



PR 2008/50 - Income tax: tax consequences of investing in ANZ Protected Equity Leveraged Solutions

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 This document has changed over time. This is a consolidated version of the ruling which was published on *21 September 2011*



Product Ruling

Income tax: tax consequences of investing in ANZ Protected Equity Leveraged Solutions

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! This publication provides you with the following level of protection:

This publication (excluding appendixes) is a public ruling for the purposes of the *Taxation Administration Act 1953*.

A public ruling is an expression of the Commissioner's opinion about the way in which a relevant provision applies, or would apply, to entities generally or to a class of entities in relation to a particular scheme or a class of schemes.

If you rely on this ruling, we must apply the law to you in the way set out in the ruling (or in a way that is more favourable for you if we are satisfied that the ruling is incorrect and disadvantages you, and we are not prevented from doing so by a time limit imposed by the law). You will be protected from having to pay any underpaid tax, penalty or interest in respect of the matters covered by this ruling if it turns out that it does not correctly state how the relevant provision applies to you.

[Note: This is a consolidated version of this document. Refer to the ATO Legal Database (<http://law.ato.gov.au>) to check its currency and to view the details of all changes.]

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. 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 scheme is carried out in accordance with the information we have been given, and have described below in the **Scheme** part of this document. If the scheme is not carried out as described, participants lose the protection of this Product Ruling.

Terms of use of this Product Ruling

This Product Ruling has been given on the basis that the entity(s) who applied for the Product 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 Product Ruling.

What this Ruling is about

1. This Ruling sets out the Commissioner's opinion on the way in which the relevant provision(s) identified in the Ruling part apply to the defined class of entities, who participate in the scheme to which this Product Ruling relates.
2. In this Product Ruling this scheme is referred to as ANZ Protected Equity Leveraged Solutions (APELS) offered by the Australia and New Zealand Banking Group Limited (ANZ), which is a financial product issued under the APELS Information Memorandum.
3. This Ruling does not address the consequences of:
 - (a) early termination of the APELS loan;
 - (b) using the APELS loan to finance the exercise price of employee options;
 - (c) using the APELS loan to finance the acquisition of trust units, or other securities which are not shares in companies listed on the Australian Securities Exchange (ASX);
 - (d) any security lending arrangements involving the Nominated Approved Security financed under APELS;
 - (e) cash settlement where the value of the Nominated Approved Security is below the Protection Level on Maturity Date; or
 - (f) roll over of the APELS loan on maturity.

Class of entities

4. The class of entities who can rely on this Product Ruling consists of those entities that are accepted to participate in the scheme specified below on or after the date this Product Ruling is published and which execute relevant Agreements mentioned in paragraph 17 of this Ruling on or before 30 June 2011. They must have a purpose of staying in the scheme until it is completed (that is being a party to the relevant agreements until their term expires), and deriving assessable income from this involvement. These entities are referred to as Investor/s.

Superannuation Industry (Supervision) Act 1993

5. This Product Ruling does not address the provisions of the *Superannuation Industry (Supervision) Act 1993* (SISA 1993). The Tax Office gives no assurance that the product is an appropriate investment for a superannuation fund. The trustees of superannuation funds are advised that no consideration has been given in this

Product ruling as to whether investment in this product may contravene the provisions of SISA 1993.

Qualifications

6. The class of entities defined in this Product Ruling may rely on it provided the scheme actually carried out is carried out in accordance with the scheme described in paragraphs 17 to 21 of this Ruling.

7. If the scheme actually carried out is materially different from the scheme that is described in this Product Ruling, then:

- this Product Ruling has no binding effect on the Commissioner because the scheme entered into is not the scheme on which the Commissioner has ruled; and
- this Product Ruling may be withdrawn or modified.

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Robert Garran Offices
National Circuit
Barton ACT 2600

or posted at: <http://www.ag.gov.au/cca>

Date of effect

9. This Product Ruling applies prospectively from 21 May 2008, the date this Ruling is published. It therefore applies to the specified class of entities that enter into the scheme from 21 May 2008 until 30 June 2011, being its period of application. This Product Ruling will continue to apply to those entities even after its period of application for schemes entered into during the period of application.

10. However, the Product Ruling only applies to the extent that:

- there is no change in the scheme or in the entity's involvement in the scheme;
- it is not later withdrawn by notice in the *Gazette*; or
- the relevant provisions are not amended.

11. If this Product Ruling is inconsistent with a later public or private ruling, the relevant class of entities may rely on either ruling which applies to them (item 1 of subsection 357-75(1) of Schedule 1 to the *Taxation Administration Act 1953* (TAA)).

12. If this Product Ruling is inconsistent with an earlier private ruling, the private ruling is taken not to have been made if, when the Product Ruling is made, the following two conditions are met:

- the income year or other period to which the rulings relate has not begun; and
- the scheme to which the rulings relate has not begun to be carried out.

If the above two conditions do not apply, the relevant class of entities may rely on either ruling which applies to them (item 3 of subsection 357-75(1) of Schedule 1 to the TAA).

Changes in the law

13. Although this Product Ruling deals with the income tax laws enacted at the time it was issued, later amendments may impact on this Product Ruling. Any such changes will take precedence over the application of this Product Ruling and, to that extent, this Product Ruling will have no effect.

14. Entities who are considering participating in the scheme are advised to confirm with their taxation adviser that changes in the law have not affected this Product Ruling since it was issued.

Note to promoters and advisers

15. Product Rulings were introduced for the purpose of providing certainty about tax consequences for entities in schemes such as this. In keeping with that intention the Tax Office suggests that promoters and advisers ensure that participants are fully informed of any legislative changes after the Product Ruling is issued.

Ruling

16. Subject to paragraph 3 of this Ruling and the assumptions in paragraph 21 of this Ruling:

- (a) The interest charge under the APELS loan reduced by an amount reasonably attributable to the cost of capital protection worked out under step 3 of the method statement in subsection 247-20(3) of the *Income Tax Assessment Act 1997* (ITAA 1997), will be deductible under section 8-1 of the ITAA 1997.

- (b) Under subsection 247-20(3) of the ITAA 1997, the amount reasonably attributable to the cost of capital protection in an income year is the amount by which the interest charge under the APELS loan exceeds:
- where interest is charged on the APELS loan from ANZ at a fixed rate for all or part of the term of the APELS loan and that fixed rate is applicable to the APELS loan for all or part of the income year, the amount of the APELS loan multiplied by the sum of the Reserve Bank of Australia's Indicator Lending Rate for Standard Variable Housing Loans and 100 basis points (the 'adjusted loan rate') at the time when the interest charge is first incurred during the term of the APELS loan, or the relevant part of the term (subsections 247-20(4) and (5)); and
 - where interest is charged on the APELS loan from ANZ at a variable rate for all or part of the term of the APELS loan and that variable rate is applicable to the APELS loan for all or part of the income year, the amount of the APELS loan multiplied by the average of the adjusted loan rates applicable during those parts of the income year when the APELS loan is at a variable rate (subsections 247-20(5) and (5A));
- (c) The amount reasonably attributable to the cost of capital protection as worked out under paragraph 16(b) of this Ruling, is treated as the cost of a notional put option (Notional Put Option) under subsection 247-20(6) of the ITAA 1997. This amount is not deductible under section 8-1 of the ITAA 1997.
- (d) Section 51AAA of the *Income Tax Assessment Act 1936* (ITAA 1936) will not apply to deny the deductibility of the interest charge allowable as a deduction under section 8-1 of the ITAA 1997.
- (e) Section 82KL of the ITAA 1936 will not apply to deny deductibility of the interest charge allowable as a deduction under section 8-1 of the ITAA 1997.
- (f) Section 82KZMF of the ITAA 1936 will not apply to set the amount and timing of deductions for prepaid interest allowable as a deduction under section 8-1 of the ITAA 1997.
- (g) Section 82KZM of the ITAA 1936 will not apply to deny the Investor immediate deductibility of any part of the interest charge allowable as a deduction under section 8-1 of the ITAA 1997, where at least one of the following applies for the year of income:

- (i) the Investor is a small business entity as defined in subsection 328-110(1) of the ITAA 1997; or
 - (ii) the Investor is an individual who does not incur the interest charge in carrying on a business.
- (h) Sections 82KZMA and 82KZMD of the ITAA 1936 will apply to set the amount and timing of deductions for the prepaid interest charge, allowable as a deduction under section 8-1 of the ITAA 1997 to an Investor (other than a small business entity for the year of income), who is a taxpayer that is not an individual and does not carry on a business.
- (i) If the Notional Put Option is exercised at the end of the term of the product, the cost of acquiring the Notional Put Option will be added to the cost base and reduced cost base of the Nominated Approved Security under section 134-1 of the ITAA 1997. Any capital gain or capital loss on exercise of the Notional Put Option will be disregarded.
- (j) If the Notional Put Option is not exercised at the end of the term of the product, capital gains tax (CGT) event C2 happens pursuant to section 104-25 of the ITAA 1997, resulting in a capital loss equal to the reduced cost base of the Notional Put Option.
- (k) For CGT purposes, the Investor's date of acquisition of their interest in the Nominated Approved Security is the Commencement Date pursuant to subsection 109-5(2) of the ITAA 1997.
- (l) The cost base and reduced cost base that an Investor has in the Nominated Approved Security will include the amount of the APELS loan used to finance the acquisition of the Nominated Approved Security, and incidental costs of acquisition and disposal pursuant to sections 110-25 and 110-55 of the ITAA 1997 respectively.
- (m) Any capital gain realised by an Investor on the sale of a Nominated Approved Security will be treated as a discount capital gain under section 115-5 of the ITAA 1997 where the Investor is an individual or a trust and the sale occurs more than 12 months after the Commencement Date.
- (n) Where the Investor repays the Loan and retains ownership of the Nominated Approved Security, the payment of the Sold Call Adjustment Amount will form part of the cost base of the Nominated Approved Security pursuant to section 110-25(6) of the ITAA 1997.
- (o) 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 Investor in respect of the APELS loan.

Scheme

17. The scheme that is the subject of this Product Ruling is described below. The scheme is incorporated within the following documents:

- (a) Application for a Product Ruling received on 20 March 2008;
- (b) Information Memorandum (IM) dated 19 October 2007 issued by ANZ, which includes the Terms and Conditions of entering into APELS; and
- (c) Additional information provided on 26 March 2008, 11 April 2008, 23 April 2008 and 1 May 2008.

Note: certain information has been provided on a commercial-in-confidence basis and will not be disclosed or released under Freedom of Information legislation.

18. The documents highlighted describe the product that an Investor may enter into. For the purposes of describing the scheme to which this Product Ruling applies, there are no other agreements, whether formal or informal, and whether or not legally enforceable, which an Investor or any associate of an Investor, will be a party to, which are a part of the scheme. The effect of these agreements are summarised as follows.

19. Unless otherwise defined, capitalised terms in this Product Ruling take their meaning as per the IM. Any use of the singular also includes the plural unless otherwise specified.

Overview

20. Following is a summary of the scheme:

- (a) APELS consists of a limited recourse loan from ANZ, used by the Investor to finance up to 100% of the purchase price of a portfolio of shares listed on the ASX.
- (b) The Investor selects from a range of shares listed on the ASX that the ANZ has approved for inclusion in APELS (Nominated Approved Security). The Investor grants a mortgage to ANZ over the Nominated Approved Security as security for the limited recourse loan (Loan). The Nominated Approved Security is held by a Nominee appointed by ANZ, on behalf of the Investor.
- (c) An Investor must complete an Application Form.

- (d) The minimum loan amount for a Nominated Approved Security is \$500,000. There is no maximum loan amount.
- (e) Investors are required to open an ANZ bank account and an ANZ sponsored CHESS account as part of the initial Application.
- (f) The Investor may elect to cap the level of capital growth in relation to a Nominated Approved Security (Cap Level). This feature allows an Investor to obtain a reduced rate of interest by agreeing to limit their entitlement to the capital growth of their Nominated Approved Security. The reduction in the interest rate will depend on the Cap Level.
- (g) If an Investor's Application Form has been accepted, the Investor may then send a Transaction Request which specifies the Nominated Approved Security they propose to acquire with the Loan, the proposed Cap Level, the proposed Protection Level (maximum 100%), the proposed maturity (maximum 5 years) and whether the Loan is at a fixed or floating rate.
- (h) Based on the requested parameters, ANZ may offer a Loan and quote a rate to the Investor.
- (i) The Loan is made on a limited recourse basis (up to the agreed level of protection) and the proceeds are used to purchase the Nominated Approved Security, which is held in the Nominee's CHESS account subject to the mortgage in accordance with the terms of APELS.
- (j) Interest on the Loan is payable annually in advance on the Commencement Date and on each anniversary of the Commencement Date.
- (k) At the Maturity Date, the Investor can elect one of three options:
 - (i) Physical Settlement:
 - Where the value of the Nominated Approved Security is less than the Protection Level, the Investor will transfer to ANZ the Nominated Approved Security for the Settlement Price less the Loan Amount Outstanding, and the principal amount outstanding of the Loan will no longer be outstanding.
 - Where the value of the Nominated Approved Security is equal to or greater than the Protection level, the Investor will authorise ANZ to sell the Nominated Approved Security and pay to the Investor the sale proceeds less Sale

Expenses, the principal amount outstanding on the Loan and the Sold Call Adjustment Amount, if any.

- (ii) Cash Settlement (Investor retains the Nominated Approved Security):
 - Where the value of the Nominated Approved Security is less than the Protection Level, the Investor pays all amounts due to ANZ in connection with the Loan and ANZ will pay a Cash Settlement Amount to the Investor, which is the difference between the Protection Level and the value of the Nominated Approved Security.
 - Where the value of the Nominated Approved Security is equal to or greater than the Protection Level, the Investor has to pay to ANZ the Sold Call Adjustment Amount, if any, together with all other amounts due to ANZ in connection with the Loan.
- (iii) Roll-over:
 - The Investor may, subject to ANZ's approval, roll-over the APELS loan on the terms specified by ANZ.

Assumptions

21. This ruling is made on the basis of the following necessary assumptions:

- (a) all of the Investors are Australian residents for taxation purposes;
- (b) The Nominated Approved Security consists solely of ordinary shares in an ASX listed company;
- (c) the Investors are not traders in investments and are not treated for taxation purposes as trading in the Nominated Approved Security, carrying on a business of investing in the Nominated Approved Security, or holding the Nominated Approved Security as trading stock or as revenue assets;
- (d) in respect of any interest charges to be paid in advance under the product, these may be prepaid only in relation to a loan interest payment period of 12 months or less and which ends on or before the last day of the income year following the expenditure year;

- (e) the dominant purpose of an Investor in entering the arrangement is to derive assessable income from their Nominated Approved Security acquired under APELS, comprising dividends and capital gains;
- (f) the arrangement will be executed in the manner described in the 'Scheme' section of this Ruling;
- (g) all dealings by the Investors and ANZ under the product will be at arms length.

Commissioner of Taxation

21 May 2008

Appendix 1 – Explanation

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

Section 8-1 and Division 247 – capital protected borrowings and deductibility of interest

22. The interest paid on a borrowing used to acquire income producing assets such as shares is generally treated as deductible under section 8-1 of the ITAA 1997 where it is expected that dividends or other assessable income would be derived from the investment (see Taxation Ruling TR 95/33). However, the ability to claim interest deductions may be subject to Division 247 of the ITAA 1997.

23. Division 247 of the ITAA 1997 limits the allowable deductions for expenditure incurred under a 'capital protected borrowing'. Broadly, a capital protected borrowing is created where an amount is borrowed under an arrangement where the borrower is protected against the fall in value of some specified shares, where that borrowing is made for the purpose of investing in those shares.

24. Division 247 of the ITAA 1997 applies to the loan under APELS, as:

- (a) the Investor uses the loan from ANZ to acquire a beneficial interest in the Nominated Approved Security comprising ASX listed shares; and
- (b) the Investor is protected against the fall in market value of the Nominated Approved Security.

25. Division 247 of the ITAA 1997 sets out a methodology for reasonably attributing the cost of capital protection incurred by a borrower under a capital protected borrowing. Division 247 ignores any amount which is not in substance for capital protection or interest in calculating the cost of capital protection, pursuant to subsection 247-20(3) of the ITAA 1997.

26. There is a cost of capital protection in an income year if the aggregate of the interest on the amount borrowed exceeds the total interest that would have been incurred for the year if the interest rate on the amount borrowed had been the adjusted loan rate (as determined when the interest rate is fixed or, if the interest rate is variable, the average of the adjusted loan rates during the variable interest rate period).

27. As there is no separate charge payable by an Investor in APELS for a put option, the cost of capital protection is only that amount worked out under subsection 247-20(3) of the ITAA 1997.

28. For an Investor in APELS, the Investor's Notional Put Option is a capital asset. As the cost of capital protection is the cost of the Investor's Notional Put Option, this expense is capital in nature. The interest charged on the loan will be deductible under section 8-1 of the ITAA 1997 only to the extent that it is not for the cost of capital protection.

Section 51AAA

29. By acquiring the Nominated Approved Security, it is contemplated that an Investor will derive assessable income by way of 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 of the ITAA 1936 has no application to an Investor who enters into APELS.

Section 82KL

30. The operation of section 82KL of the ITAA 1936 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

31. Subdivision H of Division 3 of Part III (Subdivision H) of the ITAA 1936 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 of a business, whether the Investor is a small business entity, 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 that are of a capital nature.

Subdivision 328-C of the ITAA 1997 – small business entities

32. An Investor will be a small business entity for an income year if the Investor carries on a business and either:

- (a) the Investor carried on a business in the previous income year and the Investor's aggregated turnover for the previous year was less than \$2 million; or
- (b) the Investor's aggregated turnover in the current income year is likely to be less than \$2 million.

The eligible service period for the purposes of Subdivision H

33. The interest charge on the APELS loan allowable under section 8-1 of the ITAA 1997 is, if paid in advance, in relation to a prepayment of loan interest for a period that is 12 months or less. 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, and not to the period of the APELS loan.

Sections 82KZME and 82KZMF – prepaid expenditure and ‘tax shelter’ style arrangements

34. The rules in sections 82KZME and 82KZMF of the ITAA 1936 apply, subject to the exceptions in section 82KZME, where expenditure is incurred in relation to a ‘tax shelter’ scheme for the doing of a thing that is not to be wholly done within the expenditure year.

35. For the purposes of section 82KZME of the ITAA 1936, ‘agreements’ are broadly defined to include an entire scheme of which a contract may form part. Under subsection 82KZME(4) of the ITAA 1936, the relevant agreement is all the contractual schemes and activities associated with the participation in APELS, including the financing, share acquisition and share disposal arrangements.

36. Exception 1, as contained in subsection 82KZME(5) of the ITAA 1936, applies to exclude the amount allowable for interest on borrowings under the APELS loan from the operation of section 82KZMF of the ITAA 1936, as:

- (a) the prepaid interest expenditure under the APELS loan is incurred in respect of money borrowed to acquire the Nominated Approved Security that is listed for quotation on the ASX as described in subparagraph 82KZME(5)(b)(ii) of the ITAA 1936;
- (b) the Investor can reasonably be expected to obtain dividends from the investment;
- (c) the Investor will not obtain any other kind of assessable income from the investment, except for capital gains; and
- (d) all aspects of APELS are at arm's length.

37. Deductibility of the prepaid interest must therefore be considered under the prepayment rules contained in paragraphs 38 to 43 of this Ruling.

Section 82KZM – prepaid expenditure incurred by small business entities and individuals incurring non-business expenditure

38. Section 82KZM of the ITAA 1936 operates to spread over more than one income year, a deduction for prepaid expenditure incurred by a taxpayer that is either:

- (a) a small business entity for the year of income; or
- (b) a taxpayer that is an individual and the expenditure is not incurred in carrying on a business.

39. The expenditure must not be excluded expenditure and must be incurred otherwise than in carrying on a business. Section 82KZM of the ITAA 1936 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.

40. As the eligible service period in relation to the deductible interest payment under the APELS loan 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 of the ITAA 1936 will have no application to Investors who are small business entities for the year of income, or to Investors who are individuals where 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 allowable under section 8-1 of the ITAA 1997 incurred under the APELS loan.

Section 82KZMD – prepaid non-business expenditure incurred by non-individual and non-small business entities

41. Section 82KZMD of the ITAA 1936 sets the amount and timing of deductions for expenditure for an Investor (other than a small business entity for the year of income) that is not an individual and does not incur the expenditure in carrying on a business.

42. 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.

43. For these taxpayers, the amount allowable for prepaid interest allowable as a deduction under section 8-1 of the ITAA 1997 incurred under the APELS loan will be apportioned over the relevant interest payment period.

Sections 110-25, 110-55 and 134-1 – cost base of the Investor's Notional Put Option and the Nominated Approved Security

44. The cost of capital protection forms part of the cost base and reduced cost base of the Nominated Approved Security pursuant to section 134-1 of the ITAA 1997 if the Notional Put Option is exercised.

45. The cost of capital protection forms part of the reduced cost base of the Notional Put Option under section 110-55 of the ITAA 1997 if the Notional Put Option is not exercised.

46. The Investor's cost base and reduced cost base in the Nominated Approved Security will include the amount of the APELS loan used to finance the acquisition of the Nominated Approved Security and incidental costs incurred by the Investor in acquiring and disposing of the Nominated Approved Security (this includes stamp duty and costs of transfer) under sections 110-25 and 110-55 of the ITAA 1997 respectively.

Sections 109-5 – time of acquisition

47. For CGT purposes, the Investor's date of acquisition of their interest in the Nominated Approved Security is the Commencement Date pursuant to subsection 109-5(2) of the ITAA 1997.

Sections 104-10, 104-25 and 134-1

48. Where the Closing Price on the Maturity Date is below the Protection Level and the Investor disposes of the Nominated Approved Security, there will be a CGT event A1 under section 104-10 of the ITAA 1997. The Investor will make a capital gain to the extent that the Protection Level exceeds the cost base of the Nominated Approved Security or a capital loss to the extent that the Protection Level is less than the reduced cost base of the Nominated Approved Security.

49. In this instance, the Notional Put Option will be taken to have been exercised, and its cost would be included in the cost base and reduced cost base of the Nominated Approved Security pursuant to section 134-1 of the ITAA 1997.

50. Where the Closing Price is between the Protection Level and the Cap Level (or if there is no Cap Level, the Closing Price is equal to or above the Protection Level), and the Investor disposes of the Nominated Approved Security, there will be a CGT event A1. The Investor will make a capital gain to the extent the sale proceeds exceed the cost base of the Nominated Approved Security or a capital loss to the extent that the sale proceeds are less than the reduced cost base of the Nominated Approved Security.

51. In this instance, the Notional Put Option is not exercised and it lapses, triggering CGT event C2 under section 104-25 of the ITAA 1997. The capital proceeds received on the lapsing of the Notional Put Option will be nil. The Investor will make a capital loss equal to the reduced cost base of the Notional Put Option. The reduced cost base will be equal to the cost of capital protection.

52. Where there is a Cap Level and the Closing Price is above the Cap Level, the Investor is required to pay to ANZ the Sold Call Adjustment Amount. Where the Investor repays the Loan and retains ownership of the Nominated Approved Security, the Sold Call Adjustment Amount is capital expenditure made to preserve the Investor's title to the Nominated Approved Security and will form part of the Investor's cost base in the Nominated Approved Security pursuant to subsection 110-25(6) of the ITAA 1997.

53. In this instance, the Notional Put Option is not exercised and it lapses, resulting in the same CGT consequences as per paragraph 51 of this Ruling.

Section 115-5 – discount capital gains

54. Division 115 of the ITAA 1997 allows a taxpayer a discount on capital gains in certain circumstances. In accordance with section 115-5 of the ITAA 1997, any capital gain realised by an Investor on the sale of the Nominated Approved Security will be treated as a discount capital gain where the Investor is an individual or a trust and has held the Nominated Approved Security for more than 12 months.

Part IVA

55. Provided that the arrangement ruled on is entered into and carried out as described (see the Scheme part of this Ruling), it would be accepted as an ordinary commercial transaction and Part IVA of the ITAA 1936 would not apply.

Appendix 2 – Detailed contents list

56. The following is a detailed contents list for this Ruling:

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References

Previous draft:

Not previously issued as a draft

Related Rulings/Determinations:

TR 95/33

Subject references:

- capital protected borrowings
- financial products
- interest expenses
- prepaid expenses
- product rulings
- public rulings
- taxation administration

Legislative references:

- | | |
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