IT 2282 - Income tax : chattel leasing - sub-leasing assessment of lease rental paid in advance

TAXATION RULING NO. IT 2282

INCOME TAX : CHATTEL LEASING - SUB-LEASING ASSESSMENT OF LEASE RENTAL PAID IN ADVANCE

F.O.I. EMBARGO: May be released

REF H.O. REF: 84/1934-5 DATE OF EFFECT:

B.O. REF: DATE ORIG. MEMO ISSUED:

F.O.I. INDEX DETAIL

REFERENCE NO:	SUBJECT REFS:	LEGISLAT. REFS:
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PREAMBLE This office recently had occasion to consider whether rent payable in advance under a proposed chattel leasing arrangement was to be treated as assessable income in the year of receipt or over the term of the lease agreement.

2. In the particular circumstances a finance company, engaged principally in providing chattel lease finance, proposed to purchase plant and equipment in its own right as it customarily did but, rather than lease the property directly to the intended end-user, it would lease the property to an arm's length entity or individual who, in turn, would sub-lease the property to the intended end-user.

3. The terms of both the head lease and the sub-lease were the same, say 3 years. Although the head lease provided for a monthly rental the head lessee was required to pay the whole of the amount payable for the term immediately on the signing of the lease. There was a further provision in the head lease which required the finance company, in the event that the lease was terminated before the expiration of the term and the property sold for the best price reasonably obtainable, to pay to the head lessee an amount equal to the monthly rental for the unexpired term. The possibility of this eventuality occurring was said to be unlikely. The head lease did not place any other obligations on the finance company.

4. The proposed arrangements were said to be attractive to the finance company because they represented an avenue for obtaining cheap funds for use in the leasing business. The finance company's position was fully secured in as much as it retained ownership of the property and would be paid the rental in full on signing the lease.

5. It was contended, on behalf of the finance company, that the rent paid in advance should be brought to account for income tax purposes over the term of the lease, i.e., it would

be spread over the 3 year period. Submissions were also made in respect of other aspects of the arrangements but it is not necessary to canvass them for the purposes of this ruling.

RULING

6. The finance company was advised that the rent paid in advance was considered to be wholly assessable in the year of receipt. The reason for this is that the rent paid in advance would be considered to have come home to the finance company in the sense that there was nothing more for the finance company to do to earn it. It would become a normal feature of the company's business to obtain payment of rent in advance in certain leases. The fact that some amount may be payable to a head lessee in the event that a lease is terminated before its expiration date is not considered to be a feature which affects the question of when the rent paid in advance is derived.

7. In the context of the operations of the business of the finance company it is considered that the possibility of having to make payment to head lessees is part and parcel of the conduct of the business and any amount so paid should the possibility materialize would qualify for deduction under sub-section 51(1). The position is not seen as any different from a trading enterprise which sells goods to customers on condition that, if the customer is not satisfied, the purchase price will be refunded. There can be little doubt that, in this situation, the sale price would represent income derived at the date of sale notwithstanding that the possibility exists that it may subsequently have to be refunded. Any refund so made would be a normal incident of carrying on the business and eligible for deduction under sub-section 51(1).

COMMISSIONER OF TAXATION
10 April 1986

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