

30th Apr 2012

TD 2012/1 – investment loan interest payment arrangement

Investors,

This tax determination issued last month by the ATO has some potentially far ranging implications.

In essence it is trying to put a lid or stop on debt recycling techniques where cash inflows (typically rent) are directed into a home loan or offset which has the effect of reducing interest otherwise payable on the home loan and a line of credit (LOC) is used to repay the interest and expenses of the investment property (IP).

The intention of the ATO is to apply the Part IVA (anti-avoidance rule) on the basis there is a scheme, the tax payer has obtained a tax benefit and the dominant purpose is to enable the taxpayer to obtain a tax benefit.

To make it worse, this TD applies to years of income both before and after the issue date.

There have been a number of companies, financial planners and accountants who have pushed this method as a way to pay off their home loan sooner or to obtain a greater tax deduction than you would otherwise get.

I expect this to be challenged in court in due course but it *may come down to the prime or dominant purpose of why you are using this strategy.*

If the prime purpose is to direct rental income into an offset (that just happens to be associated to a home loan) for the purpose to build funds so you can borrow again for another investment property (or next home or other asset) and use the offset to fund the settlement, then this determination may not apply. It should not matter if a secondary benefit is obtained by way of doing this, the prime purpose is to build the offset so to fund a future settlement of another property.

It will also be interesting to see if the LOC facility used is associated to an IP rather than a PPOR, whether this determination applies.

Investors may need to seek their own professional advice on this matter.

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