IT 337 - Improvements carried out by lessee - section 62A

TAXATION RULING NO. IT 337

IMPROVEMENTS CARRIED OUT BY LESSEE - SECTION 62A

F.O.I. EMBARGO: May be released

REF
H.O. REF: 79/6121 F350 DATE OF EFFECT:

B.O. REF: DATE ORIG. MEMO ISSUED: 17.02.82

F.O.I. INDEX DETAIL

REFERENCE NO:	SUBJECT REFS:	LEGISLAT. REFS:
I 1071114	LEASE - IMPROVEMENTS BY LESSEE	62A
	CASE 12 ATR 413	62A(4)
	CASE 81 ATC 4563	
	TOP OF THE CROSS CASE	

PREAMBLE

This ruling was issued as a consequence of the decision of the Federal Court of Australia in the case of FC of T v Top of the Cross Pty Ltd and Travel Holdings (Australia) Pty Ltd, reported at 81 ATC 4563; 12 ATR 413. This case dealt with the application of section 62A.

FACTS

2. The Federal Court of Australia by majority (Bowen C.J. and Ellicott J., Deane J. dissenting) dismissed the Commissioner's appeals from the judgment of the Supreme Court of New South Wales (Woodward J.), reported at 80 ATC 4167; 11 ATR 366; which allowed the companies' claims for deductions under section 62A of the Act. Subsequently, on 12 February 1982, the High Court of Australia refused to grant the Commissioner's application for special leave to appeal from the Federal Court's judgment.

3. Very briefly, the two companies are equal partners in a partnership, trading as T.H.F. Motels, which operate a motel/hotel chain of international standard in Australia. Under an agreement signed on 29 August 1969 the partnership obtained from the Commonwealth a lease of land adjacent to Tullamarine Airport, Melbourne upon which it erected the Tullamarine Travelodge Motel. The term of the lease was 30 years. The partnership also secured an authority under the Airports (Business Concessions) Act to operate the motel. Construction and furnishing etc of the motel was completed in October 1970 at a cost of $1,930,496 and commercial operations commenced soon afterwards.

4. The question in issue in the appeals was whether the companies were entitled to deductions under section 62A in respect of the costs incurred in constructing and fitting out the motel. As indicated above, the Federal Court, by majority, held that the cost of the motel, amortised over the period of the lease, is allowable as a deduction under section 62A.

5. The majority commenced their analysis by looking to the purpose of the enactment, having regard to the requirements of section 15AA of the Acts Interpretation Act 1901, to assist in determining the meaning of various key terms used in section 62A. Their Honours concluded that:

(a) there was a franchise granted authorising the companies to collect and retain revenues earned by the undertaking;

(b) the franchise was in consideration of the construction and maintenance of the undertaking; and

(c) the franchise required that the undertaking became the property of the franchisor, without compensation at the end of the period of the franchise.

Dean J., in dissent, concluded that:

(a) the overall arrangements did not, in themselves, effect a grant;

(b) neither the lease nor the franchise constituted a "franchise";

(c) if there were a franchise, neither the lease nor the authority required the companies to incur expenditure in erecting etc. the motel;

(d) the global approach which groups the building contract, lease and authority cannot be adopted because it is not possible to identify a grant, of the relevant authority, which required the companies to incur the subject expenditure and provided for the retention of resultant revenues.

6. A feature which adds to the significance of this case is the approach of the Federal Court to the application of section 15AA of the Acts Interpretation Act 1901. That section has been hailed elsewhere as a measure which should help to ensure that unintended taxation benefits are not conceded. This appears to be the first case where a court has taken the section into account.

7. Even without section 15AA it is a well established approach in construing a provision to have regard to its history and context in the Act. Here these aspects might suggest that, whatever purpose the section had, it must have been to allow deductions to a very limited class of taxpayers not already covered by the lease provisions. This is re-inforced by some of the words and phrases in section 62A. As the majority noted at pages 4572; 423, of the reasons for judgment the phrase "undertaking of public utility" in section 62A(4) seems appropriate to refer to a physical structure (here, presumably the building) rather than a business entity with fluctuating assets including goodwill. So much seems to be correct; while the words happily suggest a structure such as a

bridge or road they, and the words "construction and maintenance", are singularly inappropriate to describe the setting up of a motel business, bearing in mind the service nature of such a business, the personal exertions involved, the provision of working capital and management expertise. Then their honours suggest that "revenue earned by the undertaking" is to be read as revenue earned by means of the undertaking. Of course, a bare building is hardly an "undertaking" nor is it of utility to the public. While it may be in the public interest to have a large modern hotel/motel operating within the precincts of an airport, the business is essentially a private enterprise just as are such businesses as shops and service stations. Nor is it appropriate to speak of the taxpayer being authorised to collect and retain the revenue - the revenue comes to the proprietor of the business beneficially.

8. The court was invited to have regard to such matters. Instead, the majority (Bowen C.J. and Ellicott J.), observing that the section is directed towards relieving particular taxpayers from the burden of taxation, have chosen to give a very generous and liberal interpretation of the key words and phrases of the section. With respect, this is not a "purposive" reading of the section. Quite the contrary, their Honours' approach pre-empts any real enquiry into the purpose of the section as shown by legislative history, context in the Act and words actually used.

RULING

9. The Hight Court's refusal to grant to the Commissioner special leave to appeal requires the acceptance of the Federal Court's judgment. The application of the judgment will, of necessity, be limited by the terms of the section i.e. to franchises granted on or before 7 April 1978. Nevertheless, claims under section 62A should be critically examined to determine whether all the specific requirements of the section have been satisfied. Of course, amendment of assessments to apply the judgment should only be made where the taxpayer concerned, in addition to satisfying the tests of section 62A, has current rights of objection or appeal under Part V of the Act.

COMMISSIONER OF TAXATION

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