


TD 93/D229 - Income tax: Foreign Income: is a lump sum payment received by a CFC (Controlled Foreign Company) as consideration for the assignment of an interest stream attributable under section 456 of the Income Tax Assessment Act 1936?

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Draft Taxation Determinations (TDs) represent the preliminary, though considered, views of the ATO. Draft TDs may not be relied on; only final TDs are authoritative statements of the ATO.

Draft Taxation Determination

Income tax: Foreign Income: is a lump sum payment received by a CFC (Controlled Foreign Company) as consideration for the assignment of an interest stream attributable under section 456 of the *Income Tax Assessment Act 1936*?

1. Yes. Where a CFC assigns an interest stream in return for a lump sum payment the payment will fall within the definition of passive income under subsection 446(1). The income will therefore be attributable under section 456 if the CFC fails the active income test and, in relation to a listed country, if the income is an amount to which subsection 385(2) applies.
2. On the basis of the decisions made in *F.C. of T. v. The Myer Emporium* 87 ATC 4363, 18 ATR 693, *Henry Jones (IXL) Ltd. v. F.C. of T.* 91 ATC 4663, 22 ATR 328 and *S.P. Investments Pty. Ltd. v. F.C. of T. and Perron Investments Pty. Ltd. v F.C. of T.* 92 ATC 4496, 24 ATR 14, where an arrangement is entered into for the purposes of making a profit, that profit is income. Consequently, it follows that the consideration received for the assignment of an interest stream under that arrangement is income.
3. There are two ways by which the payment can constitute passive income as defined in subsection 446(1). Where the arrangement is made for the purposes of making a profit, the lump sum payment is tainted interest income as defined in section 317 and therefore constitutes passive income under paragraph 446(1)(d). Tainted interest, as defined, includes interest or a payment in the nature of interest.
4. Their Honours state in Myer's Case (at ATC 4371) that when a taxpayer is selling the mere right to an interest stream for a lump sum he or she is simply converting future income into present income. They also state (at ATC 4371) that interest is regarded as flowing from the principal sum and to be compensation to the lender for being kept out of the use and enjoyment of the principal sum.
5. In a loan arrangement where the assignor does not relinquish the right to the repayment of the principal sum to the assignee, it effectively receives the compensation from the assignee for being kept out of the use and enjoyment of the principal sum at the beginning of the term of the loan rather than at the end of the term of the loan. Accordingly, the assignor simply converts the future interest stream into present income that is interest or in the nature of interest. The lump sum payment is therefore passive income.

6. Alternatively, where the arrangement falls outside the principles laid down in Myer's Case, the lump sum payment is income derived from the disposal of a tainted asset and therefore constitutes passive income under paragraph 446(1)(k). In this regard, it should be considered that Myer's case does not preclude the right to receive an interest stream from being a chose in action (at ATC 4371) and therefore from being an asset. The sale of that right will constitute the disposal of a tainted asset. A tainted asset is defined in section 317. Consequently, any gain from the disposal of a tainted asset will be passive income.

Commissioner of Taxation

2/9/93

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Case Ref: F.C. of T. v The Myer Emporium 87 ATC 4363, 18 ATR 693

Henry Jones (IXL) Ltd. v F.C. of T. 91 ATC 4663, 22 ATR 328

S.P. Investments Pty. Ltd. v F.C. of T. and Perron Investments Pty. Ltd. v F.C. of T. 92 ATC 4496, 24 ATR 14

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