Burke & Associates

OFF THE PLAN PROPERTY TRANSACTIONS – ISSUES FOR ACCOUNTANTS & LAWYERS

1. INTRODUCTION

Over a number of years Burke & Associates have developed an extensive practice assisting property developers in multiple lot property developments, particularly inner urban apartment developments. Along the way we have seen multiple lot property developments from the inside out and today we will be sharing some of our experience.

In the course of the presentation we will:

- have a look at some demographics;
- consider some planning issues;
- identify the players in a development;
- give it a time line;
- look at construction funding issues in the wake of the Global Financial Crisis;
- talk about some distressed property developers;
- look at the requirement of construction lenders;
- identify the potential role of accountants;

And then we will draw upon some of our recent experiences to highlight some of the challenges confronting property developers.

But first I thought it would be interesting to start by looking at an upmarket digital fly through for a development that is nearing completion. It is not one where we are acting but it is one that has interest for me because my wife and I purchased a townhouse in this development and moved in several weeks ago. We had the surreal experience in sitting in a movie theatre one day and seeing this advertising pitch open up on the big screen and as we looked we realised that this was a digital simulation of our future home.

2. DEMOGRAPHICS

Multiple lot developments with long construction lead times are only possible if the market conditions are right. There must be some degree of confidence about a rising market and increasing demand.

It is useful to look at the underlying demographics that influence the property market in Melbourne and also the trends for the future.

Here in Victoria, the Department of Planning and Community Development has conducted some interesting research about population trends. For the purpose of this paper I have drawn upon a presentation by Jeremy Reynolds, the manager of demographic research at the Department.

The Department research reveals strong growth over time, with peaks coinciding with the Gold Rush of the 1860s, after the first World War and then again the second World War. There was a drop off about the time of the oil crisis.

The Department projects that in the thirty years from 2006 the population in Victoria will increase by over two million. Of that growth the vast majority will occur in Melbourne, in fact 85% of it. Whilst there will be some growth in regional Victoria, the rate of growth in regional Victoria will be much slower than that in Melbourne.

Of course, this creates significant challenges for Government in terms of metropolitan infrastructure and decline in the regions.

Within that increasing population we are also likely to see a marked change in household composition. We are no longer living in a society where the typical household comprises a couple with two or three children and with one dwelling accommodating four or five people. We are heading very quickly to a society where for every six people we may have four dwellings.

Several months ago the National Housing Supply Council issued a report which highlighted the undersupply of housing in the Australian market. It predicted that the national shortfall could possibly hit 640,600 dwellings by 2029 if nothing is done to fix the problem. The problem is most acute in New South Wales and Queensland, but Victoria still recorded a shortfall of about 22,000 homes. It is still commonly reported that about 2,000 people come to live in Greater Melbourne each week.

This report followed another report from the Housing Industry Association which found the demand-supply gap would hit 466,200 by 2020 if no action is taken to increase dwelling construction rates.

Adding to the cause, this month the Committee for Melbourne published a report entitled “Melbourne Beyond Five Million” which quotes the Australian Bureau of Statistics as projecting that our city will grow from 3.9 million people in 2008 to between 6.5 and 7.5 million by 2051. The report goes further and projects the possibility of a population of 8 million people by the end of the century. According to the report this is no more than a continuity of the growth we have seen over the last fifty years and continuing over the next fifty years.

So looking at these demographic factors developers see continued strong demand.

3. PLANNING TRENDS

It is now seen as sound planning policy to encourage greater density of housing. In the 1950s the standard was the quarter acre block, roughly equating to 1,000 M^2 per dwelling. That style of subdivision delivered about 9 dwellings per hectare once space was allowed for public space and streets. On Melbourne's fringe the standard has dropped from about 750 M^2 in the 1970s to around 500 M^2 now. By contrast cities such as Frankfurt, Rome and Vienna have densities of 24 to 30 dwellings per hectare, which is not that different to what we had in inner Melbourne in the 19th century.

In the Melbourne CBD nowadays there is a policy of actively discouraging cars from coming into the City. Accordingly we have had a number of developers carry out very substantial residential developments without any car parking whatsoever. One of our clients did a student accommodation development in Swanston Street, Melbourne with 221 apartments and without a single car park being required. The same developer's latest development in Franklin Street, Melbourne involves about 260 apartments and a boutique hotel and again there is no requirement for car parking.

By contrast, Council encourages designers to include energy efficient features and provision for cyclists.

Of late there is a trend for Councils to become somewhat more assertive in setting guidelines for streetscape, particularly along major arterials. One of our clients is presently waiting on a planning permit from Stonnington City Council for a 40 apartment development and in that instance the architects and planners have expressed quite some dismay at the extent to which a senior urban planner has sought to be involved in design discussions. The architects report this as a relatively new phenomenon.

4. THE PROPERTY DEVELOPMENT TEAM

Any developer embarking upon a multiple lot development will need to engage a large number of consultants and deal with a variety of others.

- Lawyers – property acquisition, subdivision arrangements, banking arrangements, "off the plan" sales, dispute resolution and final purchase settlements
- Project Manager – generally charging about 1% of the gross building cost and perhaps also including the costs of other consultants
- Builders – generally about 4.2% of gross building cost
- Architects
- Services Engineer
- Structural Engineer
- Fire Engineer
- Landscape Architect
- Land Surveyor

- Building Surveyor
- Quantity Surveyors – Initial Cost Check Report ($5,000 - $7,500) and Progress Claim Fees ($1,200 per report) – Normally 1 claim per month
- Town Planner
- Traffic Engineer
- Geotechnical Engineer
- Civil Engineer
- Property Valuers– Say $10,000 - $15,000
- Finance Brokers - Establishment fees from 0.75% - 1.00% of loan amount
- Municipal Planners – application fees and Open Space (Council) Contribution – Normally 5% of land value at start of project
- Referral Authorities – statutory fees and charges
- Local government and rating authorities – Council rates, water rates and land tax
- Referral Authorities for planning permit – VicRoads, rail authorities, power and gas authorities etc.
- Real Estate Agents – they typically charge about 2.5% plus GST, usually payable as to 50% about 6 months after the launch and the balance about a year later. More experienced agents will not consider waiting until settlement. Some agents insist on commission documents revealing a 3% or higher commission rate and then provide rebate letters subject to payment by stipulated deadlines
- Marketing Consultants – some of our clients are now outsourcing website development and digital fly throughs to China

5. DEVELOPMENT TIMELINE

Nothing happens quickly in multiple lot property developments. This is a fairly typical timeline for a multiple lot inner urban or CBD development:

- 6 months to complete purchase of a development site and obtain a planning permit – longer if an appeal to VCAT is required;
- 6 months “off the plan” marketing campaign and achieve a threshold of sales;
- 6 months to shortlist builders and complete construction contract negotiations whilst checking quotes against quantity survey reports and negotiating construction finance;
- 18 to 24 months to build;
- 6 months to mop up unsold lots.

So all up it is not unusual for a project to run from 3 to 4 years.

During a span of four or so years there can be significant changes in the market, as we have seen over the last several years. Under capitalised developers can be particularly at risk if the goalposts move during the course of the game and we have seen quite a bit of that lately.

6. DISTRESSED PROPERTY DEVELOPERS

There are increasing reports of distressed property developers. In the main these involve mid-sized developments where heavily geared developers purchased sites before the Global Financial Crisis and then prosecuted their applications for planning permits and then embarked upon pre-sales. Having achieved, in some instances, almost 100% pre-sales these developers now find that the goal posts have moved during the game and the smaller number of banks just aren't willing to fund construction. So developers have to either shelve the development, enter into a joint venture with a development partner or obtain mezzanine finance, effectively at equity rates.

If a new equity partner comes along there can be stamp duty consequences and CGT consequences. There is usually a dilution of future returns.

In the case of mezzanine finance, the effective interest rate that lenders are seeking is between 18% (if the property has already developed) and 25% if the property hasn't yet been developed.

Quite often a joint venture partner will be a foreign investor with those investors predominantly coming from Singapore, Malaysia, China, India and the Middle East. As accountants you will realise that this raises issues about Thin Capitalisation, Withholding taxes and international reporting standards.

We recently came across a situation where a non-bank lender was trying to extricate itself from a development in Bay Road, Sandringham. In that instance there were forty or so apartments all of which had been pre-sold but the developer was in default and had been in default for twelve months. Recently the lender sold its mortgage to an opportunistic and cashed up developer who will now take its chances in wrestling with the defaulting developer and capturing the project at a significant discount.

We have also heard stories of builders buying partly completed projects from distressed developers in order to protect their own position.

7. CONSTRUCTION FUNDING

In the wake of the Global Financial Crisis there has been a marked contraction in the number of lenders interested in development lending.

A number of the smaller players like Suncorp Metway, Bank West, Capital Finance and so on have left the market and it is pretty much only the four major banks that remain in the market, but their lending criteria are much more strict than two years ago.

In general, there has been a reduction in LVRs of between 10% and 15%. Margins range from 1.75% up to 3.5%. The banks now impose much stricter lending covenants and take a much stricter view of breaches. It is also taking a lot longer to get loan approval because of more stringent review by internal capital and credit committees within banks.

Whilst we don't get that closely involved in dealing with lenders, we understand that:

- ANZ on commercial developments is looking at a loan to value ratio of about 55%;
- the CBA is looking at a loan to value ratio of between 55% and 60%;
- NAB will look at a loan to value ratio of 75% based on value "as if complete";
- Westpac is only interested in the existing customers but seems to be running loans through St George Banks with a loan to value ratio of about 60%.

In a number of instances the banks will come in with Mezzanine finance but only if they are the senior lender, with the consequence that the effective interest rate is increased.

7.1 Funding Structure

A fairly typical senior debt funding arrangement with a major bank would see funding advanced (inclusive capitalised interest) to enable a developer to settle on the purchase of the development site and begin development. Funding can be drawn down on a cost to complete basis subject to certification by a Quantity Surveyor for each progress claim. Lenders require to receive 100% of the net sale proceeds of each apartment upon completion until the majority of the debt is retired.

In larger developments there is a tendency to club loans with two or major banking institutions collaborating. Both lenders advance funds on an equal basis with similar requirements.

7.2 Likely funding obstacles

Generally banks are looking to ensure that there is 80% to 100% total debt coverage from the net realisable value of presales, in other words gross sales less selling costs. Any residual debt should not exceed 25% of the residual security value. Banks are increasingly looking carefully to establish that developers have sufficient equity of their own and some banks are calling for cash to be placed on deposit as evidence of capacity to meet building cost overruns. The approach is to get in and get out, not to stay as a long term lender.

7.3 Qualifying pre-sales

Most banks apply quite vigorous restrictions on sales of lots in a multi-level residential development:

(a) Arm's length from the Borrower and any related companies;

(b) No greater than 10% of sales are to be to offshore domiciled purchasers because of the difficulty in enforcing contracts with offshore purchasers, a number of whom simply walk away from their contractual undertakings;

(c) A full 10% deposit. It is illegal to have more than 10% under the Sale of Land Act;

(d) Deposits – cash or bank guarantee with an Australian based Bank;

(e) Sunset clauses – a date sufficiently in advance to allow for a 50% overrun on the projected construction time line;

(f) The sale price must be for an amount no less than certified by the bank's panel valuer;

(g) The Net Realisable Value (Gross Realisable Value less GST and in some cases agent's commission) of presales is to be no less than 80% of total debt. But the preference is for 100% debt coverage from the Net Realisable Value;

(h) Minimum pre-sale requirement to be achieved, vetted and qualified by the bank's panel solicitor prior to any drawdown of funds.

7.4 Developer Due Diligence

To be successful, an application for construction lending on behalf of a multiple lot developer should include all of the following:

(a) Profile of the Borrower group including CV's of the Principals;

(b) Confirmation of financial capacity of the Borrower group;

(c) Corporate structure diagram;

(d) Potential builder list;

(e) Market competition research;

(f) Confirmation of equity and ability to cover cost overruns from the Borrower (Account statements demonstrating liquid cash etc.);

(g) Architectural drawings and site plan layout;

(h) Contract of Sale for the security property;

(i) Trust Deed and Constitution for the Trust / Borrowing entity;

(j) Personal Tax Returns for all Directors and Shareholders of the Borrowing entity – 2008 & 2009 (2010 if available);

(k) Signed and dated asset and liability statements for all Directors and Shareholders of the Borrowing entity;

(l) If the borrowing entity has corporate shareholders then the banks will require company tax returns and financial statements for these entities as well;

(m) Privacy Act consent form for all Directors and Shareholders;

(n) Copy of original identification documentation for all Directors and Shareholders;

(o) Draft copy of the presale "off the plan" Contract of Sale;

(p) Copy of the Commission Sales Agreement with the selling agent;

(q) Copy of the Lease Agreement with any retail tenants and any other commercial pre leases or Heads of Agreement;

(r) Geotechnical report;

(s) Planning Permit & Build Permit;

(t) Final feasibility;

(u) Fixed Price Building Contract, usually structured as design and construct contract;

(v) Confirmation of the Builder's technical & financial capacity with appropriate references;

(w) Project cost estimates and trade breakdown;

(x) resume for each of the Builder and its Principals and evidence of the builder's financial capacity by means of either financial statements or a Letter of Banker's Opinion from the Builder's own bank;

(y) Council approved stamped plans;

(z) Reference from Quantity Surveyors on the chosen Builder;

There are two industry standard software applications that are commonly used by brokers, valuers and quantity surveyors to assess the feasibility of property developments. They are Estate Master and Feastudy.

7.5 Brokerage Fees

There are a number of brokers with specialist expertise in arranging construction finance. We regularly deal with Choice Capital Pty Ltd and Balmain Advisory Pty Ltd. Generally their brokerage charges range between 0.75% and 1.00% of the senior debt amount arranged, plus GST.

7.6 Feasibility Analysis

As you will see, construction lending has become a quite specialist area of practice. But there is scope for appropriately qualified accountants to work with other development consultants to assist a developer in sourcing construction funding. The scope of work to be undertaken will typically involve the following activities:

(a) Assistance with preparation of feasibility study, cash flows, funding tables and loan structure;

(b) Source and structure suitable funding for the subject development/s;

(c) Liaison with Lender, Valuers, Quantity Surveyors, Solicitors and Builders (where appropriate)and Credit;

(d) In conjunction with the Borrower assessment of all loan structures available for the subject development/s and provide guidance on presales level and construction funding parameters;

(e) Assist with the Lender selection process;

(f) Preparation of final Credit Submission and lodgement with preferred Lender/s;

(g) Prepare the formal Credit Submission to the preferred Lender;

(h) Securing a formal Letter of Offer for consideration by the Borrower;

(i) Assessment of formal Letter of Offer and recommendations to the Borrower;

(j) Acceptance of formal Letter of Offer;

(k) Liaison with Mortgagee/s' solicitor and the Borrower's solicitor;

(l) Overseeing pre-conditions to settlement and managing satisfaction process to ensure completion in advance of settlement date;

(m) Assist generally in concluding the transaction;

(n) Ongoing liaison with the Lender/s regarding progressive drawdowns and reporting covenants and any queries;

(o) Ongoing liaison with Quantity Surveyor regarding certification of progress claims;

(p) Attendance of site meetings on a periodical and "as needed" basis.

In addition, there is an important role for accountants in assisting developers to address GST issues, CGT issues and income tax issues. There is also the possibility, if not the probability, that there will be an ATO audit. I understand that the ATO has a specialist team in Brisbane that focuses on property developers because, as you will appreciate, the ATO advances quite a lot on GST input credits as the development proceeds and needs to know that at the end of the day there will be a return on that "investment". We have come across a number of situations where the ATO has embarked on very intrusive tax audits with property developers.

8. FIRB

In a Media Release on 24 April 2010 the Assistant Treasurer, Senator Nick Sherry, announced a major tightening of foreign investment rules as they relate to residential real estate.

We don't yet have the draft legislation but it is generally the case that revenue related policy changes take effect from the date of the Ministerial Statement, even though the legislation may be enacted subsequently.

The changes target temporary residents seeking to purchase an existing property in Australia. Off the plan purchases during construction period or when the building is partially constructed (or even if completed) are treated as new dwellings as long as the property has not been sold before, and no one has lived in it for more than 12 months.

However, the Government announcement restates the policy that foreign non-residents can only invest in Australian real estate if that investment adds to the housing stock, and that investments by temporary residents in established properties are only for their use whilst they live in Australia.

As a consequence of the announcement, temporary residents will be required to notify, be screened or be approved by FIRB, in the same way as is required of foreign non-residents. In addition, temporary residents who obtain approval will now have to sell the established property upon departure from Australian and, if undeveloped land has been purchased, to commence construction on that land within twenty-four months or have the land compulsorily sold.

Until now, the legislation pursuant to which the FIRB operates has only imposed criminal penalties in the event of a breach. That regime will now be supplemented by a comprehensive civil penalties regime under which offending purchasers, sellers and agents will be targeted. There will also be explicit compulsory divestment requirements where property has been purchased in breach of the guidelines.

As part of the new enforcement regime FIRB will embark upon data matching using its own data, State and Territory land registry data and also immigration data.

Senator Sherry's announcement also foreshadows checks on real estate agents.

In acting on behalf of our multiple lot property developers we now routinely prepare contracts that require purchasers to disclose their migration status. We adopted that approach as most banks and financial institutions involved in development lending set limits on the number of offshore sales. In the absence of proper data collection in the Contract of Sale it can be very difficult to establish the immigration status of a purchaser. These new changes to Australia's FIRB guidelines make this all the more important.

In acting for our developer clients we have amended our standard Contracts of Sale so that we capture data about citizenship and migration status, but this can make for some difficulties.

We have put together a table which enables ready categorisation of transactions as to their FIRB status and a copy of that's in the paper.

9. STATE REVENUE OFFICE – STAMP DUTY EXEMPTIONS FOR THE OFF THE PLAN PURCHASERS

At present we enjoy State Revenue Office concessions when we purchase property off the plan. The concession is available to those who purchase land and building packages or refurbished lots. Put simply it allows a deduction from the contract price of the cost of construction or refurbishment which occurs on or after the contract date, with the consequence that duty is calculated on the value of the land as at the day of sale.

There is a revenue ruling DA.048 from the SRO which deals with the duty concessions and for you as accountants.

Put simply, there are two methods for calculating the off the plan concessions:

- the fixed percentage method; or

- the alternative method.

The fixed percentage method involves the use of the deemed maximum percentage amount which involves a rounding down factor.

The alternative method involves a more detailed calculation.

When all is said and done there is no benefit for a developer in going to the more difficult and time consuming alternative method as it is not the developer who pays stamp duty. In our experience in dealing with many hundreds of lots sold off the plan we have never had a purchaser quibble with the method of calculating the off the plan dutiable value. It is far simpler for our developer clients to apply the fixed percentage method and save themselves the hassle.

As an attachment to the paper we have reproduced SRO Ruling DA.040 to which you may need to have reference to from time to time.

10. DEPOSIT FUNDS

It is fairly common for developers to structure their commission payment arrangements with estate agents on the basis that say 50% of agreed commission be paid after a Contract of Sale is signed and a deposit paid or a bank guarantee provided. The balance of commission is often paid either at some agreed later date or when settlement occurs.

Whilst there is no basis in law for them to do so, it is commonplace for estate agents to retain deposit funds in their trust accounts until the first tranche of commission payments is made.

As deposit monies are stakeholder monies under the Sale of Land Act and must be protected until settlement or earlier authorised release (generally impossible with “off the plan” developments) it is important for developers to move quickly for the investment of the deposit funds.

Whilst deposit funds remain in the trust account of an estate agent the interest that accrues is appropriated by legislation for a public purpose.

So it makes no sense, and in fact costs developers, if agents delay the handover of deposit funds in the belief that they are entitled to some control over them.

For example, on the sale of a 100 lot apartment development at an average gross price of $400,000.00 there is about $4,000,000.00 in deposits to be invested. If one assumes an interest rate of 5% then a delay on the part of agents in releasing deposit funds for investments for say two months can cost the developer more than $30,000.00.

It is curious that so few developers seek to address this issue in their commission agreements with estate agents and in the process forego an entitlement to a return on the capital to which they will ultimately be entitled.

It follow of course that, from the developer's point of view it is far better to have a deposit paid by cash or cheque rather than a bank guarantee or a deposit bond because ultimately the developer will get the interest from its investment pending completion.

It is also worth noting that just recently a number of the construction lenders have insisted upon deposit funds being placed in investment bearing accounts with them, so they can see the deposit funds actually exist. Apparently in the past a number of banks were caught out when they discovered that developers were lying about pre-sales and there were no actual deposits being held.

11. MARGIN SCHEME – THE BASICS

11.1 **Who can use the margin scheme?**

Developers may be able to use the margin scheme when making taxable supplies of real property where they are:

(a) Selling a freehold interest in land;
(b) Selling a stratum unit; or
(c) Supplying a long term lease.

Developers will *not* be able to use the margin scheme if they sell property that they:

(a) Acquired through a taxable sale on which the margin scheme was not used;
(b) Inherited from a person who would not have been able to use the margin scheme;
(c) Acquired from a member of the same GST group who would not have been able to use the margin scheme, or
(d) As a participant in a GST joint venture, acquired from the joint venture operator who would not have been able to use the margin scheme.

Needless to say, purchasers who acquire residential property under the margin scheme are not entitled to claim input tax credits for the GST they pay in the purchase price, nor is the developer required to provide a tax invoice at settlement.

11.2 **Calculating the GST**

The amount of GST one normally pays on a property sale is equal to 1/11 of the total sale price. When the margin scheme is used, the amount of GST is 1/11 of the margin.

In general, the margin is the difference between the sale price and either:

(a) The amount the Developer paid for the property; or

(b) The value of the property provided in an approved valuation of the property as at 1 July 2000 (if certain conditions are satisfied).

The Margin is not:

(a) The profit margin (the margin on the sale does *not* take into account costs the Developer incurred to develop the new property or subdivide the land);

(b) The selling price minus a valuation of the property for a property purchased after 1 July 2000;

(c) Worked out the same way as a capital gain (that is, it is still possible to pay GST under the margin scheme even though there was no capital gain for income tax purposes).

11.3 **When the margin scheme applies**

A developer can use the margin scheme if:

(a) It purchased the property before 1 July 2000; or

(b) It purchased after 1 July 2000 from someone:

- who was not registered or required to be registered for GST;
- Who sold existing residential premises;
- Who sold the property as part of a GST-free going concern; or
- Who sold the property using the margin scheme.

11.4 **How to Calculate the Margin**

There are two methods to calculate the margin (depending on when you purchased):

(a) The consideration method (can be used regardless of when you purchased)

The margin is the difference between the property's selling price (including any settlement adjustments) and the original purchase price, that is:

- margin = sale price – purchase price

It does ***not*** include costs of the following:

- Costs for developing the property;
- Legal fees;
- Any options purchased;
- Stamp duty;
- Any other related purchase expenses

(though if GST is a component of the price, the Developer may be entitled to claim a GST credit for the GST in the relevant tax period in which the purchase was made)

(b) The valuation method (generally only used if the property was purchased before 1 July 2000)

The margin is the difference between the selling price and the value of the property (usually as at 1 July 2000), that is:

- Margin = sale price – value of property (usually as at 1 July 2000)

(Must be an 'approved valuation')

11.5 **Requirements to be met vary according to the following:**

In terms of the purchase, requirements vary according to whether the Developer purchased:

(a) Before 1 July 2000:

Developer can choose to use either the consideration method or the valuation method

(b) On or after 1 July 2000:

Developer can only use the consideration method

(c) On or after 9 December 2008:

From this date, the Developer cannot use the margin scheme if the entity it purchased from was not eligible to use the margin scheme and the property was purchased:

- as part of a GST-free going concern;
- as GST-free farm land;
- from an associate for no consideration.

If the entity was eligible, but the Developer purchased the property through one of the above, the Developer must include the value it and the previous seller added to the property when the Developer calculates the margin.

In terms of the sale, requirements vary according to whether the Developer made the sale:

(d) On or after 17 March 2005:

From this date, the Developer cannot use the margin scheme if it:

- purchased the property as fully taxable and the margin scheme was not used;
- inherited the property from a person who could not use the margin scheme;
- obtained the property from a member of the same GST group who could not use the margin scheme; or
- obtained the property, as a participant in a GST joint venture, from the joint venture operator who could not use the margin scheme.

(e) On or after 29 June 2005:

- All of the requirements from 17 March 2005 continue to apply; and
- There must be a written agreement between the Developer and purchaser to use the margin scheme.

From our perspective as lawyers and advisors, we need to ensure that when Developers purchase property, they have investigated the manner in which the property has been treated in the past in terms of GST and the margin scheme.

Since 2008 the new standard form Contract of Sale now includes provision for the election of the margin scheme though we have found that sometimes Developers still get it wrong and later, and prior to settlement, have to write to each individual purchaser seeking an acknowledgement in writing that the margin scheme will apply.

12. PROPERTY DEVELOPMENT AGREEMENTS

In the course of our acting for developers we also have some involvement in drafting property development agreements. This is not a technical term but it is used in contra distinction to a joint venture agreement. Essentially it is a contractual agreement between the landowner and the developer for the development of the land, without the developer taking any ownership interest in the land.

There are a number of compelling taxation and duty reasons for structuring an agreement in this way.

The landowner contributes to the land and the benefit of any zoning, planning, environmental, cultural or conceptual work done up to a certain date on the site. The developer typically contributes the expertise, experience and capital to take the development to the next stage and see construction through to completion.

For sound duty and taxation reasons the landowner remains the owner of the land at all relevant times throughout the development. But the developer has power pursuant to a power of attorney to effectively take charge of the development.

For a developer, such an agreement means that they don't have to fund the purchase of the land and so the finance costs are lower. It is not a legal or tax partnership because the parties don't jointly receive the income.

It is beyond the scope of this presentation to go into these property development agreements in detail.

13. CONCLUSION

At first blush it might be through that the legal aspects of "off the plan" property work is high volume, repetitive and not all that challenging. Invariably, the course of a multiple lot property development is always to some degree uncertain. Planning and building issues are often complex.

Increasingly the mark of an effective and successful developer is that the developer surrounds itself with a well credentialed team of consultants including lawyers and accountants.

There are significant opportunities for accountants to work with developers. In our experience, the quality of accounting advice that some of our developer clients receive is quite unsatisfactory.

Please contact us if you have any queries

Anthony Burke
Director
tony@burkes-law.com

Ana Percic
Lawyer
ana@burkes-law.com

Rachel Xia
Lawyer
rachel@burkes-law.com

Burke & Associates

PURCHASING RESIDENTIAL REAL ESTATE IN AUSTRALIA – FIRB APPROVAL STATUS

	FOREIGN INVESTORS	TEMPORARY RESIDENTS	AUSTRALIAN CITIZENS[1] NEW ZEALAND CITIZENS PERMANENT RESIDENTS
SINGLE BLOCK VACANT LAND ▪ land which is zoned to permit the construction of no more than one residential dwelling per block of land	**Approval Required** ▪ normally approved subject to: - continuous substantial construction must commence within 24 months	**Approval Required** ▪ normally approved subject to: - continuous substantial construction must commence within 24 months	**Approval not required** N/A
VACANT LAND TO BUILD MULTIPLE DWELLINGS	**Approval Required** ▪ normally approved subject to: - continuous substantial construction must commence within 24 months; and - at least 50% of the acquisition cost or the current market value of the land (whichever is higher) must be spent on development	**Approval Required** ▪ normally approved subject to: - continuous substantial construction must commence within 24 months; and - at least 50% of the acquisition cost or the current market value of the land (whichever is higher) must be spent on development	**Approval not required** N/A
NEW DWELLINGS[2] ▪ before construction; ▪ during construction; or ▪ after construction is completed ▪ includes dwellings part of extensively refurbished buildings where building's use has undergone a change from non-residential to residential. ▪ does not include refurbished or renovated established dwelling.	**Approval Required** ▪ normally approved if: - not previously sold; and - not occupied for more than 12 months[3]	**Approval Required** ▪ - normally approved if: - not previously sold; and - not occupied for more than 12 months[4]	**Approval not required** N/A

[1] Also includes a purchaser whose spouse is an Australian citizen and purchasing residential real estate *jointly.* Spouse includes de facto partner wither same sex or different.
[2] A Dwelling acquired 'off-the-plan' (that is, before construction commences or during the construction phase) *or* after construction is complete, where the dwelling: has not previously been sold (i.e. purchased from the developer); and has not been occupied for more than 12 months.
[3] No limit to number that can be sold to foreign persons as long as developer also markets in Australia.
[4] No limit to number that can be sold to foreign persons as long as developer also markets in Australia.

ESTABLISHED DWELLINGS FOR REDEVELOPMENT ▪ i.e. to demolish the existing dwelling and build new dwellings ▪ does not include refurbishing or renovating established dwelling.	**Approval Required** ▪ normally approved subject to: - the proposal must provide for an increase in the housing stock i.e. increase in the number of dwellings[5]; - the established dwelling cannot be rented out prior to demolition and redevelopment; - the established dwelling must be demolished and continuous substantial construction of new dwellings must commence within 24 months.	**Approval Required** ▪ normally approved subject to: - the proposal must provide for an increase in the housing stock i.e. increase in the number of dwellings[6]; - the established dwelling cannot be rented out prior to demolition and redevelopment; - the established dwelling must be demolished and continuous substantial construction of new dwellings must commence within 24 months.	**Approval not required** N/A
OFF-THE-PLAN WITH PRE-APPROVAL ▪ developments with 10 or more dwellings ▪ up to 50% of total dwellings	**Approval not required** N/A[7]	**Approval not required** N/A[8]	**Approval not required** N/A
ESTABLISHED DWELLINGS/SECOND-HAND DWELLINGS ▪ dwelling that is not a New Dwelling ▪ previously owned and/or occupied for more than 12 months	**Approval <u>not</u> granted** ▪ if acquisition by company: approved subject to the company undertaking to sell or rent the property if it is expected to remain vacant for six months or more	**Approval required** ▪ usually approved for <u>one</u> property only if used as PPR and sold when TRs leave Australia or ceases use as PPR	**Approval not required** N/A

DISCLAIMER: The material on these pages is intended only to provide a summary and general overview. It is not intended to be comprehensive nor does it constitute legal advice. You should seek legal or other professional advice before acting or relying on any of the content.

[5] A redevelopment proposal which does not increase the number of dwellings may be approved where it can be shown that the existing dwelling is at the end of its economic life i.e. derelict or uninhabitable, since constructing a new dwelling would effectively increase the housing stock. Valuation is required by a licensed valuer and/or builder's report.

[6] A redevelopment proposal which does not increase the number of dwellings may be approved where it can be shown that the existing dwelling is at the end of its economic life i.e. derelict or uninhabitable, since constructing a new dwelling would effectively increase the housing stock. Valuation is required by a licensed valuer and/or builder's report.

[7] Developer is required to provide a copy of their pre-approved letter to each prospective purchaser and to report all sales (Australian and Foreign) to FIRB on a 12 monthly basis until all dwellings are sold or occupied.

[8] Developer is required to provide a copy of their pre-approved letter to each prospective purchaser and to report all sales (Australian and Foreign) to FIRB on a 12 monthly basis until all dwellings are sold or occupied.