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TAX matters

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Superannuation Funds with pre 1999 Unit Trusts – Don't Get Caught Out

If your self managed superannuation fund (SMSF) invested in a unit trust prior to 11 August 1999 (pre '99 unit trust), immediate action needs to be taken. With the impending cessation of the transitional rules on 30 June 2009, many trustees are under misconceptions as to what is needed to both capitalize their trust investments and prevent breaching the restrictions to which they will unknowingly be exposed.

The transitional rules in subdivision D of Part 8 of the *Superannuation Industry*

(*Supervision*) Act 1993 (SISA) provide that an SMSF with investments acquired prior to 11 August 1999, are held not to be in-house assets, which are ordinarily restricted. Designed initially to prevent a credit crush, these rules are very effective in providing trustees of pre '99 unit trusts with tax benefits, not held by other SMSFs, such as the ability to:

- 1) reinvest trust distributions;
- 2) invest in unpaid trust units; and
- 3) extend borrowings.

Protecting your investments and yourself

The recent spate of Australian Taxation Office (ATO) rulings, determinations, and taxpayer alerts, all suggest that pre '99 unit trusts are under scrutiny by the ATO. In *Draft Self Managed Superannuation Fund Ruling SMSFR 2008/D1*, it is proposed that once finalised, all unpaid distributions after 30 June 2009 that are owed to an SMSF by a pre '99 unit trust will be deemed a loan arrangement, in breach of the in-house asset rules and assessed at the higher tax rate of 46.5% p.a.

Additionally, the ATO confirmed in *SMSFD 2007/D1* that an SMSF transfer to pre 99-unit trusts after the 30 June 2009 date will also be in breach of the in-house asset rules as provided by section 83 of the SISA.

In-house assets are limited to 5% of the total assets held by the SMSF. Further, once the above arrangements pass this limit they can give rise to a higher likelihood of the arm's length and sole purpose tests of the SISA being breached. Where such breaches occur, civil or criminal penalties may ensue.

How this may affect you

Trustees who have been accumulating unpaid distributions or relying on SMSF reinvestments to either capitalise trust assets or pay outstanding borrowings, will have until 30 June 2009 to satisfy such debts and ensure their trust assets are fully utilised. After this date, the transfer of funds between an SMSF and a trust may cause breaches of the SISA rules.

After 30 June 2009

Provided trustees have instituted the necessary measures, pre '99 unit trusts will continue indefinitely to be useful family wealth management tools after 30 June 2009, if properly managed.

An array of further benefits are also available to pre '99 unit trusts after 30 June 2009, including their commonly cited unique ability to:

- 1) invest and acquire property in an unrestricted manner;

IMPORTANT: The articles in this newsletter are in summary form and should not be relied on as a substitute for detailed advice.

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- 2) carry on a business;
- 3) own or lease back business real property to members; and
- 4) hold and increase borrowings to purchase assets. (Note: whilst section 67(4A) of the SISA allows SMSFs to borrow directly by way of limited recourse loans, pre '99 unit trusts are not restricted to limited recourse and are consequently able to borrow on more favourable terms).

Solutions to your Pre-Unit Trust Concerns

It is imperative that trustees review all their transitional in-house reinvestments and loans well **before 30 June 2009**. Further action or inaction may cause the trust assets and arrangements to breach the SISA and incur penalties.

In these uncertain economic times, it would be prudent to protect your SMSF. We have experience in strategies available to:

- 1) maximise your trust earnings;
- 2) determine how best to inject funds into these trusts through revaluations and rollovers;
- 3) reduce and remove trust debts; and
- 4) prevent any future liabilities that may arise through prudent trust management.

There is no simple answer on to how best manage a pre '99 unit trust, however, the point is clear that trustees must act quickly to prevent personal liability and ensure these trusts can be preserved for future generations to enjoy.

Contact: Chris Smailes, Daniel Fry or Richard Norton.

Superannuation Death Benefits: Payment to the “Wrong Dependant”

Did you know that Norton & Smailes advises on superannuation complaints?

The exercise of discretion by a superannuation trustee to pay all or more of a death benefit to a particular dependant is often the subject of a complaint to the Superannuation Complaints Tribunal (SCT).

NOTE: the SCT complaint procedure is not available for self managed superannuation funds and some public sector funds.

The common circumstances where a complaint arises are where a trustee is vested with discretion and there is no valid up to date binding death benefit nomination in place.

TIP: Binding death benefit nominations in a retail industry fund must be renewed every three years.

The most common complaint comes from the adult children of the deceased member where the trustee exercises its discretion to pay to the (typically) second spouse, whether married or de facto.

The SCT's task is to determine whether, having regard to the governing rules and policy terms, the trustee's decision is unfair or unreasonable (i.e. the issue is not what decision the Tribunal would itself have made on the evidence before it).

The usual considerations in a disputed estate do not apply. Rather, the question is whether the purpose of superannuation has been achieved namely, to provide for the ongoing support of the surviving spouse (unless there are minor children or other qualifying dependants).

Usually the adult children receive none of the death benefits or very

little in these circumstances. This can be contrary to the intention of the deceased expressed in his or her death benefit nomination or Will. We were involved in a case where the deceased and her de facto spouse entered into a binding financial agreement in relation to superannuation. This was given little weight in the exercise of discretion by the trustee.

This highlights the need for proper estate planning in particular, as increasingly, clients are migrating wealth into the superannuation environment. We can also assist in advising on making or resisting a complaint to the SCT.

Contact Craig McKie or Alan Krawitz.

SMSF's – The ATO is watching

The ATO is increasingly paying more attention to whether SMSF's are following the rules that allow funds to remain complying funds for tax purposes. If found not to be, there can be dire consequences as the ATO can make the SMSF non-complying and tax almost half of its assets, disqualify a trustee or prosecute through the courts.

Advisers and trustees need to ensure that SMSF's continue to stay within the rules, particularly in times of hardship when circumstances may be affecting asset levels and cash flow.

In the current economic climate, attention must be paid to ensure that a SMSF does not breach the **5% maximum in-house asset rule**. Changing market values may substantially change a fund's year-end values. If an issue arises, advisers and trustees must put a plan in place to handle this.

Another area where care should be taken in the current circumstances is meeting **minimum pension payment requirements**. The government has halved the minimum drawdown requirements for the 2008-2009 year, however some SMSF's may still be experiencing difficulties if they have a situation where funds are frozen, or in any case, may prefer to pay a lesser amount because of a decline in asset values. Care must be taken so as not to breach the payment rules and to ensure any failure to meet the required payments is reported.

Loans by SMSF's or giving financial assistance to members (even if inadvertent) or borrowings made also often come into issue.

Further, care must be taken by members and employers not to make contributions in excess of the allowed annual limits. The current set of limits for 2009/2010 are:

Type	Annual cap per person	Tax if exceed cap (%)
Concessional	\$55,000 (for aged 50-74, transitional cap until 30/6/2012 is \$100,000)	31.5
Non-concessional	\$165,000 (for under 65 may "bring forward" cap for the next 2 years e.g. \$495,000 over 3 years)	46.5

Other priority areas for the ATO include:

- 1) **new SMSF's** – auditors are required to report all contraventions within a SMSF's first year of operation and the ATO says

it will follow up on all of these;

- 2) **assets not being in the name of the SMSF;**
- 3) **early withdrawal of funds;** and
- 4) **sources of contributions to SMSF** – the ATO is looking at the income sources of SMSF's and whether they are linked to unreported or concealed income in terms of income tax returns. It has highlighted the example of real property, which has been contributed to an SMSF without capital gains tax being paid on the transfer.

We can provide advice and strategies to assist. We specialise in advising on the superannuation and tax legislation and rules, assisting with investment structuring within the rules and preparing documentation for loans or asset transfers taking into account any State transfer duty issues. We are also able to assist with resolving and rectifying issues that may precede or follow an ATO audit.

Please contact Daniel Fry or Chris Smailes.

Norton & Smailes

We advise on:

- income tax, GST, capital gains tax, FBT
- superannuation and superannuation deeds
- stamp duties, payroll tax and other State taxes
- wills, estate planning and business succession planning
- trusts and trust deeds
- objections and appeals
- tax and commercial litigation
- commercial law

Standard Documents (24 hour turnaround)

The following is a summary of our charges (excluding GST and disbursements) for the provision of final documents in duplicate and attending to stamping:

Deeds

• **Trust Deeds**

Discretionary Trust Deeds are \$240, and Unit Trust Deeds are \$295.

• **Superannuation Fund Deeds**

We provide Superannuation Fund Deeds for \$395. This includes supporting minutes, member information statements and all relevant documentation.

Other Documents

• **Enduring Power of Attorney**

An Enduring Power of Attorney is \$150, and a General Power of Attorney is \$220.

• **Wills**

We also provide Wills, including Testamentary Trusts where required. Estimates of fees can be provided on request.