


IT 2045 - Interest withholding tax - withdrawal of australian entity/aidc exemption

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TAXATION RULING NO. IT 2045

INTEREST WITHHOLDING TAX - WITHDRAWAL OF AUSTRALIAN
ENTITY/AIDC EXEMPTION

F.O.I. EMBARGO: May be released

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INTEREST WITHHOLDING TAX -

AIDC EXEMPTION

128EA

AUSTRALIAN ENTITY EXEMPTION

128G

CERTAIN GOVERNMENT BORROWINGS

128GA

PREAMBLE

The Income Tax Assessment Amendment Act (No.2) 1983 (Act No.25 of 1983) received the Royal Assent on 19 June 1983. The Act gives legislative effect to certain of the measures announced in the Government's Economic Statement of 19 May 1983. Included in the Act are provisions to effect the withdrawal of the exemption from withholding tax of interest payable on overseas borrowings of "Australian entities" and the Australian Industry Development Corporation (AIDC).

2. The exemption from withholding tax available under section 128F (widely issued bearer debentures) is not in any way affected by the changes included in the Act. Similarly, interest on overseas borrowings of the Commonwealth will continue to be eligible for exemption under section 6B of the Loans Securities Act 1919 (refer paragraphs 214 to 218 of CITCM 867).

RULING

3. The effect of the changes contained in the legislation may be summarised as follows:-

- (a) the exemptions available under section 128EA(AIDC) and section 128G ("Australian entities") no longer apply to interest on loans raised in pursuance of contractual obligations entered into after 19 May 1983 (but see sub-paragraph (d) below);
- (b) other than in those cases referred to in sub-paragraph (d) below, exemptions available under those sections will continue to apply in respect of interest on borrowings, only where made pursuant to contractual obligations entered into on or before 19 May 1983;
- (c) exemptions in respect of interest on overseas borrowings by State Governments, and Commonwealth and State authorities, which are entered into after 19 May 1983 will be available under new section 128GA, where the Treasurer certifies that the interest is to be

exempt (note that a certificate is not to be given where the Treasurer is satisfied that the funds from the borrowing, whether made by an authority itself or by a government on its behalf, will be used by an authority in direct competition with private sector enterprises);

- (d) interest on loans entered into after 19 May 1983 which meet the existing requirements of section 128EA or 128G may continue to qualify for exemption under those sections but only so much of it as:-

- (i) was paid before the date of commencement of the amending legislation (19 June 1983); and

- (ii) does not exceed the amount that might reasonably have been expected to have been payable before that date (see paragraph 8).

4. The most likely problem area involves the basic question of whether a "contractual obligation" was entered into on or before 19 May 1983.

5. In this regard, the need for care in giving information or advice is stressed. Whether or not a contractual obligation - broadly, a legally binding and enforceable agreement under which both parties are committed to the lending/borrowing - has been entered into by a particular date is a question to be determined in the light of the facts of each case. It will not, of course, be sufficient to provide evidence of other actions, e.g., the negotiation of contracts for the acquisition of substantial assets or for large construction projects, which would obviously require the borrowing of funds for their completion, or of preliminary steps having been taken which, if pursued, might be expected ultimately to lead to loan agreements being entered into. Consequently, under no circumstances should definitive oral advice be provided in answer to hypothetical questions, and discussions on what may or may not constitute a contractual obligation should be avoided. Where a definitive response is sought on the basis of established facts, the enquiry should be submitted in writing, with copies of contracts and other supporting documentation. The onus will be on the parties - Australian borrower and overseas lender - to establish, when seeking exemption from withholding tax under either section 128EA or section 128G, that a contractual obligation had been entered into on or before 19 May 1983.

6. In terms of the new sub-sections (3) inserted in sections 128EA and 128G, the existing exemptions available under those sections are not applicable to interest paid on or after the date on which the legislation received Royal Assent (19 June 1983) where the particular loan was raised in pursuance of a contractual obligation entered into after 19 May 1983. The effects of this are two-fold. Interest on loans raised (even after 19 May 1983) in pursuance of contractual obligations entered into before 20 May 1983 may still qualify for exemption under section 128EA or 128G, as the case may be, irrespective of

when the interest is paid. Also, interest on loans raised in pursuance of contractual obligations entered into after 19 May 1983 may qualify for exemption if it was paid before 19 June 1983.

7. Without some form of safeguard, it would have been possible for those who entered into contracts after 19 May 1983 to abuse the latter situation by, for example:-

- (a) "loading up" interest under contractual obligations which specify that all or a large part of the interest is or was to be paid before the date of Royal Assent (19 June 1983); or
- (b) simply prepaying, before that date, all or a large part of the interest payable under a contract.

8. Section 16 of the amending Act is designed to overcome these possibilities and provides that the exemption otherwise available under section 128EA or 128G for such interest is not available in respect of so much of it as the Commissioner is satisfied was paid before the date of Royal Assent, rather than at some later time, for the purpose of obtaining the benefit of section 128EA or section 128G. In forming his opinion for this purpose, the Commissioner is required to have regard to the amount of the loan to which the interest relates, the terms of the particular contractual obligation and the amount of the interest.

9. In other words, where, having regard to the foregoing factors, it is apparent that some interest was paid early in an attempt to defeat the withdrawal of the section 128EA or 128G exemption, the exemption does not apply to that interest.

10. In the event that it is necessary to issue any section 128H certificates in respect of interest on loans raised in pursuance of contractual obligations entered into after 19 May 1983, such certificates will need to be clearly endorsed to the effect that only interest paid before 19 June 1983, to the extent that it is not excluded from exemption under section 16, is exempt from withholding tax.

COMMISSIONER OF TAXATION
20 June 1983