



Explanatory Statement

PAYG Withholding variation for foreign resident capital gains withholding payments – no residue after a mortgagee exercises a power of sale 2020

General Outline of Instrument

1. This instrument is made under subsection 14-235(5) of Schedule 1 to the *Taxation Administration Act 1953*.
2. All legislative references in this explanatory statement are to Schedule 1 to the *Taxation Administration Act 1953* unless otherwise stated.
3. If a mortgagee exercises its rights to dispose of taxable Australian real property assets and it satisfies the definition of an “authorised deposit-taking institution” under section 5 of the *Banking Act 1959* then they do not need to obtain a variation under subsection 14-235(2) from the Commissioner of Taxation (‘the Commissioner’) in the circumstances prescribed in this legislative instrument.
4. The instrument is a legislative instrument for the purposes of the *Legislation Act 2003*.
5. Under subsection 33(3) of the *Acts Interpretation Act 1901*, where an Act confers a power to make, grant or issue any instrument of a legislative or administrative character (including rules, regulations or by-laws), the power shall be construed as including a power exercisable in the like manner and subject to the like conditions (if any) to repeal, rescind, revoke, amend, or vary any such instrument.

Date of effect

6. The instrument commences on the day after its registration on the Federal Register of Legislation.
7. Under section 12(2) of the *Legislation Act 2003* this instrument does not adversely affect the rights or liabilities of any person other than the Commonwealth.

What is the effect of this instrument

8. The effect of this instrument is to vary to nil the amount that would otherwise have to be paid to the Commissioner under section 14-200, when land is acquired in the following circumstances:
 - (a) there is a transaction where a mortgagee exercises a power of sale over the land and it is an authorised deposit-taking institution under section 5 of the *Banking Act 1959*;
 - (b) the mortgagee has determined that the residue from the sale proceeds will be zero or less than zero; and

- (c) the mortgagee has provided the transferee with a written declaration stating that the amount to withhold is varied to nil under this instrument.

9. This legislative instrument will remove the need for the mortgagee to make an application to the Commissioner for a variation under subsection 14-235(2).

10. The new instrument is of a minor or machinery nature. An assessment of the compliance cost impact indicates that both implementation and on-going compliance costs will be minor. This instrument reduces the compliance costs of the mortgagees exercising powers of sale.

Background

11. The instrument has been developed to ensure that there is certainty for transferees and mortgagees in the relevant transaction that no amount is required to be withheld where there is no residue that will be payable to the mortgagor. This instrument will ensure there are no unintended consequences for the parties to a conveyancing process in the event that failure to obtain a variation results in delay or failure to complete settlement.

12. Variations are commonly sought where a mortgagee has exercised a power of sale over the property and has determined that after satisfying the obligation to withhold at a rate of 12.5% there will be insufficient funds to discharge the mortgage over the property.

13. The amount payable to the Commissioner under the withholding regime is generally 12.5% of the first element of the cost base of the asset being acquired (the 'purchase price'), unless the Commissioner exercises the discretion under section 14-235 to vary the amount or classes of amounts.

14. The PAYG system, introduced in *A New Tax System (Pay As You Go) Act 1999*, is a simple and convenient way for individual taxpayers to meet their annual income tax liabilities either through instalments or through withholding as their income is earned. This system aims to prevent large end-of-year tax bills for relevant entities. It also ensures that the Government has the revenue it needs during the year to provide services and benefits to the community.

15. Subdivision 14-D forms part of the Pay As You Go Withholding system and its purpose is to assist in the collection of capital gains tax from foreign residents.

16. Subdivision 14-D requires that an amount be paid to the Commissioner in relation to the acquisition of certain assets from one or more entities where at least one of those entities is a foreign resident within the meaning of section 14-210 at the time the transaction is entered into.

17. Paragraph 14-200(1)(a) provides that an amount is payable to the Commissioner if "you become the owner of a relevant CGT asset as a result of acquiring it from one or more entities under one or more transactions". Under subsection 14-200(2), the amount must be paid to the Commissioner "on or before the day you became the CGT asset's owner". The amount to be withheld is 12.5% of the purchase price.

18. In limited circumstances, transferees are not required to withhold and remit part of the purchase moneys to the Commissioner in relation to the acquisition of a relevant CGT asset. For example, where the vendor has provided a valid clearance certificate on or before settlement (subsection 14-210(2)), or the property has a market value of less than \$750,000.00 (subsection 14-215(1)).

19. In the absence of a variation under section 14-235, either separately sought and made under subsection 14-235(2) and (3) or as provided under this instrument, when a person acquires land in a transaction where a mortgagee was exercising a power of sale, subsection 14-200(3) would require an amount to be paid to the Commissioner equal to 12.5% of the purchase price.

20. The 'residue' in this context is the amount remaining after expenses incidental to the sale and amounts payable to registered mortgagees over the asset are deducted from the sale proceeds. The expenses incidental to the sale include amounts that are ordinarily payable during the conveyancing process such as adjustments for council rates, land tax, water rates, legal fees and conveyancing fees.

21. For completeness, in the event that there is a residue payable to the mortgagor, but this is insufficient to satisfy the withholding obligation at 12.5%, this legislative instrument will not apply and a variation request must still be submitted to the Commissioner. A variation request must also be submitted to the Commissioner in the event that the power of sale is subject to potential challenges or disputes (such as equitable claims), or there is any other uncertainty regarding the application of sale proceeds.

22. The variation provided by this instrument is consistent with the legislative direction provided in subsection 14-235(1) that the Commissioner is to have regard to the need to protect a creditor's right to recover a debt.

Commissioner's Variation Power

23. Foreign resident owners of land are not entitled to obtain a clearance certificate and would therefore not be able to provide one to a transferee. This means there will generally be a withholding obligation on a transferee acquiring land with a market value of \$750,000.00 or more in a transaction where a mortgagee is exercising a power of sale over land owned by a foreign resident mortgagor.

24. In circumstances where the transferee has the obligation to withhold and remit part of the purchase moneys to the Commissioner, a mortgagee has the option of applying to the Commissioner for a variation to the 12.5% withholding rate, including to nil. In exercising the power to vary an amount under section 14-235 the Commissioner must have regard to the need to protect a creditor's right to recover a debt. This means that the Commissioner will generally allow a variation by a mortgagee where the sales proceeds are insufficient to discharge a mortgage and also satisfy the withholding obligation.

25. For the variation to be valid, it must be obtained by, or notified to, the transferee by the time they become the owner of the asset. If a variation cannot be obtained by the relevant time, the transferee would be required to pay the Commissioner an amount equal to 12.5% of the purchase price.

Conveyancing process

26. In all Australian states and territories, mortgagees are given a power of sale where mortgage money has become due and payable, and other conditions are satisfied.¹ Generally, the power of sale authorises the mortgagee to sell the mortgaged property by public auction or private contract, and execute all such instruments as is necessary for effective sale of the property.² There are also incidental powers available to mortgagees such as the power to sell part of the property, or things attached to the property such as mines and minerals.

¹ See *Real Property Act 1900 (NSW)* section 58; *Property Law Act 1974 (Qld)* section 83; *Property Law Act 1958 (Vic)* section 101; *Law of Property Act 1936 (SA)* section 47; *Conveyancing and Law of Property Act 1884 (Tas)* section 21; *Law of Property Act 2000 (NT)* sections 86 and 87; *Land Titles Act 1925 (ACT)* section 94; and *Property Law Act 1969 (WA)* section 57.

² This particular form of words is used in subsection 58(1) of the *Real Property Act 1900 (NSW)*.

27. As a result of exercising a power of sale, the mortgagee assumes various duties and obligations with respect to the sale proceeds. Although the particular provisions differ in each state and territory, the requirements concerning the application of the sale proceeds are broadly consistent. That is, the mortgagee is required to apply sale proceeds in the following order: (i) payment of all costs, charges and expenses incurred incidental to the sale, (ii) discharge of mortgage money, interest, costs and other moneys due under the mortgage, and (iii) where there is any residue remaining, such moneys are to be paid to the mortgagor.³ In New South Wales and the Northern Territory, the provisions specifically provide that subsequent mortgages are to be paid prior to the residue being distributed to the mortgagor.

28. Accordingly, a mortgagee exercising a power of sale will be required to ascertain all costs, mortgages, and subsequent mortgages associated with the mortgaged property and duly account for such payments from the sale proceeds.

29. A mortgagee exercising a power of sale over mortgaged property is in the best position to determine whether any part of the sale proceeds will be available to the mortgagor, and thus whether it is possible to satisfy the withholding obligation from the sales proceeds for the purposes of foreign resident capital gains withholding.

Consultation

30. Subsection 17(1) of the *Legislation Act 2003* requires that the rule-maker undertake an appropriate level of consultation that is reasonably practicable to undertake before making a legislative instrument.

31. The draft instrument and explanatory statement was published on the ATO Legal database. There was an awareness across businesses, individuals and industry associations who subscribe to that website.

32. Copies of the draft legislative instrument and explanatory statement were sent to peak industry bodies for comment. All feedback received was considered and, where appropriate, it was included to improve the instrument's application.

Legislative references

A New Tax System (Pay As You Go) Act 1999
Acts Interpretation Act 1901
Banking Act 1959
Conveyancing and Law of Property Act 1884 (Tas)
Human Rights (Parliamentary Scrutiny) Act 2011
Income Tax Assessment Act 1997
Land Titles Act 1925 (ACT)
Law of Property Act 2000 (NT)
Law of Property Act 1936 (SA)
Legislation Act 2003
Property Law Act 1974 (Qld)
Property Law Act 1958 (Vic)
Property Law Act 1969 (WA)

³ See *Real Property Act 1900 (NSW)* subsection 58(3); *Property Law Act 1974 (Qld)* section 88; *Property Law Act 1958 (Vic)* section 105; *Law of Property Act 1936 (SA)* section 50; *Conveyancing and Law of Property Act 1884 (Tas)* section 23; *Law of Property Act 2000 (NT)* section 93; *Land Titles Act 1925 (ACT)* section 94; and *Property Law Act 1969 (WA)* section 61.

Real Property Act 1900 (NSW)
Taxation Administration Act 1953

Statement of compatibility with Human Rights

Prepared in accordance with Part 3 of the *Human Rights (Parliamentary Scrutiny) Act 2011*

Title of Legislative Instrument

This Legislative Instrument is compatible with the human rights and freedoms recognised or declared in the international instruments listed in section 3 of the *Human Rights (Parliamentary Scrutiny) Act 2011*.

Overview of the Legislative Instrument

This disallowable legislative instrument avoids the imposition of an unnecessary withholding where the Commissioner would agree to vary the withholding to nil when an authorised deposit-taking institution exercises the power of sale of Australian real property owned by a foreign resident and the proceeds of sale are insufficient to discharge the mortgage.

Human rights implications

This legislative instrument does not engage any of the applicable rights or freedoms because the new instrument is of a minor or machinery nature. The instrument avoids unnecessary withholding in circumstances where no tax will be payable.

Conclusion

This Legislative Instrument is compatible with human rights as it does not raise any human rights issues.