

Windfall Gains Tax & Economic Entitlements

For Legal Practitioner's Liability Committee



01 Windfall Gains Tax

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What is the mischief?

Statement on Department of Treasury and Finance Victoria website:

Significant windfall gains can accrue to landholders when the value of their land increases due to the actions of government. This includes government decisions to rezone land.

A tax on windfall gains associated with a rezoning is an efficient and targeted way of capturing a fair share of these value uplifts for the community, contributing to infrastructure and services where the property values increase due to the actions of Government.

Overview

- *Windfall Gains Tax and State Taxation and Other Acts Further Amendment Act 2021*. Comes into operation on 1 July 2023.
- The *Taxation Administration Act 1997* also applies (section 4).
- WGT is “imposed on land that is rezoned by a WGT event” (section 6).
- See also the definition of “WGT event” and “excluded rezoning” (section 3). These definitions ensure the tax does not apply to land zoned for public places or land subject to GAIC.
- The liability arises when the WGT event occurs, which is when the rezoning that constitutes the WGT event takes effect under the *Planning and Environment Act 1987* (section 7).
- The owner of the land at the time the WGT event occurs is liable to pay the tax (section 8).

Calculation

Item	Taxable value uplift	Rate of WGT
1	Not more than \$100,000	Nil
2	More than \$100,000 but less than \$500,000	62.5% of the taxable value uplift in excess of \$100,000
3	\$500,000 or more	50% of the taxable value uplift

Calculation

- The “**taxable value uplift**” is the *value uplift* of the land, less any prescribed *deductions* as set out in the regulations (section 10).
- Presently there are no regulations. Consultation has been occurring in relation to the types of costs that should be taken into account as deductions.

Calculation

- The “value uplift” is determined as follows (section 11):

$$VU = CIV2 - CIV1$$

- **VU** is the value uplift
- For rateable land or non-rateable leviable land that is rezoned by a WGT event (section 12):
 - **CIV1** is the capital improved value in a valuation in force under Part II or IIA of the *Valuation of Land Act* (as the case may be) immediately before the WGT event occurs; and
 - **CIV2** is the capital improved value contained in a supplementary valuation under Part IIB of the *Valuation of Land Act*.
- For non-rateable non-leviable land, the Valuer-General will determine the capital improved value for the Commissioner (for CIV1 based on the date the land would have been valued if rateable or leviable).

Calculation

- If an owner holds land comprising more than one title, then (section 16):
 - WGT is assessed based on the taxable value uplift for all land on an aggregated basis.
 - The WGT is apportioned between each title based on the percentage value that each title represents of the aggregated total value.
- Joint owners are assessed as a single owner (section 17).
- If land is held on trust, the trustee is assessed. Any land held by the trustee for another trust, or for the trustee's own benefit, is ignored (section 18).
- Related entities (companies and trusts) may be grouped, in which case WGT is assessed based on the taxable value uplift for all group members on an aggregated basis (Division 4).

Calculation

- If an owner receives a notice of assessment which does not specify all of the following, the owner must notify the Commissioner within 60 days (section 26):
 - Any other land owned by the owner
 - Any other land owned jointly by the joint owners (if applicable)
 - Any other land owned by a member of a group when the WGT event occurred

Deferrals

- The owner may elect to defer up to 100% of the tax (section 31(1)).
- The election must be made prior to the date the tax is payable (section 31(2)). However, the Commissioner has the discretion to accept a late election (section 31(3)).
- The tax is payable within 30 days of the following (whichever occurs first) – section 32(1):
 - a dutiable transaction (other than an excluded dutiable transaction) occurs in relation to the land; or
 - a relevant acquisition (other than an excluded relevant acquisition) occurs in relation to a landholder that owns the land; or
 - the day that is 30 years after the WGT event.

Deferrals

- Excluded relevant acquisitions include (section 27):
 - An acquisition of an interest in a company or trust that occurs solely from a pro rata increase in the interests of all unitholders or shareholders.
 - The acquisition of a further interest by a unitholder or shareholder that already has a significant interest in the company or unit trust.
- Excluded dutiable transactions include (section 28):
 - Acquisitions of an economic entitlement.
 - No consideration transactions.
 - A relevant charitable land transaction.

Deferrals

- If a plan of subdivision is registered, and WGT has been deferred, the liability is apportioned across the lots in the plan based on area (section 33).
- Interest applies to the deferred WGT liability (section 35). It is based on the 10-year bond rate for the 10-year Treasury Corporation of Victoria bond. This was 1.52% on 31 August 2021.
- Unpaid WGT (including any penalty or interest) is a first charge on the land. Section 42.

Exemptions

- Residential land that does not exceed 2 hectares is exempt (section 37(1)).
- If the land exceeds 2 hectares, a formula applies to determine the tax payable on the portion of the land exceeding 2 hectares (section 37(2)).
- Residential land is:
 - Land with a residential premises affixed that can be lawfully used as a residence.
 - Land on which such a residence is being constructed or renovated. A building permit must have been issued.
- The Commissioner must be satisfied the land is used primarily for residential purposes (except if the land is also used for primary production).

Exemptions

- Residential land excludes (section 36(4)):
 - commercial residential premises (as defined in the GST Act)
 - residential care facilities
 - retirement villages
 - supported residential services
- The above exclusion doesn't apply to land on which there is a residence that is separately titled and owned.
- For example, this may be relevant for a independent living unit in a retirement village that is strata titled and in which each resident owns the title to their unit.

Exemptions

- Other exemptions:
 - **Section 38:** Rezoning to correct an obvious or technical error in the Victorian Planning Provisions or a planning scheme.
 - **Section 39:** Land that is subject to a contract of sale (or an option) entered prior to 15 May 2021 and the sale has not been completed when the WGT event occurs. For options, the terms of the contract must have been settled when the option was entered.
 - **Section 40:** Rezoning underway prior to 15 May 2021 – a request for amendment must have been created and registered in the Amendment Tracking System by Council prior to that date.
 - **Section 41:** Charitable land used continuously for charitable purposes for 15 years after the WGT event.

Issues to consider

- Preserve current exemptions for pre-15 May 2021 contracts and options.
- In new contracts that may complete after 1 July 2023, consider whether a special condition should be included that passes on any WGT cost to the purchaser on completion.
- Consider duty implications:
 - If the purchaser pays an additional amount for WGT, will that be subject to duty?
 - If the purchaser elects to be liable for WGT in a no consideration transaction, is that election consideration for duty purposes?
- Consider deferral issues when contemplating land dealings. Transactions involving economic entitlements, such as Property Development Agreements, may be preferred.

Issues to consider

- Optimal timing for planning changes.
- Consider the WGT implications when dealing with shares or units in entities that own land and have potentially deferred a WGT liability.
- Consider the impact of the grouping provisions for related entities.

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Economic Entitlements

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What is the mischief?

It was considered that developers could potentially avoid or defer a duty liability by acquiring an economic entitlement in land (rather than an interest in the land).

What is an economic entitlement?

- Duties Act – Part 4B.
- A person acquires an economic entitlement if they are entitled to one or more of the following (s. 32XC (1)(b)):
 - i. to participate in the income, rents or profits derived from the relevant land
 - ii. to participate in the capital growth of the relevant land
 - iii. to participate in the proceeds of sale of the relevant land
 - iv. to receive any amount determined by reference to subparagraph i, ii, iii above
 - v. to acquire any entitlement described in subparagraph i, ii, iii or iv above

The economic entitlement may be acquired through any means – including the creation or transfer of an entitlement (s32XC).

How is the duty calculated?

- Only applies if the land has a value of \$1 million or more (section 32XC).
- Concessional calculation provisions apply to land with a value between \$1 million and \$2 million (section 32XG).
- The party acquiring the economic entitlement is deemed to have acquired a beneficial interest in the land (section 32XD). Transfer duty applies accordingly.
- The duty is based on the unencumbered value of the land at the time the economic entitlement is acquired (section 32XF).
- If the arrangement doesn't specify and fix the percentage of the economic entitlement acquired, the beneficial ownership is deemed to be 100% (section 32XE(2)).
- The Commissioner can determine that a lesser percentage has been acquired (section 32EX(3)).

What about fees?

- SRO states:

'where a person providing a service in relation to land:

- *is normally engaged in a full-time capacity in providing those services,*
 - *the agreed fee/rate is within industry parameters, and*
 - *the person is unconnected (i.e. not an associated person) to any other person who has an economic entitlement in relation to the land,*
- it is unnecessary for the service agreement to be disclosed to the State Revenue Office by the service provider.'*

Example One

- A landowner and developer enter a joint venture agreement to develop land, previously used for farming, into residential lots for sale.
- The land value is \$11 million, excluding GST.
- It stays in the name of the landowner while the developer obtains the necessary approvals and undertakes all required works.
- The developer arranges for the sale of the residential lots on behalf of the landowner, achieving total sale proceeds of \$66 million, including GST at 10 percent.

Example One

- The sale proceeds belong to the landowner as the owner and vendor of the residential lots.
- The landowner is liable for GST of \$6 million, with the net proceeds being \$60 million.
- The agreement specifies that the landowner will retain from the net sale proceeds \$11.3 million, which is \$300,000 more than the pre-development land value.
- The developer is entitled to a fee equal to balance of the net sale proceeds, which is \$48,700,000 plus GST.

Example Two

- A landowner owns land worth \$5 million on which it is developing a new apartment complex.
- The landowner needs some short-term finance to complete the project and applies to a non-bank lender.
- The non-bank lender agrees to loan the required monies on the basis it will receive interest calculated as a percentage of the profits when the new apartments are sold.

Example Three

- A landowner owns two residential lots worth \$1.5 million (\$750,000 each).
- The landowner has entered a joint venture with a home builder.
- The two lots will both be sold to separate buyers as a part of 'house and land packages'.
- The purchasers will pay the price for the combined house and land to the landowner on settlement, estimated to be \$2 million each.
- The landowner will pay a portion of the proceeds from the sale to the home builder.

Issues to Consider

- Crucial to note that an economic entitlement is “land” for landholder duty purposes. Section 72(1)(c).
- If duty will be triggered, what is the optimal timing (consider value)?
- Can the interest to be acquired be fixed and specified in the agreement?
- Does the acquirer really need to receive an economic entitlement? Is an ordinary fee more appropriate?
- Don't assume the issue is limited to property development agreements only.
- Consider whether the provisions apply to financing transactions, arrangements with home builders or any other transaction where a party is entitled to receive payment based on the proceeds from the sale or use of the land.



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