IT 2220 - Income tax: leveraged lease transactions

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TAXATION RULING NO. IT 2220

INCOME TAX: LEVERAGED LEASE TRANSACTIONS

F.O.I. EMBARGO: May be released

REF
H.O. REF: 83/4911-8 DATE OF EFFECT:

B.O. REF: DATE ORIG. MEMO ISSUED: 17 December 1984

F.O.I. INDEX DETAIL

REFERENCE NO:	SUBJECT REFS:	LEGISLAT. REFS:
I 1194226	LEVERAGED LEASE TRANSACTIONS	PART IVA

PREAMBLE

Taxation Ruling No. IT 2051 sets out the minimum standards with which leveraged lease transactions must comply if they are to be accepted under the income tax law. In paragraph 4 of the preamble it is recognised that, in some leveraged lease transactions, the effect of investment allowance deductions produces a situation where aggregate losses exceed aggregate profits. Leases structured on this basis are not rejected solely on that account.

2. This office has been asked for advice on the extent to which aggregate losses may exceed profits in otherwise acceptable leases where the investment allowance deduction in respect of the leased property is retained by the lessor partnership.

RULING

3. The determination of an acceptable level of aggregate partnership losses in excess of profits over the period of the lease is not necessarily restricted to the basis of a notional adding back of the investment allowance deduction to partnership income to produce an overall tax positive position. That basis is, of course, acceptable.

4. In some cases, because of timing advantages arising from retention of investment allowance deductions by the lessor partnership, it has been shown that a reduction is warranted in lease rentals. The reduction, over the period of the lease, is greater than the actual amount of the investment allowance deductions. The direct consequence is that aggregate partnership losses are greater than profits by an amount which is in excess of the actual investment allowance. By way of simple illustration, a $1000 investment allowance deduction in year one of the lease may cause an overall reduction in lease rentals of up to $1200.

5. A leveraged lease structured on this basis is acceptable provided that it can be shown that in the same lease, assuming the investment allowance deduction had been

passed on to the lessee, the additional lease rentals that would have been necessary to provide the lessor partnership with the same after tax yield or rate of return would be sufficient to place the partnership in an overall tax positive position. A statement to this effect should be included in the first return of a lessor partnership. The statement should be in addition to and in the same format as the statement required by paragraph 3(f) at page 8 in Taxation Ruling No. IT 2051.

6. Leveraged lease transactions involving investment allowance deductions and structured on either of the bases outlined in this ruling would comply with the criteria in Taxation Ruling No. IT 2051 and would not, on that account alone, attract the operation of Part IVA of the Income Tax Assessment Act.

COMMISSIONER OF TAXATION
22 November 1985