

REAL PROPERTY CHANGES: RISK MANAGEMENT TIPS FOR SOLICITORS

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Changes concerning foreign residents

Foreign resident capital gains withholding payment

New withholding requirements for purchasers of certain property in Australia commenced on 1 July 2016. The Federal Government withholding tax is brought in by the *Tax and Superannuation Laws Amendment (2015 Measures No. 6) Act 2016* (Cth). It amends schedule 1 to the *Taxation Administration Act 1953* (Cth).

The reasoning behind the legislation is to capture some of the tax payable on capital gains by foreign residents. That tax has historically been difficult to recover after the funds from a sale of property go off shore.

A purchaser of a relevant CGT asset is required to withhold 10 per cent (or another amount specified) of the purchase price of the asset and remit that amount to the Australian Taxation Office (ATO). Failure to do so renders the purchaser liable to penalties and interest. A CGT asset for the purpose of withholding is defined as taxable Australian real property or an indirect Australian real property interest.

There are exclusions for real property or a company title interest with a market value of less than \$2 million. There are also defined exclusions concerning indirect Australian real property interests, such as approved stock exchange transactions.

All vendors disposing of real property/ company title interests are considered foreign residents unless they obtain a clearance certificate (even if they are actually Australian residents for other income tax purposes).

For indirect Australian real property interests, a purchaser must determine whether or not a vendor is a foreign resident based on:

- whether they have received a relevant declaration which they do not know to be false; or

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- Recent legislative changes require solicitors to consider additional factors when acting on transactions involving real property.
- The primary changes involve:
 1. foreign resident capital gains withholding payment;
 2. stamp duty surcharge and land tax surcharge;
 3. land tax assessment; and
 4. swimming pool compliance certificates.
- To avoid clients incurring unwarranted liabilities, solicitors should ensure that their clients are aware of, and comply with, the new legislative requirements.

- if they know, or have reasonable grounds to believe, the vendor is a foreign resident.

If all prerequisites are satisfied then the purchaser must remit to the ATO 10 per cent of the 'first element of the property's cost base' (the purchase price in most cases) to the purchaser. A request may be made to the ATO to withhold less than 10 per cent of the first element of the cost base by: the purchaser; the vendor (or grantor of an unexercised option); or an entity owed a debt by the vendor.

Risk management tips for solicitors

- Solicitors should familiarise themselves with clause 31 of the Contract for the Sale and Purchase of Land (2016 edition).
- As the withholding obligation falls on the purchaser, the purchaser must be

satisfied that the price represents the market value of the property for the purposes of applying the threshold exemption. Pay close attention to transactions where the purchase price is relatively close to the threshold amount (such as \$1.9 million). Such transactions are likely to fall under close scrutiny by the ATO. Similarly, pay close attention to properties to be sold at auction where the purchase price is not known. If the sale price is likely to be close to \$2 million, consider the potential for the withholding obligation to arise.

- When acting for either a purchaser or a vendor in a transaction concerning CGT assets, the safest course is to ensure a clearance certificate or relevant declaration is obtained as early as possible. Not obtaining a certificate/declaration or obtaining one too late may jeopardise or cause unnecessary complications or delays on settlement.
- In the case of real property transactions, the clearance certificate should be attached to the contract of sale on exchange by the vendor. If it is not attached, the purchaser's solicitor should advise the purchaser that if the vendor fails to provide a clearance certificate before completion, the purchaser's obligation to withhold arises even if the vendor is in fact an Australian resident or would otherwise be entitled to a CGT exemption.
- For indirect Australian real property interests, check that the purchaser does not know the foreign residency declaration to be false (for example, if the vendor has a foreign address and asks for the money to be transferred to a foreign bank account).
- Where the transaction includes GST considerations, be aware of the impact of GST on the calculation of any withholding amount and consider the need for the client to obtain financial advice.
- If acting for a foreign resident vendor (or a mortgagee of a property owned

by a foreign vendor) consider whether there are sufficient funds to discharge any mortgage or security and to also pay the 10 per cent withholding amount. If not, the mortgagee may refuse to discharge the mortgage and the settlement may be jeopardised.

- Consider referring your client for tax or accounting advice in appropriate cases.

Foreign resident stamp duty surcharge and land tax surcharge

It was announced in the 2016 NSW Budget that a 4 per cent stamp duty surcharge would be introduced to the purchase of residential property by 'foreign persons' from 21 June 2016. This surcharge is in addition to the duty ordinarily payable.

Foreign persons include individuals not ordinarily resident in Australia, persons who are not Australian citizens and who have been in Australia less than 200 days in the preceding 12 months, certain corporations, certain trusts and certain limited partnerships. Solicitors should be familiar with the definition of foreign persons. (For more information see: osr.nsw.gov.au/).

Foreign persons are also no longer entitled to the 12-month deferral of payment of stamp duty on off-the-plan purchases of residential property.

The surcharge applies to landholder transactions if:

- there is a landholder duty liability;
- one or more of the persons purchasing the interest is a foreign person; and
- at least part of the property owned by the landholder is residential land.

A land tax surcharge of 0.75 per cent will apply from the 2017 land tax year in respect of the taxable value of all residential land owned by a foreign person as at midnight 31 December in any year.

Risk management tips for solicitors

- Purchaser/transferee declarations must be completed by any person who enters into a transaction on or after 21 June 2016 that results in the acquisition of an interest in land in NSW.
- From and including the 2017 land tax year, foreign persons purchasing residential real estate in NSW will have to pay a land tax surcharge.
- The Office of State Revenue (OSR) website has useful information and FAQs on the application of both surcharges.

Land tax change – clearance certificate

Unpaid land tax is a charge on land (and a defect in vendor's title). In New South Wales, the practice was for purchasers of land to obtain a land tax certificate before completion to ensure there is no charge on the land. Under clause 16.6 of the 2014 New South Wales Standard Contract, if a purchaser served a land tax certificate on a vendor showing a charge on any land, on completion the vendor had to give the purchaser a clear land tax certificate (to remove any defect on the vendor's title). This provision is not included in the 2016 edition.

From 1 July 2016, New South Wales entered into agreement with the Commonwealth to establish the National Register of Foreign Ownership of Land Titles. The OSR is to collect and pass to the ATO information on nationality, citizenship details of buyers of land and additional vendor details (through changes to the *Conveyancing (Sale of Land) Regulation 2010*, clause 4, Sch 4 and by *Taxation Administration Amendment (Collection and Disclosure of Information to Commonwealth Bill) 2016*).

A term is now implied in all NSW land sale contracts entered into after 1 July 2016 obliging a vendor to serve a current land tax certificate on the purchaser at least 14 days before completion. The purchaser does not have to complete earlier than 14 days after service of the certificate or as prescribed by regulation 8A of the *Conveyancing (Sale of Land) Regulation 2010*.

As the vendor is required to apply for this certificate, the New South Wales Chief Commissioner is able to collect information about the vendor, which it can then disclose to the ATO.

Risk management tips for solicitors

- When acting for a vendor, the Contract for the Sale of Land should attach a Land Tax certificate in a schedule on exchange.
- The implied term does not require the vendor to attach a 'clear' land tax certificate, just a 'current land tax certificate'. Where the current land tax certificate attached to the contract by the vendor discloses a charge on the land for unpaid land tax, the vendor is still required to remove that charge before completion.

Swimming pool disclosure obligations

Recent regulatory changes have been made to the requirements to promote pool safety (*Swimming Pools Act 1992* (NSW)). From 29 April 2016, a vendor selling a property in NSW with a swimming pool or a spa pool must include one of the following in the contract of sale:

- a valid swimming pool certificate of compliance;
- a valid occupation certificate issued under the *Environmental Planning and Assessment Act 1979* (NSW) that is less than three years old and authorises the use of the pool; or
- a valid swimming pool certificate of non-compliance.

If a certificate of non-compliance is attached to the contract, the vendor is transferring the obligation to obtain a certificate of compliance to the purchaser. The purchaser then has 90 days from settlement to rectify the defects listed in the certificate and obtain a certificate of compliance.

Risk management tips for solicitors

- A solicitor acting for the vendor must attach the relevant certificate to this contract. Failure to include the required document may allow a purchaser to rescind the contract within 14 days of exchange.
- A solicitor acting for the purchaser should check the certificate attached, and if the certificate discloses non-compliance, advise the purchaser of its rights and obligations under the legislation. **LSJ**

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