TD 2012/19 - Income tax: when is a non-share equity interest 'issued at or through a permanent establishment' for the purposes of paragraph 215-10(1)(c) of the Income Tax Assessment Act 1997?

Taxation Determination

Income tax: when is a non-share equity interest 'issued at or through a permanent establishment' for the purposes of paragraph 215-10(1)(c) of the *Income Tax Assessment Act 1997*?

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Ruling

1. A non-share equity interest will be taken to have been 'issued at or through a permanent establishment' for the purposes of paragraph 215-10(1)(c) of the *Income Tax Assessment Act 1997* (ITAA 1997)[1] where the capital raising is a transaction 'of' the business carried on by an authorised deposit-taking institution (ADI) at or through the permanent establishment in a listed country. This means that:

- the non-share equity interest must be offered to investors in the course of the business conducted by an ADI at or through the permanent establishment in a listed country; and
- the non-share equity interest must be allocated to the investor by personnel conducting the business of the permanent establishment; and
- the transaction documents are executed at the permanent establishment; and

[1] All legislative references are to the ITAA 1997 unless otherwise indicated.

- the transaction documents provide that the non-share equity interest is transferred to the investor at the permanent establishment and consequently the non-share equity interest is transferred at the permanent establishment; and
- at the time of transfer, the personnel conducting the business at the permanent establishment relinquishes all control over the non-share equity interest.

Example 1

2. ABC Bank is an ADI in Australia with a branch located in New York.[2] *ABC Bank's New York Branch needs to raise US$500 million for use in the New York Branch's business of lending money in New York. The New York Branch intends to market and sell the notes to United States (US) retail and institutional investors through a local investment firm.*

3. The convertible note will qualify as Group and Parent Additional Tier-1 capital under Australian Prudential Regulation Authority (APRA) Basel III regulations.

4. The New York Branch requests approval from the Board of ABC Bank for the Branch to issue US$ denominated convertible notes and upon receiving that approval, branch personnel together with personnel from ABC Bank's Group Legal and Group Treasury, prepare an offer document, the transaction documents and undertake the necessary due diligence. The transaction documents are settled and executed by personnel conducting the business at the New York permanent establishment. Overall project co-ordination and timetable management is delegated by the Board of ABC Bank to management based in New York who is conducting the business at the permanent establishment in New York.

5. The marketing of the convertible note will primarily be undertaken by personnel conducting the business at the permanent establishment but Group Treasury executives from Sydney will also be involved to address any questions concerning the Bank and the Tier-1 classification of the capital raised.

6. Some tasks relating to the capital raising are done solely in Australia. Namely, personnel based in Australia from Group Legal and Group Treasury, obtain approval from APRA, obtain the necessary Australian Securities and Investment Commission (ASIC) and Australian Stock Exchange (ASX) waivers and prepare and issue announcements to the ASX and foreign stock exchanges.

7. Upon acceptance of the offer by the US investors, the notes are allocated by branch personnel to the subscribers. The New York Branch then transfers the notes to the US investors in accordance with the transaction documents.

8. The convertible notes will be classified as non-share equity interests for the purposes of Division 974 and returns paid in respect of the convertible notes will be taken to be non-share dividends.

[2] The United States of America is a listed country for the purposes of section 215-10 of the ITAA 1997. 'Listed country' means a foreign country, or a part of a foreign country, that is declared by the regulations to be a listed country for the purposes of Part X of the *Income Tax Assessment Act 1936* (ITAA 1936): see section 320 of the ITAA 1936 and subsection 995-1(1) of the ITAA 1997. At the time this Determination is published, the Income Tax Regulations 1936 provide that Canada, France, Germany, Japan, New Zealand, United States of America, United Kingdom of Great Britain and Northern Ireland are listed countries for the purposes of Part X of the ITAA 1936.

9. The convertible notes are taken to be issued at or through the permanent establishment of the ADI in New York because that is the place where the capital raising is undertaken and the capital raising is undertaken as a transaction of the business conducted by the ADI at the permanent establishment. In other words, the permanent establishment is the place where personnel conducting the business at the permanent establishment have taken all the necessary steps for issuing the notes, including the final step whereby the notes are transferred to the investors. It is also the place where the investors acquire control over the notes issued. Accordingly, paragraph 215-10(1)(c) is satisfied.

10. Assuming that all of the other conditions in section 215-10 are met, the returns paid in respect of the convertible notes will be unfrankable.

Example 2

11. XYZ Bank is an ADI in Australia with a permanent establishment in London.[3] *XYZ Bank would like to issue an A$ denominated stapled security comprising of a fully paid preference share in the ADI and a fully paid note from the London Branch to raise Group and Parent Additional Tier-1 Capital under APRA Basel III regulations. The funds are to be used to replace Tier-1 capital previously raised offshore.*

12. Under proposal 1, XYZ Bank proposes to use LMN Investment Bank, a non-resident entity, as an intermediary for the issue.

13. The transaction documents which create the note will be executed at the London Branch and the notes will be acquired by LMN Investment Bank. LMN Investment Bank will also acquire the preference shares from XYZ Bank and will staple each note to a preference share. The stapled securities will then be offered to investors by LMN Investment Bank, on behalf of the XYZ Bank. XYZ Bank has stipulated that the stapled securities be sold to a mix of Australian and United Kingdom retail investors. XYZ Bank will allocate the stapled securities once the offer period has closed.

14. Following the Board of XYZ Bank's approval of the issue of the stapled security, personnel from XYZ Bank's Group Legal and Group Treasury prepare the offer document, the transaction documents and undertake the necessary due diligence for the capital raising. The transaction documents pertaining to the issue of the note are settled and executed by personnel conducting the business at the London permanent establishment, while the transaction documents pertaining to the preference share are settled and executed by personnel in Australia.

15. Personnel based in Australia obtain approval from APRA, obtain the necessary ASIC and ASX waivers and prepare and issue announcements to the ASX and foreign stock exchanges. Australian based personnel are also responsible for appointing the investment bank and negotiating the terms of the stapled instruments and the terms of their issue to investors.

[3] The United Kingdom is a listed country for the purposes of section 215-10.

16. The stapled security, as a whole, is classified as a non-share equity interest for the purposes of Division 974 and returns paid on the stapled security will be taken as non-share dividends. Section 215-10 will not apply to treat the non-share dividends as unfrankable because paragraph 215-10(1)(c) will never be satisfied. Although the transaction documents creating the notes are executed at the London Branch, this is insufficient for a conclusion that the non-share equity interest is issued at or through the London Branch. That is, it cannot be said that the non-share equity interest, which includes the preference share which is required under Basal III APRA regulations to be issued directly by the ADI in Australia, was issued at or through the permanent establishment in London.

17. *While the fact that the preference share must be issued by the ADI directly from Australia is sufficient for concluding that the non-share equity interest was not issued at or through the permanent establishment, there are two other factors which indicate that the non-share equity interest was not issued at or through the permanent establishment*.

18. Firstly, the capital raising does not have sufficient nexus with the business conducted at the permanent establishment such that it could be concluded that it was a transaction of the business conducted at the permanent establishment. The funds raised are for the ADI as a whole and not specifically for the business of the ADI at the permanent establishment. This is evidenced in part by the fact that Group Treasury and Group Legal have overall management of the capital raising and are responsible for all major steps leading up to the issue except for the execution of the notes.

19. Secondly, when the notes are transferred to LMN Investment Bank, XYZ Bank will retain control over the notes. Therefore, XYZ Bank in Australia will retain control over the stapled securities right up until they are allocated and transferred to the retail investors.

20. Accordingly, it is XYZ Bank that issues the non-share equity interests to the retail investors.

21. Under proposal 2, XYZ Bank will issue a stapled security that is similar to that under proposal 1 but the preference share will remain unpaid until the note is extinguished. The note and the preference share will be classified as two separate equity interests under Division 974, with the note being treated as a non-share equity interest. Returns in respect of the notes will be taken to be non-share dividends.

22. Once again section 215-10 will not apply to treat the non-share dividends as unfrankable because paragraph 215-10(1)(c) will not be satisfied. As with proposal 1, although the transaction documents creating the notes are executed at the London Branch, this is insufficient for a conclusion that the notes are issued at or through the London Branch. As with proposal 1, the capital raising is not a transaction of the business carried on at the permanent establishment and when the notes are transferred to LMN Investment Bank, XYZ Bank will retain control over the notes.

23. Accordingly, it is XYZ Bank that issues the non-share equity interests to the retail investors.

Example 3

24. QRS Bank is an ADI in Australia with a permanent establishment in London.[4] *QRS Bank would like to issue US$500 million denominated perpetual notes. The funds raised will be Group and Parent Additional Tier-1 Capital under APRA Basel III regulations. The funds are to be used to replace Tier-1 capital previously raised offshore. Group Treasury have identified institutional investors in Asia and Europe as potential acquirers of the notes. As a consequence, Group Treasury is considering the possibility of issuing the notes through their London Branch.*

25. The Board of QRS Bank gives its London Branch the necessary approvals and directs Group Treasury to project manage the process for the capital raising. Group Treasury personnel together with Group Legal personnel draft, prepare and settle the offer document, the transaction documents and undertake the necessary due diligence. The Management Committee responsible for conducting the business at the QRS London Branch are advised by Group Treasury of the details of the proposed capital raising and the Management Committee is advised that when all the preliminary steps are settled, the Chair and the Secretary of the Management Committee will be required to execute the transaction documents. The Management Committee is advised by Group Treasury that the funds will be used to repay capital previously contributed to the London business by the ADI.

26. Personnel based in Australia obtain approval from APRA, obtain the necessary ASIC and ASX waivers and prepare and issue announcements to the ASX and foreign stock exchanges. Australian based personnel are also responsible for appointing the investment bank and negotiating the terms of the stapled instruments and the terms of their issue to investors.

27. Upon acceptance of the offer by the investors, the notes are allocated by Group Treasury personnel to the subscribers. The London Branch then transfers the notes to the investors.

28. The perpetual notes will be classified as non-share equity interests for the purposes of Division 974 and returns paid in respect of the perpetual notes will be taken to be non-share dividends.

29. The perpetual notes are not taken to be issued at or through the permanent establishment of the ADI in London because the capital raising is not a transaction of the business of the ADI in London. The only role personnel conducting the business at the permanent establishment have in the capital raising is the execution of the transaction documents and transferring the notes to the investors. Accordingly it cannot be said that the permanent establishment is the place where personnel conducting the business at the permanent establishment have taken all the necessary steps for issuing the notes. Accordingly, paragraph 215-10(1)(c) is not satisfied.

30. Assuming that all of the other conditions in section 215-10 are met, the returns paid in respect of the convertible notes will be frankable.

[4] The United Kingdom is a listed country for the purposes of section 215-10.

Date of effect

31. This Determination applies to years of income commencing both before and after its date of issue. However, this Determination will 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 this Determination (see paragraphs 75 to 76 of Taxation Ruling TR 2006/10).

Commissioner of Taxation
18 July 2012

Appendix 1 – Explanation

This Appendix is provided as information to help you understand how the Commissioner's preliminary view has been reached. It does not form part of the proposed binding public ruling.

Explanation

32. Generally, under the imputation system, distributions made by an Australian resident company out of realised profits, regardless of the source of those profits, are frankable.[5] Exceptions to the general rule are expressly provided for in the tax law: section 215-10 is one such exception.

33. Section 215-10 permits certain non-share dividends paid by an ADI to be unfrankable provided certain conditions are satisfied. Subsection 215-10(1) provides:

> A *non-share dividend paid by an ADI (an authorised deposit-taking institution) for the purposes of the *Banking Act 1959* is ***unfrankable*** if:
>
> (a) the ADI is an Australian resident; and
>
> (b) the non-share dividend is paid in respect of a *non-share equity interest that:
>
> (i) by itself; or
>
> (ii) in combination with one or more *schemes that are *related schemes to the scheme under which the interest arises;
>
> forms part of the ADI's Tier 1 capital either on a solo or consolidated basis (within the meaning of the prudential standards); and
>
> (c) the non-share equity interest is issued at or through a permanent establishment of the ADI in a *listed country; and
>
> (d) the funds from the issue of the non-share equity interest are raised and applied solely for one or more purposes permitted under subsection (2) in relation to the non-share equity interest.

34. Section 215-10 of the ITAA 1997 was enacted in 2002 (originally inserted as section 160APAAAA of the *Income Tax Assessment Act* 1936 (ITAA 1936)), as a consequence of the introduction of the debt/equity rules in Division 974 of the ITAA 1997 which would have resulted in certain legal form debt instruments being characterised as equity interests for income tax purposes, and distributions paid in respect of those instruments being frankable.

[5] Subject to the operation of any relevant integrity rules in the tax law.

35. The broad policy intent of section 215-10 was to '*remove a competitive disadvantage that Australian ADIs would otherwise suffer from the introduction of the new debt and equity rules*': see paragraph 2.92 of the Explanatory Memorandum to the New Business Tax System (Debt and Equity) Bill 2001 (the Explanatory Memorandum). Paragraphs 2.93 and 2.94 of the Explanatory Memorandum elaborate on the policy intent:

> 2.93 Australian ADIs are subject to APRA regulations under which there are advantages for the ADI to raise Tier 1 capital through branch structures rather than through foreign subsidiaries. At present, foreign branches and subsidiaries of Australian ADIs compete, broadly, on an equal footing with foreign independent entities which raise capital overseas by the issue of hybrid instruments. These instruments form part of the Tier 1 capital of the Australian ADI under APRA prudential standards. The new debt/equity rules will result in some hybrid instruments which are currently treated as debt interests for income tax purposes being recharacterised as non-share equity interests (eligible hybrids). A consequence is that an Australian ADI (i.e. the entity legally liable in the head office/branch structure) would need to frank the returns on these instruments (i.e. non-share dividends). This is an inherent additional cost of raising capital overseas which would not be incurred if the Australian ADI issued eligible hybrids through a foreign subsidiary and is a cost which may not be incurred by a foreign independent entity raising capital in the same way.
>
> 2.94 This measure prevents the disadvantage from arising by treating the returns on the eligible hybrids as unfrankable dividends of the ADI. Aligning the taxation treatment of foreign branches with that of foreign subsidiaries of the ADI and foreign independent entities in relation to the issue of eligible hybrids will assist Australian ADIs to grow their businesses conducted through foreign branches.

36. The purpose of section 215-10 is best understood when considered in the context of the Australian imputation system. Classical company tax systems affect the cost of capital for moneys raised in the form of equity to the extent that they impose an additional layer of taxation on profits earned by that capital. A decrease in the after-tax return on an equity investment attracts demand by investors for a higher pre-tax return, thus increasing the cost of capital. The Australian imputation system is directed at removing double taxation for Australian resident investors in respect of income that is taxed in Australia; and hence puts them in the same position as resident recipients of Australian sourced interest. Franking does not have an equivalent effect for foreign residents, where it will often only relieve an interest withholding tax liability (which may in any event have resulted in a foreign tax credit in the foreign jurisdiction, thus leaving the overall tax burden unaffected). Requiring the franking of returns for non-residents receiving income from non-share equity issued offshore results in wastage of franking credits, thus effectively increasing the issuer's cost of capital (compared with issuing non-frankable instruments to the same non-residents).

37. 'Wastage' is usually an intended feature of the system, at least for inward foreign equity investment, because it represents the intended Australian source tax on profits attributable to that investment. Dividend streaming rules are enacted to prevent the avoidance of intended wastage by the selective targeting of resident and non-resident equity investors.

38. The purpose of section 215-10 is to prevent unintended wastage for *non-resident investors* making an equity investment *in a foreign jurisdiction*. Outward equity investment is generally outside the imputation system, the result of confining franking accounts to resident companies. A foreign investor in a non-resident company earning profits not sourced in Australia generally has no Australian tax exposure, and the company therefore faces no cost of capital consequences for that equity from the Australian imputation system. However, a resident company with an offshore branch earning foreign source income that has non-resident investors faces the possibility that a distribution to investors will have to be franked, resulting in the wastage of franking credits. This problem arises regardless of the form of the equity,[6] but in the case of *non-share* equity competitive neutrality is involved. Non-share equity (that is, legal form debt) may be deductible in a foreign jurisdiction. Moreover, most other countries now operate some form of modified classical company taxation, which has the effect of making investors indifferent to whether the company invests on-shore or off-shore.

39. When non-share equity capital is raised and used in a foreign jurisdiction it will attract local tax consequences, that is, there may be a deduction for the cost of the capital in the foreign jurisdiction, and in the case of branches of foreign companies operating there, usually also exemption or a tax credit in the home jurisdiction for income *net of any deduction*. If, in addition, but only for Australian resident companies, it also attracts an adverse franking consequence in Australia, that consequence will of course increase the cost of capital for Australian companies compared with other companies operating in the same jurisdiction, putting Australian companies at a competitive disadvantage. For ADIs the cost of capital may be crucial for commercial success and this disadvantage correspondingly significant. Section 215-10 is intended to put a foreign branch of a resident ADI in the same position for the issue of the same instrument by other banks conducting business in that jurisdiction. Therefore, the section 'turns off' the Australian company tax imputation rules so that the advantages and disadvantages of the local company tax rules should apply equally to all.

40. When regard is had to what is said in the Explanatory Memorandum, as well as to how section 215-10 operates as an exception to the general operation of the imputation system, it is clear that section 215-10 is intended to ensure that ADIs do not incur the additional cost of franking returns in respect of capital that is both raised and used offshore: see paragraph 2.93 of the Explanatory Memorandum. The reference to 'raising capital overseas' in the Explanatory Memorandum is consistent with the requirement that the relevant equity interest be 'issued at or through a permanent establishment' of the ADI. Then, paragraph 215-10(1)(d) ensures that the concession only applies when the capital is used offshore in the course of the business conducted by the ADI at the permanent establishment. Accordingly, section 215-10 puts a business conducted at a permanent establishment in the same position with respect to their cost of capital for use in the business to that of a foreign resident company conducting business in the same jurisdiction.

[6] While it might seem desirable in principle for foreign source income to be distributable from Australian companies to foreign residents without wastage of franking credits, there is a practical problem of identifying the income as foreign source and not inadvertently permitting dividend streaming. Conduit rules attempt to address these problems.

The meaning of 'issued at or through a permanent establishment'

41. Having regard to the meaning of 'at or through a permanent establishment' in the context of whether a business is being carried on at a permanent establishment, section 215-10 will only apply when the non-share equity interest is a transaction *of* the business conducted by the ADI at the permanent establishment in the listed country; and as such the interest must be issued at the place where the business is conducted.

42. A 'permanent establishment' is defined for the purposes of section 215-10 of the ITAA 1997, via section 995-1 of the ITAA 1997, in section 6 of the ITAA 1936. The definition provides that a 'permanent establishment' in relation to a person means:

> '[A] place at or through which the person carries on any business and…includes a place where the person is carrying on business through an agent…'

43. Thus, a permanent establishment is a *place of business*. The preposition 'at' denotes the location of something in space: here it means that the business is done *there*, at that place. The preposition 'through' conveys a sense of instrumentality or agency, which is used to accommodate the extension of the definition to a place where someone else, an agent, carries on the person's business at that place. Hence the fundamental conception of a permanent establishment is that of a fixed place where business is transacted by a person or by a person's agent. For an agent to be taken to be carrying on the person's business at a permanent establishment, the agent must have the general authority to bind the person to contracts, and that agent must habitually exercise its general authority to negotiate and conclude contracts on behalf of the person: see *National Commercial Bank v. Wimborne* (1979) 11 NSWLR 156. The mere existence of a general authority to conclude contracts is not sufficient to constitute carrying on business at or through a permanent establishment. There must also be a habitual exercise of that authority: see *Unisys Corporation Inc v. FC of T* [2002] NSWSC 1115 2002 ATC 5146; (2002) 51 ATR 386.

44. To identify a permanent establishment, there needs to be identification of transactions which constitute the carrying on of a business at a place. A business is not carried on unless there is some repetition or continuity: see *Thiel v. Federal Commissioner of Taxation* (1990) 171 CLR 338; 90 ATC 4717; (1990) 21 ATR 531. Personnel need to be located at the place to undertake the transactions of the business.

45. For the purposes of section 215-10, the business conducted at the permanent establishment must be a banking business.

46. Section 995-1 provides that an ADI is an authorised deposit taking institution within the meaning of the *Banking Act 1959*. It therefore means a body corporate which has been authorised to carry on 'banking business'. 'Banking business' means:

> (a) a business that consists of banking within the meaning of paragraph 51(xiii) of the Constitution; or
>
> (b) a business that is carried on by a corporation to which paragraph 51(xx) of the Constitution applies and that consists, to any extent, or
>
> > (i) both taking money on deposit (otherwise than as part-payment for identified goods or services) and making advances of money; or
> >
> > (ii) other financial activities prescribed by the regulations for the purposes of this definition.

47. Thus, broadly speaking, the business of an ADI is that of a banking business which will consist of the borrowing or lending of money or like financial transactions. The permanent establishment of an ADI will be a place at which it carries on banking business. It may also carry on other business at the permanent establishment, but for section 215-10 to apply an ADI must carry on some banking business at or through a permanent establishment. The requirement that there must be some banking business is drawn from the fact that section 215-10 is dealing with Tier-1 capital which, put simply, is the equity capital an ADI must hold in regard to its banking liabilities to provide security against losses of its banking business.

48. To summarise, the identification of borrowing and lending transactions at a particular place is of the essence for the identification of a permanent establishment of an ADI at that place. In order for a non-share equity interest to be taken to have been issued at or through the permanent establishment for the purposes of section 215-10, the capital raising must be a transaction of the business carried on at the permanent establishment.

49. While the term 'issued' is not defined for the purposes of paragraph 215-10(1)(c), its meaning in relation to shares and debentures issued by a company has been considered by the courts on a number of occasions. The High Court considered the meaning of the term 'issue' in relation to when shares could be taken to be issued in *Central Piggery Co Ltd v. McNicoll and Hurst* (1949) 78 CLR 594. Latham CJ observed in his decision that:

> The issue of the shares is the act which ends the transaction and ends in the issue of the shares to a specific person...

50. Rich J came to a similar conclusion. His Honour stated that:

> 'The word 'issue' is one which has not any very definite legal import with reference to shares,' (*Spitzel v. The Chinese Corporation Ltd*). In the instant case the phrase to be construed is 'proceed to the issue,' a phrase which predicates a course of action ending in the issue. Shares are turned from nominal into effective capital upon being issued… It is not the first step which counts but the final step.'

51. Dixon J also made a similar finding when he observed, at pages 599 – 600, that:

> …. Speaking generally the word 'issue' used in relation to shares means, where an allotment has taken place that the shareholder is put in control of the shares allotted. A step amounts to issuing shares if it involves the investing of the shareholder with complete control over the shares. *Re Ambrose Lake Tin and Copper Co* (*Clarke's Case*) makes that quite clear. Cockburn L.C.J. said 'inasmuch as the term 'issue' is used, it must be taken as meaning something distinct from allotment, and as importing that some subsequent act has been done whereby the title of the allottee becomes complete, either by the holder of the shares receiving some certificate, or being placed on the register of shareholders, or by some other step by which the title derived from the allotment may be made entire and complete.

52. These observations when read together support the view that shares are issued by a company when the final step, or final series of steps are taken, which invest the shareholder with complete control over the shares. See also *Re Buckley Earthmoving Pty Ltd (in liq)* (1995) 15 ACSR 732, citing *Central Piggery Co Ltd v. McNicoll and Hurst* (1949) 78 CLR 594 as well as *National Westminster Bank plc v. Inland Revenue Commissioners* [1994] 3 All ER 1.

53. In an earlier case, *Grenfell v. The Commissioners of Inland Revenue* (1875-76) LR 1 Ex D 242, the English Divisional Court had to answer a slightly different question. Rather than determine when a security was issued, the court had to consider where a security had been issued. That is, the court had to decide whether certain bonds had been issued in the United Kingdom and thus taxable in the UK, or issued in New York. The court held that the bonds were issued in New York because that was the place where the issuing company parted with possession and control over the bonds. Kelly J. observed, at page 247, that:

> [T]he company is an American company, having its place of business in New York, and there the shares were offered to the public. Some of the bonds were taken up by the public, and then the company entered into negotiations with Messrs. Morton, Bliss & Co., for the purchase by them of the remainder. Carrying out these negotiations, the company sold the bonds, and parted with their interest in them and control over them.

54. Pollock J. made a similar observation when he said, at page 249, that:

> If I understand the word 'issue', not giving to it any technical meaning, the issue of a bond is its first creation by the company, who give thereby a right of action in favour of some person to whom the bond is given. In the present case that was done, and done completely, in New York; because, although no bond was actually handed over in the first instance, a binding contract took place, whereby Messrs. Morton, Bliss & Co. were entitled, on the one hand, to call upon the company to transfer and issue to them a number of the bonds, and, on the other hand, they incurred the correlative obligation of taking and accepting the whole of the liability upon them.

55. Having regard to these cases, it is concluded that a non-share equity interest will be issued at, or through, a permanent establishment for the purposes of section 215-10 when:

- the non-share equity interest is offered to investors in the course of the business conducted by an ADI at or through the permanent establishment in a listed country;
- the non-share equity interest is allocated to the investor by personnel conducting the business at the permanent establishment;
- the transaction documents are executed at the permanent establishment;
- the transaction documents provide that the non-share equity interest is transferred to the investor at the permanent establishment;
- the non-share equity interest is transferred to the investor at the permanent establishment by the personnel conducting the business of the permanent establishment; and
- at the time of transfer, the business conducted at the permanent establishment relinquishes all control over the non-share equity interest.

56. It is not enough that the transaction documents which create the non-share equity interests are prepared and executed at the place where the ADI conducts business. It must also be the case that the steps necessary to complete the process of transferring the non-share equity interests to the investor such that the ADI has 'parted with their interest and control' over the interests are done at the place of business.

57. Paragraph 215-10(1)(c) is satisfied when the transaction documents for creating the non-share equity interests are executed at the place of business, and the marketing and allocation of the non-share equity interests is undertaken from the place of business such that the investor is placed in possession and control of the instrument by the permanent establishment.

58. The answer is no different when a non-share equity interest is transferred to an intermediary and stapled to an equity interest. The non-share equity interests are not issued until the point in time when they are transferred to the investors by an intermediary. Where the permanent establishment of the Australian ADI has issued the non-share equity interests and satisfies all of the conditions in paragraph 55 of this Determination, the capital has been raised offshore. It will generally be the case that the non-share equity interests will have been acquired predominantly by non-resident investors.

59. When the ADI, or an intermediary on their behalf, has marketed non-share equity interests to Australian residents, it is unlikely that paragraph 215-10(1)(c) will be satisfied as the ADI will not have relinquished all control of the non-share equity interests up until the time of the transfer. When an ADI intends to offer a non-share equity interest to Australian resident investors, it is the usual practice for the documents which create the non-share equity interests to be executed at the place where the permanent establishment conducts business, but the ADI retains control over the newly created non-share equity interests of the transfer. Control is generally retained until the non-share equity interests are transferred to the ultimate investors. In retaining control the ADI usually dictates that the interests be transferred to particular intermediaries, who in turn sell the interests to the ultimate investors, after the ADI, or the intermediary on their behalf, has marketed the interests and decided to whom the interests should be sold. Where this is the case, the non-share equity interests are not issued at, or through, the permanent establishment. They are not issued until they are transferred to the Australian investors, and they are issued in Australia by the ADI or an intermediary on the ADI’s behalf.

References

Previous draft:
TD 2009/D2

Related Rulings/Determinations:
TR 2006/10; TD 2009/14

Subject references:
- debentures
- imputation system
- listed countries
- non-share equity interest
- permanent establishment
- preference shares
- securities

Legislative references:
- ITAA 1936 6
- ITAA 1936 160APAAAA
- ITAA 1936 320
- ITAA 1936 Pt X
- ITAA 1997
- ITAA 1997 215-10
- ITAA 1997 215-10(1)
- ITAA 1997 215-10(1)(c)
- ITAA 1997 215-10(1)(d)
- ITAA 1997 Div 974
- ITAA 1997 995-1(1)
- Banking Act 1959
- TAA 1953
- Income Tax Regulations 1936

Case references:
- Central Piggery Co Ltd v. McNicoll and Hurst (1949) 78 CLR 594
- Grenfell v. The Commissioners of Inland Revenue (1875-76) LR 1 Ex D 242
- National Commercial Bank v. Wimborne (1979) 11 NSWLR 156
- National Westminster Bank plc v. Inland Revenue Commissioners [1994] 3 All ER 1
- Re Buckley Earthmoving Pty Ltd (in liq) (1995) 15 ACSR 732
- Thiel v. Federal Commissioner of Taxation (1990) 171 CLR 338; 90 ATC 4717; (1990) 21 ATR 531
- Unisys Corporation Inc v. FC of T [2002] NSWSC 1115 2002 ATC 5146; (2002) 51 ATR 386

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