

Foreign resident capital gains withholding payments

Important: From 1 July 2016 Australian residents selling real estate with a market value of \$2 million or more will need to apply for a clearance certificate from the Australian Taxation Office (ATO) to ensure amounts are not withheld from the sale proceeds.

Where a valid clearance certificate is not provided by settlement, the purchaser is required to withhold 10% of the purchase price and pay this to the ATO.

Background

In May 2013 the government of the day announced that it would introduce a 10% non-final withholding tax on payments made to foreign residents who dispose of certain taxable Australian property with a market value above a specified threshold. The new legislation for this measure became law in February 2016.

The types of taxable Australian property this applies to include vacant land, buildings, residential and commercial property, leaseholds and strata title schemes.

What this means for purchasers

Where a foreign resident disposes of Australian real property with a market value of \$2 million or above, **the purchaser** will be required to withhold 10% of the purchase price* and pay it to the Australian Taxation Office (ATO) unless the seller provides you with a variation. Australian residents will need to provide a clearance certificate otherwise a withhold of 10% of the purchase price will apply.

What this means for sellers

Australian resident vendors who dispose of Australian real property with a market value of \$2 million or above will need to apply for a clearance certificate from the ATO to ensure amounts are not withheld from their sale proceeds.

All transactions involving real property with a market value of \$2 million or above will need the vendor and purchaser to consider if a clearance certificate is required.

If a purchase price negotiated between a purchaser and vendor is on an 'arm's length basis', then the purchase price may be used as a proxy for market value.

* Note: The legislation specifies that the 10% withholding is on the 'first element of the cost base'. However, as purchase price is understood by vendors and purchasers, and in many instances will be equal to the 'first element of the cost base', we have used the term purchase price for simplicity.

When will this apply?

The new withholding regime will apply to contracts entered into on or after 1 July 2016 for the sale of property with a market value of \$2 million or above.

What if there are multiple purchasers?

The market value of all purchasers' interests in the transaction must be aggregated in examining whether the \$2 million market value threshold has been reached. If the aggregated purchase price is \$2 million or above, each purchaser must withhold in proportion to their percentage of the total purchase price.



What if there are multiple vendors?

If there are multiple vendors disposing of the property, it is the total market value of the property that determines whether withholding is required by the purchaser.

That is, if the market value is \$2 million or above then the purchaser must withhold 10% of this (remembering that the purchase price may be able to be used as a proxy for market value).

If the purchaser has not been provided with a clearance certificate or a notice of variation from any of the vendors, the purchaser must withhold 10% of the purchase price.

The amount of withholding will be in proportion to each vendor's interest in the property, with the total withholding equal to 10% of the property's market value.

If any of the vendors provide a clearance certificate or a notice of variation then the amount withheld by the purchaser on that vendor's proportional interest in the property must reflect this. The purchaser must consider each vendor's circumstances separately in determining the amount to withhold from each vendor.

Clearance certificates

All real property transactions with a market value of \$2 million or above will need the vendor and purchaser to consider if a clearance certificate is required.

Where a clearance certificate is provided, the purchaser is not required to withhold an amount from the purchase price.

Vendors need to provide a clearance certificate to the purchaser on or before the settlement of the transaction. A clearance certificate must be valid at the time it is provided to the purchaser.

Clearance certificates are valid for 12 months, and can be used by the same vendor for the sale of multiple properties while valid.

Who can obtain a clearance certificate?

Only a vendor who is an Australian resident* can be granted a clearance certificate by the ATO.

* Note: Residency status for tax purposes is not the same as that for immigration purposes, or for the Foreign Investment Review Board (FIRB). If you are unsure, seek professional advice.

What if the vendor does not provide a clearance certificate?

If the vendor fails to provide the clearance certificate by settlement, the purchaser is required to withhold 10% of the purchase price and pay this to the ATO.

This means Australian resident vendors of real property with a market value of \$2 million or above must apply for a clearance certificate to ensure no funds are withheld from their sale proceeds.

When can an Australian resident vendor obtain a clearance certificate?

An Australian resident vendor may apply to the ATO for a clearance certificate at any time when considering the disposal of real property. This can be before the property is listed for sale.

How can an Australian resident vendor obtain a clearance certificate?

To obtain a clearance certificate, a vendor who is an Australian resident (or their representative) must complete an online 'Clearance certificate application for Australian residents' form. This form will be available on ato.gov.au/FRCGW from 27 June 2016.

A PDF version of the clearance certificate application will be available for contracts that are to be signed and settled within the first two weeks of July 2016. Otherwise, vendors should be encouraged to wait and use the online form from 27 June 2016.

If the vendor is automatically assessed as an Australian resident, a clearance certificate will be issued electronically within days of the application being submitted.

If there are data irregularities or exceptions, some manual processing may be required and the clearance certificate will be provided within 14–28 days.

Higher risk and unusual cases may require greater manual intervention and could take longer to process.

Variation applications

Where the vendor is not entitled to a clearance certificate, but believes a withholding of 10% is inappropriate, they can apply to the ATO for a variation. Reasons for a variation could include:

- a foreign resident not making a capital gain on the transaction (for example, because they will make a capital loss or a CGT rollover applies)
- a foreign resident not otherwise having an income tax liability (for example, because of carried-forward capital losses or tax losses)
- a scenario where there are multiple vendors, only one of which is a foreign resident.

A variation application can be made using the 'Variation application for foreign residents and other parties' form. This form will be available on ato.gov.au/FRCGW from 27 June 2016.

A PDF version of the variation application will be available for contracts that are to be signed and settled within the first two weeks of July 2016. Otherwise, vendors should be encouraged to wait and use the online form from 27 June 2016.

In the majority of cases (where the ATO has all the required information and the application is successful), the notice of variation will be provided within 28 days.

The notice of variation should be shown to the purchaser before settlement to ensure the reduced withholding rate applies.

Does the withholding need to be provided prior to settlement?

No. The withholding does not need to be provided until settlement, and it is provided by the purchaser out of the purchase price, not in addition to the purchase price.

Is the transfer of ownership affected?

No, the withholding does not affect the transfer of ownership between the vendor and the purchaser.

In some cases the vendor may wish to postpone settlement if they have not yet obtained a clearance certificate or notice of variation, to avoid the purchaser withholding 10% of the purchase price and paying it to the ATO. In this scenario, the terms of the contract will apply as normal with respect to delays at settlement.

What do I need to consider when selling a property?

Where you are engaged by a vendor you need to know what the purchase price will be to determine whether this measure applies. If the purchase price is below \$2 million, and it has been negotiated on an arm's length basis, then no action is required.

If the purchase price is \$2 million or above and the vendor is an Australian resident vendor, you should let them know they will need to obtain a clearance certificate from the ATO to avoid 10% of the purchase price being withheld at settlement.

If you are unsure about the purchase price because the property is going to auction, you should let the Australian resident vendor know they will need a clearance certificate if the purchase price reaches \$2 million.

If the purchase price is \$2 million or above and the vendor is a foreign resident, you should let them know that 10% of the purchase price will be withheld at settlement by the purchaser and provided to the ATO. You should advise them they may be able to vary the amount that is withheld at settlement in certain circumstances, and direct them to the Variation application for foreign residents and other parties form.

What if there is a short settlement period?

The same rules apply irrespective of the length of the settlement period. However, if there is a short settlement period you should advise the vendor they will need to obtain a clearance certificate or notice of variation (as appropriate) as soon as possible if they wish to avoid 10% of the purchase price being withheld at settlement.

More information

The Australian Institute of Conveyancers was extensively involved in the consultation process for this measure. As such, the ATO is not aware of any inconsistency with the terms of each state's Conveyancing Act.

This fact sheet contains general information. More detailed information about foreign resident capital gains withholding payments is available at ato.gov.au/FRCGW

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