LSJ

LAW SOCIETY OF NSW JOURNAL

ISSN 2203-8906

Managing Editor
Claire Chaffey

Legal Editor
Klára Major

Assistant Legal Editor
Jacquie Mancy

Online Editor
Kate Allman

Journalist
Amy Dale

Art Director
Alys Martin

Advertising Sales Account Manager
Jessica Lupton

Editorial enquiries
journal@lawsociety.com.au

Classified Ads
www.lawsociety.com.au/advertise

Advertising enquiries
advertising@lawsociety.com.au or 02 9926 0290

LSJ

170 Phillip Street
Sydney NSW 2000 Australia
Phone 02 9926 0333 Fax 02 9221 8541
DX 362 Sydney

DISTRIBUTION
27,578*
*AUDITED SEPTEMBER 2020

Audited Media Association of Australia

Cover design: Alys Martin

NEXT ISSUE: 1 OCTOBER 2021

Welcome to LSJ September

Who would have thought we would be here again? As Greater Sydney pushes into its third month of lockdown, and restrictions continue in the regions, it isn't just the empty buildings and streets that look different. For the second month in a row, *LSJ* is not publishing a print edition. As most of us continue to work from home in accordance with government directions, we want to ensure your favourite legal magazine does not land in a deserted office but is instead available anytime, anywhere, on your favourite device.

The current lockdown wave brings with it new upheavals, but also new reasons for hope. Unlike 2020, vaccines are here and, at the time of going to press, accessible to the entire NSW adult population. Many who have received both doses of either Pfizer or AstraZeneca are starting to ask about incentives: when they will be allowed to visit family, sit down in a restaurant or café, go to the gym or, yes, resume travel without snap state border closures or stints in hotel quarantine? Vaccine passports have been flagged as the golden ticket to freedom but, as Amy Dale's analysis on page 30 explores, enforcing them could be a bumpy ride; especially for many small businesses already buckling under the strain of prolonged closures.

Many have taken to the streets to protest the continuing restrictions, in crowded scenes that are cheered by some and scorned by others. Kate Allman's article considers what comes first when freedom of movement puts public health at risk.

From all of us, stay safe and well,
The LSJ Team

Contributors

Amy Dale
Cover story p30

Amy is a journalist at *LSJ*. She previously worked as a government social policy and media adviser, as a court reporter, and has a Masters of Criminology. This month, she explores the legalities of introducing COVID-19 vaccine passports.

Kate Allman
Feature p40

Kate Allman is a multiplatform journalist and presenter with a bachelor degrees in law and journalism from UNSW. This month, she exclusively interviews the Australian women lawyers smashing glass ceilings as leaders of global law firms.

Ross Foreman SC
Corporate law p74

Ross Foreman is a commercial barrister in PG Hely Chambers. Here, he and colleagues Kate Boyd and Jerome Entwisle examine the latest guidance on the requirements individual company directors must satisfy before declaring share dividends.

Dung Lam
Tax and Property p87

Dung is a Principal of West Garbutt Lawyers and a member of the Law Society's Property Law Committee. Here, she & Marlon Camacho explain Revenue NSW's new Ruling & the complexities of handing down the family farm duty free.

Have an idea? We would like to publish articles from a broad pool of expert members and we're eager to hear your ideas regarding topics of interest to the profession. If you have an idea for an article, email a brief outline of your topic and angle to journal@lawsociety.com.au. Our team will consider your idea and pursue it with you further if we would like to publish it in *LSJ*. We will provide editorial guidelines at this time. Please note that we do not accept unsolicited articles.

Handing down the family farm without NSW duties

Dung Lam is a Principal of West Garbutt lawyers, chartered accountants & tax specialists. **Marlon Camacho**, is a lawyer at West Garbutt.

The value of Australian farmland has risen significantly over the past 20 years at an average compound annual growth rate of 7.6% (Rural Bank, Australian Farmland Values Report 2021). Consequently, the family farm often represents a farmer's most valuable asset. Section 274 of the *Duties Act 1997* (NSW) provides an intergenerational exemption from NSW duty on the sale, transfer, lease or lease assignment of primary production land where certain conditions are met. This exemption has existed since 1994. Originally the conditions of the exemption were contained in Treasurer's Guidelines but in 2005 the guidelines were codified into law as section 274. The policy behind the duty exemption is to encourage younger members of farming families to stay on the farm and to allow older members to retire without the burden of duty.

Snapshot

- The family farm often represents a farmer's most valuable asset. Intergenerational transfers can involve complex taxation considerations.
- Revenue NSW has issued Revenue Ruling DUT 050 'Transfer of Primary Production Property between Family Members' which for the first time provides welcome guidance on section 274 of the *Duties Act 1997* (NSW).
- An exemption may apply where land is held by a company owned by a discretionary trust.
- 'Control' for the purposes of carrying on a business is explained.

Revenue NSW has recently issued Revenue Ruling DUT 050 'Transfer of Primary Production Property between Family Members' ('**Ruling**') which for the first time provides guidance on section 274. This is extremely welcome since parts of section 274 are quite obscure.

Conditions of the section 274 exemption

The conditions which need to be met before the exemption applies are:

a. the land must be used for primary production or form an integral part of the primary production business ('**land requirement**');

b. the transferor, or the person directing the transferor, is a member of the family of the transferee ('**identity of transferor**');

c. the land was used for primary production in connection with a business carried on by the transferee, or by a member of the transferee's family, (whether alone or with others) immediately before the transaction ('**identity of the person conducting primary production business on the land**'); and

d. the business is to continue to be carried on by the transferee (whether alone or with others) after the transaction ('**continuity of business**').

Family member

A 'member' of the transferee's family covers a transferee's spouse and the following relatives of a transferee or their spouse: (a) a parent; (b) a grandparent; (c) a brother, sister, nephew, niece, uncle or aunt; (d) a child or grandchild; or (e) the spouse of any of the foregoing ('spouse' includes a de facto and a former spouse or de facto).

Notably cousins are not included as a member of a transferee's family (para 8).

Person directing the transfer

The concept of a 'person directing' the transfer covers situations where the land is owned by another entity (e.g. deceased estate, company, trust or superannuation fund) but there is a level of family control/ownership.

Section 274(3) outlines situations where there is a 'person directing' the transfer as follows:

- Where the 'transferor' is the *executor of a deceased estate*, the 'person directing' will be the deceased;
- Where the 'transferor' is a *proprietary ltd company*, the 'person directing' will be shareholder/s who are: (a) beneficially entitled to shares in the company; (b) entitled to vote; and (c) entitled to not less than 25% of the company's assets on a winding up, being an entitlement which existed for at least 3 years prior to the transfer date or that existed from the date of the company's incorporation;
- Where the 'transferor' is the *trustee of a bare trust*, the person directing will be the beneficiary of the trust;
- Where the 'transferor' is the *trustee of a discretionary trust,* the 'person directing' will be the person/s who, as takers in

▸▸▸

default, are entitled to not less than a 25% interest in trust capital, being an entitlement which existed for at least 3 years prior to the transfer date or that existed from the date of the trust's establishment;

- Where the 'transferor' is a *trustee of a private unit trust*, the 'person directing', will be the unitholder/s who: (a) hold units in the trust beneficially; and (b) are entitled to not less than 25% of the unit trust's assets on winding up, being an entitlement which existed for at least 3 years prior to the transfer date or that existed from the date of the trust's establishment; and
- Finally, where the 'transferor' is a *trustee of a self managed superannuation fund* ('**SMSF**'), it is the member/s of the fund who will be the 'person(s) directing'.

Section 274(4) provides a tracing rule through chains of companies or unit trusts. It provides that where the transferor is a proprietary limited company or private unit trust ('**subsidiary entity**') that is owned by another proprietary limited company or private unit trust ('**parent entity**'), a person is taken to be directing the subsidiary entity if the Chief Commissioner of State Revenue ('**Commissioner**') is satisfied that, had the parent entity been the transferor, the person would be the person directing the parent entity in accordance with the rules in s 274(3).

Section 274(5) provides that there are no other cases of a person directing a transferor apart from the situations described in ss 274(3) and (4). This means that the duty exemption in s 274 cannot be accessed by non-proprietary companies (e.g. listed or unlisted public companies), discretionary trusts which do not have takers in default to trust capital, public unit trusts or superannuation funds which are not SMSFs (para 20).

Revenue NSW's guidance

The Ruling examines each of the requirements in s 274(1) in detail. The following highlights the Ruling's most salient points.

Land requirement

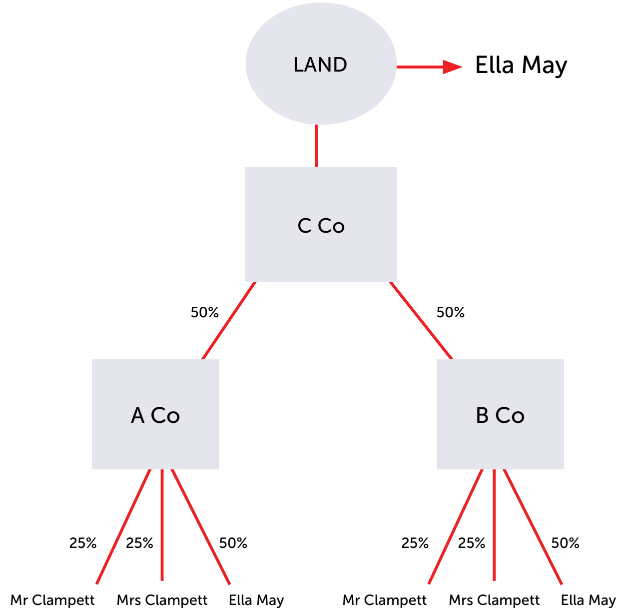
The term 'land used for primary production' means land which is exempt from land tax under the primary production exemption in s 10AA of the *Land Tax Management Act 1956* (NSW). Accordingly, Revenue NSW will have regard to the principles outlined in Revenue Ruling LT097v2 in assessing whether this requirement is met.

Where there are multiple uses, Revenue NSW may request further information to substantiate the exemption claim. Care should be taken where a landholder uses land for other purposes (e.g. solar or wind farming leasing, or farm accommodation).

Person directing

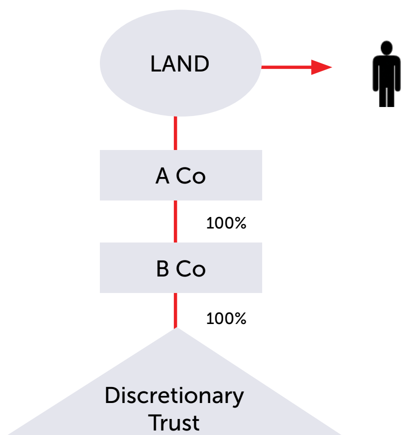
The way that Revenue NSW reads s 274(4) and allows this section to be combined with the provisions of s 274(3) is concessionary and of particular interest.

Significantly, s 274(4) is not limited in its operation to wholly owned subsidiaries or more than 50% owned subsidiaries. Consequently, a subsidiary entity can have more than one parent entity for the purposes of s 274(4). Example 5 in the Ruling illustrates this point as follows:



C Co can transfer the land to Ella May as part of Mr and Mrs Clampett's retirement. C Co is a subsidiary of both A Co and B Co. If either of A Co and B Co had been the transferor of the land (as opposed to C Co), Mr and Mrs Clampett should meet the person directing requirement under s 274(3)(b) because collectively they hold more than 25% of the shares in each of A Co and B Co.

The wording of s 274(4) literally only allows tracing through companies and private unit trusts. Despite this, Revenue NSW adopts a concessionary approach which allows for tracing through chains that include a discretionary trust. This is helpful given that a common business structure is for a company to be owned by a discretionary trust. Example 6 of the Ruling illustrates this concessionary approach as follows:



Revenue NSW considers that the 'person directing' requirement in s 274(1)(a) can be met in the above scenario by applying a combination of ss 274(3)(b), 274(3)(d) and 274(4) if on the particular facts, s 274(3)(d) would have been met if the land was held directly by the discretionary trust.

Continuity of business requirement

Sections 274(1)(b) and (c) require that:

a. the subject land be used in a primary production business carried on by the transferee or a member of their family immediately *before* the land transfer; and
b. the same primary production business continue to be carried on by the transferee (whether alone or with others) *after* the transfer.

Where the primary production business is carried on by a related company or trust, s 274(5AA) states that a reference to a business carried on by a person includes a reference to a business carried by a company or trust 'controlled' by the person. Section 274(5AA) was enacted into law in 2017 to acknowledge the fact that family farming businesses may be carried on via an associated company or trust. Oddly there is no legislative definition of what 'control' means for these purposes. In the Ruling, Revenue NSW indicates that 'control' is a question of fact and that it will apply the general principles enunciated by Justice Brereton in paragraphs 163 to 167 of *Hancock v Rinehart* [2015] NSWSC 646 in considering who 'controls' a company or trust, namely:

a. 'control' of an entity is concerned with the ultimate power to decide how an entity acts, as distinct from proprietorship;
b. for a company, control normally resides with the shareholders with majority voting rights who can determine the composition of the board of directors (who direct the company's operations);
c. typically those who own a company usually control it;
d. a trust is controlled by the trustees, or if there is a corporate trustee, then by the persons who control the corporate trustee;
e. where a trust has an appointor who has the power to replace the trustee, then the trust will be controlled by the appointor.

Revenue NSW will look at the identity of a company's directors and shareholders, and in the case of a trust the identity of the trustee, the directors of the trust company and appointor.

To meet the continuity of business requirement, Revenue NSW accepts that adjustments can be made to the primary production business without raising anti-avoidance issues where the changes are in line with the policy of intergenerational transfer. For instance, control of a business trust may be changed to the transferee by changing the trustee and appointor just before the land transfer. The ability to make these changes will be subject to the terms of the trust deed. Alternatively, an intended transferee may wish to enter into a partnership with the business entity just before the land transfer and continue to carry on that partnership business after the transfer.

Revenue Ruling DUT 050 ... for the first time provides guidance on section 274. This is extremely welcome since parts of section 274 are quite obscure.

Landholder duty

Where the primary production land is held by a company or a unit trust, then ownership of the land may be indirectly passed by transferring shares or units in the landholding entity. If the unencumbered market value of the NSW land exceeds $2 million then NSW landholder duty may be triggered by the share/unit transfer. The landholder duty rules are only triggered where an entity acquires a 50% or more interest in the landholding company or unit trust. In the situation where ownership interests in the landholding company/trust are owned by family members invariably this 50% threshold is met when associated persons' interests are aggregated. (Please see the online edition of this article for an additional explanatory graphic from Example 9 in the Ruling).

Section 163A(1)(e) of the *Duties Act 1997* (NSW) provides a landholder duty exemption if the land owned by the landholder is used for primary production and the Commissioner is satisfied that if the landholder had transferred the land to the person who acquired the interest in the landholder, the transfer would have been exempt from duty under s 274. The Ruling is therefore also relevant for this landholder duty exemption. Before considering the exemption in relation to share transfers, s 163D in relation to companies that are primary producers should be considered.

Whilst the Ruling may not provide answers to all s 274 exemption queries and private ruling applications are likely to continue to be made in relation to the exemption, Revenue NSW is to be commended for issuing the Ruling and providing guidance on some difficult aspects of s 274.

Finally, wholistic tax advice should be sought on the proposed land transfer covering not only duty but also the capital gains tax, income tax and GST consequences of the land transfer. Notably, in a rising market, the small business CGT concessions can be difficult to access. Where the land is held by a company or a self managed superannuation fund, it will need to be transferred out at market value to prevent adverse tax consequences and to comply with superannuation law. Section 274 does not replace s 63 in relation to deceased estates. **LSJ**

*The authors wish to thank Arlene Fernandez of Revenue NSW and Georgiena Ryan of Regional Business Lawyers for their valuable comments on a draft of this article.