



Taxation Determination

Income tax: will a lender under a Land Transport Facilities borrowings agreement be denied deductions in respect of their own funding costs if they lend to the borrower at a lower rate of interest?

Preamble

This Taxation Determination is a 'public ruling' for the purposes of Part IVAAA of the *Taxation Administration Act 1953* and is legally binding on the Commissioner. Taxation Rulings TR 92/1 and TR 97/16 together explain when a Determination is a public ruling and how it is legally binding.

Date of effect

This Determination applies to years commencing both before and after its date of issue. However, this Determination 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 the Determination (see paragraphs 21 and 22 of Taxation Ruling TR 92/20).

1. The extent to which the Commissioner would allow a deduction for funding costs where lenders become eligible for a tax offset (rebate) depends on the facts of each particular case.
2. In a situation where a Land Transport Facilities (LTF) lender is in a cash positive position (inclusive of the amount of the tax offset) then deductions in respect of their own funding costs will be allowed in full: **Example 1**. It is appropriate to take into account the amount of the tax offset in these circumstances because the tax offset is a concession directly provided for in the *Income Tax Assessment Act 1997*.
3. If an LTF lender is in a cash negative position (inclusive of the amount of the tax offset) then deductions in respect of their own funding costs may be reduced: **Example 2**. In Taxation Ruling TR 95/33 we stated if an outgoing produces no assessable income, or the amount of the assessable income is less than the amount of the outgoing, then it may be necessary to examine all the circumstances surrounding expenditure to determine whether the outgoing is wholly or partly deductible.

Example 1

4. Michael borrows \$500,000 at 8% per annum to fund a loan under the Land Transport Facilities tax offset scheme. He has been promised a return of 6% per annum from the project. His cash position may be summarised as follows:

<i>Funding costs</i>	<i>\$40,000</i>
<i>LTF interest received</i>	<i>\$30,000</i>
<i>Cashflow</i>	<i>\$(10,000)</i>
<i>Add back tax offset (36% of \$30,000)</i>	<i><u>\$10,800</u></i>
<i>Cash position</i>	<i>\$800</i>

5. Michael has a cash positive position. Taxation Ruling TR 95/33 and Fletcher's case have no application. A deduction of \$40,000 in respect of funding costs is wholly deductible.

Example 2

6. James borrows \$500,000 at 10% per annum to fund a loan under the Land Transport Facilities tax offset scheme. He has been promised a return of 6.5% per annum from the project. His cash position may be summarised as follows:

<i>Funding Costs</i>	<i>\$50,000</i>
<i>LTF Interest received</i>	<i>\$32,500</i>
<i>Cashflow</i>	<i>\$(17,500)</i>
<i>Add Back tax offset (36% of \$32,500)</i>	<i><u>\$11,700</u></i>
<i>Cash position</i>	<i>\$(5,800)</i>

7. James has entered into an arrangement whereby his funding costs exceed the amount of interest and tax offset received. As per paragraph 3, it is necessary to examine all the circumstances surrounding the expenditure to determine whether it is wholly deductible to James. If there is a dual purpose for the expenditure, then it would be appropriate to apportion the claim on a reasonable basis. For instance, in this Example, the deduction might be reduced from \$50,000 to \$44,200.

Commissioner of Taxation

9 June 1999

Previous draft:

TD 98/D19

Related Rulings/Determinations:

TD 1999/31; TD 1999/32

Subject references:

financing; interest expenses; interest income; interest rates; land transport facilities tax offset; negative gearing; non recourse loans

Legislative references:

ITAA97 Pt 1-3, Div 8; ITAA97 Pt 3-44, Div 396

Case references:

Fletcher and ors v. FC of T (1991) 173 CLR 1; 66 ALJR 11; 103 ALR 97; 91 ATC 4959; (1991) 22 ATR 613

ATO references:

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