PwC Stamp Duty Newsletter

2017 Issue 1

In brief

In this update we outline the key stamp duty changes introduced by the State Revenue Legislation Amendment Act 2017 (NSW). The Bill passed on 4 April 2017 and received royal assent on 11 April 2017. The amendments have effect from the date of assent.

The various changes made to the Duties Act 1997 (NSW) ('the Act') include:

- More extensive landholder duty tracing rules to capture 'diamond' or 'blocker' structures
- Extending the landholder rules to cover combined put and call arrangements
- Expanding the aggregation rules to capture association via sub-trusts
- Strengthened general anti-avoidance rules which exclude inaction as a reasonable alternative when calculating the amount of duty avoided
- More onerous requirements for the change of trustee concession
- Expanded exemptions and concessions in very targeted areas.

Up until the amendments, the NSW landholder rules have had a narrower application in many respects than those in other jurisdictions. The changes expand the operation of the rules and make them comparable to the position in other states, although there are still significant differences, particularly in the detail.

We close off by discussing other aspects of the Act that could be improved and changed to provide certainty from a taxpayer and revenue perspective without significant policy changes.

In detail

More extensive tracing rules

The landholder duty rules operate to charge duty on the acquisition of a 50 per cent or more interest (whether alone, in aggregate with associated persons or as part of one arrangement with otherwise unrelated persons) in a company or unit trust which holds $2m or more of New South Wales land or interests in land (directly or indirectly). Where an entity holds land indirectly through other 'linked'

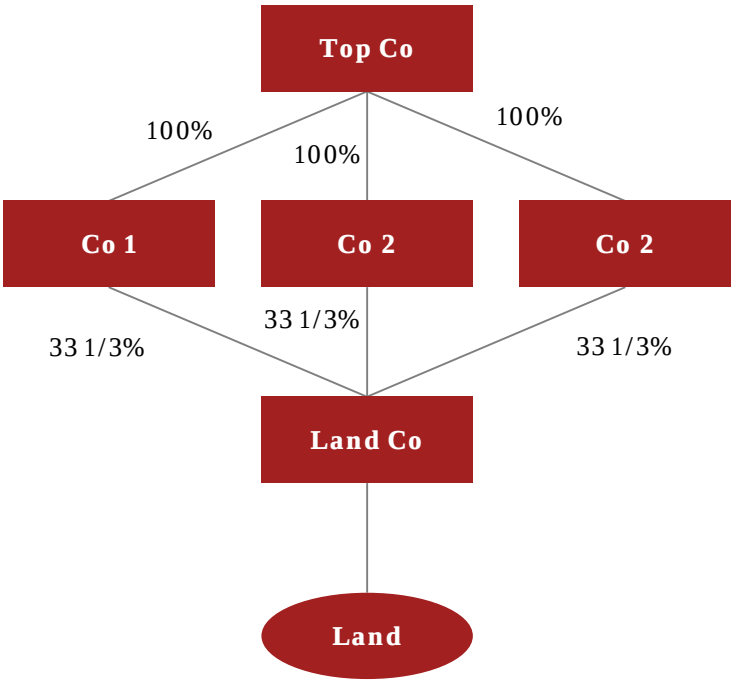
entities, the tracing rules determine whether the landholdings of the other entities are taken into account in determining if the first entity is a landholder.

Previously, a 'link' only existed where a person would be entitled to receive not less than 50 per cent of the unencumbered value of the property of another person in the event of a distribution of all the property of the other person. Accordingly, the top entity in a 'diamond' holding structure would not be a landholder if it wholly owned more than two other entities which in turn hold interests of less than 50 per cent each in a third entity which holds NSW land. This is illustrated in the diagram below.

However, under the new rules, the intention is that the top entity would now be a landholder due to the introduction of a test that links entities to the top entity (Top Co), if Top Co would be entitled to receive at least 50 per cent of the property of the entity that holds the land (Land Co) on a distribution of all of the property of all entities in a chain. This brings the NSW rules in line with, for example, the Victorian rules which operate similarly albeit with a lower interest threshold of 20 per cent.

Additionally, previously there was no express prohibition on taking liabilities into account when determining whether a link existed. Under the new rules, the liabilities of any entity in the chain must be disregarded. Accordingly, highly geared entities will no longer be able to rely on their gearing to prevent linking.

These changes do not apply retrospectively in that they do not apply to an acquisition in a landholder that is made on or after the commencement of the new rules if the acquisition is made in conformity with an agreement for sale first executed or option granted before the commencement. However, they do apply to 'fresh' acquisitions made in existing structures after the commencement date.



Top Co in the diagram is now a landholder under the new rules

Combined put and call option arrangements

Combined put and call arrangements over land are now treated in the same way as uncompleted agreements for the sale or transfer of NSW land for NSW landholder duty purposes. Each option holder

will be deemed to separately hold the whole of the land at full value even if it only has an option over the land. This aligns the position in NSW with Victoria.

Under the old rules the holder of a call option to acquire land only, until exercise, effectively held an interest in land having a value equal to the market value of the call option itself rather than the underlying land. For example, if a company entered into a put and call option with an arm's length party to acquire a $15m NSW property and paid a 10 per cent option fee of $1.5m, at the time it was granted the call option, the company would not have been a landholder under the old rules (as the value of any interest in land held was only $1.5m). That is, the company's shares could be acquired without duty. However, under the new rules this company will be deemed to be a landholder with a landholding value of $15m and a relevant acquisition of its shares would be subject to landholder duty.

Transitional provisions effectively quarantine put and call arrangements entered into before the commencement of the new rules.

Expanded aggregation rules

The aggregation rules apply to both transfer duty and landholder duty transactions and operate to charge duty on those transactions which would otherwise not be dutiable if considered in isolation. Whereas previously the aggregation rules applying to trusts only tested beneficiaries of the trusts themselves, the amended rules now apply to sub-trusts of the trusts. As a result, the following are now associated persons:

- Trustees of two trusts if any person is a common beneficiary of the trusts or their sub-trusts
- A natural person and a trustee if the natural person is a beneficiary of the trust for which the trustee acts as trustee or a sub-trust of the trust
- A company and a trustee if any related body corporate of the company is a beneficiary of the trust for which the trustee acts as trustee or a sub-trust of the trust
- A private company and a trustee if the company or its majority shareholder or director is a beneficiary of the trust for which the trustee acts as trustee or a sub-trust of the trust.

A person is considered to be a beneficiary of a sub-trust of a trust only if the interest in the trust that is held for the benefit of the beneficiary is an interest of 50 per cent or more.

Strengthened general anti-avoidance rules

Under the general anti-avoidance rules, a person is liable to pay the amount of duty avoided by the person as a result of a tax avoidance scheme that is of an artificial, blatant or contrived nature. The amount of duty payable is the amount that would have been payable or reasonably expected to have been payable by the person if the tax avoidance scheme had not been entered into or made.

The amount of duty avoided will now be calculated by reference to the duty arising under a reasonable alternative to the scheme, being an alternative that would have achieved the same economic or commercial result as the scheme. The amended test closes a gap under the old rules which would have allowed a taxpayer to argue that the transaction would not have occurred if duty was payable, and thus no duty was avoided as no duty would have arisen.

More onerous change of trustee concession rules

The change of trustee provisions provide for a nominal amount of duty ($50) to be paid on a transfer of dutiable property as a consequence of the retirement of a trustee or the appointment of a new trustee. The Chief Commissioner scrutinises such transactions closely and applies the rules strictly such that any transfer which does not fall squarely within the rules does not qualify for the concession. Such scrutiny has led to litigation in the past (in NSW and in other jurisdictions) on the construction of the provisions.

Under the old rules, to fall within the exemption the Chief Commissioner must be satisfied that the transfer is not part of a scheme for conferring an interest, in relation to the trust property, on a new trustee or any other person, whether as a beneficiary or otherwise, to the detriment of the beneficial

interest or potential beneficial interest of any person. Under the new rules, the Chief Commissioner must now also be satisfied that a transfer is also not part of a scheme to avoid duty and not cause any person to cease holding a beneficial interest (or potential beneficial interest) in that property. For what in theory (and practically) should be a simple concession to obtain, the extent of the amendments and scrutiny applied to exemption applications demonstrate that the concession is not merely a 'tick the box' exercise and that the Chief Commissioner administers these rules stringently. We highly recommend that you seek advice before undertaking any change of trustee. A significant duty liability could crystallise for which an exemption may not be available.

Additional exemptions and concessions

A number of very targeted exemptions and concessions have also been introduced. These include:

- An exemption from duty for the vesting of land occurring as a consequence of the merger of credit unions or of authorised deposit-taking institutions with mutual structures
- Extending existing exemptions from duty on transfers following the break-up of marriages and de facto relationships to cover such transfers to trustees under the Bankruptcy Act 1966 of the Commonwealth
- Extending existing exemptions from duty for transfers between family members of primary production land. This exemption will now cover transfers from a self managed superannuation fund where a member of the fund and the transferee are family members
- Nominal duty of $10 will now be payable on certain transfers of property to the custodian of a trustee of a self managed superannuation fund not in conformity with an agreement for sale or transfer where duty has been paid on the agreement and the purchaser under the agreement is the trustee.

Future changes to the Act

This round of changes has been a good opportunity for the Chief Commissioner to address a number of perceived gaps in the Act and by in large reaffirm the original policy intent of certain provisions. Now that this has been done, we believe the next round of changes should embrace a number of areas that could be improved and provide certainty from a taxpayer and revenue perspective without significant policy changes.

Custodians and the corporate reconstruction exemption

The corporate reconstruction exemption provisions only currently include custodians of managed investment schemes as being part of a "group". However, custodians are legitimately (and often required by other legislation) to be used in various commercial contexts. This includes, for example, other types of trusts (a simple unit trust including sub trusts of managed investment schemes), companies and sub custodian/nominee relationships. It makes sense to extend the rules to specifically provide relief for transactions involving custodians of all unit trusts and corporations not just managed investment schemes. It is unclear why the provisions are limited in this manner and what mischief this prevents.

Overseas entities and transactions

Australian stamp duty law is unique in having comprehensive 'long arm' land holder duty rules that can apply even if the transaction solely involves foreign bodies or the Australian land asset is far removed from the overseas target entity (for example, it is many levels down the corporate chain). Significant difficulties arise in applying the provisions given they have developed in an Australian centric manner. Given this, the rules struggle with concepts such as foreign hybrid entities, merger and amalgamation transactions and other foreign law concepts. Addressing these entities and transactions from a liability and exemption perspective would simplify the application of the provisions and provide certainty for foreign investors. Clearly enough, if a long arm tax is intended then it needs to address foreign law concepts.

Application of foreign purchaser surcharge duty to 'commercial' residential premises

Considerable uncertainty exists as to how the foreign purchaser surcharge duty applies to commercial residential premises. Student accommodation, timeshare, longer stay serviced apartments, retirement villages and aged care facilities do not always fall neatly in or out of the provisions. Often the analysis requires a thorough factual consideration of the premises in question delving into the minutiae of the included amenities and services provided. Given the policy underpinning the surcharge, it is difficult to understand why it should apply to these types of premises. Adopting an exemption to specifically remove these classes of assets from the regime would be welcomed and is already a feature of the Victorian regime.

Let's talk

For a deeper discussion of how these issues might affect your business, please contact:

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