


TA 2009/20 - Interest deduction generators involving promoter controlled companies

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Taxpayer Alert

TA 2009/20

FOI status: may be released

Taxpayer Alerts are intended to be an "early warning" of significant new and emerging higher risk tax planning issues or arrangements that the Australian Taxation Office has under risk assessment, or where there are recurrences of arrangements that have been previously risk assessed.

Taxpayer Alerts will provide information that is in the interests of an open tax administration to taxpayers. Taxpayer Alerts are written principally for taxpayers and their advisers and they also serve to inform tax officers of new and emerging higher risk tax planning issues. Not all potential tax planning issues that the Tax Office has under risk assessment will be the subject of a Taxpayer Alert, and some arrangements that are the subject of a Taxpayer Alert may on further examination be found not to be of concern to the Tax Office. In these latter cases the Taxpayer Alert will be withdrawn and a notification published which will be referenced to that Taxpayer Alert.

Taxpayer Alerts will give the title of the issue (which may be a scheme, arrangement or particular transaction), briefly describe the issue and will highlight the features which are of concern to the Tax Office. These issues will generally require more detailed analysis to provide the Tax Office view to taxpayers.

Taxpayers who have entered into or are contemplating entering into an arrangement similar to that described in this Taxpayer Alert can seek a formal determination of the Tax Office's position through a private ruling (noting that the Taxation Administration Act 1953 sets out circumstances where the Commissioner may decline to issue such a ruling). Such taxpayers might also contact the tax officer named in the Taxpayer Alert and/or obtain their own advice.

Where a Taxpayer Alert provides guidance that a particular arrangement is or will be ineffective and that guidance is subsequently found to be incorrect and the taxpayer had relied on that guidance, the taxpayer is protected from paying a shortfall penalty and any interest charge that would otherwise be payable under the law.

This Taxpayer Alert is issued under the authority of the Commissioner.

TITLE: Interest deduction generators involving promoter controlled companies

This Taxpayer Alert describes an arrangement which seeks to generate interest deductions for the taxpayer through refinancing a taxpayer's existing home loan and establishing purported investment loans to fund the purchase of shares in companies controlled by the promoter of the arrangement. The taxpayer claims large deductions for the interest purportedly incurred on the investment loans. The arrangement may be promoted as part of a 'mortgage management plan' said to assist taxpayers to repay their home loan sooner.

DESCRIPTION

The alert applies to arrangements with features substantially equivalent to the following:

1. A promoter approaches a taxpayer offering an investment plan involving investments in foreign companies, partly funded by re-financing of the taxpayer's existing home loan equity.

Generally, the taxpayers involved do not understand the operation of the arrangement and are guided by advice from the promoter or their associate.

2. The promoter arranges for the taxpayer to refinance their existing home loan through a third party financial institution.

Under the new loan, the taxpayer obtains two loan facilities: a home loan (Loan A) for the outstanding balance on their previous home loan; and an interest only investment loan (Loan B).

The Loan B amount is the maximum offered by the third party financial institution having regard to the equity in the taxpayer's home. Both Loan A and Loan B are secured over the taxpayer's home.

3. The taxpayer makes the principal and interest repayments on Loan A. The promoter undertakes to pay the interest on Loan B on behalf of the taxpayer.

4. The promoter arranges a purported unsecured investment loan (Loan C) for the taxpayer.

Loan C is provided on non-commercial terms by an entity controlled by the promoter, including either no recourse or recourse limited to the shares in the promoter controlled company.

The Loan C amount is well in excess of the taxpayer's borrowing capacity under normal arm's length lending criteria.

5. Funds from Loan B and Loan C are purportedly used to purchase shares in various companies controlled by the promoter.

None of these companies appear to be carrying on a business or otherwise producing assessable income.

Generally, the taxpayer does not derive any dividend income from the purported share investments and in all cases appears unlikely to do so in the future.

6. The taxpayer claims the interest incurred on Loan B and the interest purportedly incurred on Loan C as allowable deductions.

In addition, many taxpayers may also seek to obtain a PAYG withholding variation to reduce the amount of tax deducted from their salary or wages during the course of the financial year.

FEATURES WHICH CONCERN US

The Tax Office considers that arrangements of this type give rise to a number of income tax issues, including whether:

- (a) Loan C may be a sham at general law;
- (b) the taxpayer's purported purchase of shares in companies controlled by the promoter may be a sham at general law;
- (c) a deduction may be available to the taxpayer for any interest incurred on Loan B under section 8-1 of the *Income Tax Assessment Act 1997* (ITAA 1997);
- (d) a deduction may be available to the taxpayer for any interest purportedly incurred on Loan C under section 8-1 of the ITAA 1997 if Loan C is not a sham;
- (e) the arrangement may constitute a scheme to which the general anti-avoidance rules in Part IVA of the *Income Tax Assessment Act 1936* apply;
- (f) any fee, commission or other amount received by the promoter of this arrangement should be included as assessable income for the relevant income year;
- (g) any entity involved in the arrangement may be a promoter of a tax exploitation scheme for the purposes of Division 290 of Schedule 1 to the *Taxation Administration Act 1953*; and

The Tax Office is currently reviewing these arrangements.

Note 1: *Base penalties of up to 50% of the tax avoided can apply where Part IVA is applied. Base penalties of up to 75% of the tax avoided can apply where you make a false and misleading statement to the Commissioner. Reductions in base penalty will be available if the taxpayer makes a voluntary disclosure to the ATO. If you have any information about the current arrangement, phone us on 1800 060 062.*

Note 2: *Penalties of up to 5,000 penalty units for individuals, 25,000 penalty units for bodies corporate or up to twice the amount of consideration received or receivable may apply to promoters of tax exploitation schemes under Division 290 of Schedule 1 to the Taxation Administration Act 1953. The Commissioner can also apply to the Federal Court of Australia for restraining and performance injunctions against promoters where prohibited conduct has occurred, is occurring or is proposed.*

Note 3: *A registered tax agent may have their registration cancelled or suspended by the Tax Agents' Board under section 251K of the Income Tax Assessment Act 1936 if they are guilty of misconduct as a tax agent or are not considered a fit and proper person to prepare income tax returns. A person under a sentence of imprisonment for a serious taxation offence is not a fit and proper person.*

Note 4: *The Commissioner may amend an assessment at any time where he is of the opinion there has been fraud or evasion. See Law Administration Practice Statement PSLA 2008/6.*

Amendment history

Date	Comment
19 January 2024	Updated ATO tip-off hotline number

Subject References:

Deductions & expenses
Interest expenses
Schemes & shams
Scheme promoters

Legislative References:

Income Tax Assessment Act 1936
Part IVA
Section 251K

Income Tax Assessment Act 1997
Section 8-1

Taxation Administration Act 1953
Division 290 of Schedule 1

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