



2002-03 Budget Amendment Stamp Duty and Partnerships

This circular provides information on amendments introduced as part of the 2002-03 Budget that clarify the stamp duty consequences involving interests in partnerships. These amendments commence from 10 October 2002.

Summary

In summary, the amendments clarify the method of assessing changes in partnership interests by:

- (a) being contained in a separate Division which more clearly details the method of assessment
- (b) specifically addressing different types of partnership interests and
- (c) specifically addressing the variety of ways a person may acquire a partnership interest.

Background

When a person acquires an interest in a partnership that holds dutiable property, there is a conveyance of that property. As a consequence, this person is generally required to pay conveyance stamp duty on the conveyance of property.

These amendments do not represent any change to this underlying policy.

They provide clear legislative guidance as to how changes to, and acquisitions of, partnership interests are to be assessed for stamp duty purposes.

Partnership

A partnership is the relationship that exists between persons carrying on a business in common with a view of making a profit. Unlike a company or a person, a partnership is not a separate legal entity. Accordingly, references to partnership property will include property that is held by the partners of a partnership on behalf of that partnership.

Partnership interest

A partnership interest can be:

- the percentage of the value of a partner's entitlements in the partnership or
- the profit-sharing percentage that a partner acquires on becoming a partner, or when the person's partnership interest increases.

If either of these circumstances do not apply, a partnership interest is determined as the greater of:

- the percentage of the partnership capital that the person has contributed (or is obliged to contribute) or
- the percentage of the partnership losses that the person is required to bear.

Partnership acquisition

A partnership acquisition occurs when a person acquires an interest in a partnership that holds dutiable property. As a partnership acquisition is a conveyance of dutiable property, stamp duty at conveyance rates will be imposed.

A person acquires a partnership interest if a partnership is formed or if the person's partnership interest increases. The formation of a partnership will include a change in the membership of a partnership or the merger of 2 or more partnerships. A person's partnership interest may increase:

- under the terms of a partnership agreement

cont. over ...

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- on the retirement of a partner from a partnership or
- on a change in the terms of a partnership agreement effecting a change in the interests of the partners.

A partnership interest is **not** considered to have increased for stamp duty purposes where a partner's entitlement increases only as a result of their performance as a partner. However, such an increase will be considered to be an acquisition of an interest where the increase arises under an arrangement that creates an obligation to contribute to the capital or losses of the partnership, or where consideration is payable.

Dutiable value

The dutiable value of a partnership acquisition is the greater of:

- the consideration for the acquisition (ie. the consideration for the conveyance of the interest in the dutiable property held by the partnership) and
- the unencumbered value of the acquisition.

The unencumbered value of the acquisition is determined by multiplying the partnership interest (percentage) by the **unencumbered value** of all of the dutiable property held by the partnership. Where a person already holds a partnership interest and subsequently increases their interest, duty will only be assessed on the extent of the increase. As the partnership interest is multiplied by the **unencumbered value** of the dutiable property, any debts or liabilities of the partnership are disregarded in determining this value.

Also, in determining the unencumbered value of a partner's partnership acquisition, allowance is made for any dutiable property that the partner contributed to the partnership on its formation.

Examples

The examples given in the following pages illustrate how the amendments apply in different circumstances.

Formation of a partnership

1. A and B establish the AB partnership and execute a partnership agreement. Each partner is entitled to share equally in the capital and profits. The initial partnership capital consists of dutiable property owned by B having an unencumbered value of \$400 000. However the property is subject to a mortgage of \$300 000 which the partnership agrees to take over.

A has made a partnership acquisition because the AB partnership holds dutiable property. A's partnership interest of 50 per cent was acquired on the formation of the partnership. The dutiable value of the partnership acquisition is the greater of the consideration for the interest or the unencumbered value of that interest.

In this case, the consideration for the acquisition is \$150 000, (ie, an assumption of 50 per cent of the \$300 000 liability). However, the unencumbered value of A's partnership acquisition is \$200 000 (ie, an acquisition of a 50 per cent interest in dutiable property with an unencumbered value of \$400 000). *Note: any debts or liabilities of the partnership, such as the \$300 000 mortgage, do not reduce this value. Accordingly, the dutiable value of A's partnership acquisition is \$200 000.*

In comparison, when determining the unencumbered value of B's partnership acquisition, allowance is made for the dutiable property that B contributed to the partnership. B's partnership acquisition is therefore zero as its interest in the dutiable property of the partnership has not increased.

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Admission of a new partner

2. C, D and E are equal partners in the CDE partnership. This partnership holds dutiable property with an unencumbered value of \$200 000. They agree to admit F as an equal partner.

F made no contribution on becoming a partner, and has acquired a partnership interest of 25 per cent. The dutiable value of F's acquisition is the greater of the consideration or the unencumbered value. In this case, as no consideration has been paid, the dutiable value of F's partnership acquisition is \$50 000 (ie, 25 per cent of the value of the partnership's dutiable property worth \$200 000).

No duty is payable by C, D or E, as they have not acquired an increased interest in dutiable property arising from the admission of F.

Variation of partnership entitlements

3. X is a partner in a professional partnership that holds dutiable property. The partnership agreement provides that a partner's entitlement to share in the profits of the partnership is determined by having regard to each partner's contribution to those profits during a period. For the current period, X's profit share has been worked out at 10 per cent, which is 2 per cent higher than for the last period.

Accordingly, X has a partnership interest that varies. Where this variation in profit entitlement has occurred solely by reason of X's performance as a partner, it will be taken that X has **not** made a partnership acquisition so long as there is no arrangement fixing the extent of variations and nor has there been consideration for such variations.

Otherwise X's increase in profit entitlement will be treated as a partnership acquisition of a 2 per cent interest in the partnership.

Merger of 2 or more partnerships

A person's partnership interest in dutiable property may increase as a result of the merger of 2 or more partnerships. When calculating the unencumbered value of a partnership acquisition that occurs as the result of a merger, allowance is made for the dutiable property that a partner already held an interest in prior to the merger.

4. The JK partnership (partners J and K in equal shares) merges with the LM partnership (partners L and M in equal shares). Each partnership's dutiable property is:
- JK partnership—dutiable property with an unencumbered value of \$500 000.
 - LM partnership—dutiable property with an unencumbered value of \$250 000.

The new partnership (the JKLM partnership) will therefore hold dutiable property with a total unencumbered value of \$750 000. The partners will share in the capital and profits in the proportions of:

- 30 per cent for each of J and K and
- 20 per cent for each of L and M.

J has acquired a partnership interest on the formation of the new partnership. The dutiable value of this interest is the greater of the consideration for the interest or its unencumbered value. No consideration was paid for J's interest. Accordingly, the unencumbered value of J's interest in the JKLM partnership must be determined with allowance made for J's contribution of dutiable property to that partnership.

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The dutiable value of J's partnership acquisition without deductions is \$225 000 (ie, 30 per cent of \$750 000). However, this figure is adjusted for J's continuing interest in the dutiable property of the former JK partnership, which is transferred to the new JKLM partnership.

The unencumbered value of J's acquisition on the merger of the partnerships must be reduced by the lesser of:

- \$150 000 (ie, 30 per cent of \$500 000, being J's resulting interest in the dutiable property contributed to the JKLM partnership by the JK partnership) and
- \$250 000 (ie, 50 per cent of \$500 000, being J's original interest in the dutiable property contributed to the JKLM partnership by the JK partnership).

The dutiable value of J's partnership acquisition is therefore \$75 000 (ie, \$225 000 less \$150 000). For the same reasons, the dutiable value of K's partnership acquisition is \$75 000.

In this instance J and K have each acquired 30 per cent of the dutiable property of the LM partnership. Thus, for each of J and K, the dutiable value of their partnership acquisitions will be based on the interest that they are acquiring in the LM partnership, being 30 per cent of \$250 000 or \$75 000.

Likewise, the value on which duty will be payable on L and M's acquisition of a partnership interest in the JK partnership can also be calculated.

The dutiable value of L's partnership acquisition before deductions is \$150 000 (ie, 20 per cent of \$750 000). However, this figure is adjusted for L's continuing interest in dutiable property of the former LM partnership, which has become dutiable property of the new JKLM partnership.

The unencumbered value of L's acquisition on the merger of the partnerships must be reduced by the lesser of:

- \$50 000 (ie, 20 per cent of \$250 000, being L's resulting interest in the dutiable property contributed to the JKLM partnership by the LM partnership) and
- \$125 000 (ie, 50 per cent of \$250 000 being L's original interest in the dutiable property contributed to the JKLM partnership by the LM partnership).

The dutiable value of L's partnership acquisition is therefore \$100 000 (ie, \$150 000 less \$50 000). For the same reasons, the dutiable value of M's partnership acquisition is \$100 000.

Both L and M have each acquired 20 per cent of the dutiable property of the JK partnership. Thus, for each, duty will be based on 20 per cent of \$500 000, being the interest that they are acquiring in the JK partnership.

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Retirement of a partner

A person's partnership interest in dutiable property may increase as a result of the dissolution of a partnership or on the retirement of a partner. The following example shows how partnership interests are assessed on the retirement of a partner.

5. N, P and Q are partners in a partnership with interests of 30 per cent, 30 per cent and 40 per cent respectively. The dutiable property of the partnership has an unencumbered value of \$1 000 000. Q retires from the partnership and as a result transfers its interest to N.

N's partnership interest is now 70 per cent. However, in determining the unencumbered value of their partnership acquisition, only N's acquisition of Q's interest (being a 40 per cent interest in the partnership's dutiable property) is taken into account.

The dutiable value of N's partnership acquisition is therefore \$400 000 (ie, 40 per cent of \$1 000 000).

However, the result would be different if the consideration for N's acquisition of Q's partnership interest was \$450 000. Stamp duty would instead be assessed on \$450 000 as the consideration paid for the acquisition of the partnership interest would be greater than the unencumbered value of that interest.

No stamp duty would be payable by P and Q, as their partnership interests have not increased.

Where a partner retires from a partnership and dutiable property is transferred to the retiring partner, allowance is made for the value of the retiring partner's interest in the dutiable property for the purpose of assessing any stamp duty payable on the transfer of property.

When the unencumbered value of the property being transferred is less than the value of the partner's interest, nominal duty of \$20 is payable. However, where the unencumbered value of the property is greater than the value of the partner's interest, stamp duty is paid on the excess. The following example shows how the retiring partner's partnership interest is valued.

6. The RSTU partnership (with partners R, S, T and U having equal shares of 25 per cent each) holds dutiable property worth \$1 000 000, including land worth \$400 000. R retires from the partnership and the partners agree that the whole of the land will be transferred to R.

The transfer of the land to R is a conveyance of dutiable property. The dutiable value of the conveyance is its unencumbered value, being \$400 000. However, this is adjusted for the partnership interest that R held in the partnership immediately prior to R's retirement. Accordingly, the dutiable value of R's acquisition is reduced by \$250 000, being 25 per cent of \$1 000 000.

The dutiable value of R's acquisition of dutiable property on retirement is therefore \$150 000 (ie, \$400 000 less \$250 000).

No stamp duty would be payable by S, T or U, as their partnership interests have not increased.

Revenue Circular RA001, which sets out information on the revenue circular system, is incorporated into and is to be read as one with this Circular.

Refer to the *Taxation (Administration) Amendment Act 2002* for precise details of the changes. For general information, please contact TRM on 1300 305 353.

