

Revenue Rulings

Lease Provisions - Meaning of 'Rent Reserved'

Revenue Ruling DA.050

Ruling history	
Ruling no.	DA.050
Status	Current
Issued date	March 2010
Replaces	-
Dates of effect	
From	21 November 2008
To	-

Preamble

Section 7(1)(b)(v) of the *Duties Act 2000* (the Act) was amended in 2009 (with effect from 21 November 2008) to ensure that certain leasing arrangements are not used as a mechanism for avoiding duty.

Under section 7(1)(b)(v) of the Act, duty is now payable on the grant of a lease of land in Victoria if consideration other than rent reserved is paid or agreed to be paid, either in respect of the lease or in respect of –

- (a) a right to purchase the land or a right to a transfer of the land;
- (b) an option to purchase the land or an option for the transfer of the land;
- (c) a right of first refusal in respect of the sale or transfer of the land;
- (d) any other lease, licence, contract, scheme or arrangement by which the lessee, or an associated person of the lessee, obtains any right or interest in the land that is the subject of the lease other than the leasehold estate.

Section 3(1) of the Act defines the term 'rent reserved' to mean the rent paid or payable during the term of the lease and any amount paid or payable for the right to use the land under the lease. The following examples are cited in the definition as amounts paid for the right to use the land under the lease –

- (a) rates;
- (b) charges;
- (c) taxes;
- (d) maintenance;
- (e) utilities;
- (f) legal costs required to be paid by the lessee on behalf of the lessor in relation to the grant of the lease;
- (g) insurance premiums;
- (h) marketing costs;
- (i) car park contributions.

The purpose of this Ruling is to provide guidance on the meaning of the term 'rent reserved' and to explain what factors the Commissioner of State Revenue (the Commissioner) will take into account in determining

whether an amount payable under a lease falls within that term. The Ruling also sets out additional examples of payments made under a lease that would qualify as payments for the use of land and therefore rent reserved for the purposes of section 7(1)(b)(v) of the Act.

Ruling

Rent is typically payable under a lease in periodic instalments over the term of the lease. However, the Commissioner recognises that it may be commercially advantageous for a lessee to make an upfront payment of rent on a discounted basis at the commencement of a lease. Provided the upfront payment is rent in advance and not other consideration (such as a premium) for the grant of the lease, the Commissioner will regard the payment as a payment of rent under the lease.

In determining whether an upfront payment made by a lessee to a lessor is rent or other consideration for the grant of a lease, the Commissioner will have regard to the nature and circumstances of the transaction as a whole, including the value of the underlying land the subject of the lease, the amount paid and whether any portion of it is refundable on a termination of the lease before expiry of the term, how the payment was calculated and the duration of the lease. Where a lessee can satisfy the Commissioner that the upfront payment comprises the net present value of a bona fide market rental over the term of the lease and is not referable to the value of the freehold, the Commissioner will regard the payment as rent reserved. In considering this, the duration of the lease will often be relevant because, for example, it would not be usual for a lessee to fully pay the 'rent' in advance on a long term lease such as a lease for 99 years. An upfront payment on the grant of a long term lease is more likely to be capital in nature and based on the freehold value of the underlying land rather than the present value of the leasehold.

Besides rent, the definition of rent reserved under section 3(1) of the Act identifies other payments made for the right to use land under a lease. The Commissioner regards the items cited in the definition as being illustrative of the types of payments which

fall within the meaning of rent reserved. The list is not exhaustive and, depending on the terms of a particular lease and the facts and circumstances of a particular case, may include other amounts, provided they are payments made by the lessee for or in connection with the use of the land under the lease. Examples of other items could include –

- (a) a bond or guarantee paid by a lessee to a lessor to secure the lessee's obligations under the lease, including 'make good' payments on the conclusion of the lease;
- (b) amounts paid by a lessee to a lessor in respect of the installation or upgrade of services and utilities (such as gas, water, telephone, electricity);
- (c) contributions to expenses for the maintenance of common areas;
- (d) promotional levies and security costs; and
- (e) other costs required to be paid by the lessee to or on behalf of the lessor (e.g. the legal costs for drafting, executing and registering the lease or the costs payable in relation to the appointment of an independent expert to resolve a dispute under the lease).

In determining whether any other payment falls within the definition of rent reserved, the Commissioner will have regard to the nature, size and frequency of the payment. While the Commissioner recognises that the form and manner of the payment may be relevant, greater reliance will be placed on whether in substance the payment was made for and in connection with the right to use the land under the lease. To this end, the Commissioner will consider whether the payment is in relation to an obligation that arises within the lease period and the lessee's use of the land and not in respect of an obligation that arises solely on the grant of the lease.

The above examples and considerations are provided as a guide only and are not an exhaustive list of the matters or factors the Commissioner may consider in determining the application of section 7(1)(b)(v) of the Act. A taxpayer who is uncertain of the application of this section to their particular circumstances may apply to the Commissioner for a private ruling in accordance with the guidelines set out in Revenue Ruling GEN-009. In each case, the onus is on the taxpayer to provide the Commissioner with the necessary information to make an informed decision as to whether the grant of a lease is a dutiable transaction under Chapter 2 of the Act.

Please note that rulings do not have the force of law. Each decision made by the State Revenue Office is made on the merits of each individual case having regard to any relevant ruling. All rulings must be read subject to Revenue Ruling GEN-001.