

NSW Tax Forum

Property Development – Dual Occupancy

Presented at NSW Tax Forum on 15 May 2023

Jim Koutsokostas CTA
Hall & Wilcox

Contents

1. Introduction	3
2. What is Dual Occupancy?.....	5
3. Capital or Revenue	7
3.1 Intention is important	7
3.2 When is there a change in the intended use of property?	8
3.3 Capital asset → revenue asset	8
3.4 GST	10
4. CGT and the Main Residence Exemption	13
4.1 CGT refresher.....	13
4.2 CGT main residence exemption.....	13
4.3 Reduction of the main residence exemption benefit	14
4.4 Common errors in applying the main residence exemption	15
4.5 Granny flat arrangements.....	17
5. Land Tax and the Principal Place of Residence Exemption	19
5.1 Land tax refresher	19
5.2 The principal place of residence exemption	19
5.3 'Used and occupied'	20
5.4 'The land, and no other land ...'	20
5.5 'For no other purposes ...'	21
6. Partition and Subdivision of Land.....	23
6.1 Subdivision	23
6.2 Partition and CGT	24
6.3 Partition, CGT and strata title	26
6.4 Partition and transfer duty	27
6.5 Impact of partition on land tax	28

1. Introduction¹

Let's consider some statistics.

'Slowing supply, together with increasing household formation is expected to lead to a supply household formation balance of around -106,300 dwellings (cumulative) over the 5 years to 2027 (and around -79,300 dwellings over the projection period 2023 to 2033).'²

In the 2011 financial year, 2,712 new applications were approved in New South Wales (**NSW**) for residential second occupancy, worth \$17.8 million. By the 2021 financial year, this had grown to 7,385 new applications approved, worth \$480.2 million.³

The average site area for new houses in Greater Sydney decreased by 18% in the decade to 2021, now sitting at 423m².⁴

Randwick City Council is forecasting that nearly half of yet-to-be-approved new dwellings in the next six to 10 years, will be dual occupancy dwellings.⁵

The NSW property market has clearly seen an increase in the development of medium-high density housing, and will continue to do so in the foreseeable future. One of the main drivers has been, and will continue to be, the development of small-scale, dual occupancy properties. This leads to the obvious complexity involved with property ownership and development, amplified by the tax and duty complexities.

This paper examines the tax implications of developing small-scale dual occupancy property, comprising:

- an introduction to the broader concept of dual occupancy, with a focus on 'small scale' dual occupancy;
- a refresher on the capital gains tax (**CGT**) and land tax concessions, and an analysis of how these concessions may be affected by a new development of the property;
- an analysis of the capital / revenue account considerations:
 - when purchasing a property with the intent to develop, or
 - when a landholder makes the decision to use part of their land to generate income; and
- an assessment of the duty implications associated with the partitioning of property.

The paper also includes comprehensive examples of the foregoing principles and rules.

¹ I appreciate the efforts of Bradley White and Luke Raams of Hall & Wilcox who greatly assisted in the preparation of this comprehensive paper.

² National Housing Finance and Investment Corporation (3 April 2023), *NHFIC releases flagship 'State of the Nation's Housing 2022–23' research report*, NHFIC Website, accessed 15 April 2023.

³ New South Wales Department of Planning and Environment, *Local Development Performance Monitoring Dashboard*, Department of Planning and Environment Website, accessed 15 April 2023.

⁴ Australian Bureau of Statistics (7 June 2022), *New houses being built on smaller blocks*, ABS Website, accessed 15 April 2023.

⁵ Randwick Comprehensive Planning Proposal Local Environmental Plan (LEP) Review (May 2022), *Information Sheet: Dual Occupancy & Minimum Lot Sizes*, Randwick City Council.

In relation to land tax and duty, while there may be similarities between different states and territories, there are also key differences. This paper considers the land tax and duty outcomes in NSW resulting from the application of the respective principal NSW legislation, being:

- *Land Tax Management Act 1956* (NSW) (**LTMA**);
- *Land Tax Act 1956* (NSW) (**LTA**); and
- *Duties Act 1997* (NSW) (**DA**).

Do not assume that the same reasoning outlined in this paper applies to the regimes of other jurisdictions.

Some comments in relation to the goods and services tax (**GST**) implications are also included in this paper. A more detailed GST analysis is outside the scope of this paper.

Also, several of the examples used in this paper require us to gaze into a crystal ball and into the future. Please assume that the rules apply at the date of this paper and apply unamended into the future as relevant.

Finally, this paper contains a general discussion of the rules and issues outlined above - this paper does not constitute or convey advice. Readers should not act on the basis of the material contained in this paper. Additionally, changes in legislation can occur quickly. It is recommended that formal advice be sought before acting in any of the areas covered in this paper.

2. What is Dual Occupancy?

The term ‘dual occupancy’ refers to a property with two separate dwellings located on a single parcel of land (but not necessarily on the same title). Dual occupancy is one of the more popular methods implemented by landholders to generate value and income from their properties.

Two of the most prevalent examples of dual occupancy can collectively be defined as small-scale dual occupancies, and include:

- a lot comprising a house and a separate, self-contained granny flat; or
- a lot comprising two detached or attached houses (often sharing a common wall - such as a duplex / semi-detached).

Dual occupancy provides flexibility for landholders in unlocking value from their land. For example, the development of a duplex on a parcel of land allows the landholder to live in one dwelling and to rent out or sell the other. In recent years, planning regulations around New South Wales have been somewhat amended to encourage higher density living, including dual occupancy developments, as it is seen as a solution to increasing housing supply within an area.

This paper focuses on small-scale dual occupancies (like the ones mentioned above) and the often-complex tax implications that landowners of private residential dwellings should be mindful of when considering a dual occupancy on their land. Relevantly, a dual occupancy on one’s land can affect the manner in which CGT and land tax (and any related exemptions) may apply to the landowner. There are also transfer duty implications that may arise in circumstances under which the land is sub-divided.

Broadly speaking, the development of dual occupancy premises will involve the following steps (assuming that two individuals purchase the land and undertake the development):

1. The relevant land is acquired by the joint owners, Person A and Person B as to 50:50 each.
2. Person A and Person B then develop the land, building the dual occupancy - for example, a duplex.
3. Once the land has been developed, it is subdivided into two lots, Lot A and Lot B. Each lot contains a dwelling (that is, half of the duplex). The result of subdivision is that Person A and Person B each jointly own Lot A and Lot B.
4. Person A and Person B enter into a deed of partition under which Person A agrees to take Lot A and Person B agrees to take Lot B.
5. Pursuant to the partition deed, Person A transfers their part interest in Lot B to Person B, in exchange for Person B transferring their interest in Lot A to Person A. After the transfers have occurred, Person A will own Lot A and Person B will own Lot B.

Practical Example - the Parramatta Power Couple

For the purposes of this paper, we will consider a potential ‘real world’ example centred around a power couple in their late 40s, Cameron and Sarah (**Practical Example**). As tenants in common (50:50), Cameron and Sarah own a reasonably large block of land in Parramatta comprising a single lot as their main residence. After researching their options, Cameron and Sarah are considering developing their property either by converting their home into a duplex or building a

separate, self-contained granny flat. Cameron and Sarah intend to live in one of the dwellings as their primary residence, and renting out the other, be it the granny flat or one half of the duplex.

Cameron and Sarah are both Australian residents for tax purposes and you should assume that they remain so for the purpose of the examples set out below.

Throughout this paper we will refer to, and build upon, this Practical Example as we review the relevant tax considerations that arise when deciding to undertake a small-scale dual occupancy development.

3. Capital or Revenue

3.1 Intention is important

Before we delve into the tax outcomes of dealing with land in the context of developing a dual occupancy, do not assume that the CGT rules will always apply. A valuable, illiquid asset will not always be treated on capital account for tax purposes. Intent and actions are important.

Broadly, there are three ways in which profits (or losses) arising from the development, subdivision or sale of property can be treated for tax purposes. Determining which treatment is appropriate requires an understanding of whether the property is held as:

- a capital asset - and so enlivening the CGT rules;
- a revenue-generating asset forming part of a profit-making undertaking or scheme - and so treated on revenue account; or
- trading stock of an entity carrying on a business of property development - and so treated under the trading stock provisions.

The distinction is important. Fall into revenue territory, and any benefit that may be had under the CGT regime - such as the CGT discount and use of capital losses - may dissipate.

The focus of this paper is on small-scale developments, typically undertaken by individuals solely or in partnership. Accordingly, it is beyond the scope of this paper to undertake a detailed consideration of the application of the trading stock provisions.

How the property will be treated for tax purposes will depend on the original intended use of the property, which can be established in a multitude of ways. However, the intended use of a property is not set in stone and can change over time.

The relevant purpose is not the subjective purpose of the taxpayer, but the objective purpose that is determined after considering all of the facts and circumstances. If the taxpayer is a company, it is the intention of the people controlling the company that needs to be considered.

Where a taxpayer acquires an asset with multiple purposes, the relevant purpose is the taxpayer's 'dominant purpose'.

One of the most effective ways to objectively establish the intention in relation to the acquisition of a property is through contemporaneous third party and internal documentation. A common example is banking or finance documentation prepared when funds are borrowed to acquire property.

Regardless of how the original intended use of property is established, taxpayers must be mindful that if a dispute arises with the Commissioner, they will have the onus of establishing the facts.

Once the original intended use of property is established, determining when a change in the intended use occurs is a matter of fact, and must be understood in the context of the applicable case law and legislation.

3.2 When is there a change in the intended use of property?

The original intended use of a property can change for a multitude of reasons and, most of the time, there will be tax implications that will need to be considered as a result of that change.

Tax practitioners are commonly asked to provide advice about whether there has been a change in the intended use of land originally held as a capital asset, and the resulting tax implications. Less commonly, we are asked to provide advice about whether there has been a change in the intended use of land originally held as a revenue asset or trading stock, and the resulting tax implications.

In either case, the importance of being able to objectively establish the original intended use, and whether there has been a change, will be vital. Taxation Ruling TR 92/3 outlines the factors that the Commissioner will consider when determining the intention of the taxpayer. Relevantly, these include (but are not limited to):

- the nature and scale of the activities undertaken by the taxpayer;
- the nature, scale and complexity of the operation, development or transaction; and
- how long the property had been held for.

Accordingly, the taxpayer obtaining planning permits, engaging surveyors and applying for subdivision are all actions that would be considered by the Commissioner in determining the objective intention of the taxpayer, and whether there has been a change in that intention.

3.3 Capital asset → revenue asset

One of the most common examples of a change in original intended use of a property, is in the case of a property that is initially held as a capital asset which is then used as part of a profit-making undertaking or scheme. This scenario is most relevant to this paper as it more than likely captures most residential landowners seeking to generate value from their home.

The sale of a property held as a capital asset will be treated for tax purposes as being on capital account,⁶ and may attract the 50% CGT discount⁷ unless it is disposed of:

- as part of a profit-making undertaking or scheme; or
- in the course of carrying on a business.

A profit from the disposal of property as part of a profit-making undertaking or scheme may be taxable as ordinary income under section 6-5 of the 1997 Act.⁸ Similarly, a loss may be deductible under section 8-1 of the 1997 Act.⁹ In either case, the profit or loss will be assessed at the time of the disposal (noting, however, that there are further considerations to be had when there is a long settlement period that spans more than one income year).

⁶ Namely, CGT Event A1. See section 104-10 of the *Income Tax Assessment Act 1997 (1997 Act)*.

⁷ See Division 115 of the 1997 Act.

⁸ See also section 15-15 of the 1997 Act for properties acquired before 20 September 1985.

⁹ See also section 25-40 of the 1997 Act for properties acquired before 20 September 1985.

A question arises as to whether a taxpayer can avail themselves of the benefit (or detriment, in a loss scenario) of any change in the value of the property up until the time it is ventured into a profit-making undertaking or scheme, under the CGT regime.

One view is that at the time of disposal, a taxpayer must:¹⁰

- Calculate the increase or decrease in value (if any) from the time of acquisition until the time that the property was ventured into a profit-making undertaking or scheme. Any loss or gain should then be assessed under the CGT regime.
- Calculate the increase or decrease in value (if any) from when the property was ventured into a profit-making undertaking or scheme until the time of disposal. This would, in effect, be the true loss or gain from the profit-making undertaking or scheme. Any gain should then be taxable as ordinary income under section 6-5 of the 1997 Act,¹¹ and any loss should be deductible under section 8-1 of the 1997 Act (at the time of the disposal).¹²

A word of caution. There are no specific provisions within the income tax legislation which provide a mechanism for an apportionment on this basis. However, based on Taxation Determination TD 97/1, it appears that the Commissioner accepts that an apportionment can be appropriate.

Presumably, in this case, the anti-overlap provisions in section 118-20 of the 1997 Act would apply to reduce a capital gain (made on the eventual disposal of the developed property) by any amount included in assessable income. Similarly, sections 110-40 or 110-45 of the 1997 Act (as the case may be) may apply to reduce the cost base of the property (and therefore the capital loss) to the extent that an amount can be deducted.

Assuming this is the correct outcome, a taxpayer would need to seek a valuation of the property as at the time that it was ventured into a profit-making undertaking or scheme. The valuation can be obtained at a later date, with the valuer providing an opinion of value as at the earlier date. However, a valuation undertaken at the relevant time can also be useful additional evidence to support the change of intention at the appropriate time.

Of course, if the intention was always for the property to be used as part of a profit-making undertaking or scheme, then all of the gain made on the sale will be assessed on revenue account - and no opportunity for the step-up in cost base to be captured.

Ultimately, whether the intention for which a capital asset is held has changed, is a question of fact that is to be considered on a case-by-case basis. Before steps to commence a development are implemented, tax advice should be sought to ensure that the property is not inadvertently ventured into a profit-making scheme.

Example - Capital account

Cameron and Sarah acquire the Parramatta property together as tenants in common. When acquired, there is an existing dwelling on the land and the intention of Cameron and Sarah was to use and occupy the dwelling as their main residence.

¹⁰ See, for example Sian Sinclair, *Revenue v Capital What happens when the intended use of property changes?*, 2 November 2020, The Tax Institute Property Online Series.

¹¹ See also section 15-15 of the 1997 Act for properties acquired before 20 September 1985.

¹² See also section 25-40 of the 1997 Act for properties acquired before 20 September 1985.

After five years and rising interest rates, Cameron and Sarah are in a financial position under which they are finding it difficult to service the mortgage over the property. As a result, they decide to:

- subdivide the property into two lots, one lot holding the dwelling (**Lot A**) and the remaining lot being vacant land (**Lot B**); and
- sell Lot B.

In these circumstances, the objective circumstances support the view that the sale of Lot B is the mere realisation of a capital asset and would therefore be subject to tax on capital account.

Example - Revenue account

Cameron and Sarah together purchase the Parramatta property and use and occupy the existing dwelling on it as their main residence.

After 15 years, Cameron and Sarah realise that the value of property in the area has risen significantly due to large demand and relative undersupply of new available property. At the same time, Cameron and Sarah are feeling the years pass and no longer require such a large property. Cameron and Sarah decide to demolish the existing dwelling, subdivide the property into two lots and build a duplex with an occupancy on each of the new lots (Lot A and Lot B), with a common wall on the border of Lot A and Lot B. Cameron and Sarah intend to retain Lot A, and sell Lot B in order to fund the development and retain any excess funds.

In circumstances like these, it is possible for the Commissioner, despite the relatively minor scope of the development, to conclude that the development goes beyond a mere realisation of a capital asset.

In order to secure capital treatment, Cameron and Sarah will need to adduce evidence that they are not engaging in a profit-making undertaking or scheme by reference to the factors set out in Taxation Ruling TR 92/3.

3.4 GST

While often overlooked, an aspect to keep in mind when undertaking a development is whether there will be any GST consequences. For the purposes of this paper, and the demonstrative examples used within (except for the example in this section), we have assumed that the property (including any subdivided lots) will be treated on capital account, and that any supply is not made in the course or furtherance of an enterprise being carried on. However, we provide in this section some general comments in relation to the relevant GST framework.

GST overview

Broadly, an entity is required to register for GST where it is carrying on an enterprise and its GST turnover meets the relevant threshold (currently, \$75,000).¹³ Accordingly, the relevant consideration for any landowner engaging in a development is whether their conduct, in undertaking the development, amounts to the carrying on of an enterprise. Miscellaneous Taxation Ruling MT 2006/1 outlines some factors that the ATO will consider when determining if an entity is carrying on an enterprise and specifically addresses property developments from paragraph 262.

¹³ Division 23 of the *A New Tax System (Goods and Services Tax) Act 1999* (**GST Act**).

Having determined that the relevant entity is engaged in an enterprise, GST may then be charged on any taxable supply they make (unless an exemption applies). A taxable supply occurs if:

- you make a supply for consideration;
- the supply is made in the course or furtherance of an enterprise that you carry on; and
- the supply is connected with the indirect tax zone (this will be satisfied when dealing with Australian real property); and
- you are registered or required to be registered for GST.

Subdivision

If a lot of land is jointly held and then subdivided, the subdivision itself should not result in any GST consequences. This is because, regardless of whether the entity is registered (or required to be registered) for GST, a subdivision does not result in a supply being made. A subdivision merely splits the existing lot into further lots, each held by the same owners, such that there is no actual change in ownership. This view is also supported by the ATO and set out in paragraph 50 of GST Ruling GSTR 2009/2.

Partition

Unlike a subdivision, when a partition occurs, a transfer is taken to occur, such that a supply is made. Each joint owner transfers their interests in the resulting subdivided lots, such that they each end up holding 100% of their own lot, rather than a partial interest in each of the subdivided lots.

The relevant question then becomes whether or not the other elements of a 'taxable supply' are satisfied. Generally speaking, a supply made under a deed of partition (or partition agreement) will be for consideration, as there is a transfer of an interest in property for another interest in property. The supply will also be connected with Australia, on the basis that it is land located in Australia.

Accordingly, the focus of the analysis will be whether the supply (the transfer of land) is made in the furtherance of an enterprise that the landowner carries on, and whether the landowner is registered or required to be registered for GST. This will require an analysis of the facts, on a case-by-case basis.

Example

Cameron and Sarah acquire the Paramatta property together with another couple, Fred and John. Each couple holds a 50% interest in the Paramatta property. Immediately after purchasing the property, the couples demolish the existing dwelling and build a duplex. The land is then subdivided and partitioned. Cameron and Sarah jointly own one lot (Lot A) and Fred and John jointly own the other lot (Lot B). Each lot has its own dwelling.

Cameron and Sarah run their own successful boutique chocolate business as individuals and are required to register for GST. They intend to occupy the dwelling on Lot A as their main residence.

Fred and John are budding property developers and make a living from undertaking duplex developments. They do not intend to occupy Lot B. Instead, they plan to list it for sale almost immediately.

Cameron and Sarah

Cameron and Sarah have disposed of their interest in Lot B to Fred and John, in exchange for Fred and John's interest in Lot A. Cameron and Sarah have:

- made a supply for consideration (provided their interest in Lot B for Fred and John's interest in Lot A);
- the supply is connected with an indirect tax zone (that is, Australia, due to it being real property located in Australia); and
- Cameron and Sarah are registered for GST due to their chocolate business.

However, it is unlikely that the transfer of the Lot B interest to Fred and John would be subject to GST, as the supply is not made in the course or furtherance of an enterprise Cameron and Sarah carry on. The purpose of the supply is to aid in the acquisition of their main residence. It is clearly unrelated to the chocolate business and there are no further facts that indicate Cameron and Sarah are engaging in a property development business (that is, a new enterprise) by undertaking the supply.

Fred and John

Fred and John have disposed of their interest in Lot A to acquire Cameron and Sarah's interest in Lot B. In the above circumstances, it is likely that Fred and John will be considered to have made a taxable supply to Cameron and Sarah when they transferred their interest in Lot A to them. The subsequent sale of Lot B to a prospective buyer would also likely be a taxable supply and subject to GST.

The key distinction between the GST treatment of Fred and John, compared with Cameron and Sarah, is that the supply by Fred and John may be considered as being in the course of their property development enterprise. As such, it is likely to be subject to GST. Similarly, the sale of Lot B should also be within their property development enterprise and subject to GST.

4. CGT and the Main Residence Exemption

4.1 CGT refresher

Where an individual buys and sells a capital asset, such as land, they will be assessed on the gain they make either on 'capital account' under the CGT provisions in Part 3-1 and Part 3-3 of the 1997 Act, or on 'revenue account' as either a profit-making undertaking or scheme, or as ordinary income under section 6-5 of the 1997 Act.

As outlined in Sections 2 and 3 of this paper, a property originally acquired and held on capital account (including a property once used as a main residence) may be disposed of on revenue account where there has been a change in the intended use of land.¹⁴

Example

Adopting a 'vanilla' approach to our Practical Example whereby Cameron and Sarah dispose of their property (being their main residence) prior to undertaking any development, and which is held on capital account:

- The disposal of the property, as a CGT asset, will trigger CGT event A1 at the time they enter a contract for the disposal of the property. If there is no contract, CGT event A1 will trigger when the change of ownership occurs (that is, on settlement).
- The individuals will each realise:
 - a capital gain, if the capital proceeds from the disposal are more than the asset's cost base; or
 - a capital loss, if those capital proceeds are less than the asset's reduced cost base.

The impact of the main residence exemption will be considered below.

4.2 CGT main residence exemption

In the words of Sir Edward Coke in *Semayne's Case* (which inspired the Australian classic film, 'The Castle'): a man's home is his castle. Reflective of this, the 1997 Act provides homeowners with a lucrative tax concession: the CGT main residence exemption.¹⁵

Section 118-110(1) of the 1997 Act provides that:

A capital gain or capital loss you make from a CGT event that happens in relation to a CGT asset that is a dwelling or your ownership interest in it is disregarded if:

- (a) *you are an individual; and*
- (b) *the dwelling was your main residence throughout your ownership period; and*

¹⁴ Refer to Taxation Determination TD 92/135.

¹⁵ Subdivision 118-B of the 1997 Act.

(c) the interest did not pass to you as a beneficiary in, and you did not acquire it as a trustee of, the estate of a deceased person.

In addition to the criteria above, if the individual is a 'foreign resident' for tax purposes, the main residence exemption is unlikely to apply, as it will only do so in very limited circumstances. For example, where the cause of the individual's foreign residency is due to the terminal illness of a spouse.¹⁶

While this may seem simple at first, in some situations, the CGT main residence exemption can be deceptively complex. In fact, Subdivision 118-B of the 1997 Act, which contains the main residence exemption, includes 40 sections, each of which can impact how the exemption is to apply in certain circumstances.

The application of CGT and, where appropriate, the main residence exemption, can be materially affected where a property is developed to allow (and be used) for dual occupancy. The complexity in this instance arises because the landowner may elect to utilise part of their main residence for an income-producing purpose.

4.3 Reduction of the main residence exemption benefit

The main residence exemption applies to disregard the capital gain that is made on the sale of a main residence that has otherwise accumulated throughout an owner's ownership period. Accordingly, to the extent that a dwelling ceases to be a main residence for part of an owner's ownership period, or was used to produce assessable income, only a partial exemption may apply.

Broadly, the amount of the exemption's reduction is calculated by determining:

- the percentage of the dwelling that was used to produce assessable income;
- the amount of time during the owner's ownership period that the dwelling was used to produce assessable income; and
- the amount of time during the owner's ownership period that the dwelling was not used and occupied as the owner's main residence.¹⁷

Absences

Despite the above, it is possible to continue to treat a dwelling as a main residence whilst the owner is absent from it *and* it is being used to produce assessable income. Section 118-45 of the 1997 Act provides an owner with the ability to elect to continue to treat a dwelling as their main residence for:

- a period of six consecutive years, if the dwelling is to be used to produce assessable income during the absence; or
- indefinitely, provided the dwelling is not being used to produce assessable income.

Example

Consider the Practical Example with the following additions:

¹⁶ Section 118-110(3) to (5) of the 1997 Act.

¹⁷ Sections 118-185 and 118-190 of the 1997 Act.

- After Cameron and Sarah purchased their dwelling on 1 January 2023 for \$1 million, they decided to rent out one of the four bedrooms until 1 January 2025. The leased space and common areas amount to approximately 30% of the property.
- For all of 2025, Cameron and Sarah continued to use and occupy the property as their main residence.
- In 2026, Sarah received an exciting job offer in Queensland, such that Cameron and Sarah relocated to Queensland from 1 January 2026 to 1 January 2028, during which time they leased out their Parramatta home. During this absence, Cameron and Sarah leased a small apartment in Newstead, in inner Brisbane.
- On 1 January 2028, Cameron and Sarah chose to relocate to Queensland permanently, selling their Parramatta home for \$1.5 million.

Assuming that the rate of growth was consistent throughout Cameron and Sarah's ownership period (1 January 2023 to 1 January 2028), the Parramatta property has increased in value by \$100,000 each year.

For the first two years, 30% of the property was used to produce assessable income, resulting in 30% of the gain over those years being assessable (\$60,000).

For all of 2025, Cameron and Sarah used and occupied the property as their main residence and did not use it to produce assessable income. Accordingly, all of the gain during this year should be disregarded under the main residence exemption.

For 1 January 2026 to 1 January 2028, Cameron and Sarah are able to elect to treat the property as their main residence despite their absence from it and despite it being used to produce assessable income. As a result, the main residence exemption can apply to disregard the entire gain made during this absence.

Accordingly, Cameron and Sarah will have made a \$60,000 gain on the sale of the property. However, this gain should be eligible for the CGT discount under Division 115 of the 1997 Act, reducing it to \$30,000 (assuming they have no other capital losses in that period).

4.4 Common errors in applying the main residence exemption

It is important at this stage to address a common error that people make when seeking to understand and apply the main residence exemption. The exemption itself applies to the dwelling, rather than the land more broadly.

A dwelling is defined to include:

- a unit of accommodation that:
 - is a building or is contained in a building; and
 - consists wholly or mainly of residential accommodation; and
- a unit of accommodation that is a caravan, houseboat or other mobile home; and

- any land immediately under the unit of accommodation.¹⁸

As the exemption attaches to the dwelling, any decision to demolish the existing dwelling will need to be carefully considered.

If a dwelling is built, repaired or renovated (including demolishing an existing dwelling then building a new one), section 118-150 can allow the main residence exemption to be applied to the underlying land while a new dwelling is being constructed, for the shorter of four years, or the period from when the original dwelling was last occupied.¹⁹ This is an important exemption as, otherwise, the period of time before the new dwelling is occupied would not fall within the main residence exemption.

For the exemption to apply, the following conditions must be met:

- the new dwelling must be used and occupied as a main residence as soon as practicable after the construction is completed; and
- the dwelling must continue to be used as a main residence for at least three months.²⁰

Being cognisant of these time frames will help individuals ensure that there are no unnecessary gaps in the application of the main residence exemption to their ownership interest in the relevant land.

A situation to be avoided is where there is a need to sell relevant land after the old dwelling has been demolished but before the new dwelling has been completed. In these circumstances, it is impossible for the seller to 'use and occupy' the land as their main residence - meaning the exemption cannot apply.

See below applications to the Practical Example.

Example

Consider the Practical Example and assume that Cameron and Sarah have converted their home into a duplex.

The main residence exemption applies to the dwelling, as opposed to the land. The main residence exemption also cannot apply to multiple dwellings, as you can only use and occupy one as your main residence. Accordingly, even if the other half of the duplex was never leased to a third party, Cameron and Sarah would be unable to claim the main residence exemption for the unoccupied half of the duplex, as they would not be using and occupying it as their main residence - rather, it would be vacant. However, upon the sale of the unoccupied duplex, provided it is sold on capital account, the CGT discount should apply to reduce any resulting capital gain made by 50%.

Example

Cameron and Sarah purchased their Parramatta property on 1 January 2023. The property has an existing dwelling. Immediately after the purchase, Cameron and Sarah hatch a plan to demolish the existing dwelling and build a duplex on the land.

The development of the duplex takes longer than anticipated and is completed by 1 January 2025. Almost immediately after the development is completed, Cameron and Sarah move into one of the new dwellings (Dwelling A) and lease out the other dwelling (Dwelling B).

¹⁸ Section 118-115 of the 1997 Act

¹⁹ Sections 118-150(2), 118-150(4) and 118-150(5) of the 1997 Act.

²⁰ Section 118-150(3) of the 1997 Act.

On 1 January 2026, Sarah and Cameron decide they want a sea change and sell both Dwelling A and Dwelling B.

Due to the application of section 118-150, Cameron and Sarah are able to claim the main residence exemption for the capital gain they make on the sale of Dwelling A as they are using and occupying it as their main residence.

As only one dwelling can be treated as a main residence, the exemption will not apply to Dwelling B. However, assuming Dwelling B is treated as a capital asset, any capital gain made on its sale by Sarah and Cameron should be subject to the CGT discount, and therefore reduced by 50%.

Consider also whether the sale may be subject to tax on revenue account, given Cameron and Sarah's plan to develop the property immediately after purchase.

4.5 Granny flat arrangements

Legislation, effective from 1 July 2021, was introduced to streamline the construction and formalisation of granny flat arrangements by disregarding certain CGT implications that may arise.²¹ The aim of the legislation was to mitigate the possibility of financial mistreatment and exploitation of vulnerable Australians, including older Australians.²² Essentially, CGT does not apply where a granny flat arrangement is created, varied or terminated.

The ATO defines a granny flat arrangement as a written agreement that gives an eligible person the right to occupy a property for life (**Granny Flat Interest**). Put simply, a person has a Granny Flat Interest where they provide consideration in return for a right to accommodation for life.

Division 137 of the ITAA 1997 provides that a CGT event will not occur on the entry into, variation or termination of a granny flat arrangement if the following apply:

- the individual who holds, or is to hold, the Granny Flat Interest under the arrangement has, or will have, a right to occupy a dwelling on the property for life; and
- the individual who holds the Granny Flat Interest:
 - has reached pension age at or before that time; or
 - needs assistance to carry out most day-to-day activities because of a disability and is likely to continue to need that assistance for at least 12 months after that time.²³

Example (adapted from example 3.1 in the Explanatory Memorandum to the *Treasury Laws Amendment (2021 Measures No. 4) Bill 2021*)

David, Cameron's father, is eligible for a granny flat interest and enters into a formal granny flat arrangement with his son Cameron and his partner, Sarah. Under the arrangement, Cameron and Sarah agree to build an attached flat on their property for David to live in for the rest of his life. David agrees to pay \$500,000 to Cameron and Sarah to finance the build, which he obtains from selling shares in his investment portfolio.

²¹ Schedule 3 of the *Treasury Laws Amendment (2021 Measures No. 4) Act 2021*.

²² See the Explanatory Memorandum to the *Treasury Laws Amendment (2021 Measures No. 4) Bill 2021*.

²³ Section 137-10 of the 1997 Act.

Under the exemption, CGT event D1 (creating contractual or other rights) that would otherwise have arisen upon the creation of David's right to occupy the flat on Cameron and Sarah's property, will not happen and Cameron and Sarah will have no CGT liability resulting from the creation of the right.

However, the exemption will not apply to any CGT consequences arising from the sale of David's shares. Although the proceeds from the sale are to be used to finance the building of the attached flat, the sale is not considered sufficiently related to the creation of the granny flat interest.

5. Land Tax and the Principal Place of Residence Exemption

5.1 Land tax refresher

Land tax in NSW is a tax levied on the taxable value of all land owned by a taxpayer in NSW as at midnight 31 December the previous year, other than exempt land.²⁴ This general statement is subject to:

- a land tax-free threshold, under which no land tax applies; and
- a premium threshold, above which a premium land tax rate applies.

All lots and strata lots are considered separately for the purposes of land tax. For the 2023 land tax year, the tax-free threshold is \$969,000, above which a land tax rate of \$100 plus 1.6% of the taxable value of the taxpayer's land in NSW applies, up to the premium threshold of \$5,925,000. Above the premium threshold, a land tax rate of \$79,396 plus 2% of land value above the threshold applies.²⁵

Different rates, thresholds and rules apply to trusts and companies for land tax purposes. These will not be considered in this paper as the focus is on private, small-scale dwellings which the paper assumes will be held by individuals. Further, when a home is held through a trust or company, the principal place of residence exemption cannot be claimed.²⁶

Land tax is charged, levied, collected and paid for the period of 12 months commencing on 1 January, for land owned at midnight on 31 December in the previous year.²⁷ For example, when making an assessment for land tax liability for the 2023 land tax year, the Chief Commissioner of State Revenue (**Chief Commissioner**) would consider a taxpayer's landholdings as at midnight 31 December 2022. There is no pro-rating, meaning that if a taxpayer became the registered proprietor of land on 30 December, they would still be liable for land tax on the full taxable value of the land. Similarly, where a property is acquired after 31 December, there is no reissue of the existing assessment to the new owner. Commercially, what generally occurs in these circumstances is that the benefit of the pre-paid land tax acquired by the new buyer is addressed as a settlement adjustment.

5.2 The principal place of residence exemption

Subsection 10(1)(r) of the LTMA provides that land used as a principal place of residence (**PPR**) will be exempt from land tax. Schedule 1A of the LTMA further outlines the requirements for the exemption to apply and where it may be extended or reduced in certain circumstances.

For the PPR exemption to apply, the land must be:

- a parcel of 'residential land', or a strata lot (or in some cases, two or more strata lots);

²⁴ Section 7 of the LTMA.

²⁵ Section 3AL and Schedule 13 of the LTA.

²⁶ Clause 11, Schedule 1A of the LTMA.

²⁷ Section 3AL of the LTA.

- that is continuously used and occupied by the owner for residential purposes *and for no other purposes* for the six months preceding the relevant assessment date (that is, from 1 July to 31 December, when land tax is assessed).²⁸

For these purposes, 'residential land' will not include a building or buildings:

- comprised of strata lots or residential units; or
- that contain occupancies other than that of the owner; or
- from any part of which income is derived.²⁹

5.3 'Used and occupied'

A critical element of the PPR exemption is that, in order to apply, the land needs to be *used and occupied* as the taxpayer's principal place of residence.³⁰

While there are exemptions to this general rule, to receive the benefit of the exemption, the taxpayer will generally need to initially occupy the land.

In practical terms, the taxpayer's occupation can be demonstrated to Revenue NSW through utilities usage at the property, a home and contents insurance policy, by updating the taxpayer's address on the electoral roll, or other similar means. While this may be an afterthought to some, these supporting documents can be critical in an audit situation. It is common for Revenue NSW to analyse utility usage at a property to determine whether it has usage consistent with the occupation of the dwelling as a PPR.

An example of where issues may arise with satisfying the 'used and occupied condition', is where a taxpayer already owns a property and purchased another with the intent of moving into it. The taxpayer declares this intent on the transfer documentation when purchasing the new property but never actually moves into it. In this instance, the taxpayer will have been incorrectly claiming the PPR exemption for the new property and will need to make a voluntary disclosure to the Chief Commissioner outlining that the exemption was incorrectly claimed.

5.4 'The land, and no other land ...'

The next key concept is the phrase 'land and no other land ...'

A taxpayer can only have one PPR for land tax purposes.³¹ That means a taxpayer cannot claim the benefit of the exemption in relation to multiple properties in NSW, or in NSW and another state or territory. There are limited exemptions to this, such as when a taxpayer has recently acquired a new property or recently acquired a deceased's former PPR as a beneficiary under their Will. This is beyond the scope of this paper.

The exemption can also be denied if the taxpayer's spouse, or dependent children and stepchildren that ordinarily reside with the taxpayer are also claiming the PPR exemption in relation to another

²⁸ Clause 2, Schedule 1A of the LTMA.

²⁹ Clause 3, Schedule 1A of the LTMA.

³⁰ Clause 2(1), Schedule 1A of the LTMA.

³¹ Clause 12, Schedule 1A of the LTMA.

property.³² If more than one property is used and occupied by the members of the family as a PPR, the family will need to elect one to apply the exemption to.³³ If no election is made, the Chief Commissioner will treat the property with the highest land value as the PPR for all the members of the family.³⁴

5.5 ‘For no other purposes ...’

The final key concept to consider is the phrase ‘for no other purposes ...’

The ‘base position’ is that land must only be used and occupied by the owner as their PPR and for no other purposes.³⁵ However, there are limited circumstances where the property can be used to generate income or contain an occupancy without losing the benefit of the exemption.

For example, the PPR exemption will continue to apply where there is one additional occupancy, if the occupancy is an ‘excluded residential occupancy’ as defined in clause 4 of Schedule 1A of the LTMA.

An excluded residential occupancy can consist of one of the following combinations of no more than two separate tenancies or lettings:

- one flat, plus another room or suite of rooms which is not a self-contained flat; or
- no more than two rooms separately occupied by boarders or lodgers.³⁶

It will mean that a taxpayer that allows a third party (such as an elderly parent) to live in a detached, self-contained granny flat on their property, in exchange for market (or nominal) value rent, will not lose the benefit of the PPR exemption. Further, the taxpayer could also rent a spare room within the main home to a boarder and still retain the PPR exemption.

Example

Let’s assume Cameron and Sarah elect to construct a detached, self-contained, granny flat and charge a third-party individual market value rent for them to lease the granny flat. Cameron and Sarah will not lose the benefit of their PPR exemption provided that the dwelling in which the third party occupies consists of no more than one flat, plus another room or suite of rooms which is not a self-contained flat.

Example

After acquiring the Paramatta Property, Cameron and Sarah decide to demolish the existing dwelling and build a duplex. Once the development is completed, Cameron and Sarah occupy one of the new dwellings (Dwelling A) and lease out the other dwelling (Dwelling B).

As the process of building the duplex would have resulted in a separate title being granted for each of Dwelling A and Dwelling B, Cameron and Sarah would have had to make an election (notifying

³² Clause 12(1), Schedule 1A of the LTMA.

³³ Clause 12(2) to (4), Schedule 1A of the LTMA.

³⁴ Clause 12(5), Schedule 1A of the LTMA.

³⁵ Clauses 2 and 3, Schedule 1A of the LTMA.

³⁶ Revenue Ruling LT082v5.

Revenue NSW) of their choice to treat Dwelling A as their PPR. They would therefore not be able to receive the PPR exemption for Dwelling B as well.

If subdivision does not occur such that Dwelling B is located on the same title as Dwelling A, it may be possible for the whole of the relevant land to be subject to the PPR exemption, on the basis that Dwelling B is considered a flat, and therefore an excluded residential occupancy. This is possible because 'flat' is defined to include a room or suite of rooms (whether or not forming part of a building or a detached dwelling): (a) used or occupied as a separate dwelling, or (b) so constructed, designed or adapted as to be capable of being used or occupied as a separate dwelling.³⁷

Similarly, if a property is used primarily as a taxpayer's PPR, and no more than one room is used incidentally for business purposes, the use of the land for that business purpose can be disregarded.³⁸ This will only be the case however where the taxpayer primarily conducts their work somewhere other than their home. This is intended to ensure that individuals that maintain a home office are not prevented from claiming the PPR exemption.

Complexities arise where the taxpayer allows a third party to live in a detached, self-contained dwelling in exchange for market rent, and the structure of the dwelling occupied by the third party does not satisfy the definition of an excluded residential occupancy as provided in clause 4(1) of Schedule 1A to the LTMA. In these circumstances, the landowner may only claim the PPR exemption over the proportion of the land value that applies to the part of the land that is used and occupied as the owner's residence, determined either by an apportionment of the floor area leased as a percentage of the total floor area of all dwellings on the land, or by applying an 'apportionment factor'.³⁹

Where land is used for a combination of residential and commercial purposes, the Valuer-General may determine an apportionment factor that applies.⁴⁰

The apportionment factor should be the proportion (expressed as a percentage) that the rental value of the part of that land that is non-residential land, bears to the rental value of the land as a whole.

The application of an apportionment factor is less relevant in circumstances where a development is undertaken and the resulting titles separate the portion of the property that relates to commercial use from the portion of the property used and occupied as a PPR.

Where a parcel of land contains an additional building to the main dwelling that is not also used as a dwelling, the PPR exemption should still apply where the additional building is used and occupied for a purpose ancillary to the residential use of the land, for example, a freestanding garage or shed.⁴¹

³⁷ Section 3 of the LTMA.

³⁸ Clause 5, Schedule 1A of the LTMA.

³⁹ Clause 10B, Schedule 1A and Section 9C of the LTMA; and Revenue Ruling LT082v5.

⁴⁰ Revenue Ruling LT082v5.

⁴¹ Clause 3(2), Schedule 1A of the LTMA.

6. Partition and Subdivision of Land

Given the rising price of property, as alluded to earlier in this paper, the joint acquisition and development of property amongst individuals is becoming increasingly common. In these circumstances the parties will acquire a lot, develop the lot into two dwellings and then each will take one of the dwellings to use as their residence or as an investment (with each dwelling on its own title).

6.1 Subdivision

A subdivision occurs when an owner (or owners) of a parcel of land divides the original lot into two (or more) standalone parcels of land.

Provided that both parcels of land remain with the original owner (or owners), the subdivision should not trigger any CGT consequences, as a change in ownership should not be taken to occur.⁴²

However, it is likely that the landowner's main residence exemption will be impacted. This is because only one of the subdivided lots is capable of being claimed by the landowner as their main residence, except in certain circumstances under which the main residence exemption may extend to adjacent land.⁴³

Subdivision alone also should not result in any duty consequences. Subdividing a lot does not trigger a dutiable transaction, as the landowner's underlying interest in the dutiable property (being land in NSW) does not change.

Subdivision may, however, result in land tax consequences for the owner of the land. It is possible for the PPR exemption to extend to a parcel of residential land that is comprised of multiple lots provided that:

- the lots are adjoining;
- the lots are in the same ownership; and
- the lots are the site of a single residence (excluding any excluded residential occupancy).⁴⁴

So, if the subdivided lots contain their own separate dwellings, they will likely be subject to land tax.⁴⁵

Example

Cameron and Sarah hold the Parramatta property in their capacity as tenants in common, each with a 50% interest. Immediately after purchasing the property, they decide to subdivide it into two lots. The existing dwelling will be located on one of the new lots (Lot A), while the other lot will be vacant land (Lot B).

As a result of the subdivision, Cameron and Sarah will both have a 50% interest in each of Lot A and Lot B. The subdivision itself will not trigger a CGT event. However, Cameron and Sarah will need to consider whether they satisfy the relevant requirements for the main residence exemption

⁴² See Tax Determination TD 97/3 and section 104-10 of the 1997 Act.

⁴³ Sections 118-110 and 118-120 of the 1997 Act.

⁴⁴ Clause 13 of Schedule 1A of the LTMA.

⁴⁵ Clause 4 of Schedule 1A of the LTMA.

to extend to the adjacent vacant Lot B, if they were to sell both Lot A and Lot B (in their current states) in the future.

The subdivision should not trigger any duty consequences as neither Cameron nor Sarah has obtained a new interest in dutiable property. Their interests in the underlying property are the same as before subdivision, just reflected in two titles instead of one.

Provided Lot B remains vacant, Cameron and Sarah should satisfy the requirements necessary to have the PPR land tax exemption extend to Lot B. As a result, there may be no land tax changes as a result of the subdivision (apart from having to notify Revenue NSW of the extended claim).

6.2 Partition and CGT

In circumstances where two or more owners jointly hold the original lot, the subdivided lots will still be held by those joint owners in the same proportions as before the subdivision. To alter the interests of the respective owners such that each owns 100% of one of the newly subdivided lots (as opposed to a fractional interest in all of them), a partition needs to occur. The effect of the partition is that each of the joint owners is taken to have disposed of their fractional interest in the other lots and acquired the other fractional interest in their lot from the other owners.⁴⁶

Example

Cameron and Sarah hold the Parramatta property in their capacity as tenants in common, each with a 50% interest. If they were to develop and subdivide the property to construct a duplex on it, Cameron and Sarah would each hold 50% of Lot A and Lot B.

If Cameron and Sarah determined that they wanted to hold a lot each, a partition deed would need to be entered into between the parties that would result in:

- Sarah transferring her 50% interest in Lot A to Cameron; and
- Cameron transferring his 50% interest in Lot B to Sarah.

As such, after the partition, Cameron would hold 100% of Lot A and Sarah would hold 100% of Lot B

As this process results in the disposition of an interest in property, it can have CGT and transfer duty consequences.

From a CGT perspective, each of the landholders will trigger a separate CGT event for each fractional interest they transfer. So, for a subdivision and partition with two equal owners, both owners will trigger a CGT event on the transfer of their 50% fractional interest to the other. As a result of these transfers, the lot will have a different cost base for (a) the 50% interest originally held by the owner, and (b) the 50% interest obtained from the owner by the other owner under the deed of partition.

⁴⁶ Taxation Determination TD 92/148.

Example

Cameron and Sarah purchased the Parramatta property for \$1 million on 1 January 2023. Three years later, on 1 January 2026, they subdivided the property such that there were two resulting lots of equal size, one lot with the existing dwelling located on it (**Lot A**) and one vacant lot (**Lot B**). Both before and after the subdivision, Cameron and Sarah occupied the existing dwelling on Lot A as their main residence. At the time of subdivision, the market value of each of Lot A and B was \$700,000.

Cameron and Sarah then decided that they wanted Lot A to be in Cameron's name and Lot B to be in Sarah's name. As a result, they entered into an agreement resulting in Cameron's interest in Lot B being transferred to Sarah and Sarah's interest in Lot A being transferred to Cameron (**Partition**).

After the Partition, Cameron would hold two 50% interests in Lot A, each with a different cost base. These consist of:

- the 50% he has held in Lot A since the property's acquisition on 1 January 2023, worth \$250,000 (50% of his total initial 50% interest in the property) (**Cameron's Lot A interest**); and
- the 50% he recently acquired from Sarah on 1 January 2026 worth approximately \$350,000 (**Sarah's Lot A Interest**).

Similarly, Sarah would hold two 50% interest in Lot B, each also with a different cost base:

- the 50% interest she has held in Lot B since the property's acquisition on 1 January 2023, worth \$250,000 (50% of her total 50% initial interest in the Property) (**Sarah's Lot B Interest**); and
- the 50% interest she recently acquired from Cameron on 1 January 2026 worth approximately \$350,000 (**Cameron's Lot B Interest**).

To acquire Cameron's Lot B Interest, Sarah has exchanged her interest in Lot A which had a cost base of approximately \$250,000. As a result, Sarah has made a capital gain of \$100,000 on the disposal of her interest in Lot A. However, as Sarah's main residence is located on Lot A, the disposal of her interest in Lot A to Cameron should be exempt under the main residence exemption.

Unlike Sarah, Cameron's disposal of his Lot B interest is not the disposal of Cameron's main residence, as this is located on Lot A. Could section 118-120 of the 1997 Act apply? This provision can extend the main residence exemption to adjacent land provided the land was used primarily for private or domestic purposes in association with the dwelling. However, note that the same CGT event needs to happen to the dwelling **and** the adjacent land.⁴⁷

Alternative Example

Consider the same fact pattern above, except that, rather than Lot A having the dwelling located on it and Lot B being vacant land, the existing residence is demolished and new townhouses are built on Lot A and Lot B, with the townhouse on Lot A being used and occupied as Sarah and Cameron's main residence as soon as the occupancy certificate has been issued.

A cross transfer (or partition) between Cameron and Sarah of their interests in Lot A and Lot B would trigger capital gains for both Cameron and Sarah as set out above (albeit likely with different amounts given the development that has occurred). However, unlike the above example, Cameron would be unable to claim the exemption for land adjacent to his main residence as it cannot apply where a dwelling exists on the adjacent land.

6.3 Partition, CGT and strata title

In cases where a lot is unable to be subdivided into two (or more) new lots due to restrictions on lot size, an alternative is for strata titles to be created.

Similar to a subdivision, the conversion of a lot into strata title does not trigger a CGT event, provided the recipients of the strata title each had a right to occupy the relevant building located on the lot prior to the conversion.⁴⁸

Interestingly, when a partition occurs with respect to strata units, the CGT treatment is different from when a partition occurs with respect to lots of land. Section 124-190 of the 1997 Act provides the recipient under a partition with roll-over relief for the capital gain that would otherwise occur provided that:

- the recipient own property that gives them a right to occupy a unit in a building; and
- the building's owner subdivides it into stratum units; and
- the owner transfers to the recipient the stratum unit that corresponds to the unit the recipient had a right to occupy just before the subdivision.

Taxation Ruling TR 97/4 outlines the Commissioner's view as to how section 160ZZPG of the 1936 Act (the predecessor to section 124-190) applies. Relevantly for our purposes, paragraph 12 of TR 97/4 outlines the Commissioner's views on how the relief applies to tenants in common who subdivide land and a building under strata title law. It provides that if two or more persons:

- hold an asset in relation to land, being a land and a building, as tenants in common; and
- enter into an agreement/understanding which grants each tenant in common an exclusive right of occupation, use and enjoyment of a particular stratum unit (that is, a partition agreement); and
- subdivide the land and building into relevant stratum units; and
- transfer their interest as tenants in common and rights over the stratum units so that each tenant in common becomes the registered proprietor of their own stratum unit that corresponds with the partition agreement; and
- elect to apply the rollover,

CGT rollover relief is granted with respect to any disposal or acquisition of any interest in the land and building, the stratum units or the common property.

The cost base of the new unit will be equal to their interest as a tenant in common prior to the subdivision.

⁴⁷ Sections 118-120 and 118-165 of the 1997 Act.

⁴⁸ Section 118-42 of the 1997 Act.

6.4 Partition and transfer duty

In NSW, transfer duty is imposed on dutiable transactions.⁴⁹ A dutiable transaction is defined to include a transfer of dutiable property,⁵⁰ which includes land in NSW.⁵¹

The partition of land and the resulting cross transfer of interests are transfers of dutiable property (being land in NSW) and are therefore, prima facie, subject to transfer duty. The amount of transfer duty charged will depend on the dutiable value of the dutiable property transferred. The dutiable value of dutiable property is the greater of the consideration provided (if any) or the unencumbered (market) value of the dutiable property.⁵²

Concessional duty under section 30 of the DA applies to partitions, treating the partition as a single dutiable transaction with a dutiable value deemed to be the greater of:

- the sum of the amounts by which the unencumbered value of the dutiable property transferred, or agreed to be transferred, by the partition, exceeds the value of the unencumbered interest held by the person in the dutiable property transferred, or agreed to be transferred, by the partition agreement immediately before the partition; and
- the sum of any consideration for the partition paid by any of the parties.

Essentially, if a like-for-like swap occurs as a result of a partition without any other consideration being provided - and the market value of each interest being transferred is the same - the concession under section 30 of the Act should apply such that nominal duty (\$50) is charged on the transfer.

Example

Cameron and Sarah decide to subdivide their NSW property immediately after acquiring it for \$1 million on 1 January 2023. The subdivision results in the creation of two lots, Lot A and Lot B. Lot A is worth \$600,000 and Lot B is worth \$400,000. Each is held as tenants in common by Cameron and Sarah.

Cameron and Sarah then enter into a deed of partition whereby Cameron transfers his interest in Lot B to Sarah and Sarah transfers her interest in Lot A to Cameron. Cameron has also agreed to provide Sarah \$110,000 in addition to his interest in Lot B.

Cameron

Cameron has acquired dutiable property worth \$300,000. Pursuant to the deed of partition, Cameron has agreed to transfer dutiable property worth \$200,000. Accordingly, the partition has increased Cameron's interest in the dutiable property by \$100,000.

Cameron has also paid consideration of \$110,000 to Sarah in order to obtain his interest in Lot A.

Section 30 of the DA then applies to assess Cameron on the consideration paid to acquire Lot A as it exceeds the dutiable value of the additional dutiable property obtained by Cameron obtained as a result of the partition (that is, \$110,000 > \$100,000).

The duty payable by Cameron on \$110,000 would be calculated as follows:

⁴⁹ Section 8(1) of the DA.

⁵⁰ Sections 8(1)(a) and (2) of the DA.

⁵¹ Section 11(1)(a) of the DA.

⁵² Section 21(1) of the DA.

$\$1,405 + (\$3.50 \text{ for every } \$100 \text{ over } \$87,000)$

$= \$2,210$

Sarah

Sarah, pursuant to the deed of partition, has obtained an interest in Lot B worth \$200,000 and agreed to transfer her interest in Lot A worth \$300,000. Sarah has also provided no additional consideration to obtain the interest in Lot B.

Nominal duty of \$50 should apply to Sarah's acquisition, as:

- the unencumbered value of the interest obtained by Sarah in Lot B does not exceed the dutiable value of the interest in Lot A provided in exchange; and
- no consideration is provided by Sarah.

6.5 Impact of partition on land tax

A partition allows joint owners to each become the sole owners of a part of the original lot of land once subdivided. The land tax consequences of the partition will depend on whether:

- the joint owners are members of the same family; and/or
- whether the owners were (and will) continue to occupy the same property as their PPR.

The impact of these scenarios is best set out in the example below.

Example

Continuing from the fact scenario set out in the example in section 6.3 above, Cameron and Sarah have subdivided and partitioned the Parramatta property, such that Cameron owns Lot A and Sarah owns Lot B. Each of the lots has part of a duplex built upon it.

If Sarah and Cameron both continue to use and occupy Lot A as their PPR, Sarah will be liable for land tax on the value of Lot B.

Even if Sarah occupied Lot B as her PPR, both Sarah and Cameron could not claim the exemption, as only one dwelling can be claimed as the PPR for a family. Due to being spouses, Cameron and Sarah would need to elect to treat either Lot A or Lot B as their PPR.

A similar outcome would apply if Lot B was left unoccupied. The PPR exemption could not extend to the adjacent land in these circumstances as:

- Lot B is not under the same ownership as Lot A;⁵³ and
- the dwelling on Lot B will not satisfy the definition of an 'excluded residential occupancy' due to being located on a separate lot from the PPR of Cameron and Sarah.⁵⁴

⁵³ Clause 13(1)(b) of Schedule 1A of the LTMA.

⁵⁴ Clause 4(4) of Schedule 1A of the LTMA.