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Foreign Investment Update – Foreign Resident Withholding Regime to be imposed on Buyers from 1 July 2016

By ,

Introduction

The Federal Government has recently passed the Tax and Superannuation Laws Amendment (2015 Measures No. 6) Act 2016.

This legislation imposes a 10% non-final withholding payment on the disposal by foreign residents of certain 'Taxable Australian Real Property.' The obligation to make this payment will rest with buyers.

In very broad terms, buyers of relevant real estate assets will be required to enquire as to whether sellers are 'Foreign Persons' and whether the property being purchased is 'Taxable Australian Real Property.' If the answer to both of these questions is yes, then the buyer will be required to withhold from the funds payable to the seller, and remit to the Australian Taxation Office, 10% of the purchase price. The ATO will then credit the amount against any resultant CGT liability of the seller.

Effectively, the regime will be a collection mechanism to support the operation of the foreign resident CGT provisions.

What transactions will be affected?

There will be an obligation for the buyer to withhold an amount equal to 10% of the proceeds from the transaction and pay this amount to the ATO where the following apply:

- The seller is a 'Foreign Resident' for Australian income tax purposes.
- The transaction involves an asset that is 'Taxable Australian Real Property', an 'Indirect Australian Real Property Interest' or an option to acquire either of these.

'Taxable Australian Real Property' is real property situated in Australia (including a lease of land situated in Australia), and certain mining rights. An 'Indirect Australian Real Property Interest' will apply in relation to certain shareholdings in companies whose principal assets are Australian real property.

Are there exemptions?

The obligations for the buyer with withhold and remit the 10% payment will not apply in any of the following circumstances:

- The market value of the Taxable Australian Real Property is less than $2 million.
- The transaction is conducted on an approved stock exchange.
- Certain other narrow exemptions in the legislation apply.

What can buyers do to protect themselves?

Failing to withhold the required payment from the purchase price will result in the buyer being required to pay to the ATO the required sum from its own funds. Therefore, it is essential that buyers in affected transactions ensure that they have sufficiently verified the status of the property being purchased, and the status of the seller as a Foreign Person.

The legislation provides the following mechanisms to assist buyers:

- The seller may obtain from the ATO a clearance certificate indicating that the seller is not a foreign resident during a specified period that covers the transaction, and provide the clearance certificate to the buyer.
- The seller may provide to the buyer a declaration that the seller is an Australian Resident during a specified period that covers the transaction.

A buyer in receipt of such a clearance certificate or a declaration will not be required to withhold the 10%.

Moving Forward

The new regime will apply from 1 July 2016. However, it will also apply to option arrangements entered into before that date, where the exercise date is after 1 July.

It is important that both buyers and sellers seek legal advice before entering in to an affected transaction, so that their obligations and risk are appropriately managed.

Special consideration will need to be given to transactions involving highly geared assets, where the consideration payable (after taking out the 10% withholding tax) is insufficient to discharge the mortgage or other encumbrance over the asset.

Should you wish to discuss any matters arising out of this article, please contact the author:

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