



PR 2005/96 - Income tax: tax consequences of investing in ABN AMRO Rolling Instalment Warrants IZY Series 2005 Product Disclosure Statement - Cash Applicants and Secondary Market Purchasers

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 This document has changed over time. This is a consolidated version of the ruling which was published on *29 June 2005*



Product Ruling

Income tax: tax consequences of investing in ABN AMRO Rolling Instalment Warrants IZY Series 2005 Product Disclosure Statement – Cash Applicants and Secondary Market Purchasers

Contents	Para
What this Product Ruling is about	1
Date of effect	9
Withdrawal	11
Arrangement	12
Ruling	21
Assumptions	22
Explanation	23
Detailed contents list	55

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.

Preamble

*The number, subject heading, **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.

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 an ABN AMRO Rolling Instalment Warrant IZY Series (ABN AMRO IZY Rolling Instalment(s)) under the Product Disclosure Statement dated 22 April 2005, which provides an investment in shares listed for quotation on the Australian Stock Exchange (ASX) and a put option (Holder's Put Option) using in part a loan made by ABN AMRO Australia Limited (ABN AMRO).
2. This Ruling does not address the tax consequences of the Rollover Cashback.

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 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 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, either through Cash Applications or secondary market purchases, on or after the date of this Ruling. They will have, at the time of entering this arrangement, a 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'.

5. This Ruling does not apply to Shareholder or Conversion Applicants. These application methods are disclosed and described in the Product Disclosure Statement dated 22 April 2005.

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 29 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. The description incorporates the following documents:

- application for a Product Ruling dated 5 May 2005 received from Baker & McKenzie on behalf of ABN AMRO;
- Product Disclosure Statement for the ABN AMRO Rolling Instalments dated 22 April 2005 (PDS) issued by ABN AMRO;
- Trust Deed for ABN AMRO Rolling Instalments executed 21 April 2005 (Trust Deed) (incorporated in the PDS); and
- additional information dated 17 June 2005.

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

14. On acceptance of an Investor's application for an ABN AMRO IZY Rolling Instalment, the Investor will acquire a Loan, appoint ABNED Nominees Pty Limited to act as its nominee and will accept the ABN AMRO IZY Rolling Instalments on the terms and conditions set out in the Trust Deed. Investors can also purchase ABN AMRO IZY Instalments once they are listed on the ASX.

15. ABN AMRO IZY Rolling Instalments are offered over shares that are listed for quotation on the ASX (Underlying Entities' Share(s)). In this Ruling the shares and Accretions, if any, are referred to as the 'Underlying Parcel'.

16. ABN AMRO IZY Rolling Instalments provide a leveraged investment in the Underlying Parcel. ABN AMRO IZY Rolling Instalments are a moderately geared product that allows Investors to gain exposure to share price movements and dividends. Gearing results from the Loan provided by ABN AMRO to Investors to partly fund their investment in the Underlying Parcel.

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

- (a) ABN AMRO IZY Rolling Instalments may initially be acquired in the primary market through three types of application, one of which is Cash Application. ABN AMRO IZY Rolling Instalments will also be listed on the ASX so that they may be purchased on the secondary market;
- (b) under a Cash Application, a Cash Applicant pays the First Payment and draws down the Loan made by ABN AMRO. The First Payment and the Loan Amount is applied toward the purchase of the Underlying Parcel, payment of the First Interest Amount and payment of the Capital Protection Fee and Borrowing Fees (if any).

ABN AMRO purchases the Underlying Parcel in the name of the Security Trustee for the benefit of the Cash Applicant and takes a security interest over the Underlying Parcel. ABN AMRO grants the Cash Applicant a Holder's Put Option which lasts for the life of the ABN AMRO IZY Rolling Instalment. The ABN AMRO IZY Rolling Instalment is issued in the name of the Cash Applicant;

- (c) the amount of the Loan provided to fund the purchase of each Underlying Parcel will be fixed by ABN AMRO on acceptance of a Cash Application based on the market value of the Underlying Parcel;
- (d) the Loan Amount is fixed until the first Reset Date. The Loan Amount is reviewed on each Reset Date. Where the value of the Underlying Parcel has increased Investors may receive additional ABN AMRO IZY Rolling Instalments. Where the value of the Underlying Parcel has decreased, the Loan Amount may be reduced and Investors may be required to make a payment to cover the decrease plus the First Interest Amount, Capital Protection Fees and Borrowing Fees payable on the Reset Date or risk some or all of the ABN AMRO IZY Rolling Instalments terminating;

- (e) repayment of the Loan will be secured by a mortgage over the Underlying Parcel. Legal title to the Underlying Parcel will be held by the Security Trustee on trust for the Investor. Each trust and each Underlying Parcel to which it relates will be kept as a separate trust and there will be no pooling of interests or property to which the trust relates;
- (f) the Loan is made on a limited recourse basis. Under the Trust Deed ABN AMRO's ability to recover the Loan Amount from the Investor is limited to the amount received by ABN AMRO either:
 - (i) if the Holder's Put Option is exercised by the Investor – the amount payable to the Investor under the Holder's Put Option; or
 - (ii) if the Holder's Put Option is not exercised by the Investor – the amount recoverable by ABN AMRO on the enforcement of its rights in respect of the mortgaged property;
- (g) interest on the Loan is payable in advance for the period from the date that the Cash Application is accepted or Reset Date, as applicable, to the Second Interest Date (First Interest Amount);
- (h) interest on the Loan is also payable in advance for the period from the Second Interest Date to the next Reset Date or Expiry Date, as applicable (Second Interest Amount);
- (i) the Borrowing Fee is an amount that may be charged by ABN AMRO on Cash Application or on a Reset Date for making the Loan;
- (j) the Capital Protection Fee is an amount charged by ABN AMRO on Cash Application or on a Reset Date for providing the Holder's Put Option;
- (k) where the ABN AMRO IZY Rolling Instalments are purchased on the ASX, the purchaser acquires the ABN AMRO IZY Rolling Instalments on the same terms and conditions under which they were originally issued. In particular, the Secondary Market Purchaser will be offered and will accept a new Loan from ABN AMRO upon the transfer of the ABN AMRO IZY Rolling Instalments from the previous owner to the Secondary Market Purchaser. The Loan provided by ABN AMRO 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 on the newly acquired Loan; and

- (l) at the Expiry Date, the Investor has the following options:
 - (i) sell the ABN AMRO IZY Rolling Instalment:
The Investor's ABN AMRO IZY Rolling Instalment is sold on the ASX via a stockbroker before the close of trading on the Expiry Date;
 - (ii) make the Instalment Payment:
Investors can obtain the Underlying Parcel by making the Instalment Payment. The Instalment Payment is equal to the Loan Amount.

When the Instalment Payment is made the Loan is repaid, the security interest is discharged and the Underlying Parcel is delivered to the Investor;
 - (iii) convert the ABN AMRO IZY Rolling Instalment to a new Series:
The Investor has the ability to facilitate the payment of the Instalment Payment by rolling his or her ABN AMRO IZY Rolling Instalment into a new series of ABN AMRO Instalments, if available;
 - (iv) exercise the Holder's Put Option:
ABN AMRO must purchase the Underlying Parcel for the greater of the Loan Amount or the market value of the Underlying Parcel. The proceeds are applied to repay the Loan and the security interest is released; or
 - (v) do nothing:
If the Instalment Payment is not made and the Holder's Put Option is not exercised, ABN AMRO will sell the Underlying Parcel and any proceeds after repayment of the Loan and other costs will be paid to the Investor.

The Participants

18. ABN AMRO is the Issuer of the ABN AMRO IZY Rolling Instalments. ABN AMRO is also the provider of the Loans to Investors to fund the acquisition of the Underlying Parcel.

19. ABNED Nominees Pty Limited holds the legal title to the Underlying Parcel as Security Trustee and as nominee for the Investor.

20. The Investors may be individuals, companies, trusts or superannuation funds.

Ruling

21. Subject to the assumptions listed in paragraph 22 of this Ruling:

- (a) the First Interest Amount will be deductible to an Investor under section 8-1 of the ITAA 1997 on the date of acceptance of the Cash Application or the Reset Date, as applicable;
- (b) the Second Interest Amount will be deductible to an Investor under section 8-1 of the ITAA 1997 on the Second Interest Date;
- (c) the interest prepaid by a Secondary Market Purchaser will be deductible under section 8-1 of the ITAA 1997 on the date of acquisition of the ABN AMRO IZY Rolling Instalment;
- (d) section 51AAA of the ITAA 1936 will not apply to deny an Investor a deduction for the First Interest Amount, the Second Interest Amount or the interest prepaid by a Secondary Market Purchaser;
- (e) section 82KL of the ITAA 1936 will not apply to deny deductibility of the First Interest Amount, the Second Interest Amount, or the interest prepaid by a Secondary Market Purchaser;
- (f) section 82KZMF of the ITAA 1936 will not apply to set the amount and timing of deductions for the First Interest Amount, the Second Interest Amount, or the interest prepaid by a Secondary Market Purchaser under an ABN AMRO IZY Rolling Instalment;
- (g) section 82KZM of the ITAA 1936 will not apply to deny immediate deductibility for the First Interest Amount, the Second Interest Amount, or the interest prepaid by a Secondary Market Purchaser under an ABN AMRO IZY Rolling Instalment where at least one of the following applies for the year of income:
 - (i) the Investor is a Simplified Tax System (STS) taxpayer; or
 - (ii) the Investor is an individual who does not incur the expenditure in carrying on a business;
- (h) section 82KZMD of the ITAA 1936 will apply to determine the amount and timing of deductions for the First Interest Amount, the Second Interest Amount, and the interest prepaid by a Secondary Market Purchaser that is deductible to an 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;

- (i) the Borrowing Fees, if any, paid on Cash Application or on a Reset Date, will be deductible under section 25-25 of the ITAA 1997 for the shorter of 5 years or the remaining period of the Loan;
- (j) the Capital Protection Fee paid on Cash Application or on a Reset Date, forms part of the cost base of the Underlying Parcel under section 134-1 of the ITAA 1997 if the Holder's Put Option is exercised at the Expiry Date;
- (k) the Capital Protection Fee paid on Cash Application or on a Reset Date, forms part of 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 at the Expiry Date;
- (l) for Secondary Market Purchasers the cost base of the Holder's Put Option is calculated as follows:
 - (i) if the market value of the Underlying Entities' Share at the time of purchase is greater than the Instalment 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 ABN AMRO IZY Rolling Instalment plus the Instalment Payment) less the sum of the market value of the Underlying Entities' Share and the interest prepaid by a Secondary Market Purchaser; or
 - (ii) if the market value of the Underlying Entities' Share at the time of purchase is less than the Instalment Payment 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 ABN AMRO IZY Rolling Instalment plus the Instalment Payment) less the sum of the Instalment Payment and the interest prepaid by a Secondary Market Purchaser;
- (m) for Secondary Market Purchasers the amount determined under subparagraph 21(l) will be included in the cost base of the Underlying Parcel under section 134-1 of the ITAA 1997 if the Holder's Put Option is exercised at the Expiry Date;
- (n) for Secondary Market Purchasers the amount determined under subparagraph 21(l) will be included in the cost base of the Investor's Put Option under section 110-25 of the ITAA 1997 if the Holder's Put Option is not exercised at the Expiry Date;

- (o) for capital gains tax (CGT) purposes the date of acquisition of the beneficial interest in the Underlying Parcel, in the case of a Cash Applicant, is the date of acceptance of the application, or in the case of a Secondary Market Purchaser, is the contract date for transfer of the ABN AMRO IZY Rolling Instalment pursuant to section 109-5 of the ITAA 1997;
- (p) no CGT event arises when the legal title to the Underlying Parcel is transferred by the Security Trustee to the Investor on completion of the ABN AMRO IZY Rolling Instalment pursuant to subsection 104-10(7) of the ITAA 1997;
- (q) a CGT event will arise under section 104-10 of the ITAA 1997 to the Investor where the Instalment Payment is not made and the Underlying Parcel is sold by ABN AMRO exercising its power of sale under the Security Interest. If the sale proceeds are insufficient to repay the Loan, ABN AMRO has no recourse against the Investor to recover the shortfall. In these circumstances the Investor will need to reduce the cost base of the Underlying Parcel by the amount of the shortfall under subsection 110-45(3) of the ITAA 1997;
- (r) the Investors (and not the Security Trustee) are assessable under section 97 of the ITAA 1936 on all of the income derived from the Underlying Parcel while the Underlying Parcel is the subject of the separate trust; and
- (s) the anti-avoidance provisions contained in Part IVA of the ITAA 1936 will not apply to an Investor in respect of the ABN AMRO IZY Rolling Instalments.

Assumptions

22. This Ruling is made on the basis of the following assumptions:
- (a) all of the Investors are Australian residents for tax purposes;
 - (b) the Investors are not traders in investments and are not treated for taxation purposes as trading in the Underlying Parcel, carrying on a business of investing in the Underlying Parcel, or holding the Underlying Parcel as trading stock or as a revenue asset;
 - (c) in respect of any interest charges to be paid in advance, 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 an Investor in entering the arrangement is to derive assessable income from their investment in the ABN AMRO IZY Rolling Instalments;
- (e) the arrangement will be executed in the manner described in the 'Arrangement' section of this Ruling;
- (f) all dealings between the Investors and ABN AMRO will be at arm's length; and
- (g) the Underlying Parcel will not be the subject of any securities lending arrangement entered into by or on behalf of the Investor.

Explanation

Section 8-1 of the ITAA 1997

23. The interest paid on 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).

24. No part of the First Interest Amount, Second Interest Amount or the interest paid by a Secondary Market Purchaser, charged under ABN AMRO IZY Rolling Instalments is a capital protection fee. Investors 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 Investor acquired the ABN AMRO IZY Rolling Instalment by Cash Application or by purchase on the Secondary Market.

Section 51AAA of the ITAA 1936

25. By acquiring ABN AMRO IZY Rolling Instalments, it is contemplated that an Investor will derive assessable income by the receipt of dividend income and capital gains. As 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 acquiring ABN AMRO IZY Rolling Instalments.

Section 82KL of the ITAA 1936

26. The operation of section 82KL depends, among other things, on the identification of a certain quantum of 'additional benefits'. Insufficient additional benefits will be provided to trigger the application of section 82KL. Section 82KL 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

27. 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 and 328-G of the ITAA 1997 – STS taxpayer

28. 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.

29. 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

30. 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 or less, and not to the period of the Loan.

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

31. 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.

32. 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 ABN AMRO IZY Rolling Instalments including the financing, share purchase, shareholding and disposal arrangements.

33. Under the arrangement, when the Investor acquires an ABN AMRO IZY Rolling Instalment, they acquire beneficial ownership of the Underlying Parcel.

34. Exception 1, as contained in subsection 82KZME(5), applies to exclude the interest incurred on borrowings under the ABN AMRO IZY Rolling Instalment from the operation of section 82KZMF, as:

- the prepaid interest expenditure under the ABN AMRO IZY Rolling Instalment is incurred in respect of money borrowed to acquire shares that are listed for quotation on the ASX;
- the Investor can reasonably be expected to obtain dividends 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 ABN AMRO IZY Rolling Instalment are at arm's length.

Deductibility of expenditure must therefore be considered under the prepayment rules outlined in paragraphs 35 to 40.

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

35. 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.

36. 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.

37. As the eligible service periods in relation to the deductible interest for ABN AMRO IZY Rolling Instalments are not more than 12 months and do 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 incurred on the Cash Application Date, the Second Interest Date, the Reset Date or, the date that the Secondary Market Purchaser acquires the ABN AMRO IZY Rolling Instalment, as applicable.

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

38. Section 82KZMD sets the amount and timing of deductions for expenditure for an 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.

39. 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.

40. For these taxpayers, the deduction for prepaid interest on the ABN AMRO IZY Rolling Instalments will be apportioned over the relevant interest payment period.

Section 25-25 of the ITAA 1997: *Borrowing Fees*

41. The Borrowing Fee may be charged at the time of Cash Application or on a Reset Date, for making the Loan. No part of the Borrowing Fee, if charged, is a payment for the purchase of the Holder's Put Option. The Borrowing Fee is deductible over the shorter of five years or the remaining period of the Loan in accordance with section 25-25.

Capital Protection Fee

42. The Capital Protection Fee is the amount charged for the purchase of the Holder's Put Option. The payment ensures that the borrower is protected from liability to repay the principal if the market value of the Underlying Parcel falls below their original purchase price. In effect, the Holder's Put Option ensures that ABN AMRO will acquire the Underlying Parcel in full satisfaction of the Loan Amount if the Underlying Parcel has fallen in value below the amount borrowed.

43. The Capital Protection Fee is not deductible as it is incurred for a purpose other than to service or maintain the borrowed funds. The fee is capital in nature, being paid to acquire an asset, namely, the Holder's Put Option.

Sections 110-25, 112-35 and 134-1 of the ITAA 1997

Cost Base of Holder's Put Option – Capital Protection Fees paid on Cash Application and on a Reset Date

44. The Capital Protection Fee paid on Cash Application and on a Reset Date forms part of the cost base of the Underlying Parcel under section 134-1 if the Holder's Put Option is exercised at the Expiry Date.

45. The Capital Protection Fee paid on Cash Application or on a Reset Date, forms part of the cost base of the Holder's Put Option under section 110-25 if the Holder's Put Option is not exercised at the Expiry Date.

Cost Base of the Holder's Put Option – Secondary Market Purchasers

46. If the market value of the Underlying Entities' Share at the time of purchase is greater than the Instalment 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, the price of the ABN AMRO IZY Rolling Instalment plus the Instalment Payment less the sum of the market value of the Underlying Entities' Share and the interest prepaid by a Secondary Market Purchaser on the date that they acquire the ABN AMRO IZY Rolling Instalment.

47. If the market value of the Underlying Entities' Share at the time of purchase is less than the Instalment 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 ABN AMRO IZY Rolling Instalment plus the Instalment Payment less the sum of the Instalment Payment and the interest prepaid by a Secondary Market Purchaser on the date that they acquire the ABN AMRO IZY Rolling Instalment.

48. If the Holder's Put Option is exercised at the Expiry Date, the amount determined under subparagraph 21(l) is included in the cost base of the Underlying Parcel under section 134-1.

49. If the Holder's Put Option is not exercised at the Expiry Date, the amount determined under subparagraph 21(l) 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*

50. Section 109-5 applies to Investors to treat them as having acquired the Underlying Parcel at the time from which the Investor obtains the beneficial ownership of the Underlying Parcel. The acquisition time for a Cash Applicant, is the time the application was accepted, and for a Secondary Market Purchaser, is the contract date for the transfer of the ABN AMRO IZY Rolling Instalment.

Subsection 104-10(7) of the ITAA 1997: *time of disposal*

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

Section 104-10 and subsection 110-45(3) of the ITAA 1997

52. A CGT event will arise to the Investor if the Investor does not make the Instalment Payment and the Underlying Parcel is sold to ABN AMRO or a third party. If the sale proceeds are insufficient to repay the Loan, ABN AMRO has no recourse against the Investor to recover the shortfall. In this circumstance the Investor will need to reduce the cost base of the Underlying Parcel by the amount of the shortfall under subsection 110-45(3).

Section 97 of the ITAA 1936

53. The Investor is presently entitled to all of the income derived from the Underlying Parcel. Therefore, section 97 will apply to assess the Investor on the income derived from the Underlying Parcel. The Security Trustee will not be subject to tax on this income.

Part IVA of the ITAA 1936

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

Detailed contents list

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

	Paragraph
What this Product Ruling is about	1
Tax law(s)	3
Class of persons	4

Qualifications	6
Date of Effect	9
Withdrawal	11
Arrangement	12
The Participants	18
Ruling	21
Assumptions	22
Explanation	23
Section 8-1 of the ITAA 1997	23
Section 51AAA of the ITAA 1936	25
Section 82KL of the ITAA 1936	26
Subdivision H of Division 3 of Part III of the ITAA 1936	27
<i>Subdivisions 328-F and 328-G of the ITAA 1997 – STS taxpayer</i>	28
<i>The eligible service period for the purposes of Subdivision H of Division 3 of Part III of the ITAA 1936</i>	30
<i>Sections 82KZME and 82KZMF of the ITAA 1936: prepaid expenditure and ‘tax shelter’ arrangements</i>	31
<i>Section 82KZM of the ITAA 1936: prepaid expenditure incurred by STS taxpayers and individuals incurring non-business expenditure</i>	35
<i>Sections 82KZMA and 82KZMD of the ITAA 1936: prepaid non-business expenditure incurred by non-individual and non-STS taxpayers</i>	38
Section 25-25 of the ITAA 1997: <i>Borrowing Fees</i>	41
Capital Protection Fee	42
<i>Sections 110-25, 112-35 and 134-1 of the ITAA 1997</i>	44
<i>Cost Base of Holder’s Put Option – Capital Protection Fees paid on Cash Application and on a Reset Date</i>	44
<i>Cost Base of the Holder’s Put Option – Secondary Market Purchasers</i>	46
Section 109-5 of the ITAA 1997: <i>time of acquisition</i>	50
Subsection 104-10(7) of the ITAA 1997: <i>time of disposal</i>	51
Section 104-10 and subsection 110-45(3) of the ITAA 1997	52
Section 97 of the ITAA 1936	53
Part IVA of the ITAA 1936	54
Detailed contents list	55

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Related Rulings/Determinations:

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

Subject references:

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

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- ITAA 1936 82KZME
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- ITAA 1997 8-1
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Legislative references:

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 - ITAA 1936 82KZL(1)
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