

TD 2009/18 - 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?

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! This determination contains references to repealed provisions, some of which may have been re-enacted or remade. The determination has effect in relation to the re-enacted or remade provisions. Paragraph 32 in TR 2006/10 provides further guidance on the status and binding effect of public rulings where the law has been repealed or repealed and rewritten. Australia's tax treaties and other agreements except for the Taipei Agreement are set out in the Australian Treaty Series. The citation for each is in a note to the applicable defined term in sections 3AAA or 3AAB of the International Tax Agreements Act 1953.

! This document has changed over time. This is a consolidated version of the ruling which was published on *21 October 2009*



Taxation Determination

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?

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This publication (excluding appendixes) is a public ruling for the purposes of the *Taxation Administration Act 1953*.

A public ruling is an expression of the Commissioner's opinion about the way in which a relevant provision applies, or would apply, to entities generally or to a class of entities in relation to a particular scheme or a class of schemes.

If you rely on this ruling, the Commissioner must apply the law to you in the way set out in the ruling (unless the Commissioner is satisfied that the ruling is incorrect and disadvantages you, in which case the law may be applied to you in a way that is more favourable for you – provided the Commissioner is not prevented from doing so by a time limit imposed by the law). You will be protected from having to pay any underpaid tax, penalty or interest in respect of the matters covered by this ruling if it turns out that it does not correctly state how the relevant provision applies to you.

[Note: This is a consolidated version of this document. Refer to the Tax Office Legal Database (<http://law.ato.gov.au>) to check its currency and to view the details of all changes.]

Ruling

1. Yes. In the context of Division 855 of the *Income Tax Assessment Act 1997* (ITAA 1997),¹ the term ‘real property’ in paragraph 855-20(a) includes a leasehold interest in land.

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

TD 2009/18

Date of effect

2. This Determination applies to years of income commencing both before and after its date of issue. However, this Determination will not apply in relation to CGT events happening on or after 20 May 2009. For such CGT events, an amendment to paragraph 855-20(a) of the ITAA 1997 made by the *Tax Laws Amendment (2009 Measures No. 4) Act 2009* puts beyond doubt that a lease of land, if the land is situated in Australia, is 'real property situated in Australia' for the purposes of paragraph 855-20(a) of the ITAA 1997. This Determination will also 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 this Determination (see paragraphs 75 and 76 of Taxation Ruling TR 2006/10).

Commissioner of Taxation

26 August 2009

Appendix 1 – Explanation

1 This Appendix is provided as information to help you understand how the Commissioner's view has been reached. It does not form part of the binding public ruling.

Explanation

3. The effect of subsection 855-10(1) is that a capital gain or capital loss from a CGT event that happens in relation to a CGT asset that is not 'taxable Australian property' is disregarded if you are a foreign resident, or the trustee of a foreign trust for CGT purposes, just before the CGT event happens. The categories of CGT assets that are taxable Australian property are set out in section 855-15.² 'Taxable Australian real property' is one such category.³ Section 855-20⁴ provides that a CGT asset is taxable Australian real property if it is:

- (a) real property situated in Australia; or
- (b) 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.

4. 'Real property' is not defined in the ITAA 1997. When a term used in legislation has acquired an established legal meaning, prima facie, that term will be interpreted in accordance with that meaning unless a contrary intention appears from the context.⁵

5. The technical legal meaning of 'real property' in Australia has its origins in medieval English common law inherited on British colonisation. Under that law, a distinction developed between 'real property' and 'personal property' based on the common law remedies then available for the recovery of tangible objects:

If a person dispossessed of an object could recover that object (the *res*) as of right it was classified as real property. The distinguishing characteristic of real property was the quality of being specifically recoverable in a 'real' action. Objects not so recoverable were regarded as personal property. A person dispossessed of such objects had a 'personal' action for damages against the wrongdoer, but was not entitled to an order requiring the wrongdoer to deliver the actual object. Since only land was specifically recoverable under the early common law, it followed that the category of real property was limited to land.⁶

...

Historically, leaseholds were regarded as personal property for the reason that the early law did not permit the dispossessed leaseholder to recover the land itself. The lessee was limited to an action for damages, mainly because leases were seen as personal commercial arrangements outside the rigid feudal structure of landholding. In time [by the late 15th century],⁷ the leaseholder was enabled to recover the land itself through the action of ejectment, but by that time the anomalous classification of leaseholds as personal property was too well established to be overturned.⁸

² 'Taxable Australian property' is defined in subsection 995-1(1) as having the meaning given by section 855-15.

³ Item 1 of the table in section 855-15.

⁴ 'Taxable Australian real property' is defined in subsection 995-1(1) as having the meaning given by section 855-20.

⁵ *Attorney-General (NSW) v. Brewery Employees' Union of NSW* (1908) 6 CLR 469 per O'Connor J at 531.

⁶ Edgeworth B, Rossiter CJ, Stone MA 2004, *Sackville and Neave Property Law: Cases and Materials*, 7th Ed., LexisNexis Butterworths, Australia, pp. 55-56.

⁷ Butt, PJ 2006, *Land Law*, 5th Ed., Lawbook Co., Sydney, p. 93; Hepburn, SJ 2008, *Australian Property Law: Cases, Materials and Analysis*, LexisNexis Butterworths, Australia, p. 258.

⁸ Edgeworth B, Rossiter CJ, Stone MA 2004, *Sackville and Neave Property Law: Cases and Materials*, 7th Ed., LexisNexis Butterworths, Australia, p. 58.

6. Today, however, 'the historical origins of leaseholds as personal property are almost entirely forgotten.'⁹ Indeed:

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.¹⁰

7. Having regard to the terms, objects and context¹¹ of Division 855, the Commissioner considers that it is clear that 'real property' in paragraph 855-20(a) is intended to include leasehold interests in land even though such interests do not come within the technical legal meaning of 'real property'. Evidence of this intention can be found within Division 855 and from its surrounding context.

8. Firstly, there is nothing within Division 855 (or its extrinsic materials) to indicate that Parliament sought to distinguish between the CGT treatment of freehold and leasehold interests in land situated in Australia (for example, CGT event A1 in section 104-10 happening in relation to a leasehold interest versus CGT event A1 happening in relation to a freehold interest). This is consistent with an intention for the term 'real property' in paragraph 855-20(a) to include leasehold interests in land. Indeed, there are vast areas of Australia in which the most common interest in land is a leasehold interest (for example, certain pastoral leases and the Australian Capital Territory).

9. Secondly, the CGT treatment of leases would be inconsistent and anomalous if the meaning of 'real property' in the context of Division 855 was construed narrowly so as to exclude leasehold interests. Subsection 855-10(2) sets out for various CGT events what the CGT asset is in relation to which the particular CGT event happens. Paragraph 855-10(2)(c) provides that for CGT event F1 (about granting a lease) the CGT asset in relation to which that CGT event happens is the CGT asset that is the subject of the lease. Therefore, if a foreign resident grants a lease over land situated in Australia, the granting of that lease (CGT event F1) is a CGT event that happens in relation to 'taxable Australian real property'. Accordingly, the foreign resident cannot disregard any capital gain or loss from the granting of that lease.¹²

10. It is highly unlikely that Parliament intended to subject a foreign resident granting a lease over land situated in Australia to CGT in respect of that dealing but not to so subject a foreign resident dealing in the leasehold interest itself (for example, by way of an assignment). There is nothing in Division 855 or the extrinsic materials relating to it that indicate that Parliament intended such a differential outcome. This seemingly absurd outcome would arise if 'real property' were to have its technical legal meaning in the context of Division 855, and therefore strengthens the view that Parliament intended 'real property' to include leasehold interests in that context.

⁹ Butt, PJ 2006, *Land Law*, 5th Ed., Lawbook Co., Sydney, p. 95. See also Halsbury's Laws of Australia, 2009, definition of 'real property', LexisNexis, paragraph [355-10] and Hepburn, SJ 2008, *Australian Property Law: Cases, Materials and Analysis*, LexisNexis Butterworths, Australia, p. 258.

¹⁰ *Re Greenway Park Developments Pty Ltd* [1993] 2 Qd R 522 at 523, per Fitzgerald P and de Jersey J.

¹¹ The importance of looking at context first and not merely as an aid to the resolution of ambiguity was emphasised by the High Court in *CIC Insurance Ltd v. Bankstown Football Club Ltd* (1997) 141 ALR 618 at 634-5. See also *Re Greenway Park Developments Pty Ltd* [1993] 2 Qd R 522; [1992] QCA 430 in which Fitzgerald P and de Jersey J relevantly noted 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. Indeed, they concluded that, in the context before them, leasehold interests in land were not 'personal property'.

¹² Subsection 855-10(1).

11. Thirdly, a key aspect of the objects of Subdivision 855-A is to align Australia's tax laws more consistently with international (OECD) practice and with the approach adopted in Australia's tax treaties.¹³ In this respect, it is noted that Article 13 (alienation of immoveable property) of the OECD Model Convention with respect to Taxes on Income and on Capital¹⁴ assigns taxing rights to the contracting state in which the 'immovable property' is situated. 'Immovable property' is defined in Article 6 primarily by reference to the law of the contracting state in which the property in question is situated, and has long been accepted to include leasehold interests in land.¹⁵ Further, of Australia's 41 tax treaties¹⁶ that expressly deal with the alienation of real property,¹⁷ 39 define 'real property' to include leasehold interests in land¹⁸ and the other two cover the alienation of leasehold interests by referring to direct interests in land.¹⁹ Therefore, 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. This strengthens the view that Parliament intended 'real property' in the context of Division 855 to include leasehold interests in land. Such an interpretation assists to achieve a key aspect of the objects of Subdivision 855-A, whereas the contrary view would frustrate such achievement.

12. In light of the above, the Commissioner considers that 'real property' in paragraph 855-20(a) includes a leasehold interest in land.

¹³ See paragraph 855-5(2)(a), paragraphs 4.6 and 4.7 of the Explanatory Memorandum to the Tax Laws Amendment (2006 Measures No. 4) Bill 2006 (the EM), the Second Reading Speech relating to that Bill's introduction and the Treasurer's Press Release No. 44 of 10 May 2005 (referred to in paragraph 4.4 of the EM), which announced the Government decision to reform the CGT treatment of foreign residents.

¹⁴ OECD Committee on Fiscal Affairs, Model Convention with respect to Taxes on Income and on Capital, 17 July 2008.

¹⁵ *Freke v. Lord Carbery* (1873) LR 16 Eq 461; *Haque v. Haque (No. 2)* (1965) 114 CLR 98.

¹⁶ The tax treaties are contained in the schedules to the *International Tax Agreements Act 1953*.

¹⁷ Australia's only other non-Airline Profits tax treaty (the German Agreement) does not contain an 'Alienation of property' article. However, it is worth noting that 'income from real property' in article 6 of that agreement includes 'income from leases of land': see paragraph 2 of the Protocol to that agreement.

¹⁸ The Russian Agreement defines 'real property' to include 'land and any other interest in or over land', which includes a leasehold interest in land: see paragraphs 13(1) and 6(2).

¹⁹ See article 13 of the Swiss Agreement and article 13 and paragraph 6(2) of the Malaysian Agreement.

Appendix 2 – Alternative views

❶ *This Appendix sets out alternative views and explains why they are not supported by the Commissioner. It does not form part of the binding public ruling.*

Alternative view

13. The alternative view is that 'real property' in paragraph 855-20(a) should be construed according to its technical legal meaning. The technical legal meaning of real property does not include leasehold interests in land. Therefore, under the alternative view, a leasehold interest in land situated in Australia is not 'real property' under paragraph 855-20(a).

14. As noted in the Explanation section of this Determination, the Commissioner considers that this alternative view is not consistent with the terms, objects and context of Division 855, which clearly indicate that leasehold interests in land are intended to be 'real property' under paragraph 855-20(a). On the contrary, applying the technical legal meaning of 'real property' in the context of Division 855 would produce unintended and anomalous outcomes in relation to the treatment of leases and would frustrate achievement of one of the key aspects of the objects of Subdivision 855-A.

References

Previous draft:

TD 2009/D1

Related Rulings/Determinations:

TR 2006/10

Subject references:

- capital gains
- CGT taxable Australian property
- foreign resident
- land
- leasehold
- real property

Legislative references:

- TAA 1953
- ITAA 1997
- ITAA 1997 104-10
- ITAA 1997 Div 855
- ITAA 1997 Subdiv 855-A
- ITAA 1997 855-5(2)(a)
- ITAA 1997 855-10(1)
- ITAA 1997 855-10(2)
- ITAA 1997 855-10(2)(c)
- ITAA 1997 855-15
- ITAA 1997 855-20
- ITAA 1997 855-20(a)
- ITAA 1997 995-1(1)
- International Tax Agreements Act 1953
- International Tax Agreements Act 1953 Sch 9
- International Tax Agreements Act 1953 Sch 15
- International Tax Agreements Act 1953 Sch 16
- International Tax Agreements Act 1953 Sch 46
- Tax Laws Amendment (2009 Measures No. 4) Act 2009

Case references:

- Attorney-General (NSW) v. Brewery Employees' Union of NSW (1908) 6 CLR 469; (1908) 14 ALR 565; [1908] HCA 94
- CIC Insurance Ltd v. Bankstown Football Club Ltd (1997) 187 CLR 384; (1997) 141 ALR 618; [1997] HCA 2
- Freke v. Lord Carbery (1873) LR 16 Eq 461
- Haque v. Haque (No. 2) (1965) 114 CLR 98
- Re Greenway Park Developments Pty Ltd [1993] 2 Qd R 522; [1992] QCA 430

Other references:

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ATO references

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