) the Investor will transfer the Securities to Westpac and receive the Cap Price and the excess of the Market Value of the Securities over the Cap Price multiplied by the Participation Rate; or
    - (B) the Investor may choose to cash settle the Right, in which case the Investor is required to pay Westpac the Total Amount Owing in respect of the Loan relating to that Parcel of Securities (or roll that amount over to a new PEL Plus, if available) and the Cash Settlement

Amount. The Cash Settlement Amount equals the sum of the excess of the Market Value of the Securities over the Cap Price or, if a Participation Rate has been nominated, the excess of the Market Value over the Cap Price less the amount determined by multiplying the Participation Rate by that excess;

- (k) at the Maturity Date of a Loan, unless Westpac exercises a Right (if any), an Investor may:
  - (i) keep the Parcel of Securities and repay the Loan using their own funds;
  - (ii) sell the Parcel of Securities at the prevailing market price, apply the sale proceeds to repay the Loan and keep any surplus;
  - (iii) elect to exercise the Put Option to sell the Securities for the outstanding Loan Amount;
  - (iv) refinance the Loan and apply for a new PEL Plus (if available);
  - (v) apply to Westpac to extend the term of all or part of their Loan; or
  - (vi) do nothing, in which case Westpac will act under the Mortgage to take possession of the Securities and recover what it can from the sale of those Securities as repayment or reduction of the Loan principal outstanding;
- (l) as the legal and beneficial owner of the Securities, Investors will be entitled to all dividends, trust distributions and capital gains. However, any of the following in relation to the Securities must be held in an account opened by Westpac on the Investor's behalf (the 'Deposit Account'):
  - (i) cash returns on capital;
  - (ii) Special Dividends;
  - (iii) proceeds from the disposal or relinquishment of rights;
  - (iv) proceeds in relation to options granted to or by the Security Owner.

The Deposit Account is solely for the purposes of the PEL Plus and cannot be operated by the Investor;

- (m) if any of the Securities are:



- (i) bought back under a buy-back scheme;
- (ii) subject to a takeover, merger, or reconstruction;
- (iii) the subject of a proposed bonus issue, consolidation, scheme of arrangement or any other arrangement affecting rights in relation to the Securities,

the Investor may be required to repay a portion of the Loan balance, or to replace the affected Securities or to deposit cash or to take other actions in order to restore the value of Westpac's loan security; and

- (n) brokerage, Taxes, costs, charges and commissions, if any, in relation to the purchase and sale of Securities, and the preparation of the PEL Plus documentation, including any stamp duty and brokerage fees, are payable by the Investor.

## The Participants

15. Westpac is the provider of the PEL Plus to Investors in order to fund the acquisition of Securities. Westpac Securities Limited (trading as Westpac Broking), a related entity of Westpac, will act as a broker for the Investors.

16. The Investors may be individuals, companies or trusts.

## Ruling

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17. Subject to paragraphs 2, 3 and 18 of this Ruling:

- (a) the interest charge allowable as a deduction under section 8-1 of the ITAA 1997 is the amount that does not exceed the lower of the Reserve Bank Bulletin Indicator Lending Rates for Personal Unsecured Loans - Fixed or Variable (as applicable) and the relevant percentage of the total interest charged by Westpac under the PEL Plus calculated as follows:
  - (i) 60% (for a PEL Plus with a term of one year);
  - (ii) 72.5% (for a PEL Plus with a term of two years);
  - (iii) 80% (for a PEL Plus with a term of three years);
  - (iv) 82.5% (for a PEL Plus with a term of four years); and
  - (v) 85% (for a PEL Plus with a term of five years);

- (b) the difference between the total interest charged by Westpac and the amount allowable as a deduction under paragraph 17(a) above is not deductible under section 8-1 of the ITAA 1997 and forms part of the cost base of the Put Option under subsection 110-25(2) of the ITAA 1997;
- (c) section 51AAA of the ITAA 1936 will not apply to deny an Investor a deduction for any part of the interest charge allowable as a deduction under section 8-1 of the ITAA 1997;
- (d) section 82KL of the ITAA 1936 will not apply to deny deductibility of the interest charge allowable as a deduction under section 8-1 of the ITAA 1997;
- (e) section 82KZMF of the ITAA 1936 will not apply to set the amount and timing of deductions for the interest charge allowable as a deduction under section 8-1 of the ITAA 1997;
- (f) section 82KZM of the ITAA 1936 will not apply to deny the Investor immediate deductibility of the interest charge 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:
  - (i) the Investor is an STS taxpayer; or
  - (ii) the Investor is an individual taxpayer who does not incur the interest charges in carrying on a business;
- (g) sections 82KZMA and 82KZMD of the ITAA 1936 will apply to set the amount and timing of deductions for that part of the interest charge allowable as a deduction under section 8-1 of the ITAA 1997 to the Investor (other than an STS taxpayer for the year of income) who is a taxpayer that is not an individual and does not carry on a business;
- (h) the grant of the Right under the Reduced Rate Facility by the Investor over Securities is a Capital Gains Tax ('CGT') event which does not result in a capital gain or a capital loss to the Investor;
- (i) if Westpac exercises the Right at the Maturity Date and the Investor transfers the Securities to Westpac, CGT event A1 will occur. The Investor will make a capital gain equal to the capital proceeds received from Westpac less the Investor's cost base for the Securities;

- (j) if Westpac exercises its Right and the Investor chooses the Cash Settlement option, the Cash Settlement Amount will be included in the cost base of the Securities under subsection 110-25(6) of the ITAA 1997;
- (k) if the Put Option is not exercised on or before the Maturity Date, the Investor will make a capital loss at the Maturity Date equal to the reduced cost base of the Put Option;
- (l) where the Investor exercises the Put Option, any gain or loss on exercise of the Put Option is disregarded and the amount included in the cost base of the Put Option under subsection 110-25(2) of the ITAA 1997 will be added to the cost base of the Securities disposed of to Westpac;
- (m) any capital gain realised by an Investor on sale of the Securities will be treated as a discount capital gain pursuant to section 115-5 of the ITAA 1997 where the Investor is an individual or a trust and has held the Securities for at least 12 months; and
- (n) Part IVA of the ITAA 1936 will not be applied to deny deductibility of any part of the interest charge allowable as a deduction under section 8-1 of the ITAA 1997.

## Assumptions

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

- (a) the Investors are Australian residents for taxation purposes;
- (b) the Investors are not traders in investments and would not be treated for taxation purposes as either trading in the Securities, carrying on a business of investing in the Securities or holding the Securities as trading stock or as a revenue asset;
- (c) any interest charges to be paid in advance under a PEL Plus which are prepaid relate to a loan interest payment period of 12 months or less that ends on or before the last day of the income year following the expenditure year;
- (d) the dominant purpose of an Investor entering into the arrangement is to derive assessable income from their

- investment in the Securities comprising dividends or trust distributions and capital gains;
- (e) at all times during the arrangement, where the Underlying Parcel includes units in a trust, the trust satisfies the requirements of subparagraph 82KZME(5)(b)(iii) of the ITAA 1936;
  - (f) all dealings between Investors and Westpac will be at arm's length; and
  - (g) the arrangement ruled on will be executed in the manner described in the 'Arrangement' section of this Ruling.

## **Explanation**

### **Section 8-1 of the ITAA 1997**

19. Interest incurred on borrowings used to acquire income producing assets such as shares or units in a trust is generally treated as deductible under section 8-1 where it is expected that dividends or other assessable income would be derived from the investment (Taxation Ruling TR 95/33).

20. The deductible interest amount will be - the lower of the applicable Reserve Bank Bulletin Indicator Lending Rates for Personal Unsecured Loans - Fixed or Variable (as relevant to the particular PEL Plus) and the relevant percentage of the interest calculated in accordance with the formula described in paragraph 17(a).

21. The difference between the total interest charged on the PEL Plus and the amount allowable as a deduction under section 8-1 is the portion of interest allocated to the cost of the Put Option. The Put Option ensures that the borrower is protected from liability to repay the principal if the Market Value of the Securities falls below their original purchase price. The amount charged for the Put Option is not deductible under section 8-1.

### **Cost Base of the Put Option**

22. The amount of interest charged on the PEL Plus which is not deductible to the Investor under section 8-1 of the ITAA 1997 forms part of the cost base of the Put Option under subsection 110-25(2) of the ITAA 1997. The Put Option constitutes a separate asset for CGT purposes which is separate and in addition to the other rights created under the PEL Plus as described in this Ruling.

## **Section 51AAA of the ITAA 1936**

23. By entering into the PEL Plus it is contemplated that an Investor will derive assessable income by the receipt of dividend or trust income and capital gains. As the 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 has no application to an Investor in the PEL Plus.

## **Section 82KL of the ITAA 1936**

24. The operation of section 82KL depends, among other things, on the identification of a certain quantum of 'additional benefit(s)'. Insufficient 'additional benefits' will be provided to trigger the application of section 82KL. It will not apply to deny the deductions otherwise allowable as a deduction under section 8-1 of the ITAA 1997.

## **Subdivision H of Division 3 of Part III of the ITAA 1936**

25. This Subdivision 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 carrying on a business, whether the Investor is an STS taxpayer, 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 of expenditure that are of a capital nature.

## ***Subdivisions 328-F & 328-G of the ITAA 1997 - STS taxpayer***

26. An Investor will be an STS taxpayer for an income year if the Investor is eligible to be an STS taxpayer for that year and the Investor notifies the Commissioner of the choice to become such a taxpayer for that year.

27. An Investor will be eligible to be an STS taxpayer for an income year if the Investor carries on a business and the STS average turnover of the business and related business for that year is less than \$1 million and the business and related businesses have depreciating assets with a total adjustable value below \$3 million at the end of that year.

***The eligible service period for the purposes of Subdivision H of Division 3 of Part III of the ITAA 1936***

28. That part of the interest charge on the PEL Plus allowable as a deduction under section 8-1 of the ITAA 1997 is, if paid in advance, 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 of the ITAA 1936: prepaid expenditure and ‘tax shelter’ arrangements***

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

30. For the purposes of section 82KZME, ‘agreements’ are broadly defined to include an entire arrangement of which a contract may form part. Under subsection 82KZME(4), the relevant ‘agreement’ is all the contractual arrangements and activities associated with the participation in the PEL Plus, including the financing, share and/or unit acquisition, and share and/or unit disposal arrangements.

31. Exception 1, as contained in subsection 82KZME(5), applies to exclude the amount of interest allowable as a deduction under section 8-1 of the ITAA 1997 on borrowings under the PEL Plus from the operation of section 82KZMF, as:

- the prepaid interest expenditure under the PEL Plus is incurred in respect of money borrowed to acquire shares that are listed for quotation on the ASX or units in a unit trust as described in subparagraph 82KZME(5)(b)(iii);
- the Investor can reasonably be expected to obtain dividends or trust income from the investment;
- the Investor will not obtain any other kind of assessable income from the investment, except for capital gains; and
- all aspects of the PEL Plus are at arm’s length.

32. Deductibility of expenditure must therefore be considered under the prepayment rules outlined in paragraphs 33 to 38.

***Section 82KZM of the ITAA 1936: prepaid expenditure incurred by STS taxpayers and individuals incurring non-business expenditure***

33. Section 82KZM operates to spread over more than one income year, a deduction for prepaid expenditure incurred by a taxpayer that is either:

- an STS taxpayer for the year of income; or
- a taxpayer that is an individual and the expenditure is not incurred in carrying on a business.

34. The expenditure must not be excluded expenditure and must be incurred otherwise than in carrying on a business. Section 82KZM 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.

35. As the eligible service period in relation to the deductible interest payment under the PEL Plus 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 will have no application to Investors who are STS taxpayers for the year of income, or to Investors who are individuals and 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 amount allowable as a deduction under section 8-1 incurred under the PEL Plus.

***Sections 82KZMA and 82KZMD of the ITAA 1936: prepaid non-business expenditure incurred by non-individual and non-STS taxpayers***

36. Sections 82KZMA and 82KZMD set the amount and timing of deductions for expenditure for an Investor (other than an STS taxpayer for the year of income) who is an Investor that is not an individual and does not incur the expenditure in carrying on a business.

37. 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.

38. For these taxpayers, the amount of prepaid interest allowable as a deduction under section 8-1 of the ITAA 1997 incurred on the

borrowings under the PEL Plus will be apportioned over the relevant interest payment period.

### **Reduced Rate Facility**

39. Under the Reduced Rate Facility, the Investor grants a Right to Westpac which may be exercised if the Market Value of the Securities on the Maturity Date is equal to or greater than the Cap Price that is chosen by the Investor.

40. The grant of a Right by the Investor to Westpac under the Reduced Rate Facility is a CGT event which will not result in a capital gain or loss arising for the Investor.

41. Where the Investor chooses to sell the Securities to Westpac on exercise of the Right (rather than electing to cash settle the option), CGT event A1 will occur (section 104-10 of the ITAA 1997). Any capital proceeds received by the Investor in respect of the Right will be included as part of the capital proceeds received on the disposal of the Securities. Where the capital proceeds of the disposal exceed the Investor's cost base of the Securities, the Investor will make a capital gain.

42. The capital proceeds received by the Investor pursuant to the Right will be the Physical Settlement Amount. The Physical Settlement Amount is comprised of the amount of the Cap Price and, if a Participation Rate was nominated by the Investor, that Participation Rate multiplied by the excess of the Market Value of the Securities above the Cap Price at the Maturity Date.

43. If the Investor chooses to cash settle the Right and repay the Loan, thereby retaining ownership of the Securities, no CGT event will arise in respect of the Securities that have been retained by the Investor in these circumstances. The amount paid by the Investor, that is the Cash Settlement Amount, is capital expenditure made to preserve the Investor's title to the Securities and will form part of the Investor's cost base in the Securities (subsection 110-25(6) of the ITAA 1997). The Cash Settlement Amount equals the sum of the excess of the Market Value of the Securities over the Cap Price or, if a Participation Rate has been nominated, the excess of the Market Value over the Cap Price less the amount determined by multiplying the Participation Rate by that excess.

### **Sections 104-10, 104-25, and 134-1 of the ITAA 1997**

44. Where, at the Maturity Date, the Investor repays the PEL Plus, the Put Option will expire. The expiration of the Put Option gives rise to CGT event C2 (paragraph 104-25(1)(c) of the ITAA 1997). The



Investor will make a capital loss at the time when the Put Option expires equal to the reduced cost base of the Put Option.

45. Where the Investor exercises the Put Option, the Securities will be transferred to Westpac in satisfaction of the outstanding Loan. The amount paid by the Investor to acquire the Put Option will be included in the cost base (and reduced cost base) of the Securities (subsection 134-1(1), Item 2 of the ITAA 1997).

### **Section 115-5 of the ITAA 1997: CGT discount**

46. Division 115 allows a taxpayer a discount on capital gains in certain circumstances. Under section 115-5, any capital gain realised by an Investor from the transfer of Securities to Westpac at maturity and/or pursuant to the Right will be treated as a discount capital gain where the Investor is an individual or a trust and has held the Securities for at least 12 months.

### **Part IVA of the ITAA 1936**

47. Provided that the PEL Plus arrangement ruled on is entered into and carried out as disclosed in this Ruling, it is accepted as an ordinary commercial transaction and Part IVA would not apply.

## **Detailed contents list**

48. Below is a detailed contents list for this Product Ruling:

	<b>Paragraph</b>
<b>What this Product Ruling is about</b>	<b>1</b>
Tax law(s)	4
Class of persons	5
Qualifications	7
<b>Date of effect</b>	<b>10</b>
<b>Withdrawal</b>	<b>12</b>
<b>Arrangement</b>	<b>13</b>
Participants	15
<b>Ruling</b>	<b>17</b>
<b>Assumptions</b>	<b>18</b>
<b>Explanation</b>	<b>19</b>
Section 8-1 of the ITAA 1997	19

Case base of the Put Option	22
Section 51AAA of the ITAA 1936	23
Section 82KL of the ITAA 1936	24
Subdivision H of Division 3 of Part III of the ITAA 1936	25
<i>Subdivisions 328-F &amp; 328-G of the ITAA 1997 - STS taxpayer</i>	26
<i>The eligible service period for the purposes of Subdivision H of Division 3 of Part III of the ITAA 1936</i>	28
<i>Sections 82KZME and 82KZMF of the ITAA 1936: prepaid expenditure and 'tax shelter' arrangements</i>	29
<i>Section 82KZM of the ITAA 1936: prepaid expenditure incurred by STS taxpayers and individuals incurring non-business expenditure</i>	33
<i>Sections 82KZMA and 82KZMD of the ITAA 1936: prepaid non-business expenditure incurred by non-individual and non-STs taxpayers</i>	36
Reduced Rate Facility	39
Sections 104-10, 104-25 and 134-1 of the ITAA 1997	44
Section 115-5 of the ITAA 1997: CGT discount	46
Part IVA of the ITAA 1936	47
<b>Detailed contents list</b>	<b>48</b>

**Commissioner of Taxation**

18 February 2004

*Previous draft:*

Not previously issued in draft form

*Related Rulings/Determinations:*

TR 92/1; TR 92/20; TR 95/33;  
TR 97/16; TD 93/34; PR 1999/95

*Subject references:*

- debt deductions
- financial products
- interest expenses
- prepaid expenses
- product rulings
- public rulings
- small business investor
- taxation administration
- tax avoidance

*Legislative references:*

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- ITAA 1936 51AAA
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# PR 2004/15

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