LCR 2019/D2 - Non-concessional MIT income

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Non-concessional MIT income

Relying on this draft Ruling

This publication is a draft for public comment, and represents the Commissioner's preliminary view only on how a relevant provision could apply.

If this draft Ruling applies to you and you rely on it reasonably and in good faith, you will not have to pay any interest or penalties in respect of the matters covered, if this draft Ruling turns out to be incorrect and you underpay your tax as a result. However, you may still have to pay the correct amount of tax.

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What this draft Ruling is about

1. This draft Ruling[1] addresses Schedules 1 and 5 to the *Treasury Laws Amendment (Making Sure Foreign Investors Pay Their Fair Share of Tax in Australia and Other Measures) Act 2019* (the Act).[2] The Schedules to this Act amend various provisions of a number of other Acts[3] to improve the integrity of the income tax law for arrangements involving stapled structures, and to limit tax concessions for foreign investors in a managed investment trust (MIT). The amendments increase the MIT withholding rate on fund payments, to the extent they are attributable to non-concessional MIT income (NCMI), to 30%.

2. This Ruling covers the key aspects of NCMI, with particular focus on MIT cross staple arrangement income. It covers:

- determining when an amount derived, received or made by a MIT is attributable to NCMI
- the meaning of 'cross staple arrangement' for the purposes of determining MIT cross staple arrangement income
- the scope and application of exceptions to MIT cross staple arrangement income
- the interpretation of the terms 'facility' and 'economic infrastructure facility'
- integrity rules, particularly in respect of economic infrastructure facilities where the income is attributable to rent from land investment
- the meaning of MIT trading trust income, MIT residential housing income and MIT agricultural income, and
- transitional provisions, which allow pre-existing MIT withholding rates to apply for certain periods of time.

[1] All further references to 'this Ruling' refer to the Ruling as it will read when finalised. Note that this Ruling will not take effect until finalised.
[2] All legislative references in this Ruling are to Schedule 1 to the *Taxation Administration Act 1953* (TAA 1953) unless otherwise indicated.
[3] The *Income Tax Assessment Act 1936* (ITAA 1936), the *Income Tax Assessment Act 1997* (ITAA 1997) and the TAA 1953.

Date of effect

3. It is proposed that this Ruling will be finalised as a public ruling, effective from 1 July 2019 for those who rely on it in good faith. The Act applies to a fund payment made by a MIT in relation to an income year if:

- the fund payment is made on or after 1 July 2019, and
- the income year is the 2019–20 income year or a later income year.

Outline of the law

4. MIT withholding tax applies to fund payments made by a withholding MIT to foreign residents.[4] For recipients in an exchange of information country, the rate of MIT withholding tax is generally 15%. Under the amendments to the law pursuant to the Act, the MIT withholding tax rate becomes 30% to the extent that the fund payment is attributable to NCMI.

5. An amount will be NCMI if it is any of the following:

- MIT cross staple arrangement income
- MIT trading trust income
- MIT agricultural income, or
- MIT residential housing income.

6. Transitional rules may apply to fund payments that are attributable to existing and sufficiently committed investments. If the transitional rules apply, the concessional MIT withholding tax rate of 15% will continue to apply for the relevant transitional periods.

NCMI provisions apply only to MITs

7. The NCMI provisions apply to amounts included in the assessable income of a MIT.[5] That is, the trust must be a MIT, as defined in section 275-10 of the ITAA 1997.

8. One of the requirements for a trust to qualify as a MIT in relation to an income year is that the trust must not be a trading trust for the purposes of Division 6C of Part III of the ITAA 1936 or otherwise carry on a trading business, or control, or be able to control, directly or indirectly, the affairs or operations of another person in respect of the carrying on by that other person of a trading business within the meaning of Division 6C.[6]

9. A trading business means a business that does not consist wholly of 'eligible investment business', as defined in section 102M of the ITAA 1936.

10. The NCMI provisions do not affect the ordinary operation of Division 6C for the purpose of determining whether a trust is a MIT. Nor do they affect other legislative provisions and common law principles that would ordinarily apply to a trust and the characterisation of the income of the trust. If the trust is not a MIT because it carries on a business that is not limited to 'eligible investment business', the NCMI provisions have no application.

[4] Division 840 of the ITAA 1997. The fund payment may be received directly or indirectly from the withholding MIT.
[5] Section 12-435, paragraphs 12-437(1)(a), 12-446(1)(a), 12-448(1)(a) and 12-450(1)(a).
[6] Subsection 275-10(4) and paragraphs 275-10(3)(b) and 275-45(1)(b) of the ITAA 1997.

Investing in land within the meaning of section 102M

11. It is expected that many trust structures to which the potential application of the Act is being considered may involve investments in land. For present purposes, under section 102M of the ITAA 1936, an investment in land constitutes an 'eligible investment business' only if it is for the purpose, or primarily for the purpose, of deriving rent (primary purpose test).[7] In this regard:

- The term 'land' includes an interest in land and fixtures on land.[8]
- An investment in land is taken to include investments in certain moveable property.[9]
- The safe harbour allowance in subsection 102MB(2) of the ITAA 1936 for certain non-rental income from investments in land applies when determining whether the primary purpose test is satisfied.
- The 2% safe harbour allowance at the whole of trust level in section 102MC of the ITAA 1936 applies to effectively disregard minor breaches in determining whether a trust is carrying on a trading business.

12. Therefore, where a trust holds an interest in land, a threshold question before considering the application of the NCMI provisions is whether the trustee holds the asset for the purpose, or primarily for the purpose, of deriving rent. If this is not satisfied, the NCMI provisions have no application. The fact that the NCMI provisions may apply to amounts in the assessable income of a MIT attributable to cross staple arrangements in respect of land, residential housing or agricultural land, does not remove the requirement for the trustee to satisfy the primary purpose test in relation to such assets.

13. The purpose must be determined having regard to all the relevant facts and circumstances. In determining whether the trustee is investing in land for the purpose, or primarily for the purpose, of deriving rent, regard should be had to several factors including the following:

- the trust's investment strategy
- the length of time the interest in land is held for, and any strategy for its disposal
- the actions taken by the trustee to make the land available for leasing by prospective tenants
- the terms of the lease(s)
- any other arrangements entered into or activities undertaken by the trustee (including in relation to any development of the land, its management, and other incidental activities)
- features of the land affecting its suitability for long-term rental or its potential for profit on sale, and
- projected rental yield and capital growth.

14. No one factor is determinative and all the relevant facts and circumstances must be weighed to determine whether the primary purpose test is satisfied. Furthermore, as the test is an annual test[10], changes in facts and circumstances over time must be considered to determine whether the trustee's purpose has also changed.

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[7] Paragraph (a) of the definition of 'eligible investment business' in section 102M of the ITAA 1936.
[8] Section 102M of the ITAA 1936.
[9] Subsection 102MB(1) of the ITAA 1936.
[10] Section 102N of the ITAA 1936 refers to a trust being a trading trust 'in relation to a year of income'. Similarly, the definition of a 'managed investment trust' in section 275-10 of the ITAA 1997 applies 'in relation to an income year'.

15. Where a residential dwelling asset is used to provide affordable housing[11], the rental return on the residential dwelling asset may be below the market rate (for example, if below market rent is charged), and it may be more difficult to demonstrate that the projected rental yield for the property will significantly outweigh the projected capital growth.

16. However, this would not in itself necessarily cause the trustee to fail the primary purpose test, provided the other facts and circumstances clearly support a long-term rental purpose. An example of this is where the trustee enters into a long-term arrangement with an eligible community housing provider under which an eligible community housing provider exclusively manages the tenancy or prospective tenancy of the residential dwelling asset. Such an arrangement would be relevant in determining whether the below-market rental yield is consistent with the requisite purpose.

17. The meaning of 'rent' is discussed further in the consideration of third party rent as an exception to MIT cross staple arrangement income in paragraph 52 of this Ruling.

'Attributable to' NCMI

18. The higher rate of withholding at 30% applies to the extent a fund payment made by a withholding MIT to a non-resident is 'attributable to' NCMI.[12] Similarly, under each of the tests of NCMI, it is necessary to consider what certain amounts included in the assessable income of a MIT are 'attributable to'.[13]

19. The High Court considered the phrase 'attributable to', as used in former section 160ZK(5) of the ITAA 1936, in *Commissioner of Taxation (Cth) v Sun Alliance Investments Pty Limited (in liquidation)*[14]:

> It is the concept of causation, rather than source, with which s 160ZK(5) is concerned. In determining whether the plaintiff's loss of employment was 'attributable to' the provisions of the *Local Government Act 1972* (UK), Donaldson J in *Walsh v. Rother District Council* said:
>
> > '[T]hese are plain English words involving some causal connection between the loss of employment and that to which the loss is said to be attributable. However, this connection need not be that of a sole, dominant, direct or proximate cause and effect. A contributory causal connection is quite sufficient.'
>
> Nothing, either in the text of s 160ZK(5) or in its objects as expressed in the Explanatory Memorandum on the Bill for the Amending Act, indicates that a narrower meaning should be presently ascribed to that phrase.

20. Consistent with judicial consideration of the phrase 'attributable to' in other contexts, its use in the NCMI provisions should also be interpreted broadly. A broad interpretation is supported by both the text of the provisions[15] and the Revised Explanatory Memorandum to the Treasury Laws Amendment (Making Sure Foreign Investors Pay Their Fair Share of Tax in Australia and Other Measures) Bill 2019 (Explanatory Memorandum).[16]

21. For example, in relation to MIT residential housing income, where a MIT receives a distribution from another trust holding residential housing, some or all of that distribution

[11] **Note:** An amount included in the assessable income of a MIT is 'MIT residential housing income' and therefore NCMI to the extent it is attributable to a residential dwelling asset. However, an amount is not MIT residential housing income to the extent it is referable to the use of the residential dwelling asset to provide affordable housing. Refer to paragraph 312 of this Ruling.

[12] Subparagraph 12-385(3)(a)(iii).

[13] Refer to sections 12-437, 12-446 12-448 and 12-450.

[14] [2005] HCA 70 at [80].

[15] For example, subsection 12-450(2) expressly states that the MIT does not need to hold the residential dwelling asset itself.

[16] For example, refer to paragraphs 1.235 to 1.237 of the Explanatory Memorandum, including an example in which income from a synthetic exposure to residential dwelling assets is MIT residential housing income.

may be attributable to a residential dwelling asset. This will be the case even if the MIT only has an indirect, non-controlling interest in the trust (for example, through one or more sub-trusts). What is relevant to the question of attribution is that, in this example, the residential housing has that causal nexus to the distribution.

22. Attribution is necessarily a matter of reasonable judgment. However, it is observed that the Act does not permit streaming of NCMI and income that is not NCMI between beneficiaries.

The allocation of expenses to income that is, or is attributable to, NCMI

23. As a general rule, the Commissioner expects general trust expenses to be allocated to income that is, or is attributable to, NCMI on a fair and reasonable basis.[17] Expenses that are directly incurred in relation to the derivation of NCMI may be applied against NCMI. However, where expenditure is incurred that relates partially to the derivation of NCMI, or cannot be identified as exclusively relating to the derivation of NCMI, the Commissioner expects that such expenditure will be apportioned between amounts relevantly NCMI and other income on a fair and reasonable basis. References to NCMI in this context include income that would ultimately give rise to NCMI.[18]

24. If the relevant entity is an attribution managed investment trust (AMIT), Subdivision 276-E of the ITAA 1997 will apply to prescribe a methodology for the allocation of expenses across components of trust income. Law Companion Ruling LCR 2015/8 *Attribution Managed Investment Trusts: the rules for working out trust components – allocation of deductions* provides further guidance in relation to the application of Subdivision 276-E of the ITAA 1997.

MIT cross staple arrangement income

25. Broadly speaking, a MIT will have an amount of MIT cross staple arrangement income if the amount it derives, receives or makes is from, or is attributable to, a cross staple arrangement between an operating entity and an asset entity.[19]

Cross staple arrangement

26. An asset entity is a trust or partnership that only derives income from eligible investment business within the meaning of Division 6C of Part III of the ITAA 1936.[20] Broadly, eligible investment business is limited to investments of a passive nature such as investing in land for the purpose of deriving rent or investing in shares or financial instruments.

27. Broadly, any entity that is not an asset entity is an operating entity.[21] Accordingly, any entity that derives income from a trading business within the meaning of Division 6C of Part III of the ITAA 1936 is an operating entity.

28. A cross staple arrangement is an arrangement that is entered into by two or more entities (arrangement entities) where:

- at least one of the entities is an asset entity

[17] It is noted that the High Court in *Ronpibon Tin NL v Commissioner of Taxation (Cth)* [1949] HCA 15 also prescribed a 'fair and reasonable' basis for allocating expenditure (which served multiple objects indifferently), against assessable income and exempt income.
[18] For example, income of an asset entity (that is not a MIT) in relation to a cross staple arrangement that will ultimately be reflected in a fund payment.
[19] Section 12-437.
[20] Subsections 12-436(1) and (3); the definition of 'asset entity' in subsection 995-1(1) of the ITAA 1997.
[21] Subsection 12-436(2); the definition of 'operating entity' in subsection 995-1(1) of the ITAA 1997.

- at least one of the entities is an operating entity – that is, not an asset entity, and
- one or more other entities (external entities) each hold a total participation interest in each of the arrangement entities, and the sum of the total participation interests held by the external entities in the arrangement entities is 80% or more (common participation interest test).[22]

29. Each of the asset and operating entities that entered into a cross staple arrangement are termed 'stapled entities' in relation to the cross staple arrangement.[23] Whilst the external entities are relevant to determine the existence of a cross staple arrangement, they are not themselves stapled entities in relation to the cross staple arrangement.

Meaning of 'arrangement'

30. 'Arrangement' is defined in subsection 995-1(1) of the ITAA 1997 to include any arrangement, agreement, understanding, promise or undertaking, whether express or implied, and whether or not enforceable (or intended to be enforceable) by legal proceedings. Accordingly, it is not necessary for an arrangement to be written or legally binding. However, it does require a consensus between the parties.[24]

31. Notably, it is not necessary for the ownership interests of the asset entity and the operating entity to be stapled securities, in order for a cross staple arrangement to exist. Stapled securities are securities that are contractually bound together so that they cannot be bought or sold separately.

32. It follows that any arrangement between an asset entity and operating entity with sufficient common ownership can be a cross staple arrangement including, for example:

- a lease of land and/or fixtures, and
- financial arrangements (for example, a loan or total return swap). However, whilst a loan can be a cross staple arrangement, interest income is specifically excluded from the definition of MIT cross staple arrangement income.[25]

33. In most cases, the rights and obligations arising under a particular contractual agreement between the parties, such as a lease agreement, will be the relevant cross staple arrangement in relation to an amount of cross staple arrangement income. However, the relevant arrangement may extend beyond the legal form of a particular arrangement if any other arrangement or understanding (such as a guarantee) gives rise to an amount derived, received or made by the asset entity from the operating entity.

34. In identifying an arrangement for the purposes of whether a cross staple arrangement exists, regard should be had to matters such as:

- the nature of any rights and/or obligations
- any terms and conditions (including those relating to any payment or other consideration for them)
- the circumstances surrounding their creation and their proposed exercise or performance (including what can reasonably be seen as the purposes of one or more of the entities involved)

[22] Subsection 12-436(4); the definition of 'cross staple arrangement' in subsection 995-1(1) of the ITAA 1997.
[23] Subsection 12-436(8).
[24] *Commissioner of Taxation (Cth) v Lutovi Investments Pty Ltd* [1978] HCA 55, per Gibbs and Mason JJ .
[25] Paragraphs 12-405(1)(b) and 12-437(1)(c).

- whether any of the rights and obligations, or interests in the arrangement entities, can be dealt with separately or must be dealt with together
- normal commercial understandings and practices in relation to them (including whether they are regarded commercially as separate things or as a group or series that forms a whole), and
- the objects of these measures.[26]

35. Regard should be had to all of the matters referred to in paragraph 34 of this Ruling, although in a particular case, it may be that one matter is more influential than others.

Total participation interest in arrangement entities

36. Two separate rules apply in determining the total participation interests of an external entity in each arrangement entity:

- In working out the sum of total participation interests held by external entities in each arrangement entity, a particular direct or indirect participation interest held in the arrangement entity is taken into account only once (double counting rule).[27]
- Only the lowest common ownership percentage (effectively, the lowest participation interest that the external entity has in each arrangement entity) is taken into account (lowest common ownership rule).[28]

37. The double counting rule prevents the double-counting of participation interests held by different external entities, such as ultimate and intermediate holding companies, in the same underlying entity. However, it does not specify which particular participation interests should be taken into account and which ones should be disregarded, where two or more participation interests would otherwise be counted more than once.

38. The total participation interest of each external entity in the arrangement entities must be calculated in turn. The order in which each external entity calculates its total participation interest in the arrangement entities effectively dictates which particular participation interests are taken into account and which ones are disregarded under the double counting rule. This is because the double counting rule does not apply to the first external entity (test entity A) to calculate its total participation interest in the arrangement entities. An external entity (test entity B) that subsequently calculates its total participation interest in the arrangement entities must apply the double counting rule to disregard any participation interest already taken into account by test entity A.

39. The Act does not specify which rule should be applied before the other. The lowest common ownership rule only applies where an external entity holds a total participation interest in two or more arrangement entities and there is a difference in the participation interests held in at least two arrangement entities.[29] It follows that the double counting rule should apply before the lowest common ownership rule, since the double counting rule can affect an accurate determination of the *prima facie* total participation interest of the external entity in an arrangement entity. Further, that the double counting rule precedes

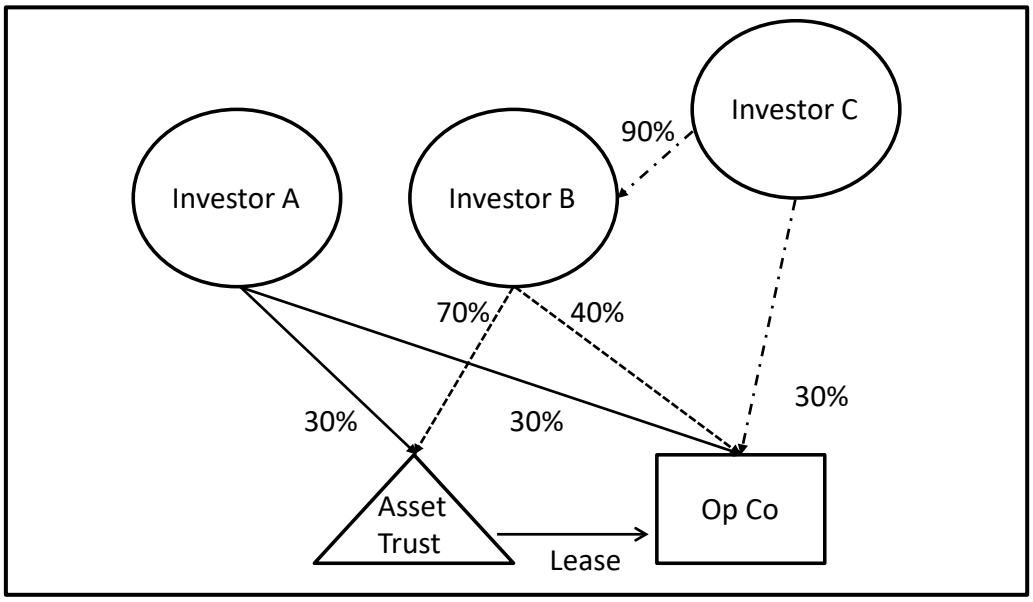
[26] See also the meaning of 'arrangement' for the purposes of Division 230 as discussed in paragraphs 14 to 21 of Taxation Ruling TR 2012/4 *Income tax: the operation of subsection 230-55(4) of the ITAA 1997 in determining what is an 'arrangement' for the purposes of the taxation of financial arrangements under Division 230 of the ITAA 1997*.
[27] Subsection 12-436(5). See also paragraph 1.45 of the Explanatory Memorandum.
[28] Subsections 12-436(6) and (7). See also paragraph 1.47 of the Explanatory Memorandum.
[29] Paragraph 12-436(6)(a).

the lowest common ownership rule in the Act is also consistent with the principle that statutory provisions should be read and applied sequentially.[30]

Example 1 – cross staple arrangement

40. *Asset Trust is an asset entity and Op Co is an operating entity. Op Co enters into a lease over land held by Asset Trust. Investor A, Investor B and Investor C are external entities as they are not parties to the lease arrangement. Assume that:*

- *Investor A holds a 30% direct interest in Asset Trust and a 30% direct interest in Op Co*
- *Investor B holds a 70% direct interest in Asset Trust and a 40% direct interest in Op Co*
- *Investor C holds a 90% direct interest in Investor B and a 30% direct interest in Op Co*



41. *Prima facie, before applying the double counting and the lowest common ownership rules:*

- *Investor A has a total participation interest of 30% in each of Asset Trust and Op Co. Neither the double counting rule nor lowest common ownership rule applies to Investor A.*
- *Investor B has a total participation interest in Asset Trust of 70% and a total participation interest in Op Co of 40%.*
- *Investor C has a total participation interest in Asset Trust of 63% (90% × 70% held via Investor B) and a total participation interest in Op Co of 66% (that is, the sum of its 30% direct interest plus 36% (90% × 40%) indirect interest via Investor B).*

42. *If Investor C calculates its total participation interest in the arrangement entities ahead of Investor B, Investor B's total participation interest in Asset Trust is reduced by 63% (that is, Investor C's indirect participation interest in Asset Trust held via Investor B) under the double counting rule. Applying the lowest common ownership rule, Investor C has a 63% total participation interest in each arrangement entity. Accordingly, Investor B would have a total participation interest in Asset Trust of 7% and, applying the lowest*

[30] Refer to *Patman v Fletcher's Fotographics Pty Ltd* (1984) 6 IR 471, at 474.

common ownership rule, Investor B will have a total participation interest in each arrangement entity of 4%.[31] *On this approach, the sum of the total participation interests held by the external entities in each arrangement entity is 97% (that is, the sum of Investor A's 30%, Investor B's 4% and Investor C's 63%). It follows that the lease entered into between Asset Trust and Op Co is a cross staple arrangement.*[32]

When an amount derived, received or made by a MIT is attributable to a cross staple payment

43. A MIT can have an amount of cross staple arrangement income, subject to certain exceptions, in one of the following scenarios:

- where the MIT is a party to the cross staple arrangement in relation to the income year and derives, receives or makes the relevant amount from an operating entity, or
- where the MIT is not a party to the cross staple arrangement in relation to the income year but an amount is included in its assessable income that is attributable to the arrangement.

44. Where the MIT is a party to the cross staple arrangement, an amount is MIT cross staple arrangement income if the relevant amount is derived, received or made by the MIT directly (for example, an amount of cross staple rent derived by the MIT from an operating entity under a lease).

45. Where the MIT is not a direct party to the cross staple arrangement, an amount will only be MIT cross staple arrangement income if it is attributable to the cross staple amount derived, received or made by the asset entity from the operating entity.

46. In practice, a MIT that is not a direct party to the cross staple arrangement will be able to identify an amount attributable to MIT cross staple arrangement income if it is notified accordingly by the entity making the payment to the MIT. The entity making the payment may be the asset entity or an entity interposed between the asset entity and the MIT (an interposed entity). Similarly, an interposed entity will be able to identify an amount attributable to MIT cross staple arrangement income if it is notified accordingly by the entity making the payment.

47. The Commissioner appreciates that MITs that are multiple distributions removed from the source of the MIT cross staple arrangement income may be at an information disadvantage when it comes to reporting the extent to which amounts are NCMI. To that end, the Commissioner expects that participants in chains of distributions will share all necessary information to enable all beneficiaries to accurately report NCMI.

48. A MIT that is a withholding MIT may also be required to notify specified details relating to fund payments (or the information must be made available) to certain recipients of such payments, including the extent (if any) to which the payment is, or is attributable to, NCMI.[33] Similar notification obligations apply to custodians and certain other entities in receipt of such payments.[34]

[31] Investor B's interest in Op Co will be 40% less Investor C's interest of 36% (90% × 40%) = 4%.
[32] Subsection 12-436(4); the definition of 'cross staple arrangement' in subsection 995-1(1) of the ITAA 1997.
[33] Paragraph 12-395(3)(ab).
[34] Paragraphs 12-395(3)(ab) and 12-395(6)(ab).

Exceptions to MIT cross staple arrangement income

49. There are five circumstances in which an amount that is attributable to a cross staple arrangement will *not* be MIT cross staple arrangement income of a MIT:

- the third party rent exception[35]
- the *de minimis* exception[36]
- the approved economic infrastructure facility exception[37]
- the capital gains exception[38], and
- the transitional rules.[39]

The third party rent exception

50. An amount included in the assessable income of a MIT that is attributable to a cross staple payment will not be MIT cross staple arrangement income to the extent it represents third party (that is, derived from an entity that is not a stapled entity) rent from land investment.

51. 'Rent from land investment' contemplates that 'rent' is derived or received, and that the rent is from investment in 'Division 6C land'.

52. The Commissioner considers that 'rent' in this context takes a traditional meaning, being payments made for periodic use of land under a lease of land.[40] Payments under a lease of land (rent) are contrasted with payments in respect of land use under an agreement which is not a lease (for present purposes, referred to as a licence).

53. The term 'Division 6C land' refers to land within the meaning of Division 6C of Part III of the ITAA 1936. This includes an investment in land contemplated under subsection 102MB(1), that is, investments in a narrow class of moveable property. Accordingly, 'rent from land investment' under the Act extends beyond the common law notion of land, to that contemplated under Division 6C.

54. It is a necessary requirement that the arrangement between the operating entity and the third party (from which the cross staple payment is sourced) can properly be characterised as a lease (or sub-lease) in order for there to be rent. In turn, only that component of the payment properly characterised as rent from land investment will qualify for the carve-out.

Payment under a lease

55. At common law[41], a lease is an interest in land, which is for a fixed or ascertainable term and confers on the grantee the right of exclusive possession over the land.[42] By contrast, a licence is a personal, contractual right of the grantee against the grantor, effectively amounting to permission to do something that it would otherwise not be permissible.

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[35] Subsection 12-437(3).
[36] Subsection 12-437(4).
[37] Subsection 12-437(5).
[38] Subsection 12-437(7).
[39] Section 12-440.
[40] *Commissioner of Stamp Duties (NSW) v JV (Crows Nest) Pty Ltd* (1986) 7 NSWLR 529; 86 ATC 4740 at 4742 and 4747; *Commissioner of Stamp Duties (NSW) v Commonwealth Funds Management Limited* (1995) 38 NSWLR 173; 95 ATC 4756 at 4762.
[41] Various state statutes may alter the common law test for what constitutes a lease in particular contexts (for example, residential tenancies). The Commissioner considers that the relevant test for the application of the third party rent rule is the common law test.
[42] *Radaich v Smith* [1959] HCA 45.

56. This distinction carries practical legal consequences, as a tenant's possession can be protected by equitable remedies against third parties such as ejectment, trespass and nuisance, whereas a licensee is limited to action personally against the licensor under contract law.[43]

57. Whether a grant of a right to use land will be characterised as a lease depends on whether, in substance (discerned objectively), the grant confers on the recipient a right of exclusive possession.[44] The terminology adopted by the parties in an instrument is a relevant consideration, but is not determinative.

58. Exclusive possession is both an entitlement to, and control by, a person over a defined area of land to the exclusion of others. As articulated in *Lewis v Bell*[45], exclusive possession means the tenant has the general right to exclude others, including the landlord, from the premises.

59. 'Possession' connotes a high degree of intentional control over the thing possessed.[46] In the context of land, the closer the tenant has to an unfettered right to use the land as their own, the more likely the arrangement will be a lease. Conversely, the more restricted the tenant's use of the land (for example, restrictions on nature of use, subleasing, assignment, access, etc) the more likely the grant does not amount to a lease.

60. The adjective 'exclusive' serves merely to emphasise its centrality to the concept of possession; that the tenant be able to exclude any person, including the landlord, from the possessed premises.[47] The grantee must be able to *'exclude any and everyone from the land for any reason or no reason.'*[48] This right encompasses the covenant of quiet enjoyment, being the landlord's obligation not to interfere with the tenant's exercise of their right to exclusive possession of the leased premises.

61. The concept of physical control, which is relevant to both aspects of exclusive possession, was considered in *Powell v McFarlane*[49], where Slade J stated:

> The question what acts constitute a sufficient degree of exclusive physical control must depend on the circumstances, in particular the nature of the land and the manner in which land of that nature is commonly used or enjoyed.
>
> …
>
> Everything must depend on the particular circumstances, but broadly, I think what must be shown as constituting factual possession is that the alleged possessor has been dealing with the land in question as an occupying owner might have been expected to deal with it and that no one else has done so.

62. As such, the physical characteristics of the area possessed and the expected intended use of the land, the substance of the rights granted and the extent of any reservations will all, to a greater or lesser extent, be relevant to whether the arrangement is characterised as a lease or a licence.

63. In determining whether exclusive possession has been conferred, the terms of the instrument must be read in the context of the nature of the premises and the use to which the premises are put.[50] No single attribute is likely to be determinative of the character of the agreement.

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[43] *Living and Leisure Australia Ltd (ACN 107 863 445) v Commissioner of State Revenue* [2018] VSCA 237. An application for special leave to appeal against this judgment was refused on 22 March 2019 [2019] HCATrans 56.
[44] *Radaich v Smith* [1959] HCA 45.
[45] (1985) 1 NSWLR 731, by the Supreme Court of NSW – Court of Appeal.
[46] *Queensland v Congoo* [2015] HCA 17 at [161], per Gageler J.
[47] In *Western Australia v Ward* [2002] HCA 28 at [503], McHugh J considered that the adjective 'exclusive' does not add to an understanding of the concept of possession, as exclusivity is central to the concept.
[48] *Western Australia v Brown* [2014] HCA 8 at [52].
[49] (1979) 38 P & CR 452.
[50] *Goldsworthy Mining Ltd v Commissioner of Taxation* [1973] HCA 7, per Mason J.

Physical characteristics

64. Certain innate physical characteristics of the land that is subject to the agreement may indicate that the land is more, or less, likely to be the subject of a lease. For example, premises that are self-contained, lockable and have physical barriers (such as walls) excluding access, more self-evidently give a tenant an ability to exercise exclusive possession than, say, if a tenant were to lease an unconfined part of a large open public space. A grant over an extremely small parcel of land, a grant where the predominant use will be of land shared with other grantees, or a grant over an area which does not readily present any effective separation of the premises that would allow a putative tenant to exercise their right to exclude others from the land, is less clearly a grant of exclusive possession.

65. This is not to say that a tenant's capacity to physically exclude is a necessary precondition for a lease. The intended use by the grantee and any particular custom will be relevant. For example, an unfenced front yard of a tenant's commercial or residential property is clearly able to be leased as part of the premises, as both the intended use and social custom would contemplate third parties having a right to access the building entry for certain purposes.

66. Where the subject land is a large, multi-faceted area, the physical characteristics of the parts of the land most critical to the intended use, and whether those parts are able to be exclusively possessed, will carry the greatest weight in determining whether there has been a grant of exclusive possession.[51]

67. Where the landlord or another third party controls the ultimate access to and from the relevant area, it is less likely that the grant will amount to exclusive possession.[52]

Example 2 – physical characteristics

68. *Storage OpTrust leases a storage warehouse from a MIT to which it is stapled, Storage HoldTrust. Storage OpTrust conducts a storage business offering lockable storage units inside the warehouse for periodic use (described as a lease) by third party customers. Subject to certain minor exceptions, customers can control access to their storage unit while it is subject to the agreement. However, Storage OpTrust controls ultimate access to the warehouse and customers can only access their storage units during nominated open hours. Storage OpTrust also controls amenities including all lighting and climate control.*

69. *The arrangement between Storage OpTrust and its customers is properly characterised as a licence. Periodic payments under the arrangements that are on-paid to Storage HoldTrust are not third party rent and are therefore not exempted from characterisation as NCMI when distributed to non-resident unitholders.*

Terms of the agreement

70. Although the nomenclature adopted will not be determinative of the character of the instrument as a lease or licence, if the instrument adopts the language of a lease, by expressly granting 'exclusive possession' or 'quiet enjoyment' to a putative tenant, this may indicate that the parties themselves intended that the grantee is a tenant under a lease. The subjective intent of the parties is relevant to the ultimate characterisation.

[51] *Living and Leisure Australia Ltd (ACN 107 863 445) v Commissioner of State Revenue* [2018] VSCA 237.
[52] *John Fuller and Sons Limited* v *Brooks* [1950] NZLR 94.

71. Certain other aspects of the agreement that may be relevant to its characterisation as a lease or otherwise include:

- the specificity (or otherwise) of the premises – a precisely defined piece of land is more amenable to a grant of a lease than an area not fixed to a precise location within a property or where the landlord can readily substitute alternatives
- the assignability (or otherwise) of the grant – an assignable grant is more likely to be a lease than a grant that is personal to the grantee and cannot be assigned, as it more closely connects the grant to the land rather than the parties
- the determinability (or otherwise) of the agreement – the easier it is for one or both parties to determine or cancel the grant, the more likely the grant is a licence, as agreed tenure is an important aspect of a lease
- the abate-ability (or otherwise) of rent payable under the grant – a lease will include a rent abatement clause, which relieves a tenant from paying rent (or makes a tenant entitled to recover rent) if there is a material impediment to the exercise of exclusive possession.

72. A tenant under a head lease may, if the lease permits, grant a sub-lease over the land which it leases from the landlord. However, a licensee of land cannot grant a sub-lease of land to a sub-tenant.[53]

Reservations from the grant

73. In most, if not all circumstances, leases and licences will contain reservations from the grant. Whether reservations from the grant have the result that the grant does not confer exclusive possession on a putative tenant will depend on the nature of those reservations in the context of the land itself and the intended usage. Specifically, regard will be had to whether the particular reservation is inconsistent with a right of exclusive possession.[54]

74. For example, it is common for a landlord to reserve for themselves a right to enter leased premises periodically (on notice) to inspect the premises. Although such a right might be said to derogate from the grant of exclusive possession, it is a function of the landlord's reversionary interest in the premises and is not so fundamentally incompatible with a right of exclusive possession that it results in the tenants not having such possession.[55] By contrast, an unfettered right for a landlord to enter without reason would be inconsistent with a grant of exclusive possession.

75. Whether such a particular reservation is ultimately inconsistent with the grant of exclusive possession will be influenced by the nature of the land and its agreed use.

76. In *Living and Leisure Ltd (ACN 107 863 445) v Commissioner of State Revenue*[56], purported leases were granted under the *Alpine Resorts Act 1983* over two Victorian ski fields which contained reservations in favour of the general public over vast sections of the subject land. The question was whether a reservation allowing freedom of public access to the land (subject to the condition that it does not unreasonably interfere with the conduct of the tenant's business) precluded the grant from being a lease. A majority of the Supreme Court of Victoria – Court of Appeal concluded that the tenant exclusively possessed the key parts of the premises relevant to the conduct of the business, such that the reservation

[53] The common law principle of *nemo dat quod non habet*.
[54] *Living and Leisure Australia Ltd (ACN 107 863 445) v Commissioner of State Revenue* [2018] VSCA 237.
[55] *Living and Leisure Australia Ltd (ACN 107 863 445) v Commissioner of State Revenue* [2018] VSCA 237 at [92], per Niall JA.
[56] [2018] VSCA 237.

from the grant in favour of the general public did not preclude a finding that the agreement conferred exclusive possession.

Example 3 – hotel operation and whether rent

77. *Hotel Trust and Hotel OpCo are stapled entities. Hotel Trust owns a building which it leases to Hotel OpCo to operate as a hotel. Hotel OpCo, in turn, grants temporary accommodation rights to third party customers to occupy one of the rooms in the hotel for payment calculated based on the number of nights of occupation. Although no other customer or guest can access the customer's room, Hotel OpCo retains the right to enter the room for a variety of purposes, including the servicing and cleaning of the room. Hotel OpCo covenants only to enter where there is a genuine need, and to minimise inconvenience to guests when entering the room.*

78. *The third party customers of Hotel OpCo do not have exclusive possession of their rooms. On that basis, they are not common law tenants and amounts paid by guests to occupy the hotel are not rent. To the extent amounts paid by Hotel OpCo to Hotel Asset Trust are attributable to receipts from guests, the amounts will be MIT cross staple arrangement income and therefore NCMI.*

Intended use

79. The purpose for which the premises are intended to be used is an influential factor in the characterisation of a grant. Specifically, courts will consider whether, objectively, a tenant would ordinarily require exclusive possession of the premises in order to properly utilise the premises in the contemplated manner.[57]

80. In *Radaich v Smith*[58], a document purporting to grant a licence over premises to operate a milk bar was found to have conferred exclusive possession. Central to the reasoning of the High Court was that, in order to effectively conduct the business of a milk bar on the premises, the tenants required exclusive possession, and that the premises in question were a 'lock-up shop' which enabled the tenant to so exclude the public.

Payment 'for' the use of the land

81. The payment under a lease will only qualify as rent to the extent it genuinely reflects a payment for the periodic use of the relevant land subject to a lease. Where a bundle of rights and benefits are conferred on a lessee of land in return for a single periodic payment, only that part of the payment that is properly referable to the third party's lease of land will be attributable to rent from land investment and avoid ultimate characterisation as NCMI.

82. The Commissioner considers that regard needs to be had to both the quantum of payment relative to the arm's length value and the method by which the purported rent is calculated. Third party receipts which are described as 'rent' but far exceed what might be the arm's length price invite questions as to whether part of the payment in fact relates to some other benefit conferred on the tenant.[59]

83. When considering the calculation methodology, while the Commissioner accepts that an incidental turnover component of a calculated periodic payment under a lease will not preclude a conclusion that the payment is rent, the more the calculation reflects something other than the arm's length value of the periodic right to use the land, the more likely some, or all, of the cross staple payment is not attributable to third party rent. For

[57] *Radaich v Smith* ([1959] HCA 45.
[58] [1959] HCA 45.
[59] See, for example, *Commissioner of Taxation v Star City Pty Limited* [2009] FCAFC 19.

example, purported rent which is a share of business profits, or is otherwise entirely exposed to the risks of the business, is unlikely to be characterised (either wholly, or in part) as rent.

84. Where the land has, or will have, assets attached to it that are central to the intended use of the land, and which:

- are properly characterised as chattels, and
- do not meet the definition of 'moveable property' in subsection 102MB(1) of the ITAA 1936

then payments under an agreement are not rent, even if so described, to the extent that they are properly referable to those assets.

85. The Commissioner also considers that payments received under an arrangement made in substitution for the payment of rent are not properly attributable to rent from third parties. For example, if the third party issued equity or other financing instrument to the landlord in satisfaction of the present and future covenant to pay rent, returns on that instrument will not be rent.

86. If the payments under the arrangements are partly rent and partly for something else (for example, a licence), a reasonable basis of apportionment of income must be applied to identify the MIT cross staple arrangement income component.

87. For example, if the relevant operating entity is deriving both licence fees and rent from third parties, and incurring expenditure referable to both, the Commissioner would regard as unreasonable a method that allocates all of the relevant operating entity's expenses to the licence fee component (thereby reducing the proportion of the ultimate amount characterised as MIT cross staple arrangement income). However, the Commissioner will generally regard as reasonable a method that reduces each revenue stream proportionately, for example, the approach set out in Example 1.6 in the Explanatory Memorandum.

The de minimis exception

88. An amount that is attributable to a cross staple arrangement will not be MIT cross staple arrangement income to the extent that the de minimis exception in section 12-438 applies.[60]

89. Whether *the de minimis* exception applies is worked out at the asset entity level. If the asset entity is not a MIT, the asset entity is treated as a MIT for the income year for the purpose of working out whether the exception applies.[61] If the exception applies where the asset entity is not a MIT, the relevant cross staple arrangement income will not be MIT cross staple arrangement income even if it is ultimately distributed to a MIT. It follows that a distribution of such income does not need to be identified as MIT cross staple arrangement income.

90. The *de minimis* exception applies to an amount of MIT cross staple arrangement income for the income year of an asset entity (in relation to a cross staple arrangement) where the MIT cross staple arrangement income of the asset entity for the previous income year does not exceed 5% of its assessable income (excluding net capital gains) for the previous income year.[62]

[60] Subsection 12-437(4).
[61] Subsection 12-438(6).
[62] Subsections 12-438(1), (3) and (4).

91. The MIT cross staple arrangement income of the asset entity for the previous income year includes any amounts derived or received from other entities, but disregards:

- the *de minimis* exception[63], and
- the approved economic infrastructure exemption.[64]

92. Other categories of NCMI that are not MIT cross staple arrangement income (that is, MIT trading trust income, MIT agricultural income or MIT residential housing income) included in the assessable income of the asset trust do not count towards the numerator in calculating the 5% *de minimis* threshold. Similarly, other cross staple payments received by the asset entity that do not otherwise give rise to MIT cross staple arrangement income[65] do not count towards the numerator in calculating the 5% *de minimis* threshold.

93. If the asset entity did not exist in the previous income year, it must work out whether the *de minimis* exception applies based on reasonable estimates of MIT cross staple arrangement income, assessable income and total assessable income for the current income year.[66]

Example 4 – de minimis exception

94. *Hold Trust is a MIT that owns all of the units in Asset Trust. Asset Trust (which is not a MIT) and Op Co are parties to a lease agreement. Accordingly, Asset Trust is an asset entity and Op Co is an operating entity in relation to a cross staple arrangement. Asset Trust did not exist in the previous income year.*

95. *In the first three months of the 2019–20 income year, Asset Trust receives $50,000 in cross staple rental income from Op Co under the lease agreement. This amount will be MIT cross staple arrangement income unless the de minimis exception applies (that is, none of the other exceptions to MIT cross staple arrangement income in section 12-437 apply).*

96. *In the first three months of the 2019–20 income year, Asset Trust has $1 million assessable income (disregarding capital gains). At the end of the first three months of the 2019–20 income year, Asset Trust makes a $1.05 million trust distribution to Hold Trust.*

97. *At the time that Asset Trust makes a trust distribution to Hold Trust:*

- *a reasonable estimate of Asset Trust's MIT cross staple arrangement income for the current income year is $200,000, and*
- *a reasonable estimate of Asset Trust's total assessable income for the current income year is $4 million.*

98. *Based on these reasonable estimates, the percentage of MIT cross staple arrangement income for Asset Trust is 5% of its total assessable income. Accordingly, the de minimis exception applies so that the $50,000 in cross staple rental income of Asset Trust is not MIT cross staple arrangement income. It follows that Asset Trust is not required to identify any amount of the trust distribution as NCMI (assuming the amount is not, or not attributable to, another class of NCMI) in its distribution statement to Hold Trust for the end of the first three months of the 2019–20 income year.*

[63] Subsection 12-438(2).
[64] Subsection 12-438(2).
[65] For example, interest income.
[66] Subsection 12-438(5).

The capital gains exception

99. An amount is not MIT cross staple arrangement income to the extent it is attributable to a capital gain made by an asset entity, where:

- an operating entity acquires an asset from the asset entity, and
- both entities are stapled entities in relation to a cross staple arrangement – that is, the asset entity and an operating entity are parties to a cross staple arrangement.[67]

100. This exception can apply regardless of which CGT event gives rise to the capital gain of the asset entity. For example, a capital gain made by an asset entity on the grant of a lease (CGT event F1) or the grant of a long-term lease (CGT event F2) can also qualify for the exception, provided all the other requirements are met.

101. If the calculation of the capital gain derives from amounts which do not reflect arm's length dealings between the operating entity and the asset entity, the Commissioner would consider whether specific provisions in the law, including the capital gains tax market value substitution, MIT non-arm's length income or general anti-avoidance provisions, would apply.

Integrity of the rules

102. The Act reflects the Government's intention to address the integrity of the Australian tax system in respect of the use of stapled structures and access to tax concessions for foreign investors.[68] The Commissioner may consider the application of the general anti-avoidance provisions of Part IVA of the ITAA 1936 to arrangements that are directed at obtaining a tax benefit from structuring around the operation of the Act. This includes, but is not limited to, schemes that, in an artificial or in a contrived manner, involve:

- the structuring of an arrangement to avoid the 80% common participation interest test
- restructure of ownership or interests in the arrangement entities to avoid the 80% common participation interest test, or
- a restructure of an existing arrangement to attract the operation of one or more of the specific exceptions covered in section 12-437.

MIT cross staple arrangement income – transitional rules

103. The transitional rules apply in relation to MIT cross staple arrangement income that is attributable to a facility that existed or is sufficiently committed to at the time of announcement of the measure.

104. The transitional rules also apply to future expansions and enhancements where assets are added to or an existing facility is otherwise improved or extended, provided the investment did not bring into existence a new, separate facility.[69]

105. Transitional rules apply in relation to MIT cross staple arrangement income that is attributable to a facility that existed or was sufficiently committed to prior to 27 March 2018. If the transitional rules apply, the general existing MIT withholding rate of 15% will apply broadly from the facility's relevant start date for a period of seven years, or 15 years if the

[67] Subsections 12-436(8), 12-437(6) and (7).
[68] Paragraph 1.15 of the Explanatory Memorandum.
[69] Paragraph 1.111 of the Explanatory Memorandum.

facility is an economic infrastructure facility. The transitional rules will apply if, *inter alia*, one of the following alternative threshold tests are met:

- where an investment is approved by an Australian government agency (first alternative threshold test)[70], or
- where there is a pre-existing or sufficiently committed investment (second alternative threshold test).[71]

106. The transitional rules may provide the following transitional benefits:

- amounts of rent from land investment[72] may be excluded from MIT cross staple arrangement income if the requirements in subsection 12-440(3) are satisfied[73], subject to the integrity rules[74], and
- an operating entity may be entitled to a deduction for an amount of rent from land investment if the requirements in section 25-120 of the ITAA 1997 are satisfied.[75]

First alternative threshold test – where an investment is approved

107. The first threshold is in subsection 12-440(1), which states:

> (1) This section applies if:
>
> (a) Before 27 March 2018, an Australian government agency:
>
> (i) decided to approve the acquisition, creation or lease of a facility; and
>
> (ii) publicly announced that decision; and
>
> (iii) took significant preparatory steps to implement that decision; and
>
> (b) either:
>
> (i) a cross staple arrangement was entered into in relation to the facility before 27 March 2018; or
>
> (ii) it was reasonable on 27 March 2018 to conclude that a cross staple arrangement will be entered into in relation to the facility; and
>
> (c) all the entities that are stapled entities in relation to the cross staple arrangement already existed before 27 March 2018; and
>
> (d) each entity that is a stapled entity in relation to the cross staple arrangement has made a choice in accordance with subsection (5).

Approval requirement

108. The first requirement comprises three elements, each of which must be satisfied in relation to an Australian government agency, dealt with in paragraphs 113 to 126 of this Ruling.

[70] Subsection 12-440(1).
[71] Subsection 12-440(2).
[72] As defined in subsection 995-1(1) of the ITAA 1997.
[73] Subsection 12-440(3). Note also paragraph 1.121 of the Explanatory Memorandum.
[74] Sections 12-441 to 12-445.
[75] Note also paragraphs 1.123 to 1.127 of the Explanatory Memorandum.

Australian government agency or authority of the Commonwealth or of a state or territory

109. An Australian government agency is defined in subsection 995-1(1) of the ITAA 1997 as:

(a) the Commonwealth, a State or a Territory; or

(b) an authority of the Commonwealth or of a State or a Territory.

110. 'Authority' is not defined but has been considered in numerous cases, whether as authority, or public authority.[76] There is no universal test for what is an 'authority'.[77] The question will be one of fact and degree.[78]

111. The Commissioner considers that in context, for a body to be an authority of a State or of the Commonwealth, the body must perform a traditional or inalienable function of government and have governmental authority for doing so.[79] The body must also be an agency or instrument of government set up to exercise control or execute a function in the public interest. It must be an instrument of government existing to achieve a government purpose.[80]

112. It follows that a local government, or any other agency established for a government purpose with the relevant authority to approve the relevant investment, would meet the requirement.

Element 1 – decided to approve the acquisition, creation or lease of a facility

113. Firstly, an Australian government agency must have decided to approve the acquisition, creation or lease of a facility. That decision to approve must be under and in accordance with a relevant power.

114. 'Approve' takes its ordinary meaning, judicially considered to be *'to confirm authoritatively; to sanction to pronounce to be good; commend'.*[81]

115. The approval must be in context, that is, the facility must be something that requires an approval or permission process resulting in a decision to approve or reject, and the approver's approval is ultimately determinative of whether the project can, or cannot, proceed.

116. A preliminary, in-principle, contingent or mere statement of approval will not be sufficient to constitute a decision to approve. The decision-making process giving rise to the decision must have concluded in all material respects. This will be a question of fact and degree to be examined in all of the circumstances. The decision must also be validly made by the decision maker.

117. An advisory body which provides advice or makes recommendations to a decision maker will not satisfy the requirement, even if that advisory body is a government department or agency and the decision maker is a Minister who customarily relies on such advice. The relevant decision in such a situation is the Minister's decision. Likewise an approval that an investment is not contrary to the national interest, or satisfies certain environmental criteria is not a relevant approval, as it will not ultimately allow the construction and eventual operation of the facility. Such an approval is merely a necessary, but not sufficient, condition in certain instances.

[76] *Western Australian Turf Club v Commissioner of Taxation (Cth)* [1978] HCA 13, per Barwick CJ. The addition of 'public' in 'public authority' does not add much, but emphases the public nature of the activity.
[77] *Commissioner of Taxation v Bank of Western Australia Ltd* [1995] FCA 1028, per Hill J.
[78] *Commissioner of Taxation v Bank of Western Australia Ltd* [1995] FCA 1028, per Hill J; *Western Australian Turf Club v Commissioner of Taxation (Cth)* [1978] HCA 13.
[79] *Renmark Hotel Inc v Commissioner of Taxation*; [1949] HCA 7; *General Steel Industries Inc v Commissioner for Railways (NSW)* [1964] HCA 69 and *Re Anti-Cancer Council (Vic); State Public Services Federation, Ex p* [1992] HCA 53.
[80] *Committee of Direction of Fruit Marketing v Australia Postal Commission ion* [1980] HCA 23, per Gibbs J.
[81] *McDonalds System of Australia Pty Ltd v McWilliams Wines Pty Ltd* [1979] FCA 142.

Acquisition, creation or lease of a facility

118. The first element of the first alternative threshold test also requires that the decision to approve be for the acquisition, creation or lease of a facility. That facility must be sufficiently identifiable at the relevant date. What relevantly constitutes the Commissioner's view on what is the *acquisition, creation or lease* of a facility is dealt with in paragraph 147 of this Ruling.

119. The Commissioner's view on what constitutes a facility is dealt with in paragraphs 152 to 203 of this Ruling, and what constitutes an economic infrastructure facility in paragraphs 204 to 225 of this Ruling.

Element 2 – publicly announced

120. The second element is that the decision to approve must be publicly announced by the Australian government agency that made the decision.[82] 'Announced' is not defined, but what will be a relevant announcement will be very much a product of the facts and circumstances.

121. In context, the requirement to publicly announce should be taken as a requirement to be made known publicly. The Commissioner expects that an announcement will follow and provide evidence of the relevant decision. An announcement of indication of policy intention or goals will not be sufficient.

122. Where the Australian government agency is under an obligation to publish the decision, for example by way of notice in the Government gazette or broadly circulated newspaper, and has in fact published the decision, the Commissioner will accept the published notice as evidence of the announcement.

Element 3 – significant preparatory steps

123. The third element[83] requires that significant preparatory steps be taken by the Australian government agency to implement the decision.

124. The term significant preparatory steps is not defined. The Commissioner considers that, having regard to the context, the phrase directs attention to objectively determinable steps that contribute, in a significant and practical way, to the relevant acquisition, creation or lease of the facility. Those steps will necessarily be preparatory or introductory in nature, however, investigatory steps or those to determine the feasibility of the proposed facility will generally be insufficient.

125. What is significant in the circumstances will be a question of fact and degree, dependent on the nature of the decision and what steps might reasonably be expected to be undertaken by the approver to implement the decision. Where only very limited further action is required from the approver to implement the decision, a material, but small step, such as publication of the decision, may be sufficiently significant. In context, where substantial further actions are required to implement the decision, publication is very unlikely to be regarded as 'significant'.

126. The Commissioner considers that steps prior to the decision to approve the acquisition, construction or lease of a facility could have the necessary character as preparatory to the implementation of the decision, but only if those steps are not more properly characterised as preparatory to the making of the decision.

[82] Subparagraph 12-440(1)(a)(ii).
[83] Subparagraph 12-440(1)(a)(iii).

A cross staple arrangement was entered into in relation to the facility

127. The second requirement of the first alternative threshold test requires a cross staple arrangement in relation to the facility.[84] The second requirement contains two alternative limbs, where either:

- a cross staple arrangement was entered into in relation to the facility before 27 March 2018[85], or
- it was reasonable on 27 March 2018 to conclude that a cross staple arrangement will be entered into in relation to the facility.[86]

128. The first alternative limb requires that a cross staple arrangement was entered into prior to 27 March 2018. This is expected to be a question of fact. It will also be a question of fact and degree as to whether any arrangement will have the necessary nexus to the facility.

129. The second alternative limb is relevant if no cross staple arrangement was entered into before 27 March 2018. An investment in relation to a facility may still satisfy the transitional rules if it was reasonable, on 27 March 2018, to conclude that a cross staple arrangement was entered into in relation to the facility.[87]

130. Whether something may reasonably be concluded is a question of an objective standard of the reasonable bystander.[88] This will require objective evidence that the cross staple arrangement structure was intended at that date. That evidence must also be contemporaneous; *ex post facto* recollections from key personnel or directors in the absence of documentary records made prior to 27 March 2018 will not be sufficient. Further, evidence that a stapled structure was suggested, contemplated, speculated about or tentatively agreed to will not be sufficient.

131. The cross staple arrangement identified by paragraph 12-440(1)(b) must be the cross staple arrangement in relation to the facility. It must be that facility for which the cross staple arrangement received the approval in relation to its acquisition, creation or lease.

132. The phrase 'in relation to' is of wide meaning and directs the reader's attention back to the object of the provision[89], indicating a connection or association (direct or indirect) between two subject matters.[90] Construing the phrase in context, although the words are of wide import, the Commissioner expects this requirement will be satisfied where it is reasonably evident that the stapled entities each have or will have an interest in the same facility, and that the operating entity will derive its interest from the asset entity.

133. The 'relationship', in context, must be sufficiently broad to accommodate yet-to-be constructed facilities. However, the facility must at least be objectively identifiable and definable at the relevant time. The arrangement will not be 'in relation to a facility' where the stapled entities' relationship with the facility is tenuous or unclear, or where the entities do not have the relationship with the facility as identified before 27 March 2018.

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[84] Paragraph 12-440(1)(b).
[85] Subparagraph 12-440(b)(i).
[86] Subparagraph 12-440(b)(ii).
[87] Subparagraph 12-440(1)(b)(ii).
[88] *Lee v R* [2007] NSWCCA 71; *Leask v Commonwealth*; [1996] HCA 29.
[89] *Pearce JJ v Commissioner of Taxation* [1988] FCA 771; see also *Hatfield, S.B. v Health Insurance Commission* [1987] FCA 462.
[90] *HP Mercantile Pty Ltd v Commissioner of Taxation* [2005] FCAFC 126, per Hill J; *Amrit, L.N v Parnell, J* [1986] FCA 89*; O'Grady v Northern Queensland Co Ltd* [1990] HCA 16, per McHugh J.

All the entities that are stapled entities in relation to the cross staple arrangement already existed before 27 March 2018

134. The third requirement of the first alternative threshold test is that each entity that is a stapled entity must exist before 27 March 2018.[91] The entities must have been properly constituted, and registered (if required), prior to 27 March 2018.

Each entity has made a choice in accordance with subsection 12-440(5)

135. The final requirement to satisfy the first alternative threshold test of the transitional rule is that each entity that is a stapled entity must make a choice in accordance with subsection 12-440(5). The choice:

- must be made by the entity in the approved form[92] and no later than 30 June 2019, or at such later time as is allowed by the Commissioner
- must be given by the entity to the Commissioner within 60 days after the entity makes the choice, and
- is irrevocable.

136. The choice must be made separately by each of the entities who are the parties to the cross staple arrangement giving rise to rent from land investment. This will generally be the operating entity which incurs the rent and the asset entity which derives the rent.[93] Thus, if the stapled entities comprise of one operating entity and one asset entity, the Commissioner must receive two separate, validly completed approved forms within 60 days after making the choice under subsection 12-440(5) before the transitional provisions can apply.[94]

137. It follows that even if the choice is made by the required time, unless the choice forms are given to the Commissioner in the required time, the transitional rules cannot apply. While the Commissioner retains the discretion to permit the late making of the choice, there is no retrospective application for any choice and taxpayers will need to be mindful of the timing of any fund payments.

Second alternative threshold test – pre-existing investments

138. The second alternative threshold test for the transitional rules to apply is where a contract or investment in relation to a facility has been entered into before 27 March 2018 in accordance with subsection 12-440(2).

139. Subsection 12-440(2) states:

> (2) this section also applies if:
>
> (a) any of the following applies:
>
> (i) an entity entered into a contract before 27 March 2018 for the acquisition, creation or lease of a facility;
>
> (ii) an entity owns, or is the lessee of, a facility at a time before 27 March 2018; and
>
> (b) either:
>
> (i) a cross staple arrangement was entered into in relation to the facility before 27 March 2018; or

[91] Paragraph 12-440(1)(c).
[92] Refer to Stapled groups – choice to apply transitional provisions on **ato.gov.au** for more information.
[93] Paragraph 1.116 of the Explanatory Memorandum.
[94] Refer paragraphs 12-440(1)(d) and (2)(d).

(ii) it was reasonable on 27 March 2018 to conclude that a cross staple arrangement will be entered into in relation to the facility; and

(c) all the entities that are stapled entities in relation to the cross staple arrangement already existed before 27 March 2018; and

(d) each entity that is a stapled entity in relation to the cross staple arrangement has made a choice in accordance with subsection (5).

Requirement for existing commitment before 27 March 2018

140. The first requirement of the second alternative threshold test of the MIT cross staple arrangement income transitional rules is satisfied if one of two alternative limbs is met.

Contract for the acquisition, creation or lease of a facility

141. The first alternative limb is that an entity must have, before 27 March 2018, entered into a contract for the acquisition, creation or lease of a facility. That entity must be one of the entities referred to in paragraphs 12-440(2)(c) and (d).

142. A contract will come into existence in accordance with the ordinary law of contract. Steps taken up to, but not including, the formation of a contract will not be sufficient.

143. The contract must be for the acquisition, creation or lease of the facility. In the context of a payment, that payment cannot be described as a consideration 'for' anything but that which is given in exchange for it.[95] A contract will be 'for' the acquisition, creation or lease of a facility when the object of the contract is one of those things, and nothing preparatory or contingent.

144. Hence, a conditional right to acquire an option or a contract for an option as, opposed to an obligation to acquire the facility will be too remote.[96] The Explanatory Memorandum sets out an example of a contract for a call option and explains that the contract is for the option, not the facility.[97]

145. A contract to acquire or lease land will not be a contract for the acquisition or lease of a facility, as land is not a facility in and of itself.[98]

146. The Explanatory Memorandum does not provide guidance of what is meant by 'acquisition, creation of lease of a facility'. However it is clear that each of these terms is taken in isolation and does not form a composite phrase.

Acquisition, creation or lease

147. For the purposes of the MIT cross staple arrangement income transitional rules, the Commissioner's views are as follows:

An entity will have entered into a contract for the:	**where:**
acquisition of the facility	the facility is in existence and the entity enters into a contract for the freehold title to the facility. This would not include a contract granting a call option over the facility[99], or for something else preparatory or contingent in relation to the facility.

[95] *Berry v Commissioner of Taxation* [1953] HCA 70, per Kitto J.
[96] *Fowler v Commissioner of Taxation* [2013] FCAFC 69.
[97] Example 1.11 of the Explanatory Memorandum.
[98] Paragraph 1.114 of the Explanatory Memorandum.
[99] Example 1.11 of the Explanatory Memorandum.

creation of the facility	the facility is identifiable in one or more contracts for the construction of that facility. The contract could not be said to be for anything preparatory or contingent to the construction. For example, where a contract is for preliminary works or the partial construction of the facility, such as preliminary earthworks, this will not be sufficient. Given the exemption ultimately relates to cross-staple rent, it is expected that the entity hold title or lease of the land upon which the facility is to be constructed in order that it be able to be the subject of a lease/sub-lease.
lease of a facility	the entity enters into a binding agreement which is properly characterised as a lease agreement. The agreement is not for an option or anything else preparatory or contingent to a lease and is properly described as a lease for the facility itself. A licence to access will not be sufficient, for example where access is permitted under statutory licence to install and maintain telecommunications facilities under the *Telecommunications Act 1997*. The lease will generally relate to an existing facility, but a present lease of a yet-to-be-constructed facility may satisfy the requirement, provided the lease is not contingent or conditional, the facility is sufficiently identifiable such that it can be said that the lease is *for* the facility and not land on which a facility will be constructed at some time in the future.

Owns or leases a facility

148. The second alternative limb of the first requirement is that an entity must own or be the lessee of a facility at a time before 27 March 2018.

Cross staple arrangements

149. The second requirement of the second alternative threshold test in paragraph 12-440(2)(b) relates to a cross staple arrangement in relation the facility. This requirement is identical in formulation to that in paragraph 12-440(1)(b), discussed in paragraphs 127 to 133 of this Ruling.

All the entities that are stapled entities in relation to the cross staple arrangement already existed before 27 March 2018

150. The third requirement in the second alternative threshold test, in paragraph 12-440(2)(c), requires that each entity that is a stapled entity in relation to the cross staple arrangement to exist before 27 March 2018. This requirement is identical in formulation to that in paragraph 12-440(1)(c), discussed in paragraph 134 of this Ruling.

Each entity has made a choice in accordance with subsection 12-440(5)

151. The final requirement to satisfy the second alternative threshold test of the transitional rules is that each entity must make a choice in accordance with subsection 12-440(5). Paragraphs 135 to 137 of this Ruling deal with this requirement.

Facility

152. The concept of 'facility' is the key aspect to the MIT cross staple arrangement income transitional rules.

153. Facility is not defined and will take its ordinary meaning coloured by its context and purpose. The Commissioner considers that given the breadth of the ordinary meaning of the word 'facility' it is necessary to consider the context of the amendments, the Act and extrinsic materials.

154. The *Macquarie Dictionary Online*[100] definition of 'facility' relevantly includes (emphasis added):

> **8. a building or complex of buildings, designed for a specific purpose,** as for the holding of sporting contests, launching of rockets, etc.

The ordinary meaning of facility indicates the word has broad and varied definitions. Facility, in certain circumstances, could include intangible and financial facilities. However, in context, one thing appears clear in that a facility must form part of the land on which the facility is built. The Commissioner considers that taxpayers should bear in mind that what might fall within the meaning of the term 'facility' will not necessarily align with the use of assets that will satisfy the eligible investment business requirements in Division 6C of the Part III to the ITAA 1936. Separate regard must be had to those requirements.

155. 'Facility' is described in the Explanatory Memorandum as a collection of assets that are connected and together perform a particular function such as, for example, an infrastructure facility or property facility.[101]

156. The ordinary meaning of the word 'facility' has been considered in a number of contexts. These cases have established broadly:

- that a facility is, at its most general, something which makes the doing or performance of something easier[102]
- physical aids come within the definition of 'facility'[103]
- that the natural meaning of facility includes the meanings 'amenity', 'opportunities' and 'programs designed for a purpose'[104]
- 'facility' can have different levels of abstraction[105], and
- the level of abstraction should support the purpose of the Act.[106]

157. In the broadest sense a facility can be almost anything other than land itself. However land[107], without more, cannot be a facility.

158. In the context of the 'facility', as defined in the *Telecommunications Act 1997*, a facility is to be distinguished from the structure upon which it is installed.[108] In *Hurstville*

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[100] Macmillan Publishers Australia, *The Macquarie Dictionary Online*, www.macquariedictionary.com.au, (*Macquarie Dictionary Online*), viewed 21 June 2019.
[101] Paragraph 1.117 of the Explanatory Memorandum.
[102] *Midland Greyhound Racing v Foley* [1973] 1 WLR 324; *Walsh v Stay and Play Australia Ltd; Ex parte Walsh* [1992] 1 Qd R 321; *AB Oxford Cold Storage Co Pty Ltd v Arnott* [2003] VSA 452.
[103] *Midland Greyhound Racing v Foley* [1973] 1 WLR 324.
[104] *Midland Greyhound Racing v Foley* [1973] 1 WLR 324; *AB Oxford Cold Storage Co Pty Ltd v Arnott* [2003] VSA 452.
[105] *Hutchinson 3G Australia Pty Ltd v Director of Housing & Anor* [2004] VSCA 99, at [39], per Morris AJA.
[106] *Hutchinson 3G Australia Pty Ltd v Director of Housing & Anor* [2004] VSCA 99, at [39], per Morris AJA.
[107] Paragraph 1.114 of the Explanatory Memorandum.
[108] *Pipe Networks Pty Ltd v Commonwealth Superannuation Corporation* [2013] FCA 608; *Hutchinson 3G Australia Pty Ltd v City of Mitcham* [2006] HCA 12; *Hutchinson 3G Australia Pty Ltd v Director of Housing & Anor* [2004] VSCA 99.

City Council v. Hutchinson 3G Australia Pty Ltd[109] Mason P, with whom Handley JA and McColl JA agreed, stated (at [67])*:*

> The definition of 'facility' can operate to its full literal extent in such situations without turning the bridge or building into part of the facility itself. Part (b) of the definition makes perfect sense if construed as being confined to any line, equipment etc or thing that is purpose built or dedicated by its inherent nature for use in or in connection with a telecommunications network or which is actually used accordingly. It is not necessary to treat an existing (non purpose-built) pole, structure or thing upon which a 'facility' is placed as the facility itself.

159. A 'facility' may be one or any number of things, including combination of assets. In this context and extrapolating from the definition, with the specific requirement that there be the acquisition, creation or lease of a facility, the Commissioner considers that there is necessarily a connection to tangible assets comprising the facility and the land on which the facility is situated.

160. A facility may also not be static. There exists the possibility that a facility might be 'expanded' or 'enhanced'.

161. The Explanatory Memorandum states that a facility is a collection of assets and sets out a number of features or characteristics to assist with interpreting the term facility. These can be seen in five categories – functional integration, separate revenue stream, legal rights, financial viability and other.[110]

Collection of assets

162. The Commissioner considers that a facility need not necessarily be a collection of assets, but that it may be a single asset which is relevantly a facility.

163. Assets comprising the facility must come together for a function or a purpose, of which the facility will make the performance easier.

164. The Commissioner also considers that the asset or assets which comprise the facility must necessarily have a connection to the land on which they are situated. Intangible or other assets and facilities will not form part of the facility unless they, for example, form part of a composite asset which is part of the facility.

165. Further, the facility does not include ancillary and peripheral assets, such as moveable property and items not characterised as fixtures.

166. Hence, investments in those items of moveable property or personal property are unlikely to affect the relevant facility, unless they themselves become fixtures. That is to say that, parts of a business will not necessarily form part of the facility. Moreover intangible assets which might form part of a business structure such as liquor or gaming licences do not form part of the facility.

167. For example, a fire truck, which is self-evidently a chattel, would not be part of a fire station facility, even if the truck was based at the station and was necessary to perform the broader function that is the reason why the station was built.

Functionally integrated

168. The Commissioner considers that the collection of assets forming the facility should be connected and coming together to form a particular function or purpose.

169. The concept of functionality has been considered by a number of cases, and in Draft Taxation Ruling 2017/D1 *Income tax: composite items and identifying the depreciating asset for the purposes of working out capital allowances* – in relation to

[109] [2003] NSWCA 179.
[110] With respect to the meaning of 'facility', paragraphs 1.117 to 1.120 of the Explanatory Memorandum.

composite assets. Composite assets are items made up of a number of components that are capable of performing a separate function. Whether a particular composite item is a depreciating asset, or whether one or more of its components are separate depreciating assets is a question of fact and degree to be determined by the circumstances of the case.[111]

170. In paragraph 6 of TR 2017/D1, the Commissioner identifies the following factors as relevant to determining whether a collection of assets is, in fact, a composite asset (albeit not determinative):

- The depreciating asset will ordinarily be an item that performs a separate identifiable function, having regard to the purpose it serves in its business context.
- The depreciating asset will often be an item that has a discrete use or operation. However, the item need not be self-contained or able to be used on a stand-alone basis.
- The greater the degree of physical or functional integration of an item with other component parts, the more likely the depreciating asset will be the larger composite item.
- When the effect of attaching an item to another item which has its own independent function is to change the function or performance of either item, it is likely that the combined asset is the depreciating asset.
- Where various components that are purchased (whether via one or multiple transactions) to function together as a system and are necessarily connected in their operation, the depreciating asset is usually the system.

171. These factors are necessarily relevant considerations in relation to the identification of a facility. However, the concept of 'facility' for present purposes and the concept of a 'composite asset' for depreciation purposes are not synonymous. Certain factual presentations may lead to a conclusion that a collection of items is a facility but is not a composite asset (or vice versa).

172. The Commissioner considers that the enquiry to identify a facility, unlike a 'composite asset', is heavily influenced by the land on which the facility is constructed and the broader functions those assets and facilities perform. While functional integration is an aid in identifying both a relevant 'facility' and a composite asset, it is those broader considerations, described in the Explanatory Memorandum (mentioned in paragraph 161 of this Ruling) that are particularly relevant in identifying a facility. The enquiry as to whether a collection of assets is a composite asset focuses more on the assets' function at a granular level.

173. A non-exhaustive list of examples of complementary 'facilities', which may not be a single facility, include:

- a storage facility integrated into a logistics or supply chain, separate to other buildings in different locations
- construction of a separate and discrete storage facility adjacent to a transport facility, and
- a road, or discrete sections of road, bridges, and tunnels having distinct identities as discrete facilities, notwithstanding that they are part of an 'integrated system' or network.

[111] See paragraph 4 of Draft Taxation Ruling TR 2017/D1. See also *Commissioner of Taxation v Tully Co-Operative Sugar Milling Association Ltd* [1983] FCA 163.

Whether the assets give rise to a separately identifiable revenue stream

174. The second consideration outlined by the Explanatory Memorandum is whether the assets give rise to a separately identifiable revenue stream.

175. The Explanatory Memorandum outlines that a revenue stream analysis will provide an indication of the level of abstraction as to whether there is relevantly more than a single facility.[112] Whether a collection of assets generates an identifiable and discrete revenue stream is a factor that, in isolation, is unlikely to be determinative.

176. The Commissioner considers that to the extent the revenue stream is a relevant consideration, the relevant revenue stream is that of the lessee operating entity. Further, how the operating entity's revenue is accounted for may provide guidance as to the revenue streams of the operating entity's business.

177. There is a level of abstraction that can be applied to the concept of a 'revenue stream'. For example:

- an airport might have numerous revenue streams, including fees for airplane parking, retail space, access to maintenance and aircraft services and landing fees.
- a stretch of tollway between toll-gantries and entrance/exit ramps. One 3km section might generate discrete revenue and incur direct expenditure, for example on maintenance, allocated against the identifiable revenue stream. It may be sufficient to function independently, notwithstanding that the tollway extends some 50km before connecting with state-owned freeway.

178. Alternatively, multiple facilities may result in a single revenue stream. An example of this might be a telecommunications network resulting in revenue from telephone contracts for the provision of communications services. A mobile telephone network may be made up of discrete facilities, for wireless and fixed line communications.

Legal rights

179. The third consideration set out by the Explanatory Memorandum is in relation to the legal rights of the parties in respect of the assets.[113] The Explanatory Memorandum provides the following list:

- the scope of any existing and proposed lease agreement
- the applicable regulatory framework, and
- any applicable licence or concession arrangements.

180. An example, albeit not determinative, is where a contract for lease of a facility with a State government includes a commitment for additional construction. The following are suggestive of a continuity and expansion of the currently identifiable facility:

- **scope** – where an existing lease of land provides for land and/or construction rights for the additional assets and facilities
- **regulatory framework** – where additional assets and facilities are of a kind, or are put to a purpose in aid of, or are similar to the function and purpose of the existing assets and facilities comprising the currently identifiable facility
- **licence or concession arrangements** – where the operation of a business is contingent upon a licence granted by a relevant Australian government agency and that licence requires the expansion of service delivery to a set standard and to a set geographical area.

[112] Paragraph 1.118 of the Explanatory Memorandum.
[113] Paragraph 1.118 of the Explanatory Memorandum.

Whether the financial viability of the assets that existed at the transition time are dependent on the expansions or the enhancements that will occur to the facility after the transition time

181. The fourth consideration set out by the Explanatory Memorandum is broadly whether the financial viability of assets and facilities existing at the transition time (being before 27 March 2018) are dependent on further expansions or enhancements. The more dependent the facility is on the expansion for financial viability, the more likely the expansion is part of the same facility.

182. Whether a facility is financially viable is a question of fact and degree. The Commissioner expects that objective and contemporaneous evidence exists (before 27 March 2018) as to the investment into the facility at the time the project receives the relevant approvals from investors and other stakeholders. This would include, but not be limited to, evidence of:

- the final investment decision
- committed funds and financing arrangements
- financial modelling
- business plans, and
- tenders.

Other considerations

183. The considerations outlined by paragraph 1.118 of the Explanatory Memorandum are not prescribed, and are neither exhaustive nor determinative. Depending on the facts and circumstances they may have little or no weight in identifying a facility, or in the enhancement or expansion to an existing facility.

184. Additional considerations could, depending on the facts and circumstances, include:

- the nature of any existing assets and/or facilities
- physical location of existing assets and facilities and degree of physical connection to any further proposed assets and/or facilities
- the time between creation of existing assets and facilities and creation of any further proposed assets and/or facilities
- changes to the business or business structure, and
- new technologies or technology mix employed.

Enhancements to existing facility

185. If a cross staple arrangement in relation to a facility satisfies the requirements for the transitional rules (that is to say, if section 12-440 applies) then there is no prohibition on merely expanding or improving that particular facility, so long as that facility remains identifiable.

186. The Explanatory Memorandum provides a number of examples which might constitute an expansion to a relevant facility for the purposes of the measure, including expansions to a toll road and a hotel.[114]

[114] Refer to Examples 1.12 and 1.14 respectively in the Explanatory Memorandum.

187. However, the transitional provisions will not apply to a facility where an expansion or improvement is made such that it constitutes a new and separate facility, or alters the existing facility so substantially that it ceases to have the identity of the relevant facility that was in existence or contemplated at the relevant time (before 27 March 2018).[115]

Example 5 – depot servicing a toll road

188. *A depot is constructed after 27 March 2018 to hold equipment and to base staff so as to operate and maintain an existing stretch of toll road. The depot itself is not physically connected to the road in any way (that is, other than a connection via an un-tolled stretch of road) and is used from time to time to store equipment and provide a temporary base for maintenance staff.*

189. *The depot is built to provide support to ensure satisfaction of obligations of Operating Entity under its licence in relation to the delivery of the services provided by the toll road. The depot does not give rise to a revenue stream, other than to support the revenue stream generated by the toll road. Asset Trust charges rent to Operating Entity pursuant to a lease calculated by reference to the total value of assets that are the subject of the cross staple arrangement (which includes the value of the depot). The depot is conveniently located for access to the toll road. The existing toll road and the depot are subject to the same regulatory regime in the sense that the depot is reasonably required for Operating Entity to meet its obligations to maintain the toll road.*

190. *Given the factors mentioned in paragraph 1.118 of the Explanatory Memorandum, the depot is considered to be a facility in and of itself and not an enhancement to the existing toll road facility for the following reasons:*

- *the depot is neither functionally, not physically integrated into a broader facility*
- *services provided from the depot maintain a facility, being the toll road*
- *the advantageous geographical location is not relevant in the context of a facility to maintain a facility, and*
- *the contractual arrangement between Asset Entity and Operating Entity is not relevant in identifying the revenue stream.*

191. *Hence, the depot is a new and separate facility to maintain a facility, not part of, or an extension of the toll road, to the extent that the toll road constitutes a facility in its own right.*

Example 6 – land held in abeyance pending new construction

192. *Asset Trust holds land on which an existing shopping centre facility is situated, which it leases to Operating Entity. Asset Trust acquires an additional parcel of land in anticipation of an expansion of the shopping centre to expand the retail space and car parking amenities. Due to regulatory approvals, including design, the construction and connection of the extension to the existing shopping centre will not occur for a number of years. The vacant land is leased to Operating Entity.*

193. *Under the lease the additional land requires a recalculation of the consideration as the rent that Asset Trust charges to Operating Entity is calculated by reference to the value*

[115] This is consistent with the Commissioner's views in TR 1994/11 *Income tax: general investment allowance - what is a unit of property?* where the Commissioner contemplates that modifications to a unit of property can in certain instances result in separate or new units of property This was the case in *Case No B 219/1983* 28 CTBR (NS) 404 where alteration to an existing unit of property was so substantial that a new unit had been created.

of assets that are the subject of the cross staple lease (which includes the value of the vacant land).

194. *The acquisition of the vacant land is not an enhancement to the existing shopping centre facility, or any facility, as it is merely vacant land. The extension and additional car parking amenities may, depending on the facts and circumstances, following completion, become part of the existing facility. However, until such time as the facility or facilities on the vacant land is completed it could not be said to be integrated into the existing facility, irrespective of whether they later, in fact, form part of the existing facility.*

Example 7 – creation of a new facility (that replaces an existing facility)

195. *Asset Trust holds a small existing factory facility for manufacturing. Operating Entity wants to leverage new opportunities by converting its manufacturing business into a retail shopping centre (retail facility) to take advantage of encroaching urbanisation.*

196. *The construction of the retail facility is a new facility which replaces part of the existing facility, whilst maintaining a number of warehouses for storage. The retail shopping centre and the factory are not linked, functionally, or in any way other than occupying the same land. Indeed, the shopping centre facility physically replaces the existing factory facility. Further, whilst there may be a single revenue stream, it could not be said to be a continuation of the revenue stream from manufacturing, as the manufacturing facility will cease to operate.*

197. *Given the above, the retail facility will be an entirely new facility.*

Example 8 – change of purpose of facility (same assets but different use)

198. *Asset Trust holds a lease to a port, and subleases it to Operating Entity. Operating Entity uses it for the purpose of operating a business for the loading and unloading of freight. The port includes storage for bulk dry commodities, a small terminal building, internal roads and access ways. Incentivised by the State government, Operating Entity reviews its business and decides to repurpose the freight port into a cruise ship port for the landing and disembarkation of passengers.*

199. *There is minimal alteration to existing structures and surfaces. Safety barriers and signage are erected in accordance with safety regulations.*

200. *As a consequence of the repurposing of the port facility:*

- *there remains a single, albeit different, revenue stream*
- *there has been no significant change to the physical composition of the port, and*
- *the purpose and function of the port remains one of transportation.*

201. *Hence, while use may have a bearing on the identification of a facility, in this case, without more, the application of the existing assets and facilities to a cruise ship port will not give rise to a new facility.*

Example 9 – integrated network not a single facility

202. *Asset Trust holds a number of land assets which include warehouses and distribution centres which it leases to Operating Entity. Operating Entity uses its rights to the land to conduct a logistics business to provide services for the delivery of goods between locations (logistics network). The logistics network includes:*

- *warehousing and distribution assets in discrete, albeit strategic, geographic locations*

- *integrated IT systems to facilitate the network's operation, and*
- *vehicles for the transport of goods.*

203. *A facility must have a relevant connection to, and include an interest in, the land on which it is situated. Despite the functional integration of the warehousing provided by the business conducted by Operating Entity, the warehouses and distribution centres will not constitute a single facility.*

Economic infrastructure facilities

204. Economic infrastructure facilities are a subset of facilities. What constitutes an 'economic infrastructure facility' is relevant to:

- the application of the approved economic infrastructure facility exception to MIT cross staple arrangement income, as determined by the Treasurer
- the application of a 15-year period to which the transitional provisions for the MIT cross staple arrangement apply, and
- in respect of both those items, integrity rules that limit the quantum of 'excepted MIT CSA income'[116], which will not be recognised as being NCMI.

205. Common to the application of the provisions in respect of each of the items in paragraph 204 of this Ruling is the requirement that there be rent from land investment.

206. Economic infrastructure facility is defined in subsection 12-439(5) as:

> (5) An **economic infrastructure facility** is a facility that is any of the following:
>
> (a) Transport infrastructure
>
> (b) Energy infrastructure
>
> (c) Communications infrastructure
>
> (d) Water infrastructure.

207. 'Infrastructure' is not defined in the Act. The *Macquarie Dictionary Online*[117] defines infrastructure as:

> *noun* **1.** the basic framework or underlying foundation (as of an organisation or a system).
>
> **2.** the roads, railways, schools, and other capital equipment which comprise such an underlying system within a country or region: **MPs had called for the government to spend its share on country roads and telecommunications infrastructure.* – AAP NEWS, 2000.
>
> **3.** the buildings or permanent installations associated with any organisation, operation, etc.

208. The Explanatory Memorandum provides some specific examples of a collection of assets which may, or may not be economic infrastructure facilities, including the following:

	Economic infrastructure facility?
Toll road networks	Yes
Ports	Yes
Mining operation	No
Water facility built for use by a single commercial business	No

[116] As defined in section 12-442.
[117] Viewed 21 June 2019.

209. It should also not be assumed that merely because an asset, or collection of assets forming part of a facility, comprise an economic infrastructure facility, that all assets and facilities forming the ultimate facility in its widest or greatest possible abstraction will constitute a single economic infrastructure facility. Regard must still be had to the factors pertinent to the identification of a 'facility' and 'economic infrastructure facility'.

210. In context, the term 'economic infrastructure facility' connotes an enduring facility that supports or enables economic activity and improves national productivity.[118] The Commissioner considers that these are key attributes and will be particularly helpful in identifying an economic infrastructure facility. The specified categories of economic infrastructure facility in subsection 12-439(5) should therefore be construed in that context.

Transport infrastructure

211. The first test for whether a facility, or an identifiable part of that facility which is a facility in its own right, is an economic infrastructure facility is whether it satisfies the term 'transport infrastructure'. 'Transport infrastructure' is not defined, and the ordinary meaning of the phrase has a generality about it.[119]

212. Some guidance may be provided in the capital allowances provisions. Subsection 40-870(1) of the ITAA 1997 defines 'transport facility' and includes a 'railway, a road, a pipe-line, a port facility or other facility for ships, or another facility that is used for (purpose of quarrying or processing rocks and minerals)'.

213. In *Queensland Rail v Commissioner of Taxation*[120]*,* Dowsett J considered that 'in rail transport' means 'in a system or means of transportation or conveyance of people or goods by rail'. Such a system must inevitably involve loading and unloading activities and maintenance activities'.

214. The Commissioner considers that transport infrastructure could be any infrastructure, which is relevantly a facility, to transport people or things from one place to another and would necessarily include fixtures for the loading and unloading of passengers and goods. It would not include infrastructure or facilities to store or hold people or things[121] for the conveyance itself (for example, the vehicles that operate on transport infrastructure).

215. It would not be sufficient that there be some transportation within a facility, for example:

- a conveyor belt within a factory
- a milk pipeline within a dairy, or
- conveyor of ore from pit to the run of mine stockpile.

Energy infrastructure

216. The second test for whether a facility, or an identifiable part of that facility which is a facility in its own right, is an economic infrastructure facility is whether it satisfies the term 'energy infrastructure'. 'Energy infrastructure' is not defined and will take its ordinary meaning in the context of a facility that is a piece of infrastructure as commonly understood.

[118] Paragraph 1.80 of the Explanatory Memorandum.
[119] *Red Hill Iron Ltd v API Management Pty Ltd* [2012] WASC 323, at [201], per Beech J.
[120] [2006] FCA 816, at [44].
[121] *Canwan Coals Pty Ltd v Commissioner of Taxation* [1974] 1 NSWLR 728.

217. Provided they are themselves a relevant facility, the Commissioner considers that the ordinary meaning of energy infrastructure could include the following:

- a bio diesel plant
- gas infrastructure, including for the transport and storage of gas, and
- electricity distribution networks and generation plants, including certain renewable energy generation and storage.

Communications infrastructure

218. The third test for whether a facility, or an identifiable part of that facility which is a facility in its own right, is an economic infrastructure facility is whether it satisfies the term 'communications infrastructure'.

219. The Commissioner considers that communications infrastructure is infrastructure which provides for communications, radio, mobile telephone, internet, etc – whether cables, transmission towers or 'low impact facilities'.

220. A facility will only be communications infrastructure where it includes the actual means of communication as a central part of the facility. For instance, a business which makes available mobile phone towers and other elevated sites for third party telecommunications operators to install their equipment will not be investing in a relevant communications facility.

Water infrastructure

221. The fourth test for whether a facility, or an identifiable part of that facility which is a facility in its own right, is an economic infrastructure facility is whether it satisfies the term 'water infrastructure'. 'Water infrastructure' is not defined.

222. Broadly, water infrastructure could be described as including assets and facilities for the extraction, storage processing and transportation of water, including water piping, dams and bores.

223. Further, water infrastructure satisfying any of the tests within the definition of economic infrastructure facility must also constitute either in whole, or part, a relevant facility, which necessarily has the relevant relationship to land (discussed in paragraphs 154 and 159 of this Ruling).

224. Where water infrastructure is installed in a location where an operator requires a licence to extract water from a particular river or lake, the intangible water licence will not form part of the water infrastructure facility despite being a necessary precondition for the function of the business.

Economic infrastructure facility examples

225. *Examples of whether or not there is an economic infrastructure facility include:*

- *An airport may be an economic infrastructure facility (as transport infrastructure). However, the ancillary or supplementary facilities, such as car parking beyond the airport itself, will not be economic infrastructure facilities either by being part of the airport, or in their own right, being complementary to the airport.*
- *A mine with a water facility, for example being a dewatering system for the removal of ground water from the mine site will not be an economic infrastructure facility.*

- *A power station may be an economic infrastructure facility (as energy infrastructure). However, administration buildings separate from the power station are not an economic infrastructure facility.*

Amount will not be MIT cross staple arrangement income

226. If either of the alternative threshold tests is satisfied, an amount derived, received or made by the MIT will not be MIT cross staple arrangement income of the MIT if it satisfies subsection 12-440(3), which states:

> (3) An amount included in the assessable income for an income year of a managed investment trust is *not* ***MIT cross staple arrangement income*** of the managed investment trust if:
>
> (a) the amount is, or is attributable to, an amount derived received or made from another entity (the ***second entity***); and
>
> (b) the amount relates to the facility; and
>
> (c) the second entity is a stapled entity in relation to the *cross staple arrangement; and
>
> (d) either:
>
> (i) if subparagraph 12-437(2)(a)(i) applies – the amount is rent from land investment paid from an *operating entity in relation to the cross staple arrangement to the managed investment trust; or
>
> (ii) if subparagraph 12-437(2)(a)(ii) applies – the amount is attributable to rent from land investment paid from an operating entity in relation to the cross staple arrangement to an asset entity in relation to the cross staple arrangement; and
>
> (e) the time when the amount was derived, received or made by the managed investment trust meets the requirements in subsection (4).

227. Hence, the amount in the assessable income of the MIT must be derived, received or made directly or indirectly from the operating entity that is a stapled entity in relation to the cross stapled arrangement. Only that proportion which is or is attributable to rent from land investment will satisfy the transitional rules[122], and only during the relevant transition period.[123]

Amount must relate to the facility

228. The second limb to the exception from MIT cross staple arrangement income in subsection 12-440(3) is that the amount of rent from land investment must relate to the facility. Where an amount is targeted at two or more objects, for example the facility and vacant land adjacent to the facility, the Commissioner expects an apportionment.

229. Critically, if there is no facility in existence, such that it has yet to be created, or an amount is in respect of vacant land, whether or not set aside for future expansions of a facility or to be used as a facility, no amount could be said to relate to the facility. Further, if land or construction is intended to expand or improve an existing facility, until such time as it is completed and integrated into the existing facility, then amounts in respect of the proportion uncompleted cannot be said to be in relation to the facility, and an apportionment of the amounts relate to the existing facility will be required.

[122] Paragraph 12-440(3)(d).
[123] Paragraph 12-440(3)(e).

230. Hence, an amount cannot relate to something that is not part of the relevant facility. This would include amounts paid in relation to:

- land which is not part of the facility, including adjacent land
- assets, including chattels which do not form part of the facility
- licences and other rights
- services provided with or within the facility, or
- a lease premium.

231. The Commissioner would expect a common sense, reasonable approach to attribution and apportionment.[124] Where an insignificant proportion of the land is not occupied by the facility as defined and payments under a lease are not properly referable to items other than the land and facility, the rent will be attributable to the facility.

Rent from land investment

232. The amount qualifying for treatment under the transitional rules must be attributable to rent from land investment. The Commissioner discusses 'rent from land investment' in the context of the third party rent exception from MIT cross staple arrangement income commencing at paragraph 51 of this Ruling.

Deduction for operating entity

233. If the transitional rules apply in relation to a cross staple arrangement, the operating entity may claim a deduction for an amount of rent from land investment derived or received by the asset entity if the requirements in section 25-120 of the ITAA 1997 are satisfied.

234. The general anti-avoidance rule in the income tax law (Part IVA of the ITAA 1936) applies only if a taxpayer has obtained a tax benefit in relation to a scheme. If a deduction is allowable to a taxpayer as a result of a choice under the income tax law, then that tax benefit is taken to be excluded in relation to the allowance of the deduction.[125] This is provided that a scheme was not entered into to give rise to statement of affairs that enabled such a choice to be made.[126]

235. Consequently, if a choice is made under subsection 12-440(5) to apply the transitional rules[127], then for the purposes of the general anti-avoidance provisions, the operating entity will not be taken to have obtained a tax benefit in relation to the deduction for the cross staple rent payment to the asset entity.[128] The exercising of a choice under the transitional provisions does not however preclude the potential application of the general anti-avoidance provisions to other identifiable tax benefits associated with the use of a stapled structure.

236. Paragraph 25-120(2)(d) of the ITAA 1997 limits the quantum of the deductions for payments that give rise to excepted MIT CSA income of the asset entity. Excepted MIT CSA income broadly covers income that would otherwise be MIT cross staple arrangement income, but for the application of either:

- the approved economic infrastructure facility exception, or

[124] *Ronpibon Tin NL v Commissioner of Taxation*; [1949] HCA 15.
[125] Refer subparagraph 177C(2)(b)(i) of the ITAA 1936, paragraph 69 of Law Administration Practice Statement PS LA 2005/24 *Application of General Anti-Avoidance Rules* and paragraph 1.125 of the Explanatory Memorandum.
[126] Subparagraph 177C(2)(b)(ii) of the ITAA 1936.
[127] And assuming the relevant requirements of section 12-440 have been satisfied.
[128] Paragraph 1.126 of the Explanatory Memorandum.

- the MIT cross staple arrangement income transitional provisions.[129]

237. Deductions that give rise to other forms of income of an asset entity are not affected by this choice.[130]

Timing requirements

238. For MIT cross staple arrangement income, the applicable transitional rule period depends on whether or not the facility is an 'economic infrastructure facility'. The time requirements of subsection 12-440(4) are:

- where the facility to which the cross staple arrangement relates is *not* an economic infrastructure facility – before 1 July 2031 and before the later of:[131]
  - 1 July 2026, and
  - the end of the period of 7 years beginning on the earliest day on which an asset being part of that facility is first put to use for the purpose of producing assessable income, or
- where the facility to which the cross staple arrangement relates is an economic infrastructure facility – before 1 July 2039, and before the later of:
  - 1 July 2034, and
  - the end of the period of 15 years beginning on the earliest day on which an asset being part of that facility is first put to use for the purpose of producing assessable income.

An asset that is part of the facility is first put to use for the purpose of producing assessable income

239. The transitional period starts when an asset which is part of the facility is first put to use for the purpose of producing assessable income.[132]

240. Whether an asset being part of the facility has been put to use for the purpose of producing assessable income will be a question of fact and degree. For an asset being part of a facility to be put to use, the facility must first be in existence.

241. Notably, use of the asset need not directly generate or produce the income, but an income producing purpose must be attributable to that asset.

What is an asset that is part of a facility?

242. 'Asset' in this context is not defined, hence it takes its ordinary meaning as informed by its context. The Commissioner considers that the relevant asset must be a tangible asset that is part of the facility, and its use is in furtherance of the facility performing the function originally intended.

243. Subparagraphs 12-440(4)(a)(ii) and (b)(ii) focus on an asset that is part of the facility. The Commissioner considers that before an asset can be part of a facility, that facility must first be completed.

[129] Section 12-442.
[130] Paragraph 1.127 of the Explanatory Memorandum.
[131] Paragraph 12-440(4)(a).
[132] Subsection 12-440(4).

Example 10 – facility forming part of an ultimate facility

244. *A facility will be conceived of in several stages, required under a contract with the relevant Australian government agency. Whilst the ultimate facility will not be completed for six years, facilities which comprise elements of the ultimate facility will be completed and the relevant operating entity is able to conduct its business from the second year. Notwithstanding that the ultimate facility is incomplete, a facility exists, which comprises one or more assets, which the relevant operating entity uses to produce assessable income. Hence, the transitional period commences on the day that the relevant operating entity uses the asset comprising that facility for the purpose of producing assessable income.*

First put to use

245. If a facility that qualifies under the MIT cross staple arrangement income transitional rules is an existing facility that is already in use and is currently producing income, the transitional rules apply to an amount that is derived, received or made before 1 July 2026, or if the facility is an economic infrastructure facility before 1 July 2034.[133]

246. If the facility that qualifies under the MIT cross staple arrangement income transitional rules is currently being constructed, or construction of the facility has not yet commenced, the transitional rules will apply to an amount that is derived, received or made after a time that an asset that is part of the facility is first put to use and starts producing assessable income and ceases in accordance with the timing requirements in subsection 12-440(4).[134]

247. Whether an asset forming part of a facility is put to use for the purpose of producing assessable income will be a question of fact and degree. 'Use' is not defined, but has been described as being of wide import.[135] The ordinary meaning of 'put to use' implies something more than just merely being available for use and suggests some activity with respect to the asset. That asset must also first exist.[136]

248. In respect of land, 'use' has regard to the purpose to which the land is put.[137] Land requires some physical use, such as '*putting' the land to use*'[138], '*making the land 'serve' some purpose*'[139] or devoting the land to a particular purpose.[140] While 'use' cannot be some notional, potential future or contemplated use, it need not be for a productive return to be present use.[141]

249. There is also an element of futurity about the expression 'used for'. In the context of earthworks on land to ultimately construct a residential development, Allsop P in *Leda Manorstead Pty Ltd v Chief Commissioner of State Revenue*[142] stated:

> The fact that the land was, at that time, at the stage of earthworks does not deny the present use of the land for commercial land development. It does not matter, in my view that the residential housing estates likely to be built in due course had not yet been completed, had not yet been taken their place in a completed residential development.

[133] Paragraph 1.130 of the Explanatory Memorandum.
[134] Paragraph 1.131 of the Explanatory Memorandum.
[135] *Newcastle City Council v Royal Newcastle Hospital* [1957] HCA 15.
[136] Paragraph 10 of Taxation Ruling IT 2658 *Income tax: use of units of industrial property for the purposes of producing assessable income*.
[137] *Commissioner of Land Tax v Christie* [1973] 2 NSWLR 526, at 533, per Bowen JA; *Educang Limited v Brisbane City Council* [2002] QSC 374, at [29], per White J.
[138] *Commissioner of Land Tax v Christie* [1973] 2 NSWLR 526; *Leda Manorstead Pty Ltd v Chief Commissioner of State Revenue* [2011] NSWCA 366, at [21] per Allsop P.
[139] *Newcastle City Council v Royal Newcastle Hospital*; [1957] HCA 15, per Kitto J and Taylor J.
[140] *Newcastle City Council v Royal Newcastle Hospital* [1957] HCA 15, per Taylor J.
[141] *Leda Manorstead Pty Ltd v Chief Commissioner of State Revenue* [2011] NSWCA 366, at [23] per Allsop P; *Minister Administering the Crown Lands Act v NSW Aboriginal Land Council* [2008] HCA 48, at [30 - 32], per Kirby J, and at [73] per Hayne J, Heydon J, Crennan J and Kiefel J.
[142] [2011] NSWCA 366.

250. While passive use of land may include rental to an operating entity, before an asset comprising part of the facility can be used, that facility must first be in existence. That asset must be used, although there need not be a present productive return. That facility need not be in its ultimate form.

For the purpose of producing assessable income

251. The phrase '*an asset that is part of a facility is first put to use for the purpose of producing assessable income'* in subsection 12-440(4), requires consideration of the purpose for which the asset is put to use. This includes an enquiry into the whole of the profit making structure. The asset used must first be part of the facility and neither the profit making structure nor the facility need be in its ultimate or final form to satisfy the test.

252. In considering whether something is used for the purpose of producing assessable income, the Commissioner accepts that is not necessary to establish a direct nexus between the use of the asset that is part of the facility and identifiable assessable income (or even a right to assessable income) attributable to that use.[143] The income producing purpose need not be the dominant purpose, nor a significant use.[144] For completeness, whether the asset is held on capital or revenue account will not preclude it from being used for the purpose of producing assessable income.

253. Hence, having regard to the facility and the business, the test will be to assess the extent to which that asset (forming part of the facility) fits into the overall business structure, organisation set up or process established for the earning of assessable income.[145] It is not relevant whether the asset is put to use by either the operating entity or the asset entity. The Commissioner would expect that, given the anticipated activities of both the operating entity and the asset entity, once completed the facility (even if not in its ultimate form) or an asset forming part thereof, will immediately be used for the purpose of producing assessable income.

254. It also follows that for the MIT cross staple arrangement income transitional rules where a facility has not yet been constructed, there may be a pre-transition period prior to the completion of the facility. If that is the case, the benefits of the MIT cross staple arrangement income transitional rules will not apply during that period.

Examples of when an asset that is part of a facility is first put to use for the purpose of producing assessable income

255. In light of the contextual understanding of 'asset', examples of the asset first being put to use will necessarily reflect the business operation or other intended use of the facility. The putting to use of the asset is likely to at least be referable to the activities of the lessee of the land on which the facility is located. The first use may occur before the ultimate completion of the facility, but the Commissioner would ordinarily expect that it would require some self-contained component or collection of assets, such that they, in and of themselves, satisfy the definition of 'facility' notwithstanding the ultimate facility is incomplete.

256. Examples where an asset that is part of a facility is first put to use for the purpose of producing assessable income (despite the project having further stages to progress before ultimately being complete) include:

- The first stage of a multi-stage retail shopping complex is opened to the public. Whilst the designs have been approved and contracted for which will

[143] Paragraph 3 of IT 2658; *NT86/10511 and NT87/7495 and Commissioner of Taxation* [1989] AATA 7.
[144] Paragraph 4 of IT 2658.
[145] See general principles in *Sun Newspapers Limited v Federal Commissioner of Taxation* [1938] HCA 73.

take several years over multiple stages, the stage completed is a facility in and of itself.

- While a water desalination and storage facility is being constructed, the desalination plant is switched on and pumps water into a city reservoir while the storage catchment is still being constructed.

In what circumstance might an investment cease to qualify for the transitional rules?

257. The MIT cross staple arrangement income transitional rules are not a 'one-off' test. The entities that are stapled entities to the cross staple arrangement in respect of the relevant facility must continue to satisfy the MIT cross staple arrangement income transitional rules.

258. This is because section 12-440 applies where the requirements in either subsection (1) or (2) are satisfied and the relevant choice is made, the MIT cross staple arrangement income transitional rules may apply for the relevant period in subsection (4) to:

- exclude an amount of rent from land investment from being MIT cross staple arrangement income, and
- provide for a deduction of an amount of rent from land investment in accordance with section 25-120 of the ITAA 1997.

259. However, even if section 12-440 applies, and subsections 12-440(4) and (5) are satisfied, it does not follow that the transitional rules will continue to have effect in respect of the facility and the cross staple arrangement where there is some change in circumstances.

260. The operative provisions giving effect to the transitional rules are ambulatory. Therefore, regard must be had on an ongoing basis, to the requirements of subsection 12-440(3) and section 25-120 of the ITAA 1997 in order to determine whether the MIT cross staple arrangement income transitional rules continue to apply. Hence, merely making the choice in accordance with subsection 12-440(5), and/or satisfying either subsections 12-440(1) or (2) will not in itself qualify a cross staple arrangement for the whole transition period.

261. Subsection 12-440(3) may provide for relief from MIT cross staple arrangement income and section 25-120 of the ITAA 1997 may provide a specific deduction where section 12-440 applies. Collectively these provisions focus on:

- the cross staple arrangement
- amounts that relate to the facility, and
- rent from land investment.

262. It follows that changes to the cross staple arrangement, ceasing to have a cross staple arrangement, or alterations to the facility, such that it ceases to be the facility identified by subsections 12-440(1) or (2), will cause the relevant entities to fail the requirements of subsection 12-440(3) and section 25-120 of the ITAA 1997.

263. The following are some examples in which the relevant entities may cease to qualify for the MIT cross staple arrangement income transitional rules:

- cessation of cross staple arrangement – there is no stapled entity, being the second entity in accordance with paragraph 12-440(3)(c), and therefore, the amount referred to in paragraph 12-440(3)(d) is not an amount derived, received or made from, or attributable to an entity which is a stapled entity. For example, this situation may have arisen because although the

arrangement is not altered, a change in ownership may cause the arrangement to fail the requirements of common ownership in paragraph 12-436(4)(c)

- replacement of cross staple arrangement – a new cross staple arrangement is entered into in relation to the facility, for example a new contract is entered into between the relevant operating entity and the relevant asset entity, different to the contract before 27 March 2018
- where the amount is no longer 'in relation to the facility' – required by paragraph 12-440(3)(b), for example where
  - an additional, new and separate facility is created, or
  - augmentation of the existing facility is so dramatic that a new facility is identified
- where the relevant asset entity no longer exists and is replaced
- where the amount derived is no longer attributable to rent from land investment

Renewed, renegotiated or otherwise affected cross staple arrangements

264. As noted in paragraph 142 of this Ruling, whether a contract is entered into will be a question of contract law. Similarly, what is an arrangement will be a question of fact and degree. Circumstances could exist in which an agreement has so fundamentally changed as to constitute a new cross staple arrangement (so as to fall outside of transitional relief). These could include changes sufficient to result in a new contract.

265. As long as the cross staple arrangement remains the same, something more than a mere extension of rights will be required. For example, a mere rent review under an existing contract will not result in a new cross staple arrangement.

266. The mere renewal of a lease agreement, covering the same facility and between the same parties would not, subject to the facts and circumstances, be expected to create a new cross staple arrangement.[146] Similarly, an ordinary exercise of an option to extend the arrangement without any material change would not be expected to cause transitional relief to cease to apply.

267. Examples of characteristics that could result in a new cross staple arrangement include:

- introduction of assets and facilities not part of the existing facility, for example where they dramatically augment the earlier facility
- amending the terms and conditions, such as altering the lease from a year on year lease to a long-term lease may be sufficient to cause a new arrangement, and
- replacing parties, such that a change in the cross staple arrangement results from the change in stapled entities to a cross staple arrangement.

268. A material change to the facility, such that it becomes a facility different to the one that existed prior to 27 March 2018 would cause transitional relief in relation to the facility to cease.

[146] Paragraph 1.122 of the Explanatory Memorandum.

Interaction of the various transitional rules

269. The MIT cross staple arrangement income transitional rules apply to assessable income that is attributable to existing or sufficiently committed investments.

270. Where that income is captured by more than one of the classes of NCMI, transitional relief will not apply unless the transitional rules applicable to each class of NCMI are satisfied. For example, where an arrangement gives rise to both MIT cross staple arrangement income and MIT agricultural income, then the transitional provisions relevant to each of those categories would need to be satisfied in order for transitional relief to apply.

Integrity rules – concessional cross staple rent

271. Integrity rules can apply to limit the amount of concessional cross staple rent. The integrity rules broadly take two forms:

- the 'non-arm's length income rules' (NALIR) in Division 275 of the ITAA 1997. The NALIR applies generally to MITs, and includes but is not limited to arrangements resulting in 'excepted MIT CSA income', and
- the concessional cross staple rent cap (CCSRC)[147], which applies to 'excepted MIT CSA income' in relation to economic infrastructure facilities only.

272. 'Excepted MIT CSA income' means income of a MIT that would otherwise be MIT cross staple arrangement income and therefore NCMI, but for either of the following applying:

- the approved economic infrastructure facility exception, or
- where the transitional MIT cross staple arrangement income rules apply in respect of an economic infrastructure facility.[148]

Integrity rule – non-arm's length income rule

273. In circumstances where the facility is not an economic infrastructure facility, only the NALIR will apply.[149]

274. If the NALIR applies, the Commissioner may make a determination to treat an amount of ordinary or statutory income as non-arm's length income, where:

- the amount is derived from a scheme the parties to which were not dealing with each other at arm's length in relation to the scheme[150], and
- that amount exceeds the amount that the entity might have been expected to derive if those parties had been dealing with each other at arm's length in relation to the scheme[151], and
- the amount is not a distribution listed in paragraph 275-610(1)(c) of the ITAA 1997.

275. If the Commissioner makes such a determination, the relevant trustee is liable to pay tax on the amount of the specified non-arm's length income at the rate of 30%.[152] If a determination is made, then the amount of net income of the MIT will be reduced and the

[147] Sections 12-441, 12-443 and 12-444.
[148] Refer to section 12-442.
[149] Subparagraph 12-441(1)(b) and paragraphs 1.132 and 1.134 of the Explanatory Memorandum.
[150] Paragraph 275-610(1)(a) of the ITAA 1997.
[151] Paragraph 275-610(1)(b) of the ITAA 1997.
[152] Subsection 275-605(2) of the ITAA 1997 and subsection 12(10) of the *Income Tax Rates Act 1986*.

amount will not form part of a fund payment, or be assessable to Australian investors in the trust under Division 6 of Part III of the ITAA 1936.[153]

276. The operation of the NALIR is discussed in detail in Law Companion Ruling LCR 2015/15 *Managed Investment Trusts: the non-arm's length income rule in sections 275-605, 275-610 and 275-615 of the Income Tax Assessment Act 1997*. However, for the purposes of the MIT cross staple arrangement income rules, the NALIR has been modified to ensure that the Commissioner will be able to apply the non-arm's length income determination where a MIT is not a party to the scheme.[154]

Integrity rule – concessional cross staple rent cap

277. The CCSRC integrity rule operates in relation to economic infrastructure facilities, and can apply in addition to the NALIR.

278. The CCSRC will cap and deny concessional transitional treatment for an amount of excessive rent. There are two broad categories of CCSRCs:

- the first category (CCSRC – Existing), which applies in relation to either an existing lease with a specified amount of, or objective method to determine the amount of, annual rent[155] (CCSRC – Existing Amount and CCSRC – Existing Method respectively) which was set before 27 March 2018, and
- the second category (CCSRC – General), which applies by default where the CCSRC – Existing Amount and CCSRC – Existing Method do not apply. The cap is calculated by way of a formula.[156]

279. The CCSRC will apply where an amount of excepted MIT CSA income is derived, received or made by a MIT for an income year under a cross staple lease entered into by the relevant asset entity and the relevant operating entity, being an amount of rent from land investment under a lease.[157] To the extent that the amount of excepted MIT CSA income of the asset entity exceeds the CCSRC, that excess will not benefit from the relevant exceptions to MIT cross staple arrangement income. This will be the case whether the asset entity is a MIT or not, as subsection 12-441(3) deems the relevant asset entity to be a MIT for the purposes of the test.[158]

280. The clarification that the amount of rent from land investment must be under a lease establishes the object of the paragraph, being the cross staple lease. The cross staple lease is that entered into by the relevant asset entity and the relevant operating entity, identified in subparagraphs 12-437(2)(a) and (b) respectively. It is this cross staple arrangement and hence the cross staple lease that will be tested against the CCSRC.

[153] Subsections 275-605(3) and (4) of the ITAA 1997.
[154] Subsections 275-610(1A) and 275-615(1A) of the ITAA 1997.
[155] Section 12-443.
[156] Section 12-444.
[157] Subsection 12-441(1).
[158] Subsection 12-441(2).

CCRSC – existing lease with specific rent or established rent method

281. The CCSRC – Existing category requires a lease to be in existence before 27 March 2018 in relation to a cross staple arrangement and a facility. It applies where an amount is identified in subsection 12-441(1) as excepted MIT CSA income[159], the cross staple lease was entered into before 27 March 2018[160], and the lease and/or the associated documents specify either:

- the amount of annual rent under the lease for the first year of the lease that ends after 27 March 2018[161], or
- an objective method for determining the amount of annual rent under the lease.[162] That method must be set out in the documentation prior to 27 March 2018.[163]

CCRSC – Existing Method

282. The CCSRC – Existing Method will apply where, in addition to other requirements, the lease or associated documents specify an objective method for determining the annual rent under the lease[164] and that method was set out in those documents before 27 March 2018. Paragraphs 1.146 to 1.154 of the Explanatory Memorandum set out the operation of this method. Importantly, the method must be an objective method.

283. While 'objective method' is not defined, the Commissioner's view is that the method must be objective in that it must be capable of measurement wholly external to the parties who have entered into the lease. The method should produce results capable of independent reproduction and should also be objectively ascertainable without reference to discretion or judgment by the parties to the lease. While the method need not be evidenced in the lease agreement, it must be capable of reference to the lease.

284. The Explanatory Memorandum provides some examples of objective methods[165], and highlights that an objective method should also be based on objectively discernible information[166]:

> In order to establish that there is a method that is set out in the documents, the method must be objective and sufficiently prescriptive so that the calculation of the rental charge relies upon objectively discernible information, and produces a result that would be the same for any reasonable person applying it.

285. Methods of arriving at rent which are not objective methods include[167]:

- a lease clause permitting the asset entity the discretion to set the rent, and
- a lease clause requiring the parties to agree on an amount of rent, without regard to arm's length or market factors to demonstrate and support the rent agreed as an amount of rent determined by an objective method.

286. Hence, a method that requires the parties to agree on the rent, or a component of the rent formula, will not be an objective method as it is not a method wholly external to the parties.

[159] Paragraph 12-443(1)(a).
[160] Paragraph 12-443(1)(b).
[161] Subparagraph 12-443(1)(c)(i).
[162] Subparagraph 12-443(1)(c)(ii).
[163] Paragraph 12-443(1)(d).
[164] Subparagraph 12-443(1)(c)(ii).
[165] Paragraph 1.153 of the Explanatory Memorandum.
[166] Paragraph 1.152 of the Explanatory Memorandum.
[167] Paragraph 1.154 of the Explanatory Memorandum.

287. If an objective method is set out in cross staple lease or associated documents, before 27 March 2018, then CCSRC – Existing Method is the amount of rent determined by that method.[168]

288. The Commissioner expects that taxpayers will be able to provide documentary evidence that the method existed prior to 27 March 2018 by producing the relevant lease, and any associated documents, such as transfer pricing or market rent reviews, including instructions to valuers and/or economists. There must be a clear connection between the cross staple lease and any associated documents.

CCRSC – Existing Amount

289. If there is an amount specified in the cross staple lease or associated documents, but no objective method is so set out, then the CCSRC – Existing Amount will apply. The amount of the CCSRC – Existing Amount is then determined by subsection 12-443(3), which is broadly determined by reference to an amount specified in the lease that was agreed to before 27 March 2018. This could be where either:

- an amount is specified for an income year, that amount corresponding to the relevant income year[169], or
- an amount is not specified for the relevant income year, then the amount in relation to the most recent year of the lease for which the amount was so specified, indexed according to Subdivision 960-M of the ITAA 1997.[170]

290. In identifying an amount specified and agreed for the purposes of subsection 12-443(3), the Commissioner expects contemporaneous documents evidencing that amount as being specified before 27 March 2018.[171] The amount need not be set out in the lease itself, but the documentation in relation to the amount must evidence, including the connection with the facility, the cross staple arrangement and relevant cross staple lease.

291. The Explanatory Memorandum provides examples of how the CCSRC – Existing Amount will operate where there is a specified amount of annual rent.[172]

292. Where an income year does not align with a particular year of the lease, subsection 12-443(4) provides that the years will correspond if the years both end after a particular 27 March, but before the next 27 March.

CCRSC – General

293. Where neither of the CCSRC – Existing provisions apply, then the CCSRC – General will apply. Hence, taxpayers will need to ensure that they have carefully reviewed the relevant lease and associated documents to determine whether section 12-443 applies.

294. The CCSRC – General applies to economic infrastructure facilities, whether approved by the Treasurer[173], or subject to the transitional rules.[174]

295. Paragraph 1.159 of the Explanatory Memorandum explains that the CCSRC – General:

[168] Subsection 12-443(2).
[169] Paragraph 12-443(3)(a).
[170] Paragraph 12-443(3)(b).
[171] Paragraph 12-443(3)(a).
[172] Examples 1.18 and 1.19 of the Explanatory Memorandum.
[173] Section 12-439.
[174] Section 12-440.

> …*broadly reflects the amount of rent that would be paid from the operating entity to the asset entity which would result in the asset entity having a current year net (taxable) income position equal to 80 per cent of the project's total notional current year taxable income*.

296. There are broadly three circumstances where the CCSRC – General may apply[175]:

- cases of economic infrastructure approved by the Treasurer[176], and
- an economic infrastructure facility where the transitional rules apply, but section 12-443 does not apply. That is:
  - the cross staple lease and associated documents did not, before 27 March 2018, specify an objective method nor the amount of rent, or
  - where the facility and the relevant cross staple arrangement are sufficiently committed to before 27 March 2018, but no cross staple lease has been entered into in respect of the facility, whether or not it has been constructed.

297. The CCSRC – General is worked out in accordance with the steps at subsection 12-444(2), which broadly establishes an '80/20' rule. That is, broadly, to the extent that the asset entity's taxable income exceeds 80% of the project's total notional current year taxable income, then that excess will not benefit from the relevant exceptions to MIT cross staple arrangement income. That notional calculation must be worked out as a 'reasonable estimate'.[177] For the purposes of working out the net or assessable income of the relevant entities, losses are to be disregarded.[178] Example 1.20 in the Explanatory Memorandum applies these steps in detail.

298. The provisions contain references to terms such as 'net income', 'tax loss', 'trust components' and 'partnership loss'. This requires the relevant entity to have regard to the income tax law to make that reasonable estimate of its income or loss for the purposes of the CCSRC – General. This includes the modification to disregard losses which would otherwise distort the application of the CCSRC – General.

299. 'Reasonable' is objective and will be determined in context. Relevantly, for the purposes of making a reasonable estimate of the relevant asset entity's and operating entity's assessable or net income for the income year, the Commissioner considers that regard should be had to all the facts and circumstances, including the object of the CCSRC – General provisions and the integrity rules.

300. A reasonable estimate should be broadly reflective of the relevant entities' notional project income for the income year.[179] It would necessarily require the relevant entities to have regard to the notional project, the current and historic income and deductions, current and expected market conditions and other relevant factors to make that reasonable estimation.

Consequences for breaching the CCSRC

301. Broadly, there are two main consequences for a MIT where the CCSRC is breached:

- firstly, to the extent that excepted MIT CSA income exceeds the CCSRC, the amount will be NCMI[180], and

[175] Paragraphs 1.157 and 1.159 of the Explanatory Memorandum.
[176] Section 12-439.
[177] Paragraph 12-444(2)(b).
[178] Subsection 12-444(3).
[179] Refer to paragraph 1.159 of the Explanatory Memorandum.
[180] Subsection 12-441(2).

- secondly, an expense allocation rule will apply.

302. Subsection 12-441(2) provides that to the extent that the amount of the relevant asset entity's excepted MIT CSA income exceeds the CCSRC for that income year, the concessions in subsections 12-437(5) and 12-440(3) do not apply. Consequently, that excess amount, to the extent it is reflected in a fund payment, is subject to withholding at a rate equal to the top corporate rate.[181]

303. Where the CCSRC is breached, a MIT, or an asset entity which is taken to be a MIT[182], is required to allocate expenses in a certain order.

304. The ordering rules applies where the asset entity in relation to a cross staple arrangement is entitled to a deduction and had derived excepted MIT CSA income (disregarding subsection 12-441(2) and section 12-445), and that amount of excepted MIT CSA income exceeds the CCSRC.

305. The amount of the deduction (identified in paragraph 12-445(1)(b)) can only be deducted against income in the following order:

- firstly, against amounts of assessable income that is excepted MIT CSA income, up to the amount of the CCSRC
- secondly, where an amount of a deduction remains after applying paragraph 12-445(2)(a), then that amount can be deducted against an amount of assessable income that is MIT cross staple arrangement income, and
- finally, if an amount of deduction remains after following paragraphs 12-445(2)(a) and (b), the amount can be deducted against other assessable income.

306. Example 1.21 of the Explanatory Memorandum provides a detailed example of the deduction ordering rule.

MIT trading trust income

307. The MIT trading trust income rules broadly ensure that distributions a MIT receives either directly or indirectly from a trading trust are treated as NCMI.

308. The rules apply if an amount is included in a MITs assessable income for an income year which is attributable to or received from another entity.[183] The amount will be MIT trading trust income where the MIT holds a total participation interest[184] in the second entity greater than nil, and the second entity is a trading trust in relation to the income year. The rules also capture amounts from a partnership or a trust that is not a unit trust, which if they were a unit trust through the income year, would be a trading trust. However, the section will not apply where the second entity is a public trading trust.[185]

309. Amounts of assessable income excluded from the meaning of a fund payment are not captured as MIT trading trust income.[186] Also excluded are amounts attributable to a capital gain arising out of CGT events E4 or E10.[187]

[181] Refer to paragraph 1.164 of the Explanatory Memorandum.
[182] Subsection 12-445(3).
[183] Subsection 12-446(1).
[184] 'Total participation interest' is defined in section 960-180 of the ITAA 1997.
[185] Subsection 12-446(2).
[186] Paragraph 12-446(1)(c) and subsection 12-405(1).
[187] Broadly, these events happen where a trust or an AMIT makes a non-assessable payment to a beneficiary or member.

MIT trading trust income – transitional provisions

310. Transitional rules may apply where MIT trading trust income is attributable to a total participation interest in a second entity that is in existence at the time of the announcement of the measure.[188] These rules maintain the general concessional 15% MIT withholding rate to relevant amounts[189] attributable to this interest for the transitional period. The transitional period applies to relevant income that was derived, received or made by the MIT before 1 July 2026.

311. An apportionment methodology applies to any relevant amount attributable to a trading trust where the relevant MIT's participation interest in the trading trust has increased since 27 March 2018.

MIT residential housing income

312. Under section 12-450, an amount included in the assessable income of a MIT will be MIT residential housing income to the extent that:

- it is attributable to a 'residential dwelling asset', and
- it is not referable to the use of the residential dwelling asset to 'provide affordable housing', as defined in section 980-5 of the ITAA 1997.

313. A 'residential dwelling asset' is defined in section 12-452. It uses the existing definition of 'dwelling' in section 118-115 of the ITAA 1997, and treats certain adjacent land and adjacent structures as though they were also a dwelling by extending the application of section 118-120 of the ITAA 1997.

314. Broadly, a residential dwelling asset is an asset that is:

- a dwelling
- taxable Australian real property, and
- residential premises but not commercial residential premises.

315. A residential dwelling asset does not however include a dwelling that:

- is used primarily to provide specialist disability accommodation[190], or
- is used primarily to provide disability accommodation of a kind prescribed in the regulations.[191]

316. The terms 'residential premises' and 'commercial residential premises' each take their meaning from the *A New Tax System (Goods and Services Tax) Act 1999*.[192]

Use of residential dwelling to provide affordable housing

317. Income attributable to a residential dwelling asset will constitute MIT residential housing income. However, such income will not constitute MIT residential housing income to the extent it is referable to the use of the residential dwelling asset to provide affordable housing.

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[188] Section 12-447.

[189] The relevant amount is identified at paragraph 12-447(1)(a). It is the amount that would be MIT trading trust income of the MIT if the section were disregarded.

[190] Within the meaning of the *National Disability Insurance Scheme (Specialist Disability Accommodation Conditions) Rule 2018*, and that dwelling is enrolled in accordance with section 6 of that Rule.

[191] As prescribed for the purposes of paragraph 12-452(1)(e).

[192] 'Residential premises' and 'commercial residential premises' are defined in subsection 995-1(1) of the ITAA by reference to the *A New Tax System (Goods and Services Tax) Act 1999*.

318. Broadly, a residential dwelling asset will be provided for affordable housing if it is either tenanted or available to be tenanted under the management of an eligible community housing provider and the community housing provider has issued to the owner of the asset a certificate covering the asset for the relevant period.[193] There are additional requirements, including that the tenants or occupants must not own a 10% or greater interest in the MIT which owns the residential dwelling asset.

Example 11 – residential apartment building

319. *The trustee of a widely-held unit trust holds land on which a residential apartment building stands. This is the only asset held in the trust. The trust's investment strategy and the offering documents provided to investors state that the trust intends to invest in residential property suitable for providing long-term rental options to tenants, with 50% of the apartments available for affordable housing. The trust is open-ended, with the offering documents stating that the property is intended to be held for at least 15 years with no ability for investors to redeem their units in that time.*

320. *As the trustee expects to provide the affordable housing to tenants at below-market rent, the forecast rental return for the property is lower than would be the case had it all been leased at market rates. The rental return is therefore not expected to significantly exceed the forecast capital growth.*

321. *The trustee enters into long-term arrangements with an eligible community housing provider who manages the tenancy and prospective tenancy for 50% of the apartments in the residential apartment building. The remaining apartments in the residential apartment building are marketed for leases at market rates. The trustee leases the apartments for terms of up to five years, with tenants having an option to renew their leases for a further three years, plus any subsequent extension as agreed between the parties.*

322. *Due to the fact that the provision of affordable housing reduces the overall rental return, the forecast figures alone might indicate that the investment in land is not held primarily for the purposes of deriving rent. However, no single factor is determinative, and it is necessary to have regard to all the facts and circumstances. In this case, the investment strategy, the expected holding period of the property, the marketing plan and lease terms indicate that the investment in land is primarily for the purpose of deriving rent. Furthermore, the long-term arrangements with the eligible community housing provider and the stated purpose of providing affordable housing provide the necessary context for establishing that the below-market rental yield is consistent with the investment in land being for the primary purpose of deriving rent.*

323. *Assuming all other requirements in section 275-10 of the ITAA 1997 are met, the trust is likely to be a MIT. Consequently, it is necessary to consider whether any amount included in its assessable income for the income year is MIT residential housing income, as defined in section 12-450.*

Example 12 – residential apartment building with retail area

324. *Expanding on Example 11 (and assuming the trust is a MIT), the trustee leases all the apartments to tenants, with 50% of the apartments used to provide affordable housing, as defined. The ground floor of the apartment building also contains a small retail/commercial area. This is leased to various tenants, who operate their respective businesses on the premises.*

325. *The trustee receives $2 million a year in total rent from the site. Of this total, 5% is rent from the commercial premises, 40% from the apartments used to provide affordable housing, and 55% from the remaining apartments.*

[193] Section 980-5 of the ITAA 1997.

326. *The trustee determines that the $1.1 million it receives as rent on the apartments leased at market rates is MIT residential housing and therefore NCMI. It is income that is attributable to residential dwelling assets.*

327. *The remaining $900,000 is not NCMI as:*

- *the $800,000 received in relation to the remaining apartments is not MIT residential housing income. Whilst attributable to a residential dwelling asset, it is referable to the use of those residential dwelling assets to provide affordable housing (as defined), and*
- *the $100,000 rent from the commercial premises is not MIT residential income, as it is not attributable to a residential dwelling asset.*

MIT residential housing income – transitional provisions

328. The rules apply to payments made from 1 July 2019 that are attributable to the 2019–20 income year or later. However, transitional rules[194] provide relief for amounts attributable to the following circumstances:

- where a MIT had direct or indirect interests in a residential dwelling asset prior to 14 September 2017[195], or
- the MIT would otherwise have qualified for transitional relief as it (or another entity from whom the MIT derived the relevant amount) had entered into a contract prior to 14 September 2017 in respect of a facility that consists of or contains a residential dwelling asset.

329. This transitional relief period is until 1 October 2027.

330. An apportionment methodology applies to any relevant amount attributable to a residential dwelling asset where the relevant MIT's participation interest in the entity that holds, or contracted for the asset, has increased since 14 September 2017.

MIT agricultural income

331. An amount is MIT agricultural income under subsection 12-448(2) to the extent it is attributable to an asset that is 'Australian agricultural land for rent'. The term 'Australian agricultural land for rent' is specifically defined in subsection 12-448(3) to mean 'Division 6C land' situated in Australia that:

- is used, or could reasonably be used, for carrying on a primary production business, and
- is held primarily for the purposes of deriving or receiving rent.

332. Paragraphs 333 to 337 of this Ruling set out the Commissioner's view on the first requirement – 'is used, or could reasonably be used, for carrying on a primary production business'. Whether land is held primarily for the purpose of deriving rent is considered at paragraphs 11 to 17 of this Ruling.

Carrying on a primary production business

333. Whether an activity amounts to the carrying on of a primary production business[196] is a question of fact. Whilst each case will turn on its own particular facts, the

[194] Section 12-451.
[195] Specifically, prior to 4:30pm by legal time in the Australian Capital Territory, on 14 September 2017.

determination of the question is generally the result of a process of weighing all the relevant indicators.

334. General guidance on what constitutes carrying on a primary production business is available in Taxation Ruling TR 97/11 *Income tax: am I carrying on a business of primary production?*

Is used, or could reasonably be used

335. Under subsection 12-448(3), it is not essential that the land is actually being used by the lessee or another entity to carry on a primary production business. It is sufficient that the land 'could reasonably be used' for carrying on a primary production business.[197]

336. TR 97/11 provides general guidance on what constitutes the carrying on of a primary production business. Relevant factors in determining whether the land 'could reasonably be used' for such a business include:

- any zoning or regulatory restrictions on the use of the land – if the carrying on of primary production is expressly not allowed under the applicable zoning, then it is unlikely the land could reasonably be used to carry on a primary production business
- prior usage of the land
- characteristics of the land (for example, soil and water analyses performed and expert opinion on the suitability of the land for primary production), and
- land capacity and the scale of activity that could be conducted on the land – whilst a very small parcel of land may not be suitable for carrying on a primary production business, it is not necessarily the case that the land must be capable of sustaining a primary production business in isolation. For example, the characteristics of adjoining land may indicate that the land could reasonably be used for a primary production business carried on over several adjoining properties.

337. This is not an exhaustive list of the relevant factors and no single factor is determinative. All the facts of circumstances of each case must be considered and relative weight placed on the relevant factors.

Example 13 – agricultural land

338. *The trustee of a widely-held unit trust acquires agricultural land. Its investment strategy is to maximise the total return to investors over a five year period. At the time of acquisition, the land was leased to the owner of a neighbouring property to graze cattle. The trustee retains the existing lease arrangement and renews the lease on a year by year basis. The trustee receives a moderate amount of rent from the lease. The land is located on the urban fringe, and the trustee anticipates that the area will be re-zoned in two to four years, significantly increasing its resale value. During this time, the trustee engages with the local council on the re-zoning process and undertakes some preliminary works on the property that would facilitate any future subdivision of the land.*

339. *Although the trustee leases the land and derives rent at all times, it is unlikely that the investment in the land is primarily for the purpose of deriving rent. The expected holding period is relatively short and the trustee's activities are focussed on maximising the profit on sale rather than the rental return. If, having regard to all the facts and*

[196] The term 'primary production business' is defined in subsection 995-1(1) of the ITAA 1997.

[197] The definition of 'agricultural land' in section 4 of the *Foreign Acquisitions and Takeovers Act 1975* and section 4 of the *Register of Foreign Ownership of Water or Agricultural Land Act 2015* similarly refers to land 'that is used, or that could reasonably be used, for a primary production business'.

circumstances (including as relevant to the application of the safe harbour rules), the investment in land does not satisfy the primary purpose test, then the trust will not be a MIT. If the trust is not a MIT, the NCMI provisions will have no application to distributions that are attributable to the agricultural land.

MIT agricultural income – transitional provisions

340. The rules apply to payments made from 1 July 2019 that are attributable to the 2019–20 income year or later. However, transitional rules[198] provide relief for amounts attributable to the following circumstances:

- where a MIT had direct or indirect interests in the asset that is Australian agricultural land for rent before 27 March 2018[199], or
- the MIT would otherwise have qualified for transitional relief as it (or another entity from whom the MIT derived the relevant amount) had entered into a contract before 27 March 2018 for the acquisition or lease of the relevant asset.

341. This transitional relief period is until 1 July 2026.

342. An apportionment methodology applies to any relevant amount attributable to an asset that is Australian agricultural land for rent where the MIT's participation interest in the entity holding the asset has increased since 27 March 2018.

Fund payment attributable to more than one type of NCMI

343. Section 12-435 provides that NCMI comprises four discrete types of income. The Act does not provide for an ordering or hierarchy of these classes of NCMI. Where two or more apply, the withholding amount remains the same. This is so even if one of the types of NCMI may benefit from a transitional rule.

344. For example, where an amount included in the assessable income for an income year of a MIT is attributable to MIT agricultural income or MIT residential housing income, it will be NCMI regardless of whether it is excluded from MIT cross staple arrangement income.

345. Conversely, the specific exceptions to MIT cross staple arrangement income in subsections 12-437(3) to (7) do not apply in determining MIT trading trust income, MIT agricultural income or MIT residential housing income.

Commissioner of Taxation
26 June 2019

[198] Section 12-449.
[199] Specifically, prior to 4:30pm by legal time in the Australian Capital Territory, on 14 September 2017.

Appendix – Your comments

346. You are invited to comment on this draft Ruling including the proposed date of effect. Please forward your comments to the contact officer by the due date.

347. A compendium of comments is prepared for the consideration of the relevant Public Advice and Guidance Panel or relevant tax officers. An edited version (names and identifying information removed) of the compendium of comments will also be prepared to:

- provide responses to persons providing comments, and
- be published on **ato.gov.au**.

Please advise if you do not want your comments included in the edited version of the compendium.

Due date: **23 August 2019**

Contact officer details have been removed following publication of the final ruling.

Amendment history

Date of Amendment	Part	Comment
2 September 2019	Paragraph 263	Sixth bullet point deleted: 'where the external entities are replaced, or their participation interests are varied. For example, there is a change in ultimate economic ownership of the asset entities and operating entities'
	Paragraph 267	Words omitted from third bullet point: 'or a change in the external entities holding those stapled entities'

References

ATOlaw topic(s)	Income tax ~~ Trusts ~~ Managed investment trusts ~~ Stapled securities
Legislative references	TAA 1953 TAA 1953 Sch 1 TAA 1953 Sch 1 12-385(3)(a)(iii) TAA 1953 Sch 1 12-395(3)(ab) TAA 1953 Sch 1 12-395(6)(ab) TAA 1953 Sch 1 12-405(1) TAA 1953 Sch 1 12-405(1)(b) TAA 1953 Sch 1 12-435 TAA 1953 Sch 1 12-436(1) TAA 1953 Sch 1 12-436(2) TAA 1953 Sch 1 12-436(3) TAA 1953 Sch 1 12-436(4) TAA 1953 Sch 1 12-436(4)(c) TAA 1953 Sch 1 12-436(5) TAA 1953 Sch 1 12-436(6) TAA 1953 Sch 1 12-436(6)(a)

	TAA 1953 Sch 1 12-436(7) TAA 1953 Sch 1 12-436(8) TAA 1953 Sch 1 12-437 TAA 1953 Sch 1 12-437(1)(a) TAA 1953 Sch 1 12-437(1)(c) TAA 1953 Sch 1 12-437(2)(a) TAA 1953 Sch 1 12-437(2)(a)(i) TAA 1953 Sch 1 12-437(2)(a)(ii) TAA 1953 Sch 1 12-437(2)(b) TAA 1953 Sch 1 12-437(3) TAA 1953 Sch 1 12-437(4) TAA 1953 Sch 1 12-437(5) TAA 1953 Sch 1 12-437(6) TAA 1953 Sch 1 12-437(7) TAA 1953 Sch 1 12-438 TAA 1953 Sch 1 12-438(1) TAA 1953 Sch 1 12-438(2) TAA 1953 Sch 1 12-438(3) TAA 1953 Sch 1 12-438(4) TAA 1953 Sch 1 12-438(5) TAA 1953 Sch 1 12-438(6) TAA 1953 Sch 1 12-439 TAA 1953 Sch 1 12-439(5) TAA 1953 Sch 1 12-440 TAA 1953 Sch 1 12-440(1) TAA 1953 Sch 1 12-440(1)(a)(ii) TAA 1953 Sch 1 12-440(1)(a)(iii) TAA 1953 Sch 1 12-440(1)(b) TAA 1953 Sch 1 12-440(1)(b)(i) TAA 1953 Sch 1 12-440(1)(b)(ii) TAA 1953 Sch 1 12-440(1)(c) TAA 1953 Sch 1 12-440(1)(d) TAA 1953 Sch 1 12-440(2) TAA 1953 Sch 1 12-440(2)(b) TAA 1953 Sch 1 12-440(2)(c) TAA 1953 Sch 1 12-440(2)(d) TAA 1953 Sch 1 12-440(3) TAA 1953 Sch 1 12-440(3)(b) TAA 1953 Sch 1 12-440(3)(c) TAA 1953 Sch 1 12-440(3)(d) TAA 1953 Sch 1 12-440(3)(e) TAA 1953 Sch 1 12-440(4) TAA 1953 Sch 1 12-440(4)(a) TAA 1953 Sch 1 12-440(4)(a)(ii) TAA 1953 Sch 1 12-440(4)(b)(ii) TAA 1953 Sch 1 12-440(5) TAA 1953 Sch 1 12-441 TAA 1953 Sch 1 12-441(1) TAA 1953 Sch 1 12-441(1)(b) TAA 1953 Sch 1 12-441(2) TAA 1953 Sch 1 12-441(3) TAA 1953 Sch 1 12-442 TAA 1953 Sch 1 12-443 TAA 1953 Sch 1 12-443(1)(a) TAA 1953 Sch 1 12-443(1)(b) TAA 1953 Sch 1 12-443(1)(c)(i) TAA 1953 Sch 1 12-443(1)(c)(ii) TAA 1953 Sch 1 12-443(1)(d) TAA 1953 Sch 1 12-443(2) TAA 1953 Sch 1 12-443(3) TAA 1953 Sch 1 12-443(3)(a) TAA 1953 Sch 1 12-443(3)(b)

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