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Australia: Can something start as "land", and then become something else?

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In brief

Meridian Energy Australia Pty Ltd v Chief Commissioner of State Revenue [1]

The case sheds light on how the **source** of a property right is relevant to the meaning of "land" or "interest in land" in the context of the Duties Act.

Namely, the case considers how the "correct approach" is **not** to assume that property interests created by statute (and the consequences of this right on the transferee and transferor) will have similar outcomes as the common law.[2]

In particular, the case contemplates how a statutory instrument may cause something to lose its character as "land" and become something unnamed and in a "class of its own" (i.e., *sui generis*).

> *"Property **interests** owing their **existence** to **statute should be characterised in light of the relevant statutory provisions**, **without attaching** undue **significance** to **similarities** in a **common law** analogue."*[3]

This was the guiding principle applied by the Supreme Court of NSW in relation to how property rights **conferred by statute** should be interpreted within the meaning of "land" and "land holdings" in the Duties Act 1997 (NSW) ("**Duties Act**").[4]

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In particular, the case contemplates how a statutory instrument may cause something to lose its character as "land" and become something unnamed and in a "class of its own" (i.e., *sui generis*).

In this context, the Court cautions against the "fallacy of assimilating" the exercise of a statutory right (here, a *sui generis* interest) to categories of interest in land known to the common law.[6] This would be something like fitting a square peg into a round hole. A property right conferred by statute is answerable solely by reference to the provisions of that statute - its **source**, and not general law principles.

It is noted that:

- Although the current definition of "land holdings" under the Duties Act adopts a "fixed to land" model (i.e., physically affixed assets, irrespective of whether the asset is a fixture at law, can be caught under the provisions), these provisions

[1] *Meridian Energy Australia Pty Ltd v Chief Commissioner of State Revenue* [2022] NSWSC 1074 ("**Meridian**").
[2] Meridian, above, [87], citing the High Court in *Asciano Services Pty Limited v Chief Commissioner of State Revenue* (NSW) (2008) 235 CLR 602.
[3] Meridian, above, [85], citing the High Court in *R v Toohey* (1982) HCA 69, [344] (our **emphasis** added).
[4] Duties Act 1977 (NSW), s 146.
[5] Meridian, above, [87], citing the High Court in *Asciano Services Pty Limited v Chief Commissioner of State Revenue* (NSW) (2008) 235 CLR 602.
[6] Meridian, above, [86], citing the High Court in *Commissioner of Main Roads v North Shore Gas Co Ltd* [1967] HCA 41.

were not in force at the time of the relevant acquisition in this case. However, this case provides additional guidance on what constitutes an interest in land.

- At the time of publication of this article, the Chief Commissioner of State Revenue filed a Notice of Appeal in the NSW Court of Appeal.

Background

In 2018, Meridian Energy Australia Pty Ltd's ("**Meridian**") acquired 100% of the shares in GSP Energy Pty Ltd (GSP) from Trustpower Limited for over AUD 160 million. GSP operated three hydro-electric power stations in NSW ("**Power Stations**") and was the lessee of the land ("**Leases**") on which the Power Stations are situated. GSP's access to the water required for the operation of the Power Stations (and its licence to access the Power Stations themselves) was pursuant to Water Agreements entered into with the State Water Corporation.

The Chief Commissioner determined that GSP was a "land holder" for the purposes of s 146(1) of the Duties Act, with the consequence that the acquisition of the shares by Meridian triggered a liability for land holder duty. Land holder duty is paid on the acquisition of entities with land holdings (i.e., interests in land) valued at AUD 2 million or more. The Chief Commissioner assessed land holder duty in the amount of AUD 7,979,740.37, calculated on land holdings and goods valued by the Chief Commissioner in the amount of AUD 145.35 million.

At the time of the relevant acquisition, the Power Stations were the subject of a statutory Vesting Order. Relevantly, the Vesting Order excluded the Power Stations from the schedule which **exhaustively** listed a number of "interests in land", and instead listed the Power Stations under a separate schedule for "interests **other** than land".

The key issue in dispute by Meridian was therefore whether GSP was a "land holder" when one gives regard to the effect of the statutory vesting order. In other words, did GSP have interests in land with a value of at least AUD 2 million?

The Statutory Instruments

The EGA Act conferred power on the Treasurer to exercise all such functions as are necessary or convenient for the purposes of an authorised transaction, including the making of Vesting Orders.[7] The EGA Act and Vesting Orders are referred to as the "**statutory instruments**" (which created the relevant property interest discussed in this case).

At the time of the relevant acquisition, the Power Stations were subject to a Vesting Order in 2014 (as well as earlier vesting orders in 2013 and 2000). The 2014 Vesting Order was materially identical and therefore did not change the purpose of the 2013 Vesting Order and therefore, primary regard was had to the 2013 Vesting Order.

Meridian placed emphasis on the statutory instruments in construing the nature of the property interest (being the source of the interest), and submitted that the effect of the structure, language and object of the statutory instruments was to **alter** the character of the Power Station interest, if that interest were to be conceived or construed with respect to general law principles regarding land.

Meridian submitted that the EGA Act expressly enabled the vesting of something which is part of land without vesting the whole of the interests of the transferor in that land.[8] The Vesting Order then deliberately omitted the Power Station assets from a schedule listing "interests in land" (and instead listed them in "interests other than land"), and in doing so, severed the Power Stations from the land and vested ownership of them (a *sui generis* interest) in the transferee. The general law principles could not "intrude" to change the character of the right conferred by statute, and the property interest is answerable solely to the statute that conferred the right.[9]

The Chief Commissioner remained silent with respect to this structural distinction in the Vesting Order between "interests in land" and "interests other than land", instead disputing Meridian's interpretation regarding the overall **effect** of the Vesting Order, relying upon general law principles regarding fixtures to assert that the Power Stations formed part of the land (addressed directly below).

[7] Electricity Generator Assets (Authorised Transactions) Act 2012 (NSW) s 7 and s 13.
[8] Meridian, above, [94].
[9] Meridian, above, [89].

Characterising the Power Stations as a fixture - an interest in land

The Chief Commissioner stated that the effect of the statutory instruments was merely to transfer the existing assets of the tenant of the leased land to the future tenant of the leased land.[10] The Vesting Orders did not have the effect of severing the Power Stations (as fixtures) from the leased land, nor extinguishing the rights of the owner of the leased land with respect to the Power Stations nor created any *sui generis* property interest.[11]

Regarding the latter point, the Chief Commissioner emphasised that the **operator** of the Power Stations was never the **owner** of the leased land on which the Power Stations operated. In this regard, the effect of the Vesting Order could not have been to transfer the fixtures owned by the owner of the land, but only to transfer the operator's interest as lessee or tenant of the leased land. This was supported by the lack of any reference to the owner of the land in the Vesting Order.

This accords with the general law principles regarding tenants' fixtures, which as held by the same Court in SPIC Pacific Hydro about a year earlier,[12] will remain part of the freehold land until and unless the fixtures are physically removed. [13]

The Power Stations, according to the Chief Commissioner, remain as fixtures, forming part of the leased land which Meridian acquired (and therefore at the time of the GSP acquisition, Meridian held an interest in land for stamp duty purposes). [14]

Characterising the Power Stations as sui generis - a non-land interest

Meridian disputed that GSP was a "land holder", submitting that the effect of the statutory instruments was that they severed the Power Stations from the land, and rendered them outside the meaning of land, fixtures or goods for the purposes of the NSW landholder duty regime (i.e., a *sui generis* interest).

In response to the Chief Commissioner's contentions that the statutory instruments did not mention the owner of the land, and therefore could not convey the land holder's interest in the Power Station (but only the tenant's interest in the lease), Meridian submits that the statutory instruments expressly enabled the vesting of the something which is part of land without vesting the whole of the land.[15]

Meridian asserted that "whatever impediment" that exists at general law to a conveyance of the Power Stations separately from the land should therefore not apply here.[16]

Meridian cites Western Australia Supreme Court Authority regarding the meaning of land, where the interest in pipelines was similarly conferred by statute. In that case, the Court held that the interest in the pipelines was "answerable solely by reference" to the statutory instruments, and therefore, general law principles "could not intrude to change the character" of this interest.[17]

Which way did the Court go?

The Court ultimately held that the interest in the Power Stations vested in GSP were not an interest in land. This meant that the Court had to determine the correct valuation of the Leases upon which the Power Stations were situated (i.e., the agreed interests in land) to conclude whether the AUD 2 million land holder value threshold was met for GSP.

Although not strictly necessary, the Court also determined for completeness that the Power Stations were not "goods" for the purposes of the Duties Act.

The Power Stations

The Court did not reject the general law principles relied upon by the Chief Commissioner regarding tenants' ownership, noting that these had "much support at first blush".[18] However, the Court did not ultimately need to consider the application of these general law principles in the present facts and circumstances, as the property right in question was conferred by statute.

In this context, the Court held the "correct approach" is to characterise the right by reference to the object of the Statute (which was to create an interest in the Power Stations in a category "other than land").[19]

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[10] Meridian, above, [11].
[11] Meridian, above, [105].
[12] *SPIC Pacific Hydro Pty Ltd v Chief Commissioner of State Revenue* [2021] NSWSC 395, [139]. See *SPIC Pacific Hydro Pty Ltd v Chief Commissioner of State Revenue* by Peter McMahon, Janet Cho and Sidney Yiu (Baker McKenzie) in the June 2021 issue of this publication for further detail regarding this case.
[13] Meridian, above, [137].
[14] Meridian, above, [137].
[15] Electricity Generator Assets (Authorised Transactions) Act 2012 (NSW) Cl 7(1) of Sch 4.
[16] Meridian, above, [94].
[17] Meridian, above, [89], citing *Epic Energy (Pilbara Pipeline) Pty Ltd v Commissioner of State Revenue* (2011) 43 WAR 186.
[18] Meridian, above, [46].
[19] Meridian, above, [86].

The Court cited NSWCA and High Court authority for this position,[20] noting in particular that it would constitute a "fallacy" to "assimilat[e] the exercise of a statutory right to categories of interest in land known to the common law" and that where Parliament confers an innominate statutory right, “there is no need for lawyers to insist on finding an old name for them, when they are in fact *sui generis*”.[21]

As such, the Court held that "whatever impediment" that exists at common law to the transfer does not apply as the *sui generis* interest in the Power Stations is to be characterised by reference to the object of the Statute.[22] The statutory instruments expressly enabled this and the general law "could not intrude to change this".[23] The Court held "there is nothing to be gained" by characterising a property right conferred by statute by reference to general law principles. [24]

The Court noted that the "statutory language [of the EGA Act and Vesting Order] is not limited" in its capacity to create a *sui generis* interest that is outside the common law categories of land, and instead, expressly enabled the transfer of the Power Stations separately to the land.[25]

As regards to the transfer of the ownership of the Power Stations (without the operator being the land owner on which the Power Stations operated, contrary to general law principles), the Court accepted Meridian's emphasis on the object and language of the Vesting Order that "sole legal and beneficial" ownership will transfer, and this interest would not be "derivative of, nor dependent on, the grant of a leasehold interest by a third party".[26] Further, the EGA Act enabled the Treasurer to vest an interest "in respect of land" (which did not have to be the whole of the interests of the transferor in that land).[27]

In this case, the effect of the statute was to vest the Power Station assets separately from any interests in the underlying land (i.e., they could, and did, sever the Power Station from the land - creating an innominate *sui generis* interest, not being an interest in land). That is, the transferee of the interest, under the vesting order, would commence holding the Power Stations in gross and not in connection with any interest in land.

Separately, the Chief Commissioner (as does Meridian) refers to The Noordam, where it was said that the word “goods” was of very general “and quite indefinite import” and primarily derived its meaning from the context in which it was used. The Chief Commissioner submitted that the term “goods” is of sufficient breadth to capture the Power Stations, if they are not otherwise classified as land. In response, the Court also did not accept the Chief Commissioner's submissions that the Power Stations were "goods", similarly citing North Shore Gas Co.[28] Namely, the Vesting Order granted an innominate statutory right, which here, is constituted by "immovable physical generator assets affixed to the land but statutorily severed and held in gross". It was therefore "erroneous to attempt to assimilate the Power Station assets to either category of goods or land".[29]

It is interesting that the Court also explored the timing difference between the transfer of the Power Stations and the commencement time of the underlying lease. However, the Court did not comment on the relative significance of this factor, relative to the overall object, structure and language of the statutory instruments, nor how determinative this timing difference was in this matter.[30]

Relevantly, Meridian points out that under the 2014 Vesting Order, GSP acquired its interest in the Power Stations as at 11.59 pm on 17 July 2014; and GSP did not acquire its leasehold interest in the respective Leases until 18 July 2014. Meridian says that, between the effective time of the 2014 Vesting Order and the commencement time of the Leases, GSP held the Power Stations in gross (similar to the manner in which the prior transferee held the Power Stations under the 2013 Vesting Order); and that there is no mechanism in the EGA Act that changes the nature of GSP’s interest in the Power Stations after the commencement of the Leases.

The Court does note however that things built on the land **after** the asset has been transferred as a *sui generis* interest (under, for example, a vesting order) would depart from this *sui generis* characterisation, and take on the chattel vs fixture distinction at common law once again.[31] Assets of this kind included "skids" in the switchyard which are bolted into concrete footings that are embedded in the soil and contain a series of electrical equipment mounted on them. The Court also accepted the Pacific Hydro

[20] *Chief Commissioner of State Revenue v Pacific National (ACT) Limited* [2007] NSWCA 325, [68] and approved by the High Court on appeal in *Asciano Services Pty Limited v Chief Commissioner of State Revenue* (NSW) (2008) 235 CLR 602.
[21] Meridian, above, [133].
[22] Meridian, above, [94].
[23] Meridian, above, [89].
[24] Meridian, above, [87].
[25] Meridian, above, [125]; Electricity Generator Assets (Authorised Transactions) Act 2012 (NSW) Cl 7(1) of Sch 4.
[26] Meridian, above, [123].
[27] Meridian, above, [124].
[28] Meridian, above, [279].
[29] Meridian, above, [279].
[30] Meridian, above, [100].
[31] Meridian, above, [286].

Methodology (specifically for the valuation of assets installed after the Vesting Order, but not for the *sui generis* interest) as they "have the features of something that would ordinarily be seen as a tenant's fixture".[32]

Valuation: Is the Supreme Court doing away with the Pacific Hydro Methodology, just a year later?

Meridian submitted that the Leases had nil value because the rent paid under the Leases was comparable to market rent. The Chief Commissioner submitted that the Leases ought to be valued at AUD 144.85 million (thereby significantly exceeding the AUD 2 million land holder value threshold), adopting the valuation methodology applied by Payne JA in SPIC Pacific Hydro ("**Pacific Hydro Methodology**"). It was further submitted (and the Chief Commissioner did not oppose) that the Water Agreements had material value but as they did not constitute interests in land, their value was not relevant to the calculation of the relevant duty base.

The "Pacific Hydro Methodology" refers to the approach accepted by the Court in SPIC Pacific Hydro at [157], which valued the interest in land in the context of a hypothetical sale of a going concern where the hypothetical purchaser will also have access to and receive the benefit of other assets of the land holder which affect land value. Thus, the methodology valued the leasehold interest on the assumption that the plant and equipment constituted fixtures that may be removed at any time and must be removed at the end of the lease. In this regard, the Chief Commissioner sought to focus on the right to exploit and use the fixed plant and equipment in the Power Stations, and to the value of the lease of the bare land.

Meridian submitted that the Pacific Hydro Methodology was not appropriate in valuing the Power Stations and that this case distinguished from SPIC Pacific Hydro in two main respects:

- First, GSP owns the Power Stations located on the land the subject of the Leases and consequently GSP has the right to use them by virtue of its ownership of them and not the Leases (as it is a *sui generis* interest vested separately from the land); whereas in SPIC Pacific Hydro all the wind generator assets on the land were owned by the lessor and the lessee's right to use them was derived solely from the right to use the land conferred by the lease. As noted above, the EGA Act expressly enabled the interest in the Power Stations to be vested and would not be "derivative of, nor dependent on, the grant of a leasehold interest by a third party".
- Second, that State Water Corporation has the right under the Water Agreements to acquire the Power Stations at termination for AUD 1. Hence, it is said that the land owner (on which the Power Stations operated) does not benefit from having the Power Station assets on the land at termination. Meridian submitted this supports its position regarding the primacy of the Water Agreement over the Lease.

The Court ultimately agreed that it was inappropriate to apply the Pacific Hydro Methodology, stating that it was not intended to "lay down some inflexible rule as to valuation of such assets".[33] The Pacific Hydro Methodology is only one valuation methodology endorsed in the specific context of the valuation question in SPIC Pacific Hydro.[34] This was similarly expressed by the Supreme Court of Victoria Court of Appeal decision in *Valuer-General Victoria v AWF Prop Co 2 Pty Ltd*.[35]

In the alternative, the Court acknowledged that there was broad agreement between the parties to use the 'residual valuation approach' where it was difficult to readily ascertain the market value of particular assets. Meridian submitted that, to the extent that there was a difference between the market value of GSP's shares at the time of Acquisition and GSP's assets and liabilities other than the Water Agreements and the Leases ("**residual**"), the whole of this residual should be allocated to the Water Agreements as the key asset, and not the Leases.

The Court largely accepted this argument, pointing to the following factors in support:[36]

- The Leases merely confer an ancillary right (being to keep the things which GSP owns on the land and then to allow the State Water Corporation to acquire them at termination). This supports the view that the Leases are mere contributory assets and that the primary asset is the Water Agreements.

[32] Meridian, above, [269].
[33] Meridian, above, [268].
[34] Meridian, above, [190].
[35] *Valuer-General Victoria v AWF Prop Co 2 Pty Ltd* [2021] VSCA 274, [126].
[36] Meridian, above, [271].

- While the position of the land on which the Power Stations are located is a "contributor to the profits of the business", the Court was "persuaded that the fundamental driver" ("**go, no-go asset**") is the Water Agreement, without which the Lease could have no value.

Conclusion

So where are we now?

About a year earlier, the same Court in SPIC Pacific Hydro held that tenants' fixtures will remain part of the freehold land until and unless the fixtures are physically removed (and therefore, at the time of an acquisition, the transferee would be acquiring an interest in land).[37] That is, a tenant's interest in unsevered leasehold improvements is a purely legal interest in land which arises from and is governed by the terms of the particular lease and rights under the common law, rather than any separate equitable interest in land held by the tenant.

While ostensibly departing from SPIC Pacific Hydro, the Court in this case sheds light on how the **source** of a property interest may move the needle on the analysis regarding when a property interest will come within the meaning of "land holdings" and specifically, an interest in land.

Namely, the source of Meridian's property interest is distinguished, as it was conferred by statute, and the effect of the statutory instruments was that they severed the Power Stations from the land and vested a *sui generis* interest which fell outside the meaning of "land". It should be noted that:

- Importantly, the Court did not specifically reject the general law principles more generally, in fact it noted that any assets installed on the land after the *sui generis* interest had been created by statute would revert back to the traditional chattel vs. fixtures analysis (as discussed in SPIC Pacific Hydro).
- The Court held the correct approach is to characterise the right by reference to the object of the statute (which was to create an interest in the Power Stations in a category "other than land").[38]

Whilst this is a "win" for the taxpayer, as noted above, the Chief Commissioner filed a Notice of Appeal in the NSW Court of Appeal. Further, the statutory framework governing the meaning of "land holdings" was expanded effective 24 June 2020 to specifically capture assets that are fixed to land, whether the thing:

a. constitutes a fixture at law, or

b. is owned separately from the land, or

c. is notionally severed or considered to be legally separate from the land as a result of the operation of any other Act or law. [39]

Accordingly had the relevant acquisition taken place after June 2020, it would no doubt have been a different outcome for the taxpayer as the Power Stations would arguably be a "land holding" under the current rules.

Regardless, where certain physical structures are the subject of a statutory instrument, this case provides helpful clarity in:

- A NSW transfer duty context as there is no similar expansion of the definition of "land" to include physically affixed assets, unlike the NSW land holder duty regime. Also, NSW transfer duty is calculated on the dutiable value of goods if those goods are the subject of an arrangement that includes any other dutiable property (e.g., land). Given that this case provides support to the proposition that a physical structure can be neither "land" nor "goods", this can produce a significantly different transfer duty outcome on an asset sale transaction.
- An Australian capital gains tax context whereby Australian assets are assessed as to whether they constitute "taxable Australian real property" for the purpose of determining whether a capital gain or loss made by a foreign resident may be disregarded. As "real property" encompasses interests in land, it will need to be considered whether any statutory instrument affects the asset's characterisation as land or as an innominate *sui generis* property interest.

[37] Meridian, above, [137].
[38] Meridian, above, [86].
[39] Duties Act 1977 (NSW), s 147A(1)(c).

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