TD 2009/18EC - Compendium

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Ruling Compendium – TD 2009/18

This is a compendium of responses to the issues raised by external parties to draft TD 2009/D1 – Income tax: does the term 'real property' in paragraph 855-20(a) of the Income Tax Assessment Act 1997 include a leasehold interest in land?

This compendium of comments has been edited to maintain the anonymity of entities that commented on the draft ruling.

Summary of issues raised and responses

Issue No.	Issue raised	Tax Office Response/Action taken
1.	The final Determination should adopt the view that the expression 'real property' in paragraph 855-20(a) of the *Income Tax Assessment Act 1997* (ITAA 1997)[1] does not include a leasehold interest in land.	The final Determination continues to adopt the view taken in the draft Determination that, in the context of Division 855, the term 'real property' in paragraph 855-20(a) includes a leasehold interest in land. The Determination explains how that view has been reached. The responses below deal with specific issues raised in relation to that reasoning process.
2.	There is no clear intention for 'real property' in paragraph 855-20(a) to have a meaning different from its ordinary common law meaning (technical legal meaning), which does not include leasehold interests in land. The reference in paragraph 4.28 of the Explanatory Memorandum to Tax Laws Amendment (2006 Measures No. 4) Bill 2006 (the EM) [which as enacted introduced Division 855] to real property, 'within the ordinary meaning of that term', is a reference to the ordinary common law meaning (technical legal meaning) of 'real property'.	The Commissioner acknowledges in paragraph 5 of the draft Determination that the ordinary common law meaning (or technical legal meaning) of 'real property' in Australia does not include a leasehold interest in land. The quotes in paragraph 6 of the draft Determination were not seeking to suggest otherwise. They were merely noting a respected property law text author's view that the historical origins for treating leasehold interests in land as 'personal property' rather than 'real property' are almost entirely forgotten today and that author's view that for most legal purposes leases are today regarded as real property, not personal property. The Commissioner understood that author's second view to mean that for most legal purposes the law treats leases in a similar way to real property (in its technical legal meaning). To avoid confusion relating to the second quote in paragraph 6 of the draft Determination, that quote has been replaced with the following quote from Fitzgerald P and de Jersey J's judgment in *Re Greenway Park Developments Pty*

[1] All subsequent legislative references are to the ITAA 1997 unless otherwise indicated.

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		Ltd [1993] 2 Qd R 522 at 523 in paragraph 6 of the final Determination: > while in the historical development of the law leases have been characterised as 'chattels real' and thus personalty, the modern tendency has been to differentiate leases, or chattels real, from 'pure personalty' and to treat the law relating to leases as an element of the law of real property. While the Commissioner acknowledges in the draft Determination that the ordinary common law meaning (technical legal meaning) of 'real property' in Australia does not include a leasehold interest in land, the Commissioner does not accept that the reference in paragraph 4.28 of the EM to 'real property', 'within the ordinary meaning of that term', is intended to be a reference to the ordinary common law meaning (technical legal meaning) of 'real property'. The Commissioner considers that, in addition to the reasons set out in paragraphs 9 to 12 of the draft Determination and paragraphs 8 to 11 of the final Determination for concluding that 'real property' in paragraph 855-20(a) of the ITAA 1997 is intended to have a meaning that includes leasehold interests in land, the Explanatory Memorandum to Tax Laws Amendment (2009 Measures No. 4) Bill 2009 (the amendment's EM) provides further clear support for such a conclusion. The intent and effect of the amendment to section 855-20 of the ITAA 1997 in that Bill are explained in Table 5.9 of the amendment's EM at page 100 as follows: > A foreign resident is liable for CGT if the relevant CGT asset is 'taxable Australian property' (as defined). This includes real property in Australia. > **The amendment puts beyond doubt that 'taxable Australian real property' in this context includes a lease over land. This accords with the intended application of the provisions when introduced.** > A lease in this context would include a sublease. > The amendment applies in relation to CGT events happening on or after 20 May 2009, the date on which the amendment was first foreshadowed. > The amendment is to be disregarded for interpreting the provisions in their previous form in relation to CGT events happening before 20 May 2009. The effect of this is to ensure that no inference can be drawn from the amendment that the law operated differently before the amendment. This is important because **the intention of the**

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		amendment is not to change the existing law but merely to clarify how it was always intended to apply. [Emphasis added] The Commissioner considers that this clearly shows that 'real property' in paragraph 855-20(a) was always intended to have a meaning that includes leasehold interests in land. Therefore, the reference in paragraph 4.28 of the EM to 'real property', 'within the ordinary meaning of that term', cannot be a reference to the ordinary common law meaning (technical legal meaning) of 'real property' in Australia, which the Commissioner acknowledges does not include a leasehold interest in land. Paragraph 8 of the draft Determination, which refers to paragraph 4.28 of the EM, has been deleted to avoid any further confusion on this issue.
3.	It is not appropriate for the Commissioner to have recourse to extrinsic materials such as an explanatory memorandum to determine the meaning of 'real property' in paragraph 855-20(a) of the ITAA 1997 because that term is not ambiguous and adoption of the ordinary common law meaning (technical legal meaning) of that term would not lead to a result that is manifestly absurd or unreasonable. Thus, recourse to an explanatory memorandum for the desired purpose is not permissible under section 15AB of the *Acts Interpretation Act 1901* (the AIA).	Under the modern approach to statutory interpretation, and independently of section 15AB of the AIA, the common law permits recourse to extrinsic materials such as explanatory memoranda to assist in determining the meaning of a legislative provision. Moreover, the modern approach to statutory interpretation permits recourse to such extrinsic materials as part of consideration of the context ('context' being used in its widest sense) which the common law insists be considered in the first instance, not merely at some later stage when ambiguity might be thought to arise: see the High Court decisions of *CIC Insurance Ltd v. Bankstown Football Club Ltd* (1997) 187 CLR 384 at 408; 141 ALR 618 at 634-5; and *Newcastle City Council v. GIO General Ltd* (1997) 191 CLR 85 at 99-100 and 112-3; 149 ALR 623 at 631 and 641-2.
4.	If regard is had to extrinsic materials, it reveals that Division 855 was introduced to narrow the range of assets on which a foreign resident is subject to Australian CGT. This is consistent with the legislative history. Under the former Division 136, which Division 855 replaced, a leasehold interest in land was covered as land in Australia or 'an	While the Commissioner acknowledges that one aspect of Division 855's objects was the narrowing of the range of assets on which a foreign resident is subject to Australian CGT, the Commissioner does not accept that an exclusion of leasehold interests in land was part of that intended narrowing. The Commissioner considers that there is nothing within the extrinsic materials relating to Division 855 that shows that an exclusion of leasehold interests in land was part of the intended narrowing of the range of assets on which a foreign

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	interest in land in Australia, or a right, power or privilege to do with land in Australia', which were included in the categories of CGT assets having 'the necessary connection with Australia'. Whereas under Division 855, Parliament intentionally chose to use the narrower concept of 'real property', which has a technical legal meaning that does not include leasehold interests in land.	resident is subject to Australian CGT. On the contrary, the Commissioner considers that, in addition to the clear passages from the amendment's EM that are referred to in issue 2, there are a number of passages in the Treasurer's Press Release and the Second Reading Speech relating to Division 855's introduction that indicate an exclusion of leasehold interests in land was not part of the intended narrowing of the range of assets on which a foreign resident is subject to Australian CGT. Paragraph 4.4 of the EM states: This measure implements the Government's decision to reform the CGT treatment of foreign residents. The decision was announced in the Treasurer's Press Release No. 44 of 10 May 2005. That Treasurer's Press Release relevantly stated the following about that reform: The Government has decided to better target and strengthen the application of CGT to non-residents in Australia's domestic law practice by: • aligning Australia's law more closely with OECD practice through narrowing the current range of assets on which a non-resident is subject to Australian CGT to real property, and the business assets of Australian branches of a non-resident; and • protecting the integrity of these rules by applying CGT to non-portfolio interests in interposed entities (including foreign interposed entities), where the value of such an interest is wholly or principally attributable to Australian real property. **'Real property' for these purposes will be consistent with our treaty practice, extending to other Australian assets with a physical connection with Australia, such as mining rights and other interests related to Australian real property.** The proposed interposed entities rule will reinforce Australia's rights to tax Australian real property held by non-residents. **As the Government is preserving Australia's source country taxing rights over land**, it would not be appropriate to include an exemption from the measure where the gain on the sale of an interposed entity is subject to tax in listed countries, as was proposed in the Review of Business Taxation. … **The changes will enable Australia's tax treaties to be further aligned to the OECD standards.** [Emphasis added]

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		The Commissioner considers that statements in that document such as 'real property for these purposes will be consistent with our treaty practice, extending to … interests related to Australian real property' and 'the Government is preserving Australia's source country taxing rights over land' strongly indicate an exclusion of leasehold interests in land was not part of the intended narrowing of the range of assets on which a foreign resident is subject to Australian CGT. Further, given that, as is pointed out in paragraph 12 of the draft Determination and 11 of the final Determination, that all 41 of Australia's tax treaties that expressly deal with the alienation of real property cover the alienation of leasehold interests in land, the Commissioner considers the statement in the Second Reading Speech relating to Division 855's introduction that those amendments 'align Australia's domestic law with the approach adopted in Australia's tax treaties' also supports the view that an exclusion of leasehold interests in land was not part of the intended narrowing of the range of assets on which a foreign resident is subject to Australian CGT. See issue 6 of this compendium for further discussion of the relevance of Australia's tax treaty treatment of the alienation of leasehold interests in land.
5.	Contrary to what is said in paragraph 12 of the draft Determination, aligning Australia's tax laws more consistently with international (OECD) practice and with the approach adopted in Australia's tax treaties is not an object of Subdivision 855-A. The objects of that Subdivision are set out in subsection 855-5(1) as 'to improve (a) Australia's status as an attractive place for business and investment; and (b) the integrity of Australia's capital gains tax base.' Subsection 855-5(2) explains that aligning Australia's tax laws with international practice is merely one of the means by which those objects are achieved. Further, paragraph 855-5(2)(a) refers	As Pearce DC & Geddes RS 2006, *Statutory Interpretation in Australia*, 6th Ed., LexisNexis Butterworths, Australia, p. 33 states, 'like any other provision in legislation, a purpose or objects clause must be interpreted in its context.' As such, the Commissioner considers that subsection 855-5(1) must be read with subsection 855-5(2). Indeed, paragraph 4.6 of the EM indicates that paragraphs 855-5(1)(a) and (2)(a) are very much linked. It states that 'the amendments will encourage investment in Australia by aligning Australian law more consistently with international practice.' Thus, the Commissioner considers it reasonable to describe the aligning of Australia's tax laws more consistently with international practice as a key aspect of the objects of Subdivision 855-A. Further, the various extrinsic materials relating to the introduction to Division 855 referred to in issue 4, indicate that the reference to 'international practice' was intended to also encompass Australia's international tax treaty practice. For example, in the Treasurer's Press Release No. 44 of 10 May 2005 (referred to

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	only to 'international practice', not to international practice and Australia's tax treaties.	in paragraph 4.4 of the EM), which announced the Government decision to reform the CGT treatment of foreign residents, it was stated that the reform would align: Australia's law more closely with OECD practice through narrowing the current range of assets on which a non-resident is subject to Australian CGT to real property, and the business assets of Australian branches of a non-resident; and that **'real property for these purposes will be consistent with our treaty practice**, extending to … interests related to Australian real property'. [Emphasis added] Indeed, both the Second Reading Speech relating to Division 855's introduction and paragraph 4.7 of the EM state that the amendments are intended to align Australia's tax laws with the approach adopted in Australia's tax treaties. Thus, the Commissioner considers it reasonable to describe the aligning of Australia's tax laws more consistently with the approach adopted in Australia's tax treaties as a key aspect of the objects of Subdivision 855-A. Minor changes have been made to paragraph 12 of the draft Determination, now paragraph 11 in the final Determination, to make these points clearer.
6.	Contrary to what is said in paragraph 12 of the draft Determination, the specific inclusion of leasehold interests in the definition of 'real property' for the purposes of the 'alienation of property article' in Australia's tax treaties has no necessary implication for the interpretation of the term 'real property' in Division 855. These tax treaty definitions of 'real property' do not apply in the context of Division 855.	The Commissioner does not suggest in paragraph 12 of the draft Determination that where an Australian tax treaty applies to a foreign resident in relation to a CGT event that the term 'real property' in section 855-20 has the meaning that term has for the purposes of that tax treaty. However, in the context where: • Division 855 and the extrinsic materials relating to it indicate that Subdivision 855-A was intended to align Australia's tax laws more consistently with international (OECD) practice and with the approach adopted in Australia's tax treaties; • there is nothing within Division 855 or the extrinsic materials relating to it that shows that an exclusion of leasehold interests in land was part of the intended narrowing of the range of assets on which a foreign resident is subject to Australian CGT. On the contrary, those extrinsic materials indicate an

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		exclusion of leasehold interests in land was not part of the intended narrowing of the range of assets on which a foreign resident is subject to Australian CGT; • as is pointed out in paragraph 12 of the draft Determination and paragraph 11 of the final Determination, all 41 of Australia's tax treaties that expressly deal with the alienation of real property cover the alienation of leasehold interests in land, with 39 of those doing so by defining 'real property' to include leasehold interests in land; and • as is also pointed out in paragraph 12 of the draft Determination and paragraph 11 of the final Determination, international (OECD) practice, as evidenced by the OECD Model Convention with respect to Taxes on Income and on Capital, uses the concept of alienation of 'immoveable property' (rather than 'real property') which has long been accepted to include leasehold interests in land, the Commissioner considers this all strengthens the view that Parliament intended 'real property' in the context of Division 855 to include leasehold interests in land. If the meaning of 'real property' in the context of Division 855 was construed narrowly so as to exclude leasehold interests in land, the operation of Division 855 (so far as leasehold interests in land situated in Australia are concerned) would be, contrary to what was intended, less, rather than more, aligned with Australia's tax treaties and the OECD Model Tax Convention. The Commissioner's view that 'real property' in the context of Division 855 includes leasehold interests in land assists to achieve a key aspect of the objects of Subdivision 855-A, whereas the contrary view would frustrate such achievement. Minor changes have been made to paragraph 12 of the draft Determination, now paragraph 11 of the final Determination, to make these points clearer.
7.	The fact that when Australia's tax treaties treat leases as 'real property' they do so by expressly defining 'real property' to include leasehold	The Commissioner's view as to why the fact that all 41 of Australia's tax treaties that expressly deal with the alienation of real property cover the alienation of leasehold interests in land, with 39 of those doing so by defining 'real property' to include

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	interests in land, makes it more, not less, likely Parliament never intended 'real property' in the context of section 855-20 to cover leases.	leasehold interests in land, strengthens, rather than weakens, the view that Parliament intended 'real property' in the context of Division 855 to include leasehold interests in land, is discussed in issue 6.
8.	Although it is accepted that leasehold interests in land are immoveable property, paragraph 12 of the draft Determination is wrong in suggesting Parliament used the term 'real property', but actually intended to refer to 'immoveable property.	The Commissioner does not suggest in paragraph 12 of the draft Determination and paragraph 11 of the final Determination that Parliament intended to refer to 'immoveable property' when it referred to 'real property'. The reference in that paragraph to 'immoveable property' was made in the context of noting that: • Division 855 and the extrinsic materials relating to it indicate that Subdivision 855-A was intended to align Australia's tax laws more consistently with international (OECD) practice and with the approach adopted in Australia's tax treaties; • international (OECD) practice, as evidenced by the OECD Model Tax Convention, uses the concept of alienation of 'immoveable property' (rather than 'real property') which has long been accepted to include leasehold interests in land; and • all 41 of Australia's tax treaties that expressly deal with the alienation of real property cover the alienation of leasehold interests in land, with 39 of those doing so by defining 'real property' to include leasehold interests in land. It was thus noted that interpreting 'real property' in the context of Division 855 to include leasehold interests in land would be consistent with the effect of both the Model OECD practice and Australia's tax treaty practice in relation to alienation of leasehold interests in land, whereas adoption of a contrary interpretation would produce a result that was inconsistent with both such practices.
9.	Contrary to what is said in paragraphs 10 and 11 of the draft Determination, there is nothing inconsistent, anomalous or seemingly absurd with the differing result that a foreign resident granting a lease over land situated in Australia would be	The Commissioner's view is that there is nothing in Division 855 or the extrinsic materials relating to it that indicate that Parliament intended such a differential outcome. Further, as the High Court noted in *CIC Insurance Ltd v. Bankstown Football Club Ltd* (1997) 187 CLR 384 at 408; 141 ALR 618 at 635:

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	subject to Australian CGT in respect of that dealing, whereas a foreign resident dealing in the leasehold interest itself (for example, by way of assignment) would not be subject to Australian CGT in respect of that dealing, were 'real property' to have its technical legal meaning in the context of Division 855. Indeed, the terms of paragraph 855-10(2)(c), which provides that the CGT asset in relation to which CGT event F1 happens is the CGT asset that is the subject of the lease, is more consistent with the view that a leasehold interest in land is not 'real property' in the context of Division 855 than the opposite view. If a leasehold interest in land were 'real property' in the context of Division 855, paragraph 855-10(2)(c) would focus on the leasehold interest itself, rather than the CGT asset that is the subject of the lease.	improbability of result may assist the court in preferring to the literal meaning an alternative construction which is reasonably open and more closely conforms to the legislative intent. Paragraph 855-10(2)(c) recognises that CGT event F1 may also apply to the granting of a lease over property other than land. In other words, apart from in relation to 'taxable Australian real property' under section 855-20 (to which the meaning of 'real property' is relevant), CGT event F1 could apply to one of the other categories of CGT assets that are 'taxable Australian property' (see section 855-15). For example, CGT event F1 could apply to the granting, renewal or extension of a lease over a CGT asset (other than land) that: (a) you have used at any time in carrying on a business through a permanent establishment (within the meaning of section 23AH of the *Income Tax Assessment Act 1936*) in Australia; and (b) is not covered by item 1, 2 or 5 of the table in section 855-15. See item 3 of the table in section 855-15. Indeed, former Division 136 of the ITAA 1997, which Division 855 replaced, contained a rule of similar effect to paragraph 855-10(2)(c). Under former section 136-10, 'the CGT asset the subject of the lease' was the CGT asset in the context of CGT event F1 that had to be assessed as to whether it had the 'necessary connection with Australia' in order for a foreign resident to be able to make a capital gain or capital loss from that CGT event. Further, just like paragraph 855-10(2)(c), former section 136-10 recognised that CGT event F1 may also apply to the granting of a lease over property other than land. This is evident from the last column of the row in the table in former section 136-10 relating to CGT event F1. That column recognised, for the purposes of CGT event F1, that a CGT asset the subject of the lease that came within the description of category numbers 1 or 2 in the table in former section 136-25 had the 'necessary connection with Australia'. Category number 1 in the table in former section 136-25 read: Any of these:

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		(a) land, or a building or structure, in Australia; (b) an interest in land in Australia, or a right, power or privilege to do with land in Australia; (c) a *stratum unit in Australia, or an interest in a stratum unit in Australia; (d) a *share in a company that owns a building on land in Australia that gives you a right to occupy a flat or home unit in the building. Category number 2 in that table read: A *CGT asset that you have used at any time in carrying on a *business through a *permanent establishment in Australia. It is evident that a leasehold interest in land in Australia clearly came within paragraph (b) of category number 1 in the table in former section 136-25. Thus, former Division 136 recognised a leasehold interest in land in Australia was a CGT asset that had the necessary connection with Australia that could be relevant for many CGT events (including, for example, CGT event A1 happening on the assignment of such a leasehold interest), even though for the purposes of CGT event F1 the focus was instead on whether the CGT asset the subject of the lease (for example, land) has the necessary connection with Australia (for example, as land in Australia). Similarly, it is the Commissioner's view that Division 855 recognises a leasehold interest in land in Australia as 'real property' situated in Australia for the purposes of paragraph 855-20(a), and so therefore 'taxable Australian real property' and 'taxable Australian property', even though for the purposes of CGT event F1 the focus is instead on whether the CGT asset the subject of the lease (for example, land) is one of the categories of 'taxable Australian property' (for example, as real property situated in Australia and so 'taxable Australian real property'). Nothing turns on the fact that subsection 855-10(2) does not refer to CGT events F2 to F5, which also relate to leases. Unlike former sections 136-10 and 136-15 which were comprehensive in specifying for each relevant CGT event what the CGT asset was that had to be assessed as to whether it had the 'necessary connection with Australia', subsection 855-10(2) specifies the CGT asset in relation to which a CGT

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		event happens for only four CGT events. Paragraph 4.20 of the EM does, however, indicate that, like for CGT event F1, it is the CGT asset that is the subject of the lease which is the CGT asset in relation to which CGT events F2 to F5 happen for the purposes of applying subsection 855-10(1). Again, that is consistent with the effect of the entries for those CGT events in the table in former section 136-10.
10.	If 'real property' in the context of section 855-20 included leasehold interests in land, paragraph (b) of the definition of 'mining, quarrying or prospecting right' would be entirely superfluous. It is a general principle of statutory construction that words should not be considered as superfluous.	Paragraph 855-20(b) provides that a CGT asset is 'taxable Australian real property' if it is: a *mining, quarrying or prospecting right (to the extent that the right is not real property), if the minerals, *petroleum or quarry materials are situated in Australia, The words '(to the extent that the right is not real property)' recognise there are at least some 'mining, quarrying or prospecting rights' that can come within the meaning of 'real property' in the context of section 855-20. Paragraph (b) of the definition of 'mining, quarrying or prospecting right' in subsection 995-1(1) provides that 'a lease of land that allows the lessee to mine, quarry or prospect for minerals, petroleum or quarry materials on the land' is a 'mining, quarrying or prospecting right'. That paragraph would not be superfluous if 'real property' in the context of section 855-20 includes leasehold interests in land. The definition of 'mining, quarrying or prospecting right' pre-dates the introduction of Division 855 in 2006. The current definition of 'mining, quarrying or prospecting right' was inserted in subsection 995-1(1) in 2001 as a consequential amendment relating to the introduction at that time of a uniform capital allowance system, which includes Division 40. Paragraph 40-30(2)(a) provides that a 'mining, quarrying or prospecting right' that is not trading stock is a depreciating asset. As such, the definition of 'mining, quarrying or prospecting right' (including paragraph (b)) has significant relevance for the application of Division 40 which, among other things, provides deductions for the decline in value of depreciating assets.

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11.	Suggest adjusting the reference, in the second sentence of footnote 11 to paragraph 7 of the draft Determination, to Fitzgerald P and de Jersey J's judgment in *Greenway Park Development Pty Ltd v Cridland* [1992] QCA 430 to make it clear that whether or not a lease is personal property within the meaning of a particular statute is *most likely* to be determined by reference to the statutory context.	Changes in line with the suggestion have been made to the second sentence of footnote 11 of the final Determination.
12.	Paragraph 9 of the draft Determination refers to pastoral leases without qualification. However, *Wik Peoples v Queensland* (1996) 187 CLR 1 indicates that certain pastoral leases are not leasehold interests as a matter of common law.	The word 'certain' has been added to qualify the reference to 'pastoral leases' in paragraph 8 of the final Determination.