



PR 2005/89 - Income tax: tax consequences of investing in Macquarie Self Funding Instalments SMU Series 2005 Product Disclosure Statement - cash applicants and on-market purchasers

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 This document has changed over time. This is a consolidated version of the ruling which was published on *1 June 2005*



Product Ruling

Income tax: tax consequences of investing in Macquarie Self Funding Instalments SMU Series 2005 Product Disclosure Statement – cash applicants and on-market purchasers

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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

The Tax Office **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.

Potential 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 and how the product fits an existing portfolio. We recommend a financial (or other) adviser be consulted for such information.

This Product Ruling provides certainty for potential participants by confirming that the tax benefits set out 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, participants lose the protection of this Product Ruling. Potential participants may wish to seek assurances from the promoter that the arrangement will be carried out as described in this Product Ruling.

Potential participants should be aware that the Tax Office 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.

Potential participants may wish to refer to the Tax Office website at www.ato.gov.au or contact the Tax Office directly to confirm the currency of this Product Ruling or any other Product Ruling that the Tax Office has issued.

Terms of use of this Product Ruling

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

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 acquisition of a Macquarie Self Funding Instalment SMU Series (Macquarie SMU Self Funding Instalment(s)) under the 2005 Product Disclosure Statement which provides an investment in shares and/or units that are listed for quotation on the Australian Stock Exchange (ASX) and a put option (Holder's Put Option) using a loan made by Macquarie Bank Limited (Macquarie).
2. This Ruling does not address the Holder's entitlement to franking credits.

Tax law(s)

3. The tax laws dealt with in this Ruling are:
 - section 8-1 of the *Income Tax Assessment Act 1997* (ITAA 1997);
 - section 25-25 of the ITAA 1997;
 - section 104-10 of the ITAA 1997;
 - section 104-25 of the ITAA 1997;
 - section 109-5 of the ITAA 1997;
 - section 110-25 of the ITAA 1997;
 - subsection 110-45(3) of the ITAA 1997;
 - section 112-35 of the ITAA 1997;
 - section 115-5 of the ITAA 1997;
 - section 134-1 of the ITAA 1997;
 - section 51AAA of the *Income Tax Assessment Act 1936* (ITAA 1936);
 - section 82KL of the ITAA 1936;
 - section 82KZM of the ITAA 1936;
 - section 82KZMA of the ITAA 1936;

- section 82KZMD of the ITAA 1936;
- section 82KZME of the ITAA 1936;
- section 82KZMF of the ITAA 1936;
- section 97 of the ITAA 1936; and
- Part IVA of the ITAA 1936.

Class of persons

4. The class of persons to whom this Ruling applies is those who enter into the arrangement described below, through Cash Applications or on-market purchases, on or after the date this Ruling is made. They will have a purpose of staying in the arrangement until it is completed and deriving assessable income from their involvement as set out in the description of the arrangement. In this Ruling these persons are referred to as 'Holders'.

5. This Ruling does not apply to Shareholder or Rollover Applicants. These application methods are disclosed and described in the Product Disclosure Statement.

Qualifications

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

7. 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

9. This Ruling applies prospectively from 1 June 2005, 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).

10. 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

11. This Product Ruling is withdrawn and ceases to have effect after 30 June 2008. 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

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

- Application for a Product Ruling dated 12 April 2005 received from Mallesons Stephen Jaques on behalf of Macquarie;
- Macquarie Self Funding Instalment Warrants Trust Deed dated 21 July 2003, as amended by the Supplemental Deed of Amendment on 5 February 2004, Second Supplemental Deed of Amendment on 5 March 2004, Third Supplemental Deed of Amendment on 14 July 2004 (Trust Deed); and

- Self Funding Instalments Combined Product Disclosure Statement and Financial Services Guide SMU Series dated 5 January 2005 (PDS) issued by Macquarie (which includes the terms of the Loan Agreement).

13. In this Ruling, unless otherwise defined, capitalised terms take their meaning as in the PDS.

14. Macquarie SMU Self Funding Instalments are a moderately geared product that allows Holders to gain exposure to share price movements and dividends without paying the full price of the share. The gearing level is approximately 50% of the underlying share price and may vary from that time depending on a number of factors including interest rates, dividends and prices of the underlying shares.

15. Macquarie SMU Self Funding Instalments are offered over certain shares, units or stapled securities listed on the ASX (Share(s)). Where the Share is a stapled security, the stapled security is comprised of shares and units that are jointly listed for quotation on the ASX. Each Macquarie SMU Self Funding Instalment is comprised of one 'Underlying Share' which consists of one Share and any Accretions in respect of that Share.

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

- (a) Macquarie SMU Self Funding Instalments provide a leveraged investment in the Underlying Share using a Loan made by Macquarie. There are three methods by which Macquarie SMU Self Funding Instalments are created, one of which is by Cash Application:

The Cash Applicant pays the varying First Payment. The First Payment is applied by Macquarie to partially fund the purchase of the Underlying Share and to pay the Borrowing Fee. Macquarie lends the Completion Payment amount to the Cash Applicant. The proceeds of the Loan are applied toward:

- prepayment of interest to Macquarie; and
- the purchase of the Underlying Share,

Macquarie buys the Underlying Share in the name of the Security Trustee and takes a security interest over the Underlying Share. The Macquarie SMU Self Funding Instalment is issued in the name of the Cash Applicant;

- (b) Macquarie SMU Self Funding Instalments can also be acquired by an on-market purchase;
- (c) Holders can obtain the Underlying Share at any time before the Maturity Date by making the Completion Payment;
- (d) the Completion Payment is equal to the Loan Amount on the date the Completion Payment is made;

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- (e) the Loan is made on a limited recourse basis, secured by a mortgage over the Underlying Share which will be held by the Security Trustee as nominee for the Holder;
- (f) in the case of a Cash Applicant, the Borrowing Fee will comprise two components, a fee for the grant of the Holder's Put Option and an amount which is paid for acquiring the Loan from Macquarie;
- (g) interest is also payable on each Annual Interest Date, and is funded by drawing down on the existing Loan;
- (h) during the term of the Macquarie SMU Self Funding Instalment, the Holder directs the Security Trustee to pay the full amount of distributions received in respect of the Underlying Share to Macquarie and directs Macquarie to apply those distributions to reduce the Holder's outstanding Loan;
- (i) where the Security Trustee is required to withhold an amount from a distribution received in respect of the Underlying Share because a TFN/ABN has not been quoted and the dividend is unfranked, the Holder's outstanding Loan will still be reduced by the full amount of the distribution, and the Holder will be required to fund the amount withheld by making a cash payment or by forfeiting Macquarie SMU Self Funding Instalments to the same value;
- (j) at Maturity, the Holder has four options:
 - (i) pay the Completion Payment:

Holders can obtain the Underlying Share by making the Completion Payment. The Loan is repaid, the security interest is extinguished and the Shares are delivered to a holding in the Holder's name;
 - (ii) exercise the Holder's Put Option:

The Underlying Share is purchased by Macquarie at the higher of the Completion Payment or the market price and the proceeds are applied to repayment of the Loan with any residual paid to the Holder;
 - (iii) rollover:

A rollover is economically equivalent to the Holder completing the expiring series by making the Completion Payment and then investing in the new series by way of a Shareholder Application. Under the rollover, the Underlying Share is not sold rather, the expiring warrant is cancelled and the Holder is allotted a Macquarie instalment in the new series;

- (iv) do nothing:

At Maturity if the Completion Payment is not made, and the Holder's Put Option is not exercised, the Underlying Share will be sold and any surplus from net proceeds after repayment of the Loan and costs will be paid to the Holder. If the sale proceeds are insufficient to repay the Loan, Macquarie has no recourse against the Holder to recover the shortfall;
- (k) at any time during the life of the Macquarie SMU Self Funding Instalments, the Holder has the option to make the Completion Payment, rollover into a new series of instalment warrants or sell their instalments on the ASX; and
- (l) where the Macquarie SMU Self Funding Instalments are purchased on the ASX, the on-market purchaser acquires the Macquarie SMU Self Funding Instalments on the same terms and conditions under which they were originally issued. In particular, the on-market purchaser will be offered and will accept a Loan from Macquarie upon the transfer of the Macquarie SMU Self Funding Instalments from the previous owner to the on-market purchaser. The Loan provided by Macquarie will be equal to the previous owner's Loan and will be applied to discharge the previous owner's Loan, refund part of the interest prepaid by the previous owner and to prepay the Interest Amount on the newly acquired Loan.

The Participants

17. Macquarie is the Issuer of the Macquarie SMU Self Funding Instalments. Macquarie is also the provider of the Loans to Holders to fund the acquisition of the Underlying Shares.

18. Belike Nominees Pty Ltd holds the legal title to the Underlying Shares as Security Trustee and as nominee for each Holder.

19. The Holders may be individuals, companies, trusts or superannuation funds.

Ruling

20. Subject to the Assumptions listed in paragraph 20 of this Ruling:

- (a) section 8-1 of the ITAA 1997 will apply to allow a Holder a deduction for the interest charged under the Loan Agreement;

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- (b) section 51AAA of the ITAA 1936 will not apply to deny a Holder a deduction for the interest allowable under section 8-1 of the ITAA 1997;
- (c) section 82KL of the ITAA 1936 will not apply to deny deductibility of the interest allowable under section 8-1 of the ITAA 1997;
- (d) section 82KZMF of the ITAA 1936 will not apply to set the amount and timing of deductions for the interest charge incurred under the Macquarie SMU Self Funding Instalment;
- (e) section 82KZM of the ITAA 1936 will not apply to deny a Holder immediate deductibility of any part of the Macquarie SMU Self Funding Instalment interest charge allowable under section 8-1 of the ITAA 1997, where at least one of the following applies for the year of income:
- the Holder is an STS taxpayer; or
 - the Holder is an individual who does not incur the interest charge in carrying on a business;
- (f) section 82KZMD of the ITAA 1936 will apply to set the amount and timing of the deductions for the Macquarie SMU Self Funding Instalment interest charge that is deductible to a Holder (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;
- (g) the portion of the Borrowing Fee that is paid for acquiring the Loan from Macquarie will be deductible to the Holder under section 25-25 of the ITAA 1997;
- (h) the part of the Borrowing Fee which is applicable to the purchase of the Holder's Put Option forms the cost base to the Cash Applicant of the Underlying Share under section 134-1 of the ITAA 1997 if the Holder's Put Option is exercised;
- (i) the part of the Borrowing Fee which is applicable to the purchase of the Holder's Put Option forms the cost base to the Cash Applicant of the Holder's Put Option under section 110-25 of the ITAA 1997 if the Holder's Put Option is not exercised;
- (j) for on-market purchasers the cost base of the Holder's Put Option is calculated as follows:
- if the market value of the Share at the time of purchase is greater than the Completion Payment (the Loan Amount) the cost base of the Holder's Put Option is the total consideration as determined by section 110-25 and section 112-35 of the ITAA 1997 (the price of the Macquarie SMU Self

- Funding Instalment plus the Completion Payment) less the sum of the market value of the Share and the interest prepaid on the newly acquired Loan; or
- if the market value of the Share at the time of purchase is less than the Completion Payment the cost base of the Holder's Put Option is the total consideration as determined by section 110-25 and section 112-35 of the ITAA 1997 (the price of the Macquarie SMU Self Funding Instalment plus the Completion Payment) less the sum of the Completion Payment and the interest prepaid on the newly acquired Loan;
- (k) for on-market purchasers the amount determined under paragraph 20(j) above will be included in the cost base of the Underlying Share under section 134-1 of the ITAA 1997 if the Holder's Put Option is exercised;
- (l) for on-market purchasers the amount determined under paragraph 20(j) above will be included in the cost base of the Holder's Put Option under section 110-25 of the ITAA 1997 if the Holder's Put Option is not exercised;
- (m) for capital gains tax (CGT) purposes, including for the purposes of the CGT discount, the date of acquisition of the Underlying Share for Holders, is the date on which they acquire the related Macquarie SMU Self Funding Instalment;
- (n) no CGT event arises when the legal title to the Underlying Share is transferred by the Security Trustee to the Holder;
- (o) a CGT event will arise under section 104-10 of the ITAA 1997 to the Holder where the Completion Payment is not made or where a TFN/ABN has not been quoted and the dividend is unfranked, and the Underlying Share is sold;
- (p) if the sale proceeds are insufficient to repay the Loan, Macquarie has no recourse against the Holder to recover the shortfall and the Holder will need to reduce the cost base of the shares by the amount of the shortfall under subsection 110-45(3) of the ITAA 1997;
- (q) any capital gain realised by a Holder on sale of an Underlying Share received pursuant to completion of a Macquarie SMU Self Funding Instalment, will be treated as a discount capital gain pursuant to section 115-5 of the ITAA 1997 where the Holder is an individual, a complying superannuation entity, or a trust and has held the Macquarie SMU Self Funding Instalment for at least 12 months;

- (r) a CGT event will occur under section 104-25 of the ITAA 1997 on the Maturity Date if the Holder's Put Option is not exercised and expires. The capital proceeds received on expiration of the Holder's Put Option will be nil;
- (s) the Holders in Macquarie SMU Self Funding Instalments (and not the Security Trustee) are assessable under section 97 of the ITAA 1936 on all of the income derived from the Underlying Share while the Underlying Share is the subject of the Separate Trust; and
- (t) the anti-avoidance provisions contained in Part IVA of the ITAA 1936 will not be applied to deny deductibility of the interest incurred by the Holder in respect of borrowings used to fund the purchase of the Underlying Share.

Assumptions

21. This Ruling is made on the basis of the following assumptions:
- (a) all of the Holders are Australian residents for taxation purposes;
 - (b) the Holders are not traders in investments and are not treated for taxation purposes as either trading in the Underlying Share or carrying on a business of investing in the Underlying Share, or holding the Underlying Share as trading stock or as a revenue asset;
 - (c) in respect of any interest charges to be paid in advance under the Loan Agreement, these may be prepaid, but only in relation 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 a Holder in entering the arrangement is to derive assessable income from their investment in the Macquarie SMU Self Funding Instalments;
 - (e) the arrangement will be executed in the manner described in the 'Arrangement' section of this Ruling;
 - (f) all dealings by the Holders and Macquarie will be at arm's length;
 - (g) the Underlying Share will not be the subject of any securities lending arrangement; and
 - (h) at all times during an arrangement, where the Underlying Share includes units in a trust, the trust satisfies the requirements of subparagraph 82KZME(5)(b)(iii) of the ITAA 1936.

Explanation

Section 8-1 of the ITAA 1997

22. The cost (or interest paid) of a borrowing used to acquire income producing assets such as shares 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 (see Taxation Ruling TR 95/33).

23. No part of the interest charged on an investment in Macquarie SMU Self Funding Instalments is a capital protection fee. The capital protection is provided by the Holder's Put Option. Therefore, Holders will not be denied a deduction for any part of the interest under section 8-1, provided that the other requirements of that section are satisfied. This is the case regardless of whether the Holder acquired the Macquarie SMU Self Funding Instalment by cash application or by purchase on the ASX.

Section 51AAA of the ITAA 1936

24. By investing in Macquarie SMU Self Funding Instalments, it is contemplated that a Holder will derive assessable income by the receipt of dividend 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 a Holder in Macquarie SMU Self Funding Instalments.

Section 82KL of the ITAA 1936

25. 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 under section 8-1 of the ITAA 1997.

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

26. 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 Holder is an 'STS taxpayer', whether the Holder is an individual and whether the Holder 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

27. A Holder will be an STS taxpayer for an income year if the Holder is eligible to be an STS taxpayer for that year and the Holder notifies the Commissioner of the choice to become such a taxpayer for that year.

28. A Holder will be eligible to be an STS taxpayer for an income year if the Holder 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

29. The interest allowable under section 8-1 of the ITAA 1997 is in relation to a prepayment of loan interest for a period that is not more than 12 months. 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, which is 12 months, and not to the period of the loan.

Sections 82KZME and 82KZMF of the ITAA 1936: prepaid expenditure and 'tax shelter' type arrangements

30. 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' type arrangement for the doing of a thing that is not to be wholly done within the expenditure year.

31. 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 Macquarie SMU Self Funding Instalments, including the financing, share purchase, shareholding and disposal arrangements.

32. Under the arrangement, when the Holder acquires the Macquarie SMU Self Funding Instalment, they acquire beneficial ownership of the Underlying Share.

33. Exception 1, as contained in subsection 82KZME(5), applies to exclude the interest incurred on borrowings under the Macquarie SMU Self Funding Instalments from the operation of section 82KZMF, as:

- the prepaid interest expenditure under the Macquarie SMU Self Funding Instalments is incurred in respect of money borrowed to acquire shares that are listed for

quotation on the ASX or units in a trust as described in subparagraph 82KZME(5)(b)(iii);

- the Holder can reasonably be expected to obtain dividends or trust income from the investment;
- the Holder will not obtain any other kind of assessable income from the investment, except for the capital gains; and
- all aspects of the Macquarie SMU Self Funding Instalments are at arm's length.

Deductibility of expenditure must therefore be considered under the prepayment rules outlined in paragraphs 34 to 39 below.

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

34. 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.

35. 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.

36. As the eligible service period in relation to the deductible interest for Macquarie SMU Self Funding Instalments 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 Holders who are STS taxpayers for the year of income, or to Holders who are individuals and the expenditure is not incurred in carrying on a business. Holders who satisfy these tests will be able to claim an immediate deduction for the allowable interest incurred.

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

37. Section 82KZMD sets the amount and timing of deductions for expenditure for a Holder (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.

38. Section 82KZMA requires that 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.

39. For these taxpayers, the deduction for prepaid interest on the Macquarie SMU Self Funding Instalment will be apportioned over the relevant interest payment period.

Borrowing Fee

40. Part of the Borrowing Fee is for the purchase of the Holder's Put Option and the balance represents a payment for acquiring the Loan from Macquarie. The latter payment is deductible under section 25-25 of the ITAA 1997 over the shorter of the period of the Loan or 5 years.

41. The part of the Borrowing Fee that is applicable to the Holder's Put Option ensures that the Holder is protected from liability to repay the principal if the market value of the shares falls below their original purchase price. In effect, the Holder's Put Option ensures that Macquarie will acquire the shares in full satisfaction of the Loan Amount if the shares have fallen in value below the amount borrowed. The payment is capital in nature, being paid to acquire an asset, namely, the Holder's Put Option.

Cost Base of the Holder's Put Option for Cash Applicants

42. If the Holder's Put Option is exercised the part of the Borrowing Fee which is applicable to the purchase of the Holder's Put Option is included in the cost base of the Underlying Share under section 134-1 of the ITAA 1997.

43. If the Holder's Put Option is not exercised the part of the Borrowing Fee which is applicable to the purchase of the Holder's Put Option forms the cost base of the Holder's Put Option under subsection 110-25(2) of the ITAA 1997.

Cost Base of the Holder's Put Option for on-market purchasers

44. If the market value of the Share at the time of purchase is greater than the Completion Payment (the Loan Amount) the cost base of the Holder's Put Option is the total consideration as determined by sections 110-25 and 112-35 of the ITAA 1997 (the price of the Macquarie SMU Self Funding Instalment plus the Completion Payment) less the sum of the market value of the Share and the interest prepaid on the newly acquired Loan.

45. If the market value of the Share at the time of the purchase is less than the Completion Payment the cost base of the Holder's Put Option is the total consideration as determined by sections 110-25 and 112-35 (the price of the Macquarie SMU Self Funding Instalment plus Completion Payment) less the sum of the Completion Payment and the interest prepaid on the newly acquired Loan.

46. If the Holder's Put Option is exercised, the amount determined under paragraph 20(j) above is included in the cost base of the Underlying Share under section 134-1 of the ITAA 1997.

47. If the Holder's Put Option is not exercised, the amount determined under paragraph 20(j) above is included in the cost base of the Holder's Put Option under section 110-25.

Section 109-5 of the ITAA 1997: time of acquisition

48. Section 109-5 applies to Holders to treat them as having acquired the Underlying Share at the same time that the Holder obtains the beneficial ownership of the Underlying Share. The acquisition time for a Cash Applicant, is the time the application was accepted, and for an on-market purchaser, is the contract date for the transfer of the Macquarie SMU Self Funding Instalment.

Subsection 104-10(7) of the ITAA 1997: no CGT event when Completion Payment made

49. When the Completion Payment is made, no CGT event will arise in respect of the transfer of the legal title to the Underlying Share from the Security Trustee to the Holder by virtue of subsection 104-10(7).

Section 104-10 of the ITAA 1997: CGT event A1

50. A CGT event will arise to the Holder if the Holder does not make the Completion Payment or does not quote a TFN/ABN and the dividend is unfranked, and the Underlying Share is sold to Macquarie or to a third party.

51. If the sale proceeds are insufficient to repay the Loan, Macquarie has no recourse against the Holder to recover the shortfall. In this circumstance the Holder will need to reduce the cost base of the Underlying Share by the amount of the shortfall under subsection 110-45(3) of the ITAA 1997.

Section 115-5 of the ITAA 1997: CGT discount

52. Division 115 allows a taxpayer a discount on capital gains in certain circumstances. In accordance with section 115-5, any capital gain realised by a Holder on the sale of the Macquarie SMU Self Funding Instalment or the sale of an Underlying Share received pursuant to the completion of a Macquarie SMU Self Funding Instalment will be

treated as a discount capital gain where the Holder is an individual, a complying superannuation entity, or a trust and has held the Macquarie SMU Self Funding Instalment for at least 12 months.

53. In accordance with section 115-5, the 12 month period for the purposes of the CGT discount will run from the date of acquisition of the Macquarie SMU Self Funding Instalment.

Section 104-25 of the ITAA 1997

54. Where, at the Maturity Date, the Holder's Put Option is not exercised, the Put Option will expire. The expiration of the Holder's Put Option gives rise to CGT event C2 (paragraph 104-25(1)(c) of the ITAA 1997). The capital proceeds received on the expiration of the Holder's Put Option will be nil.

Section 97 of the ITAA 1936

55. The Holders are presently entitled to all of the income derived from the Underlying Share. Therefore, section 97 will apply to assess the Holders on the income derived from the Underlying Share. The Security Trustee will not be subject to tax on this income.

Part IVA of the ITAA 1936

56. Provided that the arrangement ruled on is entered into and carried out as disclosed (see the Arrangement part of this Ruling), it is accepted that the arrangement is an ordinary commercial transaction and Part IVA will not apply.

Detailed contents list

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

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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

PR 2005/89*Subject references:*

- financial products
- interest expenses
- prepaid expenses
- product rulings
- public rulings
- STS taxpayer
- taxation administration
- tax avoidance

- ITAA 1936 82KZME(5)(b)(iii)
- ITAA 1936 82KZMF
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- ITAA 1997 104-10
- ITAA 1997 104-10(7)
- ITAA 1997 104-25
- ITAA 1997 104-25(1)(c)
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- ITAA 1936 82KZL(2)(a)
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