TD 93/187 - Income tax: is a lease acceptable if the lessee or an associate has an option to purchase the shares of, or a controlling interest in, the lessor company?

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Australian Taxation Office

Taxation Determination TD 93/187

This Determination, to the extent that it is capable of being a 'public ruling' in terms of Part IVAAA of the *Taxation Administration Act 1953*, is a public ruling for the purposes of that Part . Taxation Ruling TR 92/1 explains when a Determination is a public ruling and how it is binding on the Commissioner. Unless otherwise stated, this Determination applies to years commencing both before and after its date of issue. However, this Determination does not apply to taxpayers to the extent that it conflicts with the terms of a settlement of a dispute agreed to before the date of issue of the Determination (see paragraphs 21 and 22 of Taxation Ruling TR 92/20).

Taxation Determination

Income tax: is a lease acceptable if the lessee or an associate has an option to purchase the shares of, or a controlling interest in, the lessor company?

1. No. IT 28 states that a lease which provides the lessee with an option to purchase the leased goods will be treated as a contract for the sale of the goods. This position was confirmed in IT 2051. IT 28 extended this treatment to arrangements which permitted or enabled the lessee to retain the use of the goods, for example, through the property in the goods passing to the lessee's nominee or agent.

2. It is considered that an arrangement under which the lessee or an associate may gain control of the company which holds the leased goods falls within this category, and hence will not be accepted as a lease. It would correspondingly be unacceptable if the lessor had a right or option to require the lessee or an associate to purchase the shares of, or a controlling interest in, the lessor company.

3. The lease payments will include outgoings of a capital nature which will not be deductible for income tax purposes. The lessee will be entitled to claim depreciation on the leased asset and any interest components of the lease payments.

4. This position is consistent with the decision in *Littlewoods Mail Order Stores Ltd. v. I.R. Commrs.* [1969] 3 All E.R. 855, (1969) 1 W.L.R. 1241, where part of the rent paid in relation to land which was owned by a subsidiary of the lessee was held to be capital. This case was accepted by Gibbs A.C.J. in *F.C. of T. v. South Australian Battery Makers Pty Ltd.* 78 ATC 4412, 8 ATR 879. The *South Australian Battery Makers case* decided that lease payments were fully deductible where the lessee was not itself the holder of an associated option to purchase the leased asset, would not itself benefit either directly or as a shareholder of the option holder from the exercise of the option, and was not a party to the arrangement under which the option arose. If such a situation arose today, it is considered that Part IVA would apply to treat the lease payments as having a significant non-deductible component.

Commissioner of Taxation
23/9/93

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Related Determinations:

Related Rulings: IT 28

Subject Ref: Leasing, options

Legislative Ref:

Case Ref: *Littlewoods Mail Order Stores Ltd. v. I.R.Commrs.* [1969] 3 All E.R. 855, (1969) 1 W.L.R. 1241; *F.C. of T. v. South Australian Battery Makers Pty Ltd* 78 ATC 4412

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