

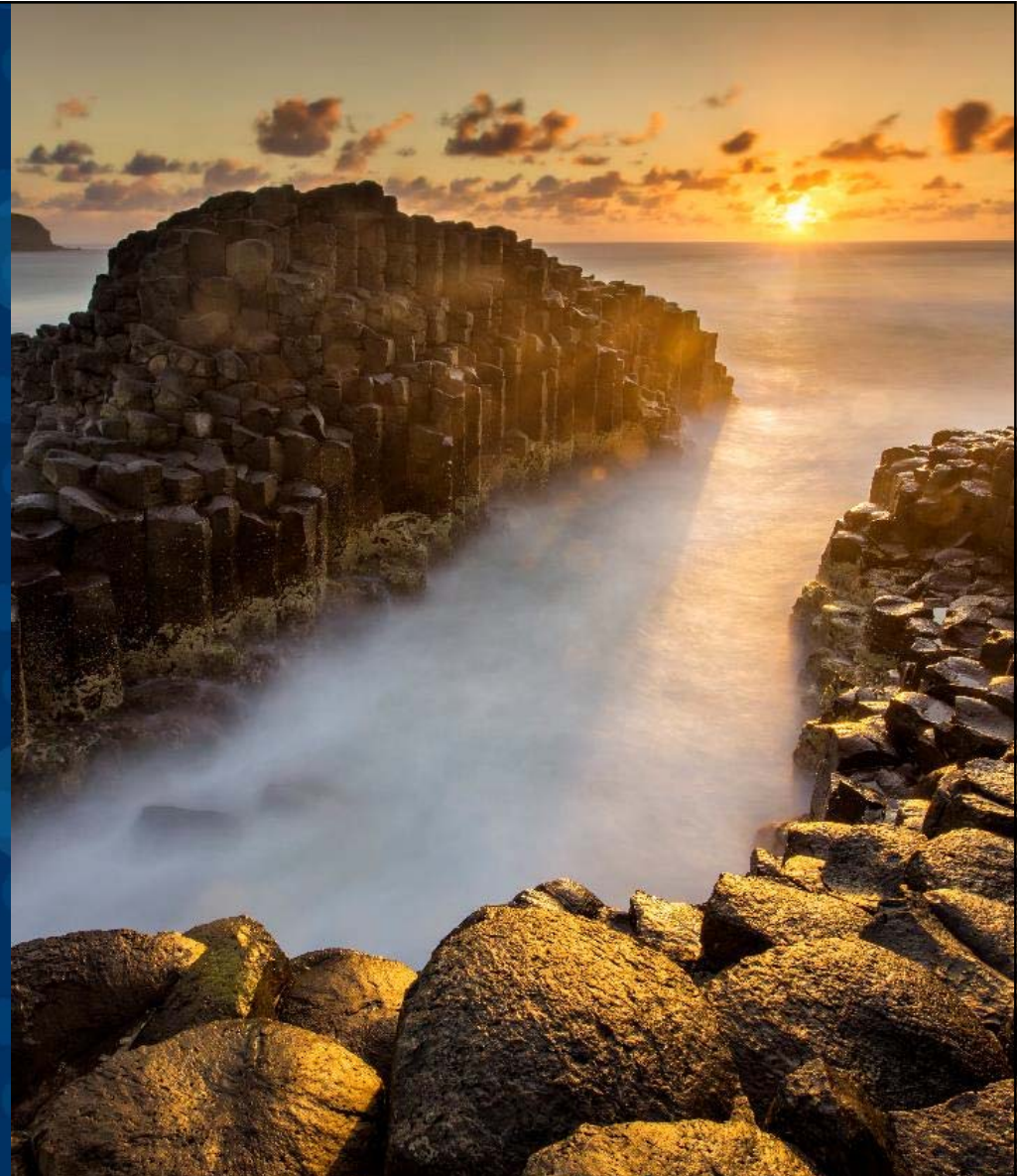
Property Funds Association Tax and Accounting Update

Simon Tucker & Rami Eltchelebi

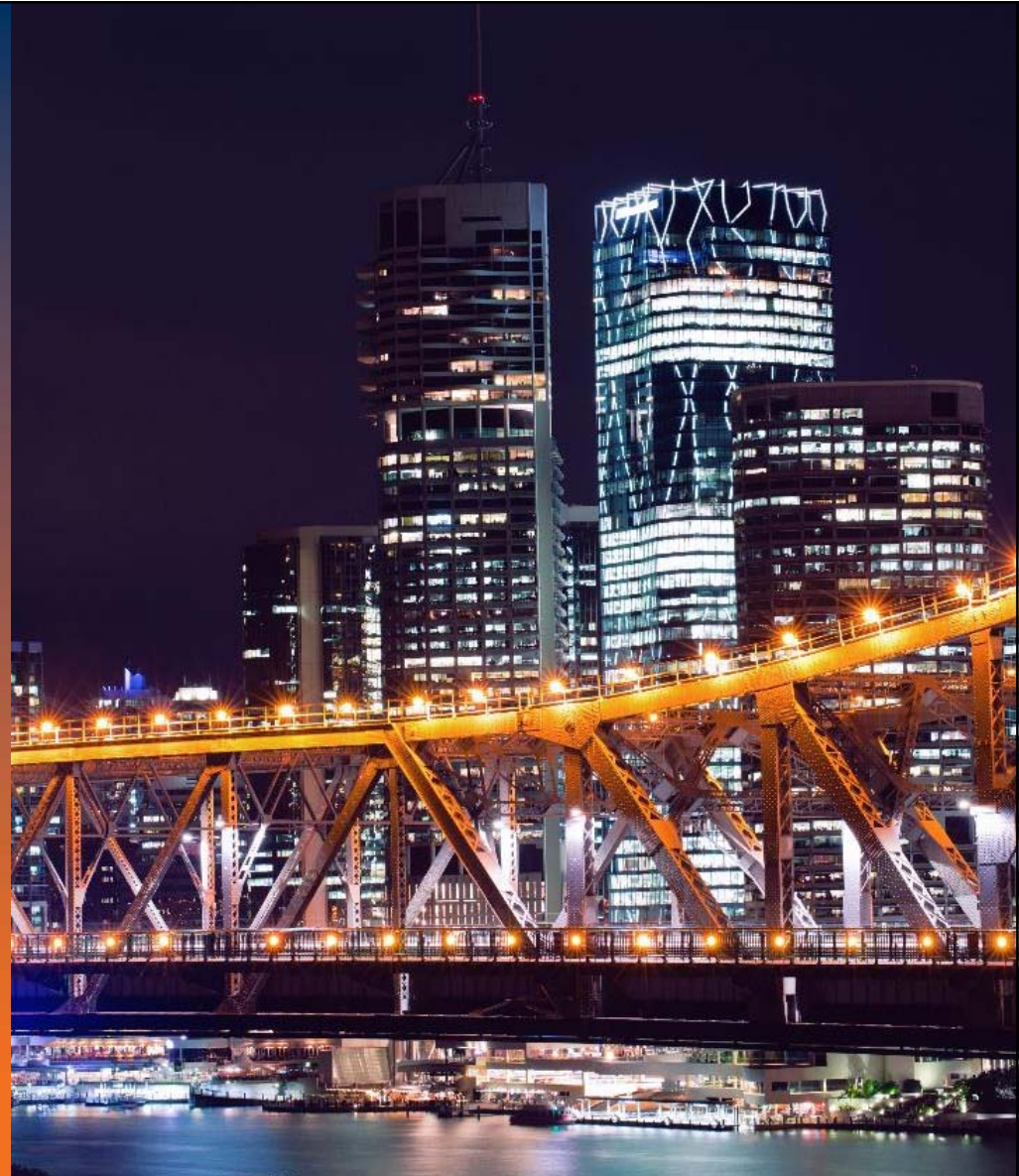
25 July 2019

Outline

1. Victorian State Tax Changes
2. Stapled Structures
3. AMIT technical amendments
4. Changes in Accounting standards



1. Victorian State Budget – Duty changes



Victorian State Budget – Duty changes

Take the lead

- Victorian State Budget announced a number of changes in relation to State property taxes, including
 - Amending the Corporate Reconstruction relief – 90% concession to apply instead of exemption
 - Further increase to the foreign purchaser duty – now 8%
 - Further increase to the rate of absentee owner land tax surcharge - now 2%
 - Imposition of stamp duty on the acquisition of fixtures
 - Duty concession for transfers of commercial and industrial land in regional Victoria

Victorian State Budget – Duty changes

Take the lead

- Amendments introduced in *State Taxation Acts Amendment Act 2019* which included the above announcements also included a further unannounced change to the Economic Entitlement Duty provisions which took effect from 19 June 2019
- An economic entitlement arises where the parties to the arrangement are entitled, amongst other things to,
 - participate in the dividends, income, rents derived from the land
 - participate in the capital growth of the land
 - participate in the proceeds of the sale of the land
 - receive any amount determined by reference to any of the above matters
 - acquire any entitlement described above

Victorian State Budget – Duty changes

Take the lead

- Prior to 19 June 2019 duty was payable on an acquisition of a greater than 50% interest in an economic entitlement in a *private unit trust scheme* or *private company* holding at least \$1,000,000 of Victorian land.
- The provision did not apply to acquisitions in respect of:
 - Land held by:
 - an individual
 - a discretionary trust
 - Acquisitions of economic entitlements in a *private landholder* of less than 50%

Victorian State Budget – Duty changes

Take the lead

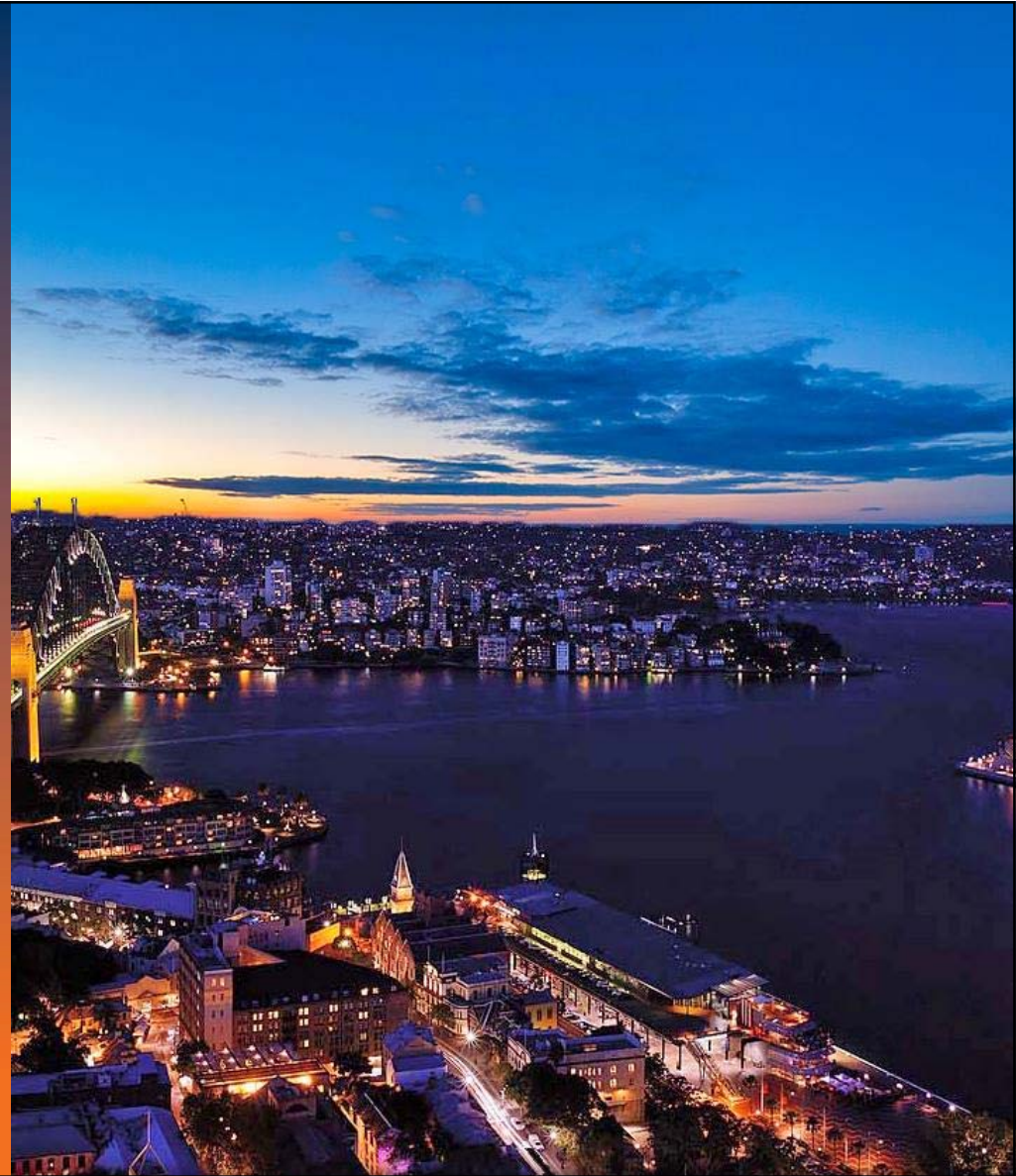
- From 19 June 2019:
 - Economic Entitlement transfer duty applies in respect of land held by any landowner of Victorian land with a value of greater than \$1,000,000
 - Economic Entitlement landholder duty applies to the acquisition of a *significant interest* in a private company or trust which itself holds an economic entitlement in land with a value of greater than \$1,000,000
- The new rules include 100% deeming rule where percentages of interest in not specified
- Contracts entered into prior to 19 June 2019 will not subject to duty and will be grandfathered
- Acquisitions of significant interests in a private company/ trust holding grandfathered contracts will also attract economic entitlement landholder duty

Victorian State Budget – Duty changes

Take the lead

- The new provisions are very broad in the 'potential' application given the removal of the 50% threshold
- The SRO has explained that service fees are not intended to be subject to the provisions, this would include:
 - Real Estate sale commissions
 - Architects - fees can include a percentage of building costs
 - Project managers - fees can include a percentage of project value
 - Planning consultants – fees can include a percentage of the value uplift
 - Private advisory firms –contingency fees for assisting a landowner to take their land to market
- This leave a lot of scope for interpretation of other fees particularly in relation to items such as outperformance fees etc

2. Stapled Structures



Stapled Structures – Legislative Amendments

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- Treasury Laws Amendment (Making Sure Foreign Investors Pay Their Fair Share of Tax in Australia and Other Measures) Act 2019
- Application date from 1 July 2019, subject to transitional rules
- Main concern is that income is being shifted via cross-staple payments

Summary of Amendments

Take the lead

Heading	Comments
Non-concessional MIT income	Stapled structures and trading trusts
Thin capitalisation	“associate entity test” is lowered from 50% to 10% through flow through entities
Superannuation funds for foreign residents withholding tax exemption	Interest and dividend WHT exemptions no longer available for non-portfolio exemptions
Sovereign immunity	No longer exempt from tax on non-portfolio investments

Non-concessional MIT income

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- Non-concessional MIT Income will be subject to a 30% withholding tax rate:
 - Managed Investment Trust (MIT) cross staple arrangement income
 - MIT trading trust income
 - MIT agricultural income
 - MIT residential housing income

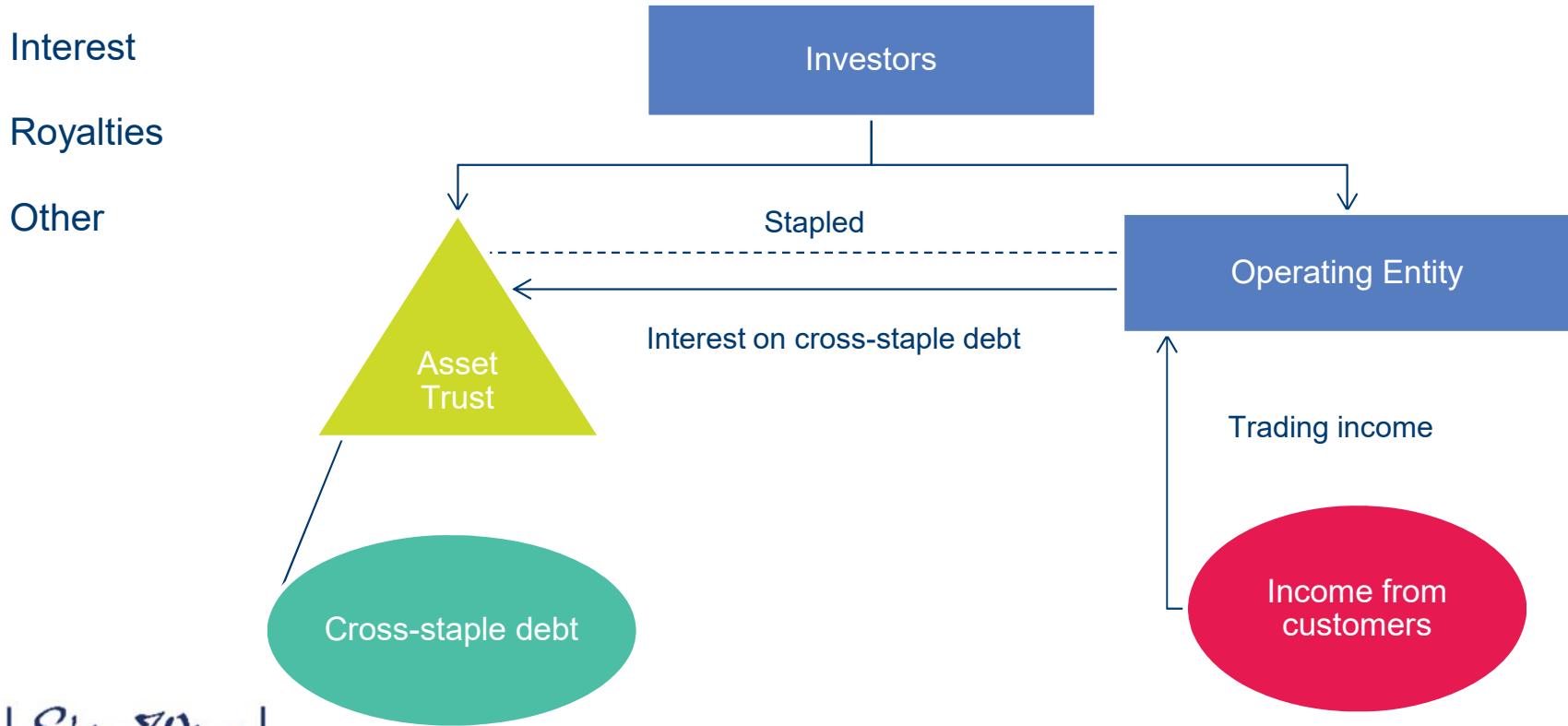
Non-concessional MIT Income

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- From 1 July 2019, fund payments attributable to ‘non-concessional MIT income’ and distributed by a MIT to a foreign investor will be subject to final MIT WHT at 30%, unless eligible for transitional relief
- Amongst other things, an amount of a fund payment will be ‘non-concessional MIT income’ if it is attributable to an amount derived from certain **cross staple arrangements**
- Interest income from cross staple loans are not considered to be ‘non-concessional MIT income’

Cross stapled arrangements

Take the lead



Cross stapled arrangements

Take the lead

- In order to have a 'cross staple arrangement', the sum of all of the investor's participation interests across Asset Trust and Operating Trust must be 80% or more
- An investor's total participation interest in Asset Trust and Operating Trust is equal to the lowest participation amount in each of those entities

Example: If an investor held a 100% interest in an Asset Trust and a 50% interest in an Operating Trust, that investor would have a total participation interest of 50%. Please refer to the diagram

Transitional Arrangements

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Transitional arrangements apply to fund payments that are attributable to existing investments. Therefore, the existing MIT withholding tax rate of 15% will continue to apply until, broadly

- For MIT cross staple arrangement income relating a facility that is not an economic infrastructure facility – 1 July 2026
- For MIT cross staple arrangement income relating to a facility that is an economic infrastructure facility – 1 July 2034
- For MIT trading trust income – 1 July 2026
- For MIT agricultural income – 1 July 2026
- For MIT residential housing income – 1 October 2027

3. AMIT technical amendments



AMIT Technical Amendments

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Treasury Laws Amendment (2018 Measures No. 5) Act 2019 (Act No. 15 of 2019)

Part 1 makes modifications to the MIT and AMIT rules to:

- allow a MIT with a single unitholder that is a specified widely held entity to access the AMIT regime
- extend the list of specified widely held entities to include the Future Fund Board of Guardians
- ensure that, in calculating rounding adjustments and trustee shortfall tax under the AMIT regime, discount capital gains are treated appropriately
- clarify that, in relation to an amount that is a discount capital gain that is not attributed to members, the trustee of an AMIT is liable to pay income tax on the amount as though it were not a discount capital gains

AMIT Technical Amendments

Take the lead

Part 2 makes modifications to the MIT and AMIT CGT rules to:

- clarify that the amount of the capital gain under CGT event E10 will be the cost base net amount where the cost base of the asset is nil at the start of the income year
- align the CGT outcomes for MITs with AMIT.

AMIT Technical Amendments

Take the lead

Part 3 makes modifications to the withholding tax rules for MITs and AMITs to:

- clarify that withholding tax liabilities arise on amounts of actual or deemed fund payments and dividend, interest and royalty payments to foreign members by an AMIT or a custodian
- ensure that in calculating fund payments made by MITs and AMITs, capital losses from non-taxable Australian property that have been applied against capital gains from taxable Australian property are added back
- clarify that AMITs that only make deemed payments to members can be withholding MITs
- clarify how the TFN withholding rules apply to AMITs that make deemed payments to members

AMIT Technical Amendments

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Part 4 makes modifications to the operation of the AMIT transitional rules to:

- ensure that former public trading trusts and corporate unit trusts can continue to use accumulated franking credits until 30 June 2019
- ensure early balancing trusts can elect into the AMIT regime from the 2016–17 income year

Presenter



Simon Tucker

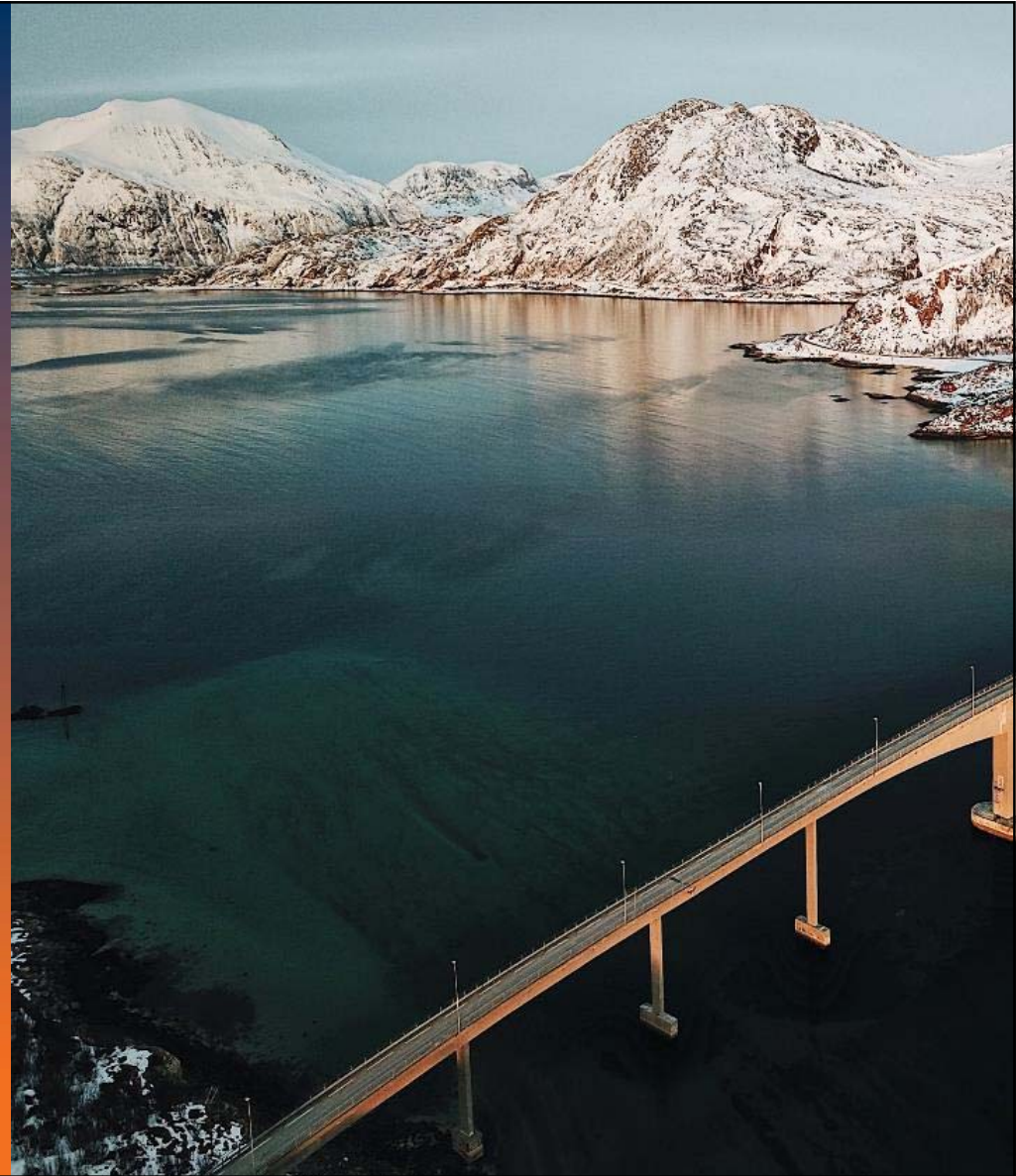
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Changes in Accounting Standards



New and Future Accounting Standards – 3 significant new standards

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New accounting standards on accounting for:

- Financial instruments
- Revenue
- Leases

Financial instruments

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Why new standard?

- Simplify accounting for investments, loans etc
- Hedge simplification
- Objective achieved?

Financial instruments

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HOT TOPIC: Introduction of the “expected credit loss model”

- Account for financial asset impairment losses up front
- Using historic data, forward looking data, reasonable and supportable information
- Consider credit risk for tenancy debtors
- Take into account credit enhancers e.g. bank guarantees

No impact expected for new / single asset fund. Impact expected for multi-asset funds with historical losses

Financial instruments

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HOT TOPIC: Treatment of loan modification

- Amendment to loan (refinance) – treated as modification or extinguishment?
- Non-substantial modification
 - E.g. amended loan note terms resulting in <10% change in discounted cash flows projected
 - May need to recognise a gain/loss
- Substantial modification
 - E.g. refinancing resulting in >10% change in discounted cash flow projected
 - Derecognise, recognise new liability
 - No profit/loss impact expected

Revenue Recognition

- Why new standard?
 - Single model for revenue across industries
 - International convergence
- What has changed?
 - Definition of revenue
 - Estimates and judgements
 - Direct link to “contracts with customers”
 - “Performance obligations”

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Revenue Recognition

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Management fees

- Fees charged by the fund: part of the effective interest rate calculation, not revenue
- Fees charged by the fund manager = revenue

Establishment fees

- Previously recognised as income up front
- Now must allocate fee to “performance obligations” and recognise revenue as performance obligations are satisfied
- May result in being recognised over time, e.g. the life of the fund?
- Recommendation:
 - Clearly define the services performed for the establishment fee
 - Review fee structure and contracts with customers

Performance fees

- No change expected in when / how much revenue
- Change expected in mechanism and accounting policy
- From “risk and rewards” to “control”

Leases

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Lessee accounting:

- Eliminates 'operating' or 'finance' lease distinction
- Bring lease asset and liability onto balance sheet
- E.g. property or equipment leases
- Capturing historical lease data will be time consuming
- Any agreement linked to EBITDA will be affected – lending, earn-out etc.

Lessor accounting:

- No change from current standard

Hot topic

- Is the lease asset ("right of use") a tangible or intangible asset?
- Impact on NTA where the finance lease liability will most certainly be a liability for NTA purposes
- Currently awaiting guidance from legislators and standard setters

Presenter



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Questions?

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