



Trusts deemed to be “Foreign Trusts State Revenue Changes relating to Stamp Duty

“As from 1st March 2020 all discretionary trusts will be deemed foreign trusts is a significant change to the SRO’s practical approach and will catch out numerous trustees who will be hit with duty of up to 13.5%, when they may have made provision for duty costs not exceeding 5.5% of the purchase price of the property”.

Are you considering purchasing Victorian property through a discretionary trust? Think again, because from 1 March 2020 the State Revenue Office (**SRO**) will deem all discretionary trusts to constitute foreign purchasers.

As a result, the trustee of a discretionary trust will automatically be liable to pay foreign purchaser additional duty (**FPAD**), in addition to the standard duty rates which are applied progressively with a top rate of 5.5%. The result is that total duty may be as high as 13.5%.

However, with some careful planning, this outcome can be avoided.

What is the foreign purchaser additional duty?

The FPAD was introduced in 2015 as a measure to improve housing affordability in Victoria, with the Government recognising that the percentage of property acquisitions by foreign purchasers (up to 20%) was putting pressure on supply and keeping many Victorian families out of the property market.

The FPAD is intended to disincentivise foreign purchasers from investing in Victorian property. Victoria and New South Wales have the highest foreign purchaser duty rates, both at 8%, soon to be followed by Tasmania with legislation currently before Parliament to increase its rate from 7% to 8%. Queensland, Western Australia and South Australia have a current rate of 7%. The ACT and Northern Territory currently do not have foreign purchaser surcharges.

In addition to these surcharges, beware also foreign ownership land tax surcharges that are imposed on residential land owned by foreign persons.

Who is a foreign purchaser?

The FPAD is imposed where a foreign purchaser acquires residential property in Victoria. A foreign purchaser is a transferee who is a foreign natural person, a foreign corporation or the trustee of a foreign trust.

A 'foreign trust' is defined as a trust in which a foreign corporation, foreign natural person or trustee of another foreign trust has a 'substantial interest' in the trust estate.

What is a 'substantial interest' in a trust estate?

Under the *Duties Act 2000*, a person or entity has a *substantial interest* in a trust estate if:

- (a) they have a beneficial interest of more than 50% in the capital of the trust estate; or
- (b) the Commissioner determines that the person or entity has the capacity to influence the outcome of decisions about the administration and conduct of the trust.

Where the purchaser is a fixed trust or a unit trust, it is generally straightforward in determining if a foreign person or entity has a substantial interest in the trust estate.

This analysis is difficult in the case of discretionary trusts, which typically have a very broad class of objects including a wide family class, and related entities such as companies and trustees of other trusts.

Due to this difficulty, the SRO has applied a 'practical approach' in determining if a foreign entity has a substantial interest in a discretionary trust. Under this approach, discretionary trusts with foreign objects who have not, and who are, based on available information, unlikely to receive any distributions in the future, would not be considered to be foreign trusts.

From 1 March 2020, the SRO will no longer apply the practical approach and will deem every discretionary trust which has a potential foreign beneficiary to constitute a foreign trust.

What is 'residential property' for the purposes of the FPAD?

The FPAD applies to acquisitions of 'residential property', which is defined as 'land capable of being used solely or primarily for residential purposes, and that may lawfully be used in that way.' This definition is very broad, and includes vacant land on which a person intends to construct a building for residential purposes. Accordingly, property developers will be caught by these provisions.

Residential property does not include commercial residential premises (such as hotels and motels), residential care facilities, supported residential services or retirement villages.

In Summary:

The blanket treatment of all discretionary trusts as foreign trusts from 1 March 2020 is a significant change to the SRO's practical approach, and will catch out numerous trustees who will be hit with duty of up to 13.5%, when they may have made provision for duty costs not exceeding 5.5% of the purchase price of the property.

In order to ensure that a discretionary trust is not a foreign trust, it will be necessary to vary the trust deed to explicitly exclude any foreign entities from constituting a beneficiary.

Any discretionary trust that does not include an express beneficiary exclusion clause for foreign natural persons, foreign corporations or trustees of foreign trusts will automatically be deemed to be a foreign trust.

We can assist you in varying your trust deed to exclude foreign beneficiaries, and we can also advise you in considering the use of other purchase vehicles for your property acquisition.

The SRO has announced that under transitional arrangements, the new approach will not apply to contracts of sale that were entered into (or nominations made) before 1 March 2020.

If it is necessary to nominate the trustee of a discretionary trust in respect of a contract of sale that has been executed, but the nomination has not yet occurred, we recommend that you contact us urgently. Any nomination made after 1 March, in respect of a contract of sale entered into before this date, will be caught by the new measures.



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