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LITIGATION MASTERCLASS

What's Happening in State Taxes Litigation

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1 Introduction

It has been a busy few years for state taxation in all respects. Litigation in superior courts has been relatively frequent with significant decisions handed down in the Supreme Court of Victoria (including the Court of Appeal), the NSW Court of Appeal and others. A steady flow of decisions has also emanated from the Victorian Civil Claims and Administrative Tribunal (**VCAT**).

New taxes or surcharges have also emerged over the last few years. These include the foreign purchaser duty surcharge, the absentee owner land tax surcharge and recently, the Vacant Residential Property Tax.

To some degree, state taxes may be viewed as a microcosm of federal taxation. The State Revenue Office (**SRO**) possesses many of the same powers as the ATO. Taxpayers who wish to dispute state tax liabilities do so through an objection regime contained in Part 10 of the *Taxation Administration Act* 1997 (Vic) that is akin to Part IVC in the federal taxes arena. Disallowed objection decisions are, at the taxpayer's choice, referred to either VCAT (merits review) or to the Supreme Court of Victoria (statutory appeal). The factors relevant to venue selection between VCAT and the Supreme Court are similar to taxpayers considering litigating in the AAT or Federal Court: see in this regard *Conte Mechanical and Electrical Services Pty Ltd v Commissioner of State Revenue* [2011] VSC 104 and *Mould v Commissioner of State Revenue* [2014] VSC 268. As is the case with a Part IVC dispute, it is the taxpayer who carries the onus and who must discharge the burden of proof.

Many of the legal concepts encountered in federal taxation, such as changes in beneficial ownership (for capital gains), are concepts that are central to state taxation (duty). Further, state taxation cases, like their federal counterparts, are cases that are generally heavy on statutory interpretation.

However, state taxation also has some unique features. The concepts central to some state taxes, such as land tax and payroll tax do not have a ready counterpart at federal level. The SRO's administrative powers, whilst similar, are not identical. Finally, the approaches of the SRO and ATO to dispute resolution, in my view, differ.

This paper focuses on issues that are commonly litigated. A brief overview will be given of the High Court decision in *Commissioner of State Revenue v ACN 005 057 349 Pty Ltd* [2017] HCA 6 in "Other Developments". The issues and intricacies of that judgment are a topic in itself. However, in my experience, the issues raised by *ACN* are less frequently encountered than those that have been given primacy in this paper.

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2 Land tax, primary production and exemption: messages from the recent cases

Melbourne's expansion into broad acres farmland has had significant land tax implications on land owners. An exemption from land tax for primary production, once common, can now be difficult to obtain. Litigation in the area has been significant, with recent decisions in the Victorian Court of Appeal, the Supreme Court of Victoria and the NSW Court of Appeal shaping the landscape. These cases have helped clarify how the "use" of the land is to be construed, and at what point in time.

2.1.1 The legislation

Land tax is imposed annually pursuant to the *Land Tax Act* 2005 (**LTA**) on the "owner" of land, having regard to the "taxable value" (site value) of land owned by the owner as at midnight, 31 December on any given year: s 38. The intricacies of who an owner is and what the taxable value of land is are beyond the purposes of this paper.

Four primary production exemptions exist. They are contained in ss 65, 66, 67 and 68 of the LTA. The location of the land (whether in "greater Melbourne" or not and if so whether in an "urban zone" or not) and, in the case of the more onerous s 67, who the owner of the land is, are the main points of distinction.

Section 65 deals with land outside "greater Melbourne" and is in the following terms:

> (1) Land outside greater Melbourne that is used primarily for primary production is exempt land.
>
> (2) If a part of any land outside greater Melbourne is used primarily for primary production that part is exempt land even if an activity other than primary production is carried on on any other part of the land.

Section 66 deals with land wholly or partly in "greater Melbourne" but not in an "urban zone". It provides:

> Land is exempt land if the Commissioner determines that the land comprises one parcel—
>
> (a) that is wholly or partly in greater Melbourne; and
>
> (b) none of which is within an urban zone; and
>
> (c) that is used primarily for primary production.

The requirements for exemption become considerably more stringent if the land is located both within "greater Melbourne" and in an "urban zone". As with s 66, land will only be exempt pursuant to s 67 if the Commissioner determines that:

> (a) the land comprises one parcel that is

—

(i) wholly or partly in greater Melbourne; and

(ii) wholly or partly in an urban zone; and

(iii) used solely or primarily for the business of primary production; and

(b) the owner of the land is a person specified in subsection (2).

The ownership criteria in subsection (2) vary according to who the owner of the land is. An owner of land may be:

- a natural person who is normally engaged in a substantially full time capacity in the business of primary production of the type carried on on the land;
- a company (not acting as trustee) in which all the shares are beneficially owned by natural persons and the principal business of which is primary production of the type carried on on the land;
- a trustee of a trust (other than a discretionary trust (as defined)) the principal business of which is primary production of the type carried on on the land, where each beneficiary is a natural person who is entitled under the deed to an annual distribution of income and at least one of the beneficiaries, or a relative of at least one of the beneficiaries is normally engaged in a substantially full time capacity in the business of primary production of the type carried on on the land; or
- a discretionary trust whose principal business must be primary production of the type carried on on the land. Each specified beneficiary must be either:

  (a) a natural person; or

  (b) at least one of the specified beneficiaries must be a natural person and the other specified beneficiaries who are not natural persons must be a charitable institution, a company or a trust that satisfy additional criteria: see s 67(2)(d) LTA.

  A central requirement is that at least one of the specified beneficiaries is a natural person and that person, or a relative of at least one of the specified beneficiaries, is normally engaged in a substantially full time capacity in the business of primary production of the type carried on on the land.

In the case of a company, the LTA provides that the principal business of a proprietary company is not primary production of the type carried on on the land unless the main undertaking of the company is primary production of the type carried on on the land and certain other requirements are met: s 67(3).

An exemption is also contained in s 68 for land being prepared for use for primary production. It provides:

(1) Land is exempt land for a tax year if the Commissioner is satisfied that—

(a) the land is being prepared for use primarily for primary production; and

(b) the land will become exempt land under section 65, 66 or 67 within 12 months after the day on which the preparation referred to in paragraph (a) commenced.

(2) The Commissioner may extend the period referred to in subsection (1)(b) by a further period of 12 months.

Many of the terms contained in the exemptions are defined in s 64. These include (but are not limited to) "discretionary trust", "greater Melbourne", "primary production" and "urban zone".

The term "discretionary trust" is separately defined for the primary production provisions (it is otherwise similarly defined in the dictionary in s 3 of the LTA). It means:

a trust under which the distribution or vesting of the whole or any part of the trust income or property—

(a) is required to be determined by a person either in respect of the identity of the beneficiaries or the quantum of interest to be taken, or both; or

(b) will occur in the event that a discretion conferred under the trust is not exercised;

The term "greater "Melbourne" means the aggregate area consisting of:

(a) the area within the municipal district of each Council listed in Part 1 of Schedule 2; and

(b) the area within an urban growth boundary specified in a planning scheme that is in force in the municipal district of each Council listed in Part 2 of Schedule 2;

It is noted that the definition of "greater Melbourne" was amended in 2014. Prior to that time "greater Melbourne" was defined by reference to the Third Schedule of the *Melbourne and Metropolitan Board of Works Act* 1958. For a discussion about the meaning of "greater Melbourne" in that context, which was ultimately decided in favour of the Commissioner, see *Commissioner of State Revenue v EHL Burgess Properties Pty Ltd* [2015] VSCA 269.

The expression " primary production" is defined in s 64 to mean:

(a) cultivation for the purpose of selling the produce of cultivation (whether in a natural, processed or converted state); or

(b) the maintenance of animals or poultry for the purpose of selling them or their natural increase or bodily produce; or

(c) the keeping of bees for the purpose of selling their honey; or

(d) commercial fishing, including the preparation for commercial fishing or the storage or preservation of fish or fishing gear; or

(e) the cultivation or propagation for sale of plants seedlings mushrooms or orchids;

Finally, "urban zone" means:

a zone, or part of a zone, under a planning scheme in force under the Planning and Environment Act 1987 of a type declared under subsection (2) to be an urban zone for the purposes of this Division.

(2) The Governor in Council may by Order published in the Government Gazette declare specified types of zones under planning schemes to be urban zones for the purposes of this Division.

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Melbourne's outward expansion has seen more and more land rezoned. The requirement in s 67 for a company or trust to carry on a business and, for a trust, to have a beneficiary or relative of a beneficiary engaged in a substantially full-time capacity in the business of primary production makes s 67 immeasurably more difficult to satisfy than either ss 65 or 66. As is apparent, the rezoning of land can imperil a primary production exemption that may have been held for decades.

2.1.2 Use of the land and timing

It will be a question of characterisation in each case whether the primary production activity was the predominant use of the land so as to impart to the whole of the land the necessary character. In *Rainn Pty Ltd v Commissioner of State Revenue* [2016] VSCA 338, the Victorian Court of Appeal, in considering s 66 of the LTA, unanimously confirmed that the taxable status of the land in question is to be determined as at the assessment date, namely, midnight on 31 December of the preceding year: at [15]. However, ascertaining the use of the land at that date may depend on additional evidence about what was happening on the land "shortly before and/or shortly after the date in question": at [17].

The Victorian Court of Appeal amplified the same views in *CDPV Pty Ltd v Commissioner of State Revenue* [2017] VSCA 89. The court in *CDPV* also considered s 66 of the LTA. The court found that the relevant issue for decision, namely, whether the land was being used primarily for cultivation for the purpose of selling the produce of cultivation, was at midnight on 31 December on each of the relevant years in dispute, "taking account of events and circumstances 'during a period not overlong and not over short' either side of that point in time": at [50].

2.1.3 Purpose of cultivation

In several instances, the principal dispute has been whether the cultivation that took place in was for the purpose of selling the produce of cultivation. *CDPV* was a case that concerned land in greater Melbourne, but not in an urban zone, in relation to 167 acres in Plumpton. The taxpayer purchased the land in 2004. At that time it was covered in rocks and infested with weeds.

By 2009, the value of the land had risen significantly and the taxpayer entered a terms contract to sell the land to a developer for $27.5m. The contract of sale required the purchaser to pay the applicants a "spraying amount" of $10,000 annually to reimburse the applicants for keeping the land free of weeds. The Commissioner issued reassessments for the 2009 to 2012 land tax years to the applicants denying the primary production exemption. The taxpayer objected on the ground that the land was used for the purpose of primary production pursuant to an oral share farming agreement (s 66, LTA). In the Supreme Court, leave was also given for the taxpayer to also rely on s 68.

Evidence about the use of the land was given by a director of one of the applicants, a share farmer who, it was alleged, was responsible for cultivating the land and a senior land management officer from the City of Melton. The evidence was that a "gentlemen's" oral share farming agreement had been made by which the sharefarmer used part of the land for growing wheat and barley and worked on the rest to prepare it for further primary production. Pursuant to that agreement, the share farmer would keep 75% of the proceeds after expenses and the director would receive 25% of the proceeds.

The share farmer's evidence was that crops of wheat or barley had been sewed every year under review except one in which further rock clearing and weed removal occurred. For all of the years in dispute, there had not been enough grain harvested for any part of it to be sold. No sharing of profits ever occurred as the crop was too small and/or no income was ever derived.

The trial judge (Croft J) found the taxpayer's evidence to be unsatisfactory, vague, self-serving and inconsistent and had to be approached with a "high degree of caution": at [64]. In particular, Croft J concluded that at best, the cultivation of the land for the purpose of selling the produce of cultivation was a "side benefit" rather than the primary purpose. Of primary importance was that the weeds were controlled and the land maintained.

On appeal, the primary argument agitated by the applicants was that the trial judge had erred in considering the subjective purpose of the taxpayers (and the share farmer). It was contended that the purpose of the cultivation of the land is an objective purpose to be determined by what was actually done on the land, rather than subjective intentions or motivations. The objective evidence, it was contended was not to control weeds but to grow a crop for sale.

This argument was rejected. The question of "purpose" directs attention to the activities constituting the use of the land and the purpose of the person(s) engaging in that use. The test is objective and subjective in that the surrounding circumstances may include the subjective intention of the person engaging in the use of the land.

The court found that it was "well open" for the trial judge to find that the share farmer's purpose in cultivating the land was to ensure that weeds did not invade the neighbouring land (on which he also worked) that he was farming and that if he derived any crops or seeds from his efforts, that would be a side benefit: at [64]. The evidence that there would be any profit arising from selling produce was "sparse and unconvincing" such that the trial judge was correct to conclude that it had not been shown that the purpose of cultivation was to sell the produce: at [66]. At best, the prospect of sale of the crops was one possible outcome of the cultivation rather than its purpose.

Regard should also be given to the NSW Court of Appeal decision in *Chief Commissioner of State Revenue v Metricon Qld Pty Ltd* [2017] NSWCA 11. Metricon had purchased rural land in the Tweed Valley for over $60m for future development. It had undertaken some preliminary activities for obtaining approval for future residential development however the land was physically used for the maintenance of cattle for the purpose of selling them or their natural increase or bodily produce (some of the land was leased residentially).

Section 10AA(3) of the *Land Tax Management Act* 1956 (NSW) stipulated that land used for primary production (as referred to in s 10AA(2)) means land the dominant use of which is for:

(a) cultivation, for the purpose of selling the produce of the cultivation, or

(b) the maintenance of animals (including birds), whether wild or domesticated, for the purpose of selling them or their natural increase or bodily produce, or

(c) commercial fishing (including preparation for that fishing and the storage or preparation of fish or fishing gear) or the commercial farming of fish, molluscs, crustaceans or other aquatic animals, or

(d) the keeping of bees, for the purpose of selling their honey, or

> (e) a commercial plant nursery, but not a nursery at which the principal cultivation is the maintenance of plants pending their sale to the general public, or
>
> (f) the propagation for sale of mushrooms, orchids or flowers.

In issue was whether that use was the "dominant use" of the land or whether the dominant use of the land was land banking or land development. That is, could an intangible use, such as land banking or future land development, be a "dominant use" as opposed to a physical use (such as cattle grazing).

At first instance, the Supreme Court of NSW (White J) found that although s 10AA(3) allowed competing non-physical use of the land such as land banking to be taken into account, Metricon's use of the land as a land bank was not a current or present use. Each of the assessments was set aside.

The Court of Appeal dismissed the Commissioner's appeal. It found that the concept of "use" in relation to s 10AA is one of physical deployment of the land in pursuance of a particular purpose of obtaining present benefit or advantage from it. That is, s 10AA(3) called for a comparison with only physical uses of the land. In particular, "land banking", namely land acquired with a view to future development could not be regarded as being of itself, use of the land. As the court stated:

> "Inactivity in the form of mere holding, although accompanied by a present intention to subdivide and sell at some future point, is not the source of present benefit or advantage and therefore does not constitute a use for the purposes of s 10AA(3)".

The court noted that the expenditure incurred by Metricon on planning residential development did not occur in a vacuum. However, this did not make "use" of the land; there was no deployment of the land in pursuit of a purpose of obtaining present benefit and advantage from it: at [70]. Although Metricon had embarked upon a property development venture, that venture was preparatory to the commencement of a "use" of the land. Holding the land as a "land bank" was for a future use and did not amount to use for the purposes of s 10AA.

It is worth noting that the taxpayer in *CDPV* submitted that the decision in *Metricon*, decided after the decision at first instance was delivered, was authority that eschewed reliance on subjective purpose in ascertaining purpose. This was rejected. The court in *CDPV* found that *Metricon* was concerned with the dominant "use" of the land, not purpose; in any event the court noted that *Metricon* did not stand for the proposition that subjective intention was irrelevant to the determination of purpose.

Although the decision in *Metricon* was decided in the NSW Court of Appeal having regard to NSW legislation, it will, in my view, be highly relevant to ascertaining, for the purposes of ss 65 and 66 of the LTA, whether land is "used primarily for primary production". That is, whether an alternate activity (such as a planned development) involves a physical use of the land.

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3 Transfer of partnership interests – implications of the decisions in *Danvest*

The taxpayer has been successful (at first instance) against the Commissioner in the Supreme Court of Victoria decision of *Danvest v Commissioner of State Revenue* [2017] VSC 125. Shortly stated, the court (Croft J) found that the transfer of a partnership interest where the partnership property included land in Victoria was not dutiable as it was not a presently existing proprietary interest in the underlying land. The decision is significant and is on appeal. It deals with the broadly drafted "change of beneficial ownership" provisions contained in s 7(1)(b)(vi) of the *Duties Act* 2000 (**DA**). In my view, legislative amendment is a real prospect if the Commissioner's appeal is refused.

In 2002, a Deed of Unit Partnership was created with three partners, Danvest Pty Ltd (20%), Northpeak Pty Ltd (40%) and Lopet Pty Ltd (40%). The Manager of the Partnership, Gold Age Australia Pty Ltd (**GAA**), held three properties on trust for the partnership. The properties were leased by GAA, which conducted an aged care business.

In December 2013, pursuant to a Partnership Sale Agreement, Northpeak and Lopet sold their interests in the partnership to Danvest and Bullhusq Pty Ltd. The properties were not transferred and GAA continued to own them as Manager of the partnership.

After the sale, Danvest and Bullhusq applied for a private ruling from the Commissioner to the effect that the transactions were not dutiable. The Commissioner expressed the view that Danvest and Bullhusq had acquired an 80% interest in the property of the partnership, some of which was dutiable property. In the alternative, the Commissioner was of the view that Danvest and Bullhusq had acquired a direct beneficial interest in the underlying assets of the partnership: ss 7(1)(a), 10(1)(a)(i) and 10(1)(ac). Consequently, there was a change in the beneficial ownership of dutiable property pursuant to s 7(1)(b)(vi) of the DA.

An assessment in excess of $1.765m issued in April 2015.

The key issue was characterising the partnership interests transferred. The sale would be dutiable if the partnership interests themselves were dutiable property or if they effected a change in the beneficial ownership of dutiable property.

"Dutiable property" is defined by s 10(1) of the DA to include an estate if fee simple or an interest in any dutiable property: ss 10(1)(a)(i) and 10(1)(ac). A dutiable transaction includes a transfer of dutiable property (s 7(1)(a)) or "any other transaction that results in a change in beneficial ownership of dutiable property" (s 7(1)(b)(vi)). The expression "*beneficial ownership"* is defined to include, but is not limited to, ownership of dutiable property by a person as trustee of a trust. The expression "c*hange in beneficial ownership*" is defined to include, but is not limited to—

- the creation of dutiable property;
- the extinguishment of dutiable property;
- a change in equitable interests in dutiable property;

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- dutiable property becoming the subject of a trust;
- dutiable property ceasing to be the subject of a trust.

In reaching its conclusion, the court considered the authorities including, in particular, the High Court decisions in *Commissioner of State Taxation (SA) v Cyril Henschke Pty Ltd* (2010) 242 CLR 508 as well as *Canny Gabriel Castle Jackson Advertising Pty Ltd v Volume Sales (Finance) Pty Ltd* (1974)131 CLR 321 and *CPT Custodian Pty Ltd v Commissioner of State Revenue* (2005) 224 CLR 98.

The court concluded that the interest held by a partner is a chose in action entitling the partner to a proportion of the surplus after the realisation of the assets and the payment of debts and liabilities: at [61]. Contrary to what was advanced by the Commissioner, the court found that a partner's interest did not confer an equitable interest in assets of the partnership. The court found that a partner enjoyed a right to surplus, if any, upon dissolution of the partnership and a right to participate in annual profits. A partner having this chose in action did not have a presently existing interest because the assets and liabilities were in flux and could not be identified with sufficient particularity. It is implicit from the decision that the nature of this unvested interest, which was not presently enforceable or calculable, implicitly did not answer the meaning of "interest in any dutiable property" in s 10(1)(ac) of the DA.

The court found that the position of both the manager and the partners was analogous to the trustee and unit holders respectively in *CPT Custodian*. The court stated that the present facts were like those in *Livingstone v Commissioner of Stamp Duties (Qld)* (1960) 107 CLR 411 and *CPT Custodian* where, "a trustee owns both legal and equitable ownership for others": at [96]. All that was conferred on the others are equitable rights against each other and against the trustee. It was not an interest in the sense used in s 10(1)(ac) of the DA.

The court concluded that the equitable chose in action acquired by Danvest and Bullhusq conferred no interest in the partnership property and did not cause any change in the beneficial ownership of such property.

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4 Duty and changes in beneficial ownership – recent developments

The Commissioner had more success in contending that a change in beneficial ownership of dutiable property occurred in *Rakmy Pty Ltd v Commissioner of State Revenue* [2017] VSC 237.

That case involved a change in capacity in which Rakmy Pty Ltd (**Rakmy**) held land in Richmond. Rakmy initially held the land as trustee for the Rakmy Investment Trust (**RIT**). There were three unit holders: Robert King, Maree Yann and Rakmy as trustee for the Rakmy Superannuation Fund (**RSF**). Although each held 500,000 units, the units were partly paid and varied from being almost fully paid to almost completely unpaid.

In June 2013, King and Yann entered a contract of sale to purchase the Richmond property for $825,000. At a meeting of unit holders in June 2014, the units of King and Yann were redeemed after they failed to pay the remainder of their units, after being called to do so. At the same meeting, a special resolution was passed that the Richmond property be vested in Rakmy as trustee for the RSF. The effect of these steps was that the Richmond property ceased to be an asset forming part of the RIT fund and became an asset forming part of the RSF.

It was common ground that there was no transfer of dutiable property that effected a dutiable transaction for the purposes of s 7(1) of the DA. Rather, the Commissioner assessed duty on the basis that the change in Rakmy's position as trustee was an "other transaction that resulted in a change of beneficial ownership" for the purposes of s 7(1)(b)(vi) of the DA.

Rakmy resisted the Commissioner's argument by contending that there was no change in the underlying equitable interests and that nothing that could be described as a change in ownership had occurred. It argued that the ultimate owner of the Richmond property, in substance, was the RSF (or its members) and that was the case both before and after the transaction.

The ambit of s 7(1)(b)(vi) was expanded following the decision in *Trust Company of Australia Ltd (as trustee for the Clayton 3 Trust) v Commissioner of State Revenue* (2007) 19 VR 111. Although Rakmy conceded that the amendments would overcome the decision (against the Commissioner) in the *Clayton 3* case, it contended that the facts in Rakmy were different. This was because Rakmy had beneficial ownership of the Richmond property at all times. Although Rakmy accepted that the Richmond property had ceased to be subject to the RIT, it maintained it already had beneficial ownership of it and that since the transaction did not increase or decrease that ownership, there was no change in beneficial ownership.

Rakmy's arguments were rejected. The definition of "beneficial ownership" in s 7(4) includes ownership of property "as trustee of a trust". The court accepted this plainly directed attention to the capacity in which a person holds dutiable property. When there is a transfer of dutiable property between two different trusts, there is a person who "obtains the beneficial ownership", namely ownership of the dutiable property, as trustee of the receiving trust. The fact that it may be the same legal person who relinquished "beneficial ownership" as trustee of the transferring trust was of no consequence for the purpose of charging duty on the deemed transfer. The court accepted that the suggestion that the movement of property between trusts cannot trigger duty unless there is also a

change in "underlying equitable interests" is inconsistent with the definition of "change in beneficial ownership" in s 7(4) of the DA.

Rakmy's argument that "nothing had changed" was rejected on the basis that the two trusts involved were markedly different. The RIT was a unit trust in which Rakmy held units but had no proprietary interest in the trust assets; it had no power to demand any property forming part of the fund to be conveyed to it. However, when the Richmond Property was transferred to Rakmy as trustee of the RSF, it had the full range of powers in respect of that property specified in the RSF Deed. The suggestion that the RSF or its members were the "owner[s]" of the Richmond Property immediately before the transaction was, the court found, consequently, misguided and contrary to authority.

In reaching its conclusions, the court found that Rakmy's approach started with and was driven by, an asserted purpose underlying the relevant provisions and that this was contrary to principles of statutory construction that had been amplified in cases such as *Certain Lloyds Underwriters* [2012] HCA 56.

For all of these reasons, there was no good reason why such a change of trusts should avoid duty simply because the trustee of each trust is the same person. The court was of the view that quite clearly, duty was to be imposed in the circumstances before it.

The Commissioner had allowed Rakmy a partial exemption as to one-third for the transfer of dutiable property from a trustee to a beneficiary pursuant to s 36B of the DA. Rakmy contended in the alternative that if the transaction was dutiable, it was entitled to a full exemption pursuant to s 36B of the DA. For the reasons set out in the "Transfers from trust to beneficiaries" section of this paper, the court similarly dismissed Rakmy's appeal in this regard.

The decision in Rakmy is not on appeal.

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5 Transfers from trusts to beneficiaries - duty exemption granted or denied?

Exemptions are contained in ss 36, 36A and 36B of the DA in relation to the transfer of dutiable property from the trustee of a fixed trust, discretionary trust or unit trust scheme respectively to a beneficiary. An exemption is also contained in s 41A for the transfer of dutiable property transferred from a superannuation fund to a beneficiary of the fund.

It is not the function of this paper to provide a detailed description of each of the exemptions available. However, it is noted that the terms "fixed trust", "discretionary trust" and "unit trust scheme" are all defined terms in the DA. Careful regard needs to be given to the deed at hand and the type of trust it answers. Beyond this, each of the exemptions broadly requires that:

a. the duty (if any) charged by the DA when the dutiable property was vested in the transferring trust has been paid or the Commissioner is satisfied will be paid;

b. the beneficiary was a beneficiary at the time the dutiable property was vested in the transferring trust (fixed trust and UTS) or in the case of a discretionary trust, became a beneficiary after that time by reason of falling within a class of specified relations to a beneficiary (such as becoming a spouse, domestic partner, lineal descendant or step child of a beneficiary);

c. the transfer is either to the beneficiary absolutely or to the beneficiary as trustee of another trust which answers strict criteria; and

d. the Commissioner is satisfied that the transfer is not part of a sale or other arrangement under which there exists any consideration for the transfer. The Commissioner is not to treat a transfer as part of a sale or arrangement if, after the transfer, a beneficiary or a unit holder gives or assumes a mortgage/liability under a mortgage to secure the same or a greater amount as that to which the property was subject if the Commissioner is satisfied that the giving of the mortgage or assumption of liability is not part of a sale/other arrangement: s 36C.

The requirements above should not be seen as conclusive by any means.

The exemption for transfers from trusts to beneficiaries is a frequently litigated area. In many instances, the timing requirements of the legislation (in terms of the receiving trusts/beneficiaries existing at the time the properties were acquired) is not satisfied: see *Liu v Commissioner of State Revenue* [2016] VCAT 87. In other instances, the taxpayer is unable to lead cogent evidence as to the creation or existence of a trust: see *Kloester v Commissioner of State Revenue* [2016] VCAT 16.

One of the key common requirements is that the transfer not be part of a sale or other arrangement under which there exists any consideration for the transfer. The concept of "consideration" in particular, is widely construed by the Commissioner. It extends to loan accounts that will be discharged or by necessity forgiven by reason of the transfer (likely if the only asset of significance is the property being transferred). The decision of Macnamara DP (as he then was) in *Westella Nominees v Commissioner of State Revenue* [2010] VCAT 1786 and Hollingworth J in *Shop, Distributive and Allied Employees Assoc (SDAEA) v Commissioner of State Revenue* [2005] VSC 484

provides further guidance about how courts approach this issue. Careful regard should be given to the SRO's evidentiary manual as to the documents that will be required (including three years of accounts) before the transaction is undertaken.

As always, the requirements of the relevant exemption need to be carefully considered against the deed in question. In *Commissioner of State Revenue v Antonino Arrigo* [2016] VSCA 339, five investors established a unit trust to purchase a property. The property was to be developed and subdivided into 5 separate lots. The units in the unit trust were divided into five nominated classes with one hundred units in each class. It was envisaged that after development and subdivision, each lot or apartment would be distributed to the respective unit holder.

At first instance, Dyer J in VCAT held that, upon registration of the plan of subdivision, a fixed trust came into existence and that the subsequent transfer of the lot to the respondent unit holder was pursuant to a fixed trust, with the result that s 36, and not s 36B, applied to the transfer. No duty was payable.

The Commissioner's appeal was allowed. The court noted that the expression "fixed trust" and unit trust scheme" were defined in in the DA and did not carry their ordinary meaning: [48]. The court found that on proper construction of the deed, a single unit trust was created. The Court of Appeal found that the Trust Fund was capable of comprising more than the parent property and contemplated not only the conversion of the Trust Fund but also the subdivision of any real property comprising all or part of it. The trust which existed both before and after the subdivision was a trust to which a unit trust scheme related. The orders of the VCAT were set aside and the matter remitted to the tribunal for further hearing and determination.

In *Rakmy*, it was uncontroversial that the RIT was a unit trust scheme. The Commissioner accepted that all of the requirements in s 36B(1) were satisfied save for paragraph (d). It is in the following terms:

> (1) No duty is chargeable under this Chapter in respect of a transfer of dutiable property that is subject to a unit trust scheme (***the principal scheme***) to a unitholder in the scheme if—
>
> ...
>
> (d) the dutiable value of the property transferred as a proportion of the net assets of the principal scheme does not exceed the value of that proportion of the net assets of the principal scheme represented by the unitholding of the unitholder in the principal scheme at the relevant time; and ...
>
> ...
>
> (3) If a unitholder would be entitled to an exemption from duty under subsection (1) but for subsection (1)(d), the unitholder is entitled to a concession from duty in respect of that proportion of the dutiable value of the dutiable property that does not exceed that proportion of the net assets of the scheme represented by the unitholding of the unitholder in the principal scheme at the relevant time.

In issue in Rakmy was the "proportion of the net assets of the principal scheme represented by the unitholding of the unitholder in the principal scheme at the relevant time ", namely, 24 January 2014. The Commissioner contended that that the proportion was one-third, based on the number of units in RIT that the RSF owned on 24 January 2014. Rakmy contended that the differing rights of

fully paid units as opposed to partly paid units must be taken into account. On that basis, the relevant proportion was 99.98%.

Rakmy did not dispute that the dutiable value of the Richmond property as a proportion of the net assets of the RIT was at least 64%. It was entitled to a full exemption, it maintained, on the basis that the proportion of the net assets represented by its unit holdings was 99.98%.

However, after examining the terms of the RIT deed, the court found that when the Richmond property became subject to the RIT, Rakmy held one-third of the issued units. The main consequence of some units being partly unpaid was the existence of a liability to the trustee for the unpaid amount. That is, the partly paid units of King and Yann still conferred an equal interest in the trust fund.

The court found that in order to satisfy the requirement in s 36B(1)(d), the property transferred to Rakmy as trustee for the RSF cannot exceed the value of one-third of the net assets of the RIT. That requirement was not satisfied (the dutiable value of the Richmond property as a proportion of the net assets of the RIT was at least 64%). However, since Rakmy did hold one-third of the units in the RIT at the relevant time, it was entitled to a proportionate concession as to one-third of the value of the Richmond property.

Ascertaining the correct construction of the formula in paragraph (1)(d) above has long been an issue for practitioners practising in the area. Rakmy submitted that the provision contained an obvious error since it required a comparison between a proportion to a value which did not make sense. Rakmy agitated that the words "value of that" after the word "exceed the" in s 36B(1)(d). The Commissioner agreed that although s 36B(1)(d) required a comparison between a proportion and a value, it may be applied on the basis that it required a comparison between the proportion of the net assets of the trust represented by the unit holding and the proportion of the dutiable value of the net assets represented by the property transferred. Ultimately, the Commissioner's position was accepted – namely the property transferred to Rakmy as trustee for the RSF cannot exceed the value of one-third of the net assets of the RIT.

6 Other developments

There are numerous other aspects of state taxation in which there have been some developments. It is beyond the purpose of this paper to cover them all. Two further areas that will be considered are the High Court decision in *ACN 005 057 349 Pty Ltd* and some recent cases involving the change of trustee duty exemption.

The Commissioner was successful in the High Court in *Commissioner of State Revenue v ACN 005 057 349 Pty Ltd*. The taxpayer in *ACN* discovered that a "duplicate property" error had been made in relation to its 1990-2002 land tax assessments for two adjoining properties (after receiving refunds for the same error in relation to the 2008-2011 land tax years). The taxpayer was out of time to object to the 1990-2002 years but requested the Commissioner issue amended land tax assessments for those years pursuant to s 19 of the LTA 1958 (predecessor to the LTA 2005). Section 19 was in the following terms:

> "The Commissioner may from time to time amend an assessment by making such alterations or additions to it as he thinks necessary to ensure its completeness and accuracy, and shall notify to the taxpayer affected every alteration or addition which has the effect of imposing any fresh liability or increasing any existing liability and unless made with the consent of the taxpayer every such alteration or addition shall be subject to objection in the same manner and to the same extent as the original assessment but the validity of an assessment shall not be affected by reason only that any of the provisions of [the LTA] have not been complied with."

The Commissioner refused the taxpayer's request, on the basis that s 90AA did not permit the refund sought. That provision stated, essentially, that proceedings for a refund of tax paid under the Act must not be brought against the Commissioner unless an application for the refund was lodged within three years of the payment being made.

The taxpayer commenced two proceedings. The first was for an action for mandamus directing the Commissioner to issue the amended assessments and refund the excess amount ($363,680) with interest. The second proceeding, by a writ indorsed with a statement of claim, sought restitution of the excess amount, with interest.

The taxpayer was unsuccessful before Sloss J in the Supreme Court. The Court of Appeal however allowed the taxpayer's appeals. It held that, as the Commissioner knew alterations were necessary to ensure the completeness and accuracy of the assessments, he had a duty under s 19 of the LTA to issue amended assessments and refund the excess amount. It also took the view that the Commissioner's failure to amend the assessments and issue the refund constituted conscious maladministration.

In the final chapter of this trilogy, the High Court allowed the Commissioner's appeal. It found that s 19 granted the Commissioner the power, rather than an obligation to amend the assessments. Further, no refund could be made as the application for refund was not made within 3 years of the payments as required by s 90AA(6). In any event, s 90AA barred the taxpayer's claims for a refund since it provided that proceedings for the "refund or recovery of tax" could not be bought "except as provided in this section": at [70], [74]. Accordingly, it found that the Court of Appeal had erred in

allowing the proceedings to be brought. In relation to the claim for restitution, the court found that as the payment discharged a debt, the Commissioner had not been unjustly enriched.

Finally, the High Court found there had been no conscious maladministration by the Commissioner in not amending the assessments. It was not contended, and there was no basis to find, that the refusal by the Commissioner to amend the assessments was not in good faith or bona fide, being based on a construction of the LTA that was not only open, but correct: at [4], [83].

A further aspect of state taxation that is commonly litigated is the duties exemption relating to a change in trustee. Section 33(3) of the DA is in the following terms:

> No duty is chargeable under this Chapter in respect of a transfer of dutiable property to a person other than a special trustee if the Commissioner is satisfied that the transfer is made solely—
>
> (a) because of the retirement of a trustee or the appointment of a new trustee, or other change in trustees; and
>
> (b) in order to vest the property in the trustees for the time being entitled to hold it.

As is apparent, of critical importance is whether the transfer is "solely" because of the retirement of a trustee or appointment of a new trustee. As Hansen JA stated in *Commissioner of State Revenue v Konnan Pty Ltd* [2015] VSCA 278:

> "It is important to bear in mind the dominant importance of the language in which the exemption is granted, read in the context of the Duties Act and considered in the light of the evident policy to save from duty transfers of land made 'solely because of' a change in trustee. Without overlooking the full terms of s 33(3), that is the nub of it, or the broad policy involved".

The exemption only applies to the appointment of a trustee to a pre-existing trust, not a new trust. In *Michaelides & Anor v Commissioner of State Revenue* [2016] VSC 256, two friends purchased a property for development through a company acting as trustee of a partnership (of trusts). The trustee was to develop two townhouses. Towards the end of the development, the property was transferred from the trustee to the directors of the trustee. They were assessed to duty. The applicants were unsuccessful in VCAT and on appeal in the Supreme Court. The tribunal found that prior to the transfer, the trustee company held the property on trust "as a whole undivided interest" but that subsequent to the transfer, each of the taxpayers held a half interest as tenants in common. The exemption did not apply to the appointment of a newly created trust or to a different or separate trust. There was no evidence the applicants had been appointed as trustees of the same trust (which was not in writing) that held the property prior to transfer.

In *White Rock Properties Pty Ltd v Commissioner of State Revenue* [2015] VSCA 77, the reverse occurred. Five testamentary trustees each held a one-fifth interest in land as tenants in common prior to the transfer. After the transfer, the appellant held the entire fee simple estate in the land as trustee agent for a partnership between the testamentary trustees. The Court of Appeal decided that the appellant held the land on a new and different trust so that the exemption under s 33(3) was not available.

The taxpayer was successful in relation to the s 33(3) exemption in *Commissioner of State Revenue v Konann Pty Ltd* [2015] VSCA 278. The property in *Konann* was originally but mistakenly registered to two individuals as trustee of a family trust. However, it should have been registered to the two individuals as trustees for a corporate beneficiary, which had funded the purchase. Some time later,

the property was transferred to Konann to facilitate the retirement of the two individual trustees. The taxpayer was unsuccessful in VCAT however its appeal was allowed in the Supreme Court. The Commissioner's appeal to the Court of Appeal was dismissed. The Court of Appeal found that the corporate beneficiary was the beneficial owner (because of a resulting trust) because it supplied the funds for the purchase and the purpose of the transfer to Konann was to change the trustee of the same resulting trust in favour of it. It did not include the purpose of changing the beneficiary of that trust.

Finally, one contentious issue involving s 33(3) litigation is how widely the term "solely" should be interpreted and the extent to which the taxpayer's wider agenda can be considered. In this regard, the decision of Hollingworth J in *Commissioner of State Revenue v Challenger Property Nominees Pty Ltd* [2006] VSC 203 is a decision that in my view, favours the taxpayer. At first instance, the VCAT member noted that there will always be a reason for a change in trustee. In the Supreme Court, Hollingworth J agreed that the proper approach is to ask "is the only purpose of the transfer to give effect to the change of trusteeship?'" as opposed to "why did the trustee resign?" Although it is appropriate to look at the context in which the transfer occurred and to perform some sort of "reality check", it was nevertheless necessary to analyse what had happened from a legal point of view and having regard to the actual transaction: at [36].

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