Hall&Wilcox
Lawyers

december 2006

legal news for accountants

Phone +61 3 9603 3555 **Fax** +61 3 9670 9632 **Email** information@hallandwilcox.com.au

INSIDE

- Corporate Insolvency

  Key issues arising from recent insolvency law reforms are summarised.
- A significant change to the small business CGT concessions

  We have great news for people with companies and unit trusts held via discretionary trust; the CGT concessions may now be available on a share or unit sale.
- CGT relief for marriage breakdowns

  New laws have been passed extending the marriage breakdown CGT rollover
- A super idea: duty free in specie contributions

  We outline opportunities to get real property into super funds to capitalise on this $1 million transitional rule – all free of duty.
- Super made simple: some key aspects of the new system

  Draft legislation containing the proposed super changes has been released. We highlight some of the main issues.
- Document retention and destruction legislation

  We provide a summary of the new legislation and its implications for your business practices.
- Amendments to new CGT rules for non-residents

  Important changes to the taxation of non-residents are discussed in this article.
- Hiding from bankruptcy: super idea?

  When can a trustee in bankruptcy claw back super contributions?
- Changes to Division 7A: the Government's Christmas present to small business

  The Government has announced some very welcome changes to the private company loan provisions – including a discretion not to assess them as dividends.
- Calculation of Trust Law income: why everyone should be reading their clients' trust deeds

  Hall & Wilcox has a win in this important Full Federal Court decision on trust distributions.
- Superannuation Death Benefits

  We discuss an overlooked provision to effectively recover tax.

New Partner

We are delighted to announce the appointment of Michael Parker as a Partner in the Taxation section from 1 January 2007. Michael joined Hall & Wilcox 8 years ago from Ernst & Young.

His practice covers a broad range of income tax advice. His particular focus is structuring and transaction advice encompassing capital gains tax, consolidations, share buy backs and employee share plans.

Michael recently represented CPA Australia on the ATO consultative group for the CGT small business concession changes introduced into Parliament on 7 December 2006 - see his article in this edition.

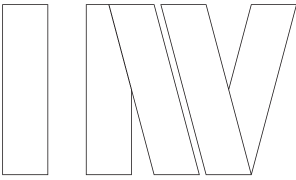
As many of you know Michael is a frequent presenter on the tax seminar circuit.

He is a Taxation Institute of Australia Victorian State Councillor and a member of its education committee.

He is also a Melbourne Football Club tragic (yet to witness a premiership!).

PRIVACY STATEMENT: Please tell us if you do not wish to receive this publication in the future. You may contact us by calling our Privacy Officer on +613 9603 3555 or emailing information@hallandwilcox.com.au.

IMPORTANT: This is not advice. Readers should not act solely on the basis of the material contained in this newsletter. Items herein are general comments only and do not constitute or convey advice per se. Changes in legislation may occur quickly. We recommend that our formal advice be sought before acting in any of the areas covered in this newsletter. © Copyright 2006.



Corporate insolvency reforms

Gerard Magner, Partner and Chris Fenwick, Senior Associate

For the first time since the Harmer Review in 1988, Australia's insolvency laws are the subject of comprehensive law reform.

On 13 November 2006, the Parliamentary Secretary to the Treasurer released the exposure draft of the *Corporations Amendment (Insolvency) Bill 2007* for public comment. New law is expected to be passed next year.

The changes are not dramatic, but will have some impact on most insolvency administrations.

Below is a snapshot of the four key areas of reform:

Improving outcomes for creditors

Creditors will be better protected and informed during the winding up process.

Employee entitlements will be strengthened by:

- requiring that a deed of company arrangement ("DOCA") adheres to the priority requirements of the *Corporations Act 2001* ("the Act");
- improving the standing of employee creditors in voluntary administrations by mandating their priority debt ranking; and
- extending priority treatment to superannuation entitlements.

Creditors will be better informed by:

- requiring administrators to provide a statement of independence to creditors at the time of giving notice of the first creditors' meeting which lists any potential conflicts of interest;
- allowing creditors to appoint a different person as liquidator when a company proceeds into liquidation; and
- providing for closer judicial scrutiny of administrators' fees.

External administration processes will be streamlined by:

- removing the requirement to publish notices in a national newspaper, except where there is a strong policy rationale for such publication;
- allowing notices to be sent by email, facsimile or other electronic means provided the recipient of the notice has nominated a particular mode of communication and has provided relevant contact details; and
- providing consistency by giving both liquidators and administrators the ability to consent to the transfer of shares if they are satisfied that such a transfer is in the best interests of creditors.

A statutory "pooling" mechanism will be introduced to legislate the procedures and preconditions that must be satisfied before an external administrator can unify a corporate group by combining their assets and liabilities.

During a voluntary administration, a pooling decision can only be made by the administrator with the unanimous consent of the creditors. Such a decision will have the effect of:

- making each company jointly and severally liable for the debts of all other companies in the pooled group; and
- extinguishing any debts between companies in the group.

Deterring corporate misconduct

Corporate misconduct will be further deterred and punished by measures including:

- clarifying and strengthening ASIC's powers to investigate liquidators' conduct generally;
- giving ASIC power to apply for a court order to prevent a company officer from avoiding liability, for example, by sending funds out of the jurisdiction; and
- imposing a time limit of six months for the lodgement of reports by liquidators about the possible commission of offences by officers of corporations.

Improving regulation of insolvency practitioners

Insolvency practitioners are already heavily regulated. The reforms aim to improve the existing law by:

- clarifying the experience and education requirements for registration of liquidators;
- requiring registered liquidators to hold professional indemnity insurance; and
- clarifying ASIC's involvement in the regulation of insolvency practitioners.

Fine-tuning voluntary administration

The draft legislation proposes to address some technical issues that have arisen in relation to the current voluntary administration procedures, including:

- narrowing the circumstances in which creditors will be entitled to terminate a DOCA;
- slightly extending the time for the holding of creditors' meetings;
- clarifying aspects of the operation of a liquidation following an administration, for example, affording priority in liquidation for borrowings during a prior administration.

Views and comments to the exposure draft must be given by 23 February 2007. It is unlikely that any of the above reforms will prove controversial.

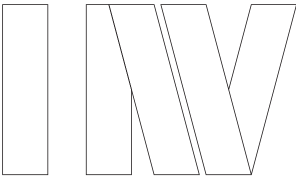
FURTHER ENQUIRIES

Gerard Magner +61 3 9603 3549
Partner
gerard.magner@hallandwilcox.com.au

Chris Fenwick +61 3 9603 3562
Senior Associate
chris.fenwick@hallandwilcox.com.au

PRIVACY STATEMENT: Please tell us if you do not wish to receive this publication in the future. You may contact us by calling our Privacy Officer on +613 9603 3555 or emailing information@hallandwilcox.com.au.

IMPORTANT: This is not advice. Readers should not act solely on the basis of the material contained in this newsletter. Items herein are general comments only and do not constitute or convey advice per se. Changes in legislation may occur quickly. We recommend that our formal advice be sought before acting in any of the areas covered in this newsletter. © Copyright 2006.



Superannuation Death Benefits

Andrew O'Bryan, Partner and Rebecca James, Lawyer

Section 279D is invariably overlooked for its potential benefit. When a fund is paying out a tax free death benefit, section 279D provides a mechanism for the trustee to effectively recoup the 15% tax on the contributions which have funded the death benefit. If the trustee pays the "gross" amount, it is entitled to a tax deduction for the extra it pays out. The fund must claim the tax deduction in the year of payment and have sufficient taxable income against which to apply the deduction. The problem is often working out the amount of the deduction.

The Australian Taxation Office ("ATO") recently released Interpretative Decision 2006/290 (ID 2006/290) approving an alternate formula for calculating the notional payment reduction resulting from contributions tax on member accounts where the actual amount is unable to be calculated by a fund.

The alternate formula in ID 2006/290 is:

(0.15P) / (R – 0.15P) x C

Where:

P = number of days in component R that occur after 30 June 1988;

R = total number of days in the eligible service period that occur after 30 June 1983; and

C = amount of post-June 1983 component of the 'actual payment' after excluding any insured amount for which deductions have been claimed.

Example 1

Adrian joined a regulated superannuation fund, Cabsav Superannuation Fund in 1976. The fund is an accumulation fund where member benefits are comprised of contributions and investment earnings over the membership period. Furthermore, an election has not been made to have a taxed ETP component treated as an untaxed component (section 27AB(4) 1936 Act). Adrian died on 30 June 2006 with unamended death benefits totalling $600,000. Assuming the post-June 1983 component of the actual payment is $500,000, the notional payment reduction is calculated as follows:

(0.15 x 6570) / (8395 – 0.15 x 6570) x $500,000 = $66,502.46

The death benefit payable to Adrian's dependants could be increased to $666,502.46. The fund would receive a corresponding deduction of $66,502.46 in respect of the anti-detriment payment on the assessable income of the fund.

Under section 279D(2) of the 1936 Act the formula is:

Notional payment reduction due to contributions tax /
complying superannuation tax rate

Example 2

Using the example above and assuming that the notional payment reduction due to contributions tax is $90,000 the standard formula is calculated as follows:

$90,000 / 0.15 = $600,000.00

Using the standard formula, Adrian's dependants receive $600,000 in death benefits. Applying the standard formula does not increase the death benefits payable. The member's dependants receive $66,502.46 more if the alternate formula suggested in Interpretive Decision 2006/ 290 is applied. Furthermore, for the fund to receive the full benefit of the corresponding deduction of $90,000, the fund must have at least $600,000 of taxable income to apply the tax deduction against.

The standard formula assumes a defined death benefit that fails to consider variables, such as insurance, that may alter the final death benefit payable. The ATO approved the alternate formula because it is consistent with the intention of the 1936 Act and provides a method for increasing the death benefits payable to a deceased member's dependants or estate.

Funds unable to calculate the notional payment reduction resulting from contributions tax should consider applying an alternate formula that results in an increased lump sum death benefit to the deceased member's dependants or estate, in accordance with the spirit of the legislation. Dependants should request a fund make an anti-detriment payment, while funds should consider maintaining a reserve account (if they do not already do so) to offer this service as an additional benefit to members.

FURTHER ENQUIRIES

Andrew O'Bryan +61 3 9603 3514
Partner
andrew.obryan@hallandwilcox.com.au

Rebecca James +61 3 9603 3483
Lawyer
rebecca.james@hallandwilcox.com.au

PRIVACY STATEMENT: Please tell us if you do not wish to receive this publication in the future. You may contact us by calling our Privacy Officer on +613 9603 3555 or emailing information@hallandwilcox.com.au.

IMPORTANT: This is not advice. Readers should not act solely on the basis of the material contained in this newsletter. Items herein are general comments only and do not constitute or convey advice per se. Changes in legislation may occur quickly. We recommend that our formal advice be sought before acting in any of the areas covered in this newsletter. © Copyright 2006.

documents - eForms

to complete and send your instructions online, simply click on the 'eForms' link on our website homepage

Discretionary trust	$440
Unit Trust	$550
Unit partnership	$2,200 - $3,300
Superannuation fund	$495
Pty Limited company	$862 (agents fee included)
Public company limited by shares	$2,200 (agents fee included)
Public company limited by guarantee	$2,200 - $3,300 (agents fee included)
New company constitution	$440
Division 7A Loan Agreements	$440
Debit/Credit Loan Agreement	$660
Deed of Acknowledgment of Debt	$150
Tax Sharing Agreement	$4,400 single, POA for multiple

All prices are GST inclusive but exclude stamp duty.

recovery services

Hall & Wilcox's Debt Recovery practice offers you a dedicated team of lawyers who will excel at the recovery of business debts for you and your clients.

Our legal team **will**:

- pursue each recovery to its full potential
- provide you with regular, comprehensive reporting
- provide prompt turnaround
- provide value for money
- be your trusted service providers
- give you the 'peace of mind' that comes from knowing that an experienced legal team is acting on your behalf

Our legal team **will not**:

- charge commissions
- charge loading on service provider fees
- carry out illegal search procedures

We are not a collection agency. We do not do factoring. We do not keep a share of recoveries.

We are lawyers with experience in recovery litigation and enforcement and who understand:

- how to conduct litigation in all jurisdictions
- the applicable laws
- enforcement procedures

For more information, or to discuss your recovery needs, contact:

Matt McDonald, Partner **+61 3 9603 3564**
matthew.mcdonald@hallandwilcox.com.au

Chris Fenwick, Senior Associate **+61 3 9603 3562**
chris.fenwick@hallandwilcox.com.au

www.hallandwilcox.com.au

CONTACTS

Keith James +61 3 9603 3512
Taxation, Family Business & Wealth Management
keith.james@hallandwilcox.com.au

Andrew O'Bryan +61 3 9603 3514
Taxation, Family Business & Wealth Management, Superannuation
andrew.obryan@hallandwilcox.com.au

Garry Sebo +61 3 9603 3535
Taxation
garry.sebo@hallandwilcox.com.au

Michael Parker +61 3 9603 3540
Taxation
michael.parker@hallandwilcox.com.au

Jerome Tse +61 3 9603 3573
Taxation
jerome.tse@hallandwilcox.com.au

Andrea Watson +61 3 9603 3541
Family Business & Wealth Management, Corporate & Commercial
andrea.watson@hallandwilcox.com.au

Wendy Sylva +61 3 9603 3532
Family Business & Wealth Management
wendy.sylva@hallandwilcox.com.au

Emma Woolley +61 3 9603 3551
Family Business & Wealth Management
emma.woolley@hallandwilcox.com.au

Harry New +61 3 9603 3559
Financial Services
harry.new@hallandwilcox.com.au

Adrian Verdnik +61 3 9603 3579
Financial Services, Superannuation
adrian.verdnik@hallandwilcox.com.au

Mark Dunphy +61 3 9603 3591
Employment & Workplace Relations
mark.dunphy@hallandwilcox.com.au

Karl Rozenbergs +61 3 9603 3583
Employment & Workplace Relations
karl.rozenbergs@hallandwilcox.com.au

Tony Macvean +61 3 9603 3582
Corporate & Commercial, Financial Services
tony.macvean@hallandwilcox.com.au

Deborah Chew +61 3 9603 3550
Corporate & Commercial
deborah.chew@hallandwilcox.com.au

Peter Jenkin +61 3 9603 3554
Property & Construction, Corporate & Commercial
peter.jenkin@hallandwilcox.com.au

Bruce McFarlane +61 3 9603 3567
Corporate & Commercial, Property & Construction
bruce.mcfarlane@hallandwilcox.com.au

Noel Batrouney +61 3 9603 3506
Banking & Finance, Commercial Litigation, Intellectual Property & IT practice groups
noel.batrouney@hallandwilcox.com.au

Gerard Magner +61 3 9603 3549
Commercial Litigation
gerard.magner@hallandwilcox.com.au

Hall&Wilcox
Lawyers

Level 30, Bourke Place
600 Bourke Street, Melbourne
Victoria 3000 Australia

Phone +61 3 9603 3555
Facsimile +61 3 9670 9632
www.hallandwilcox.com.au

PRIVACY STATEMENT: Please tell us if you do not wish to receive this publication in the future. You may contact us by calling our Privacy Officer on +613 9603 3555 or emailing information@hallandwilcox.com.au.

IMPORTANT: This is not advice. Readers should not act solely on the basis of the material contained in this newsletter. Items herein are general comments only and do not constitute or convey advice per se. Changes in legislation may occur quickly. We recommend that our formal advice be sought before acting in any of the areas covered in this newsletter. © Copyright 2006.

A significant change to the **small business CGT concessions**

Michael Parker, Special Counsel

In our October 2006 edition we outlined the proposed changes to the Small Business CGT concessions announced in the May 2006 Federal Budget. Following an extensive consultation process between Treasury and the professional bodies, legislation was introduced into Parliament on 7 December 2006. The consultation process has resulted in a further change to the concessions which should be welcomed by many advisors and their clients.

As announced in the Budget, Treasury has decided to replace the existing "controlling individual" test with a new "significant individual" test.

The old Controlling Individual test

The controlling individual test was applicable for CGT events occurring up until 30 June 2006. It was relevant in three main situations:

- where a company or trust was trying to access the 15 year exemption;
- where a company or trust wished to utilise the $500,000 retirement exemption; and
- importantly, where the relevant asset being sold was shares in a company or interests in a trust.

To satisfy the controlling individual test for a company, it was necessary to show that an individual had direct ownership of shares carrying at least 50% of rights to income, return of capital and voting power. Similarly, for a fixed trust, an individual had to own units or other fixed interests giving the right to at least 50% of income and capital distributions. Finally, in the case of a discretionary trust, an individual had to receive at least 50% of any income or capital distributions made by the trust in the year/s the test needed to be met.

As a result, it was only ever possible for a company or trust to have a maximum of two controlling individuals; limiting the ability to utilise the concessions.

Importantly, where shares or units were held via other entities such as family trusts, the controlling individual test could not be met.

The new Significant Individual test

The new significant individual test is applicable in the same three situations. However, it only requires that a company or trust has an individual with at least a 20% interest in dividends, capital and voting (for a company) or distributions of income and capital (for a trust). This 20% interest can be held directly or indirectly through tiers of entities.

So, for instance, in a case where a company is held equally by two family trusts, it will be possible for the company to access the 15 year exemption and the retirement exemption where the company or unit trust sells an active asset. The company needs to show that the family trusts have made distributions in such a manner that an individual has an indirect 20% interest in the company.

Assuming the first family trust distributes 50% of its income and capital to each of mum and dad, mum and dad will each have a 25% indirect interest in the company (50% × 50%). Mum and dad will be significant individuals of the company as they each have at least a 20% indirect interest.

Assume the second family trust distributes income and capital of 30% to brother, 50% to sister and 20% to sister's husband. In this case, brother only has a 15% indirect interest and is not a significant individual. Sister has a 25% interest and is a significant individual. Sister's husband has a 10% interest. While this is less than 20%, sister's husband can still qualify for the concessions as he is a CGT concession stakeholder; being the spouse of a significant individual.

In this example, the company could utilise the $500,000 retirement exemption for mum, dad, sister and sister's husband. Better yet, if the company has held the relevant asset for at least 15 years and has had a significant individual for at least 15 of its years of ownership (even if only one significant individual and even if not the same person in each year), then it should be able to utilise the 15 year exemption for each of mum, dad, sister and sister's husband as they are CGT concession stakeholders in the year of the gain.

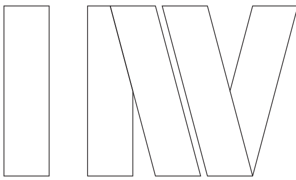
This ability to trace indirect interests can run through further layers of entities.

How does it apply to a sale of shares or units?

Following the Budget announcements there was some uncertainty about how the significant individual test would apply in the case of a sale of shares or units. Treasury's initial view was that it would be necessary

PRIVACY STATEMENT: Please tell us if you do not wish to receive this publication in the future. You may contact us by calling our Privacy Officer on +613 9603 3555 or emailing information@hallandwilcox.com.au.

IMPORTANT: This is not advice. Readers should not act solely on the basis of the material contained in this newsletter. Items herein are general comments only and do not constitute or convey advice per se. Changes in legislation may occur quickly. We recommend that our formal advice be sought before acting in any of the areas covered in this newsletter. © Copyright 2006.



A significant change to the **small business CGT concessions**

continued

for the significant individual to hold their shares or units directly rather than indirectly through other entities.

As a result of the consultation process, Treasury has drafted the amendments in a manner that allows the concessions on a sale of shares or units where there are indirect significant individuals. However, this is limited to cases where the indirect significant individuals (and spouses) have at least a 90% interest in the taxpayer entity (i.e. the entity selling the shares or units).

Continuing the example but assuming the family trusts are selling their shares in the company, in the case of the first family trust, it can be eligible for the small business concessions on the sale of its shares. This is because significant individuals combined (mum and dad) have a greater than 90% interest in the first family trust (they have a 100% interest).

However, the second family trust cannot access any of the small business concessions on a sale of shares as significant individuals and CGT concession stakeholders (sister and her husband) only have a 70% interest in the second family trust which is less than the required 90% interest.

From this example it can be seen that there will be tensions between different owners. Mum and dad would likely prefer a share sale in the example. Whereas, sister and her husband are likely to prefer an asset sale. In some cases, the parties may be amenable to choosing the sale structure that results in the lowest incidence of tax on the shareholders collectively.

The new amendments are contained in Tax Laws Amendment (2006 Measures No. 7) Bill 2006. If passed, the amendments are to take effect for CGT events arising on or after 1 July 2006.

FURTHER ENQUIRIES

Michael Parker +61 3 9603 3540
Special Counsel
michael.parker@hallandwilcox.com.au

CGT relief for marriage breakdowns

Wendy Sylva, Special Counsel and Paul Zanelli, Lawyer

We have previously reported on extensions to the marriage breakdown CGT rollover in the October 2006 edition of Legal News for Accountants.

The CGT rollover is to be extended to cover transfers of assets because of:

- binding financial arrangements;
- awards made in an arbitration under the *Family Law Act 1975*; or
- any other written agreement that is binding because of a State or Territory law relating to de facto marriage breakdowns that cannot be overridden by a court.

Legislation containing the amendments has now been passed and received Royal Assent on 12 December. The amendments apply to CGT events occurring on or after 13 December 2006.

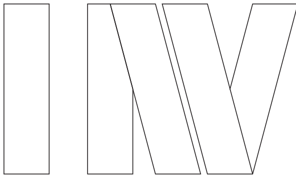
FURTHER ENQUIRIES

Wendy Sylva +61 3 9603 3532
Special Counsel
wendy.sylva@hallandwilcox.com.au

Paul Zanelli +61 3 9603 3503
Lawyer
paul.zanelli@hallandwilcox.com.au

PRIVACY STATEMENT: Please tell us if you do not wish to receive this publication in the future. You may contact us by calling our Privacy Officer on +613 9603 3555 or emailing information@hallandwilcox.com.au.

IMPORTANT: This is not advice. Readers should not act solely on the basis of the material contained in this newsletter. Items herein are general comments only and do not constitute or convey advice per se. Changes in legislation may occur quickly. We recommend that our formal advice be sought before acting in any of the areas covered in this newsletter. © Copyright 2006.



A Super Idea: Duty Free In Specie Contributions

Andrew O'Bryan, Partner and Rachel Bates, Lawyer

There has been a surge of activity by people making undeducted contributions to superannuation to take advantage of the $1 million transitional rule before 30 June 2007.

Significant benefits can be achieved by making an in specie contribution of business real property to a self-managed superannuation fund ("SMSF"). The process should be carefully managed to utilise the stamp duty concessions and avoid unnecessary costs.

Business real property

If permitted by the SMSF's trust deed, members can make an undeducted contribution of business real property to their SMSF.

A complying superannuation fund is generally prohibited from acquiring an asset from a member: section 66 of the *Superannuation Industry (Supervision) Act* 1993. However, a fund can acquire an asset that is "business real property" and is acquired for market value. In general terms, "business real property" is one that is used wholly and exclusively in a business by someone.

The property cannot be subject to a mortgage, so any mortgage must be discharged before the transfer.

Property held in a trust

Property that is held in a family trust will need to be distributed to the individual before it can be contributed to their SMSF. It cannot go directly from the trust to the SMSF without incurring stamp duty (in any event, such a contribution would be a taxable contribution).

An issue often overlooked is the fact that the trust must have sufficient profits or capital to make the distribution from the trust without being in breach of the trust by causing a deficiency in the trust fund. In many cases, the trust's net assets are minimal. So, before you launch into acting, work out the accounting entries! The distribution of the property must be in accordance with the requirements and procedures set out in the trust deed.

A stamp duty exemption is available for transfers of dutiable property from trusts to beneficiaries for no consideration (section 36A of the *Duties Act* 2000 (Vic) for discretionary trusts).

The exemption can only apply where there is no consideration provided by the beneficiary and the transfer is not part of a sale. Where the beneficiary gives a mortgage to secure at least the same amount as that outstanding under a mortgage over the property prior to the transfer, or assumes the liabilities under an existing mortgage over the property, the beneficiary will not necessarily be precluded from applying the stamp duty exemption. However, the beneficiary must discharge the mortgage before contributing the property to the SMSF.

Where the same entity is the trustee of both the trust and the SMSF, the transfer from the trust to the individual, and then to the fund, must still be stamped non-dutiable and processed on title. The transfers cannot simply be implemented by journal entries.

It is vitally important to demonstrate the chain of title so that an auditor of the SMSF or an Australian Taxation Office auditor can see that the SMSF has proper title. This requires proof that stamp duty was paid on the transfer of the property to the SMSF or the transfer was stamped non-dutiable on the basis that it was exempt.

Stamp duty

An exemption from stamp duty is available under section 41 of the *Duties Act* where dutiable property is transferred by someone into their fund. The State Revenue Office requires a number of documents to be lodged, including statutory declarations by both the trustee and the member confirming that the fund is (or within 12 months will be) a complying superannuation fund; the member is a beneficiary of the fund; and no consideration has passed between the parties.

The transfer must be an in specie contribution, rather than a sale. If any form of consideration is provided by the trustee for the transfer, the stamp duty exemption will not be available.

The contribution should reflect the members' ownership of the property. For example, if two members own a property as joint tenants or tenants in common in equal shares, each member will be making an undeducted contribution of half of the value of the property.

The trustee should obtain at least two opinions of valuation of the property. Opinions of valuation generally provide a range, which can be used to determine the amount of the contribution. The market value of the property must be reflected in the fund's accounts. A member will be recorded as having made a contribution of their proportion of the market value of the property.

Capital Gains Tax ("CGT")

The distribution and/or contribution may trigger a CGT liability. The CGT discount and small business concessions may be available to reduce the net capital gain. In the long-run, the concessional tax treatment achieved by holding the property in the SMSF may significantly outweigh the CGT liability the member incurs to get the property into their SMSF.

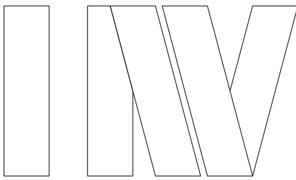
FURTHER ENQUIRIES

Andrew O'Bryan +61 3 9603 3514
Partner
andrew.obryan@hallandwilcox.com.au

Rachel Bates +61 3 9603 3563
Lawyer
rachel.bates@hallandwilcox.com.au

PRIVACY STATEMENT: Please tell us if you do not wish to receive this publication in the future. You may contact us by calling our Privacy Officer on +613 9603 3555 or emailing information@hallandwilcox.com.au.

IMPORTANT: This is not advice. Readers should not act solely on the basis of the material contained in this newsletter. Items herein are general comments only and do not constitute or convey advice per se. Changes in legislation may occur quickly. We recommend that our formal advice be sought before acting in any of the areas covered in this newsletter. © Copyright 2006.



Super made simple: some key aspects of the new system

Andrew O'Bryan, Partner, Adrian Verdnik, Senior Associate and Rebecca James, Lawyer

We reported on the proposed changes to superannuation in the October edition of Legal News for Accountants. The Government introduced the draft legislation *(Tax Laws Amendments (Simplified Superannuation) Bill 2006)* to Parliament on 7 December 2006. There have been a few changes but no changes to a few things we had hoped to see come out of the consultation process. The following issues are worth noting:

- The cap on concessional (deducted) contributions ($50,000) will be indexed annually in $5,000 increments, but the transitional cap of $100,000 for persons turning 50 or older between 1 July 2007 to 30 June 2012 will not be indexed. The non-concessional (undeducted) contributions cap will be 3 times the deducted cap (so $150,000 initially).
- Excess deducted contributions will be subject to an additional 31.5% tax (on top of the 15% contributions tax), and will count towards the taxpayer's undeducted cap. Excess undeducted contributions will be taxed at 46.5%. The taxpayer will be able to release money from a fund to pay the liability on excess deducted contributions, but must pay the tax on excess undeducted contributions returned from a fund.
- Contributions made between 10 May 2006 and 30 June 2007 in excess of the age-based limits will count as non-concessional contributions and come out of the undeducted contribution limit.
- The Commissioner will have a discretion to allow withdrawal of excess undeducted contributions made before 7 December 2006 without penalty, provided the application is made before 30 June 2007.
- Lump sum death benefits will be tax free when paid to a tax dependant, and will be taxed at either 15% (for the taxed element) or 30% (for the untaxed element) when paid to tax non-dependants e.g. adult children. Income streams paid to dependants will mostly be tax free when paid to a dependant over age 60 (the untaxed element will be taxed at marginal rates with a 10% offset), but will be taxed at marginal rates when paid to dependants under age 60 (with a 15% offset for the taxed element). However, income streams cannot be paid to non-dependants as income streams after 1 July 2007, so pensions and annuities being paid to dependant children will have to be commuted when the child reaches 25 (except in cases of permanent incapacity), although the income will be non-assessable and non-exempt. Income streams being paid to non-dependants that were commenced prior to 1 July 2007 will be taxed in the same manner as dependants.
- The self-employed will be entitled to a full deduction for contributions made where they are under 75 years and less than 10% of their assessable income and fringe benefits is derived as an employee. This is consistent with the test that currently applies for the government co-contribution.
- No TFN contributions (i.e. contributions made by a member where a TFN has not been quoted) will be taxed at 46.5% (subject to the exemption for pre-1 July 2007 members for contributions not exceeding $1,000 in a year), although the fund will be entitled to an offset for the current financial year and preceding 3 financial years after a TFN is quoted.
- To access the tax concessions associated with employment termination payments (first $140,000 taxed at 15% where the employee has reached preservation age), the termination payments will generally need to occur within 12 months of the termination. The Commissioner has the discretion to extend the time period beyond the initial 12 months. An employment termination payment made over two financial years will be aggregated and then applied against the $140,000 cap. Employment termination payments made in the same financial year by two separate employers will also be aggregated when determining whether the termination payment exceeds the $140,000 cap.

FURTHER ENQUIRIES

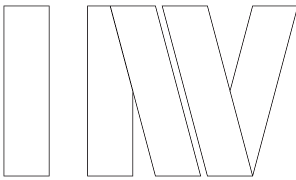
Andrew O'Bryan +61 3 9603 3514
Partner
andrew.obryan@hallandwilcox.com.au

Adrian **Verdnik** +61 3 9603 3579
Senior Associate
adrian.verdnik@hallandwilcox.com.au

Rebecca James +61 3 9603 3483
Lawyer
rebecca.james@hallandwilcox.com.au

PRIVACY STATEMENT: Please tell us if you do not wish to receive this publication in the future. You may contact us by calling our Privacy Officer on +613 9603 3555 or emailing information@hallandwilcox.com.au.

IMPORTANT: This is not advice. Readers should not act solely on the basis of the material contained in this newsletter. Items herein are general comments only and do not constitute or convey advice per se. Changes in legislation may occur quickly. We recommend that our formal advice be sought before acting in any of the areas covered in this newsletter. © Copyright 2006.



legal news for accountants
december 2006

Document **retention and destruction** legislation

Noel Batrouney, Managing Partner

Document retention has long been a complex issue. The new legislation recently passed concerning document retention and destruction will have widespread implications on companies regarding their obligations and the way in which they store and destroy all documents.

This update will assist in bringing you up to date with the changes to the Act and the implications on your business.

The Act

On 1 September 2006 the Crimes (Document Destruction) Act 2006 came into effect in Victoria. This Act is an amendment to the Crimes Act 1958 (Vic).

The genesis for the Act is the McCabe case in the Supreme Court of Victoria in which light was shed on the so called "document retention" policy of the defendant, British American Tobacco.

The offence

The Act makes it an offence for a person who knows that a document "or other thing of any kind" is or is reasonably likely to be required in evidence in a legal proceeding and, with the intention of preventing it being so used, either:

- destroys or conceals it or renders it illegible, undecipherable or incapable of identification; or
- expressly, tacitly or impliedly authorizes or permits another person to do so (and that person in fact does so).

Definition of "legal proceeding"

A "legal proceeding" has the *Evidence Act* (Vic) meaning which "includes any civil criminal or mixed proceeding and any enquiry in which evidence is or may be given before any court or person acting judicially".

The Act applies with respect to a legal proceeding "that is in progress or is to be, or may be, commenced in the future". This may include more than proceedings that are simply anticipated.

Corporate liability

Liability also attaches to bodies corporate for a breach of the Act by an associate, being an employee, agent or officer of the body corporate acting within the actual or apparent scope of their employment or authority.

Knowledge and intention

For the purpose of ascribing acts of associates to a body corporate:

- Knowledge of the nature of a document by an associate of a body corporate must be attributed to that body corporate.
- Intention to destroy a document by:
  - a board of directors or
  - an officer of a body corporate must be attributed to that body corporate.
- Intention of an agent or ordinary employee of a body corporate will be attributed to the body corporate if there is a corporate culture that directed, encouraged, tolerated or led to the formation of that intention by the agent or ordinary employee.
- A contravention of the Act by an officer of a body corporate will be taken to also be a contravention by the body corporate itself unless the body corporate proves that it exercised due diligence to prevent the contravention by the officer.

Penalties

The penalties are significant: up to 5 years imprisonment or a fine of up to 600 penalty units (currently $64,458) or both for an individual and a fine of up to 3,000 penalty units (currently $322,290) for a body corporate.

Document unavailability legislation

The Act

A counterpart to the *Crimes (Document Destruction) Act 2006* is the *Evidence (Document Unavailability) Act 2006*. This Act amends the Evidence Act (Vic) and provides that if, in a civil proceeding, it appears to the court that a document (or a reproduction) is unavailable and the unavailability is likely to cause unfairness to a party, the court may make a ruling:

- that an adverse inference will be drawn from the unavailability of the document;
- that a fact in issue between the parties be presumed to be true in the absence of evidence to the contrary;
- that certain evidence not be adduced;
- that all or part of a defence or statement of claim be struck out;
- that the evidential burden of proof be reversed in relation to a fact or issue.

This list is not exhaustive.

Before making such an order, the Court must, amongst other things, have regard to the circumstances in which the document became unavailable.

Recommendation

We do not believe there is any counterpart in other States for the amendment to the *Evidence Act*, but there are crimes in other States in relation to the destruction of evidence.

For the purpose of assisting your business to satisfy a Court:

PRIVACY STATEMENT: Please tell us if you do not wish to receive this publication in the future. You may contact us by calling our Privacy Officer on +613 9603 3555 or emailing information@hallandwilcox.com.au.

IMPORTANT: This is not advice. Readers should not act solely on the basis of the material contained in this newsletter. Items herein are general comments only and do not constitute or convey advice per se. Changes in legislation may occur quickly. We recommend that our formal advice be sought before acting in any of the areas covered in this newsletter. © Copyright 2006.

Document **retention and destruction** legislation

continued

- in relation to agents or employees, that there is no corporate culture leading to the proscribed conduct by associates; and
- in relation to "officers", that your business has exercised due diligence to prevent that contravention by officers; and
- that no adverse inferences should be drawn in relation to evidentiary matters in civil litigation in which your business is involved,

it might be useful to undertake some education about the Acts and to implement a policy in relation to document destruction/ retention.

If documents in a civil proceeding are unavailable (and it is probably rare for there not be some missing documents) there is every reason to think that any policy for document retention (and any absence of such a policy) will be subjected to examination.

FURTHER ENQUIRIES:

Noel Batrouney +61 3 9603 3506
Managing Partner
noel.batrouney@hallandwilcox.com.au

Amendments to new **CGT rules** for non-residents

Keith James, Partner and Rachel Bates, Lawyer

In our October edition of *Legal News For Accountants*, we reported on proposed changes to the capital gains tax provisions as they relate to non-residents. The *Tax Laws Amendment (2006) Measures No. 4) Bill* 2006 ("TLAB 4"), which was originally introduced in the House of Representatives on 22 June 2006, was recently passed by the Senate and is awaiting Royal Assent. The amendments come into effect on the day TLAB 4 receives Royal Assent, which we expect to be before the end of 2006.

TLAB 4 will amend the CGT provisions to limit the types of CGT assets that can give rise to a CGT liability for non-residents. Under the old regime, foreign residents only made a capital gain or loss if a CGT event occurred in relation to an asset that had the "necessary connection with Australia". Once TLAB 4 receives Royal Assent, capital gains and capital losses made by foreign residents will be disregarded for Australian tax purposes unless the CGT event happens to "taxable Australian property", which will include:

- taxable Australian real property – real property situated in Australia and mining, quarrying or prospecting rights if the minerals, prospecting or quarrying materials are situated in Australia;
- an indirect Australian real property interest;
- business assets of an Australian permanent establishment;
- an option or right in the above items; and
- an asset that is taken to be taxable Australian property when a taxpayer ceases to be an Australian resident and chooses to disregard a capital gain or loss that would otherwise result from CGT event I1 happening.

A foreign resident will have an "indirect Australian real property interest" if they have a membership interest in an entity and that interest passes two tests known as the "non-portfolio interest test" and the "principal asset test". If the underlying assets of the entity change, the membership interest can start being or cease to be an indirect Australian real property interest. So membership interests can move into and out of the class of assets that are indirect Australian real property interests.

If a foreign resident held a membership interest in a non-resident company or trust on 10 May 2005 (when these changes were announced), the foreign resident will adopt the market value of the interest as at 10 May 2005 as its cost base. Prior to amendments in the Senate, this market value substitution rule was limited to membership interests that were indirect Australian real property interests on 10 May 2005. Following consideration by a Senate Committee, the government made minor amendments to extend the rule to apply to all membership interests in non-resident companies and trusts. This amendment will be relevant for a membership interest that becomes an indirect Australian real property interest after 10 May 2005 because the market value cost base rule will now apply.

FURTHER ENQUIRIES

Keith James +61 3 9603 3512
Partner
keith.james@hallandwilcox.com.au

Rachel Bates +61 3 9603 3563
Lawyer
rachel.bates@hallandwilcox.com.au

PRIVACY STATEMENT: Please tell us if you do not wish to receive this publication in the future. You may contact us by calling our Privacy Officer on +613 9603 3555 or emailing information@hallandwilcox.com.au.

IMPORTANT: This is not advice. Readers should not act solely on the basis of the material contained in this newsletter. Items herein are general comments only and do not constitute or convey advice per se. Changes in legislation may occur quickly. We recommend that our formal advice be sought before acting in any of the areas covered in this newsletter. © Copyright 2006.

Hiding from **bankruptcy**: super idea?

Andrew O'Bryan, Partner and Adrian Verdnik, Senior Associate

The *Bankruptcy Legislation Amendment (Superannuation Contributions) Bill 2006* was introduced into Parliament on 6 December 2006 to amend the *Bankruptcy Act 1966* to allow a trustees in bankruptcy to recover superannuation contributions made by or on behalf of a bankrupt.

The Government decided not to proceed with earlier proposals which would have allowed for the recovery of "excessive" superannuation contributions made prior to bankruptcy - a problem highlighted in the High Court decision in *Cook v Benson* in June 2003. Instead the Government has focussed on contributions made with "the intention to defeat creditors". The amendments - once passed - will apply retrospectively from 28 July 2006.

The onus under the amended legislation will be on the bankrupt to prove that a contribution that led to insolvency was not made with the intention of defeating creditors. The court will be required to consider whether the payments were out of character with the bankrupt's historical contributions pattern.

However, at a time when the Government is reforming superannuation to encourage people to make greater personal contributions to superannuation - including the transitional measure allowing personal contributions of up to $1M until 30 June 2007, and the ability to make personal contributions of up to $450,000 in respect of a three year period thereafter - it is likely that many people will be making substantial "one-off" contributions to superannuation which are not in character with their contributions history.

The Government may have inadvertently given bankrupts a good argument for making the contributions which will make the job of trustees in bankruptcy more difficult.

FURTHER ENQUIRIES

Andrew O'Bryan +61 3 9603 3514
Partner
andrew.obryan@hallandwilcox.com.au

Adrian Verdnik +61 3 9603 3579
Senior Associate
adrian.verdnik@hallandwilcox.com.au

Changes to Division 7A: the Government's Christmas present to small business

Michael Parker, Special Counsel and Jerome Tse, Senior Associate

On 6 December 2006, the Government announced that it will reduce compliance costs in dealing with Division 7A in the following ways:

- Dividends under Division 7A will no longer be subject to the "double penalty" of being subject to a debit to the private company's franking account whilst being taxable in the shareholder or associate's hands without access to franking credits.
- The Commissioner of Taxation ("the Commissioner") will now have a discretion in deciding whether to assess shareholders or associates of companies that have technically breached Division 7A.
- Section 108, the precursor to Division 7A, will be repealed as the Government considers section 108 to be redundant.

While much has been made about the removal of the "double penalty", in our view it is likely to be a hollow victory in many instances. In a large number of cases, a deemed dividend arises under Division 7A because a private company has made a non-complying loan to its shareholders or their associates. This is assessed as an unfrankable dividend in the year the loan was made.

Later, if the company declares a real dividend in favour of the borrower and offsets it against the loan, that later dividend will be treated as non-assessable non-exempt income, but will still have franking credits attached to it under section 109ZC. A shareholder on the tax rate of 46.5% won't pay top-up tax on the future dividend because it's non-assessable and non-exempt income. So, the franking credits are wasted on them. A shareholder at < 30% may get a refund of franking credits.

In other cases, the only way for the company to utilise the franking credits will be if it has non-taxable accounting profits; for example, the 50% active asset component of a capital gain.

Further amendments will be announced in the new year to reduce compliance costs dealing with Division 7A and the fringe benefits tax regime.

The Government has proposed that the Commissioner's new discretion will apply retrospectively from 1 July 2002 and that the FBT amendments to be announced will apply from 1 April 2007. All other changes will apply from 1 July 2006.

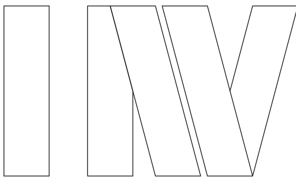
FURTHER ENQUIRIES

Michael Parker +61 3 9603 3540
Special Counsel
michael.parker@hallandwilcox.com.au

Jerome Tse +61 3 9603 3573
Senior Associate
jerome.tse@hallandwilcox.com.au

PRIVACY STATEMENT: Please tell us if you do not wish to receive this publication in the future. You may contact us by calling our Privacy Officer on +613 9603 3555 or emailing information@hallandwilcox.com.au.

IMPORTANT: This is not advice. Readers should not act solely on the basis of the material contained in this newsletter. Items herein are general comments only and do not constitute or convey advice per se. Changes in legislation may occur quickly. We recommend that our formal advice be sought before acting in any of the areas covered in this newsletter. © Copyright 2006.



Calculation of trust law income: why everyone should be reading their client's trust deeds

Keith James, Partner and Jerome Tse, Senior Associate

In the landmark Full Federal Court decision of *Cajkusic & Anors v Commissioner of Taxation* ("Cajkusic"), the Court held that the definition of trust law income must be calculated with reference to the powers of the trustee in the trust deed.

The proportionate view of taxation of trust distributions states that if a beneficiary receives a certain percentage of the trust's income (i.e trust law income), the beneficiary can only be assessed on that same percentage of the trust's net income (i.e. tax law income). If there is no trust law income, the trustee is assessed on the trust's net income.

In this case, the trust had made a trust law and tax law loss for the 1997 income year after expensing and deducting certain costs relating to an employee benefit arrangement ("EBA"). It had made a small profit in the 1998 year despite incurring further costs relating to the EBA, but not enough to recoup its prior year losses. The Commissioner of Taxation ("the Commissioner") denied the deductions in both income years and issued amended assessments to the trust's default beneficiaries including the increased net income of the trust in the beneficiaries' assessable incomes.

At first instance, in the Administrative Appeals Tribunal ("AAT"), the Commissioner admitted that its amended assessments in the 1997 income year were excessive as there was no net income to distribute to beneficiaries. For the 1998 income year, the AAT determined that the trust had incorrectly deducted the costs relating to an EBA. The AAT then held that the net income of the trust in the 1998 year should be increased and that the Commissioner's amended assessments were correct.

On appeal, Hall & Wilcox, acting for the taxpayers, made two main contentions. The contentions were that the provisions of the trust deed must be taken into account in determining the trust's trust law income and, in the alternative, the trustee's right of indemnity resulted in the beneficiaries having no present entitlement to the trust's net income.

Dealing with the first contention, the trust had made a loss (for trust and tax law purposes) in the 1997 year. The Commissioner conceded that any profits derived by the trust in the 1998 year must be offset against the prior year loss in calculating whether there was any trust law income. However, the Commissioner disputed the ability for the trustee to claim an accounting expense for the EBA costs and if he were correct, there would be trust law income in both income years.

The taxpayers argued that the trustee, as evidenced in the trust's financial accounts, determined that the expenses relating to the EBA were expenses for trust law purposes, even if they were non-deductible for tax purposes. Therefore, after expensing the EBA costs and offsetting the prior year loss, the taxpayers submitted that there was no trust law income in the 1998 year.

The Commissioner's argument was that what was income for trust law purposes could not be governed by what was said in the trust deed.

The Full Court unanimously rejected the Commissioner's argument, holding that "the terms of the trust instrument will prevail over any accounting principles" in calculating trust law income.

The Full Court found it unnecessary to consider the second contention in any great detail, given it found in favour of the taxpayers already.

FURTHER ENQUIRIES

Keith James +61 3 9603 3512
Partner
keith.james@hallandwilcox.com.au

Jerome Tse +61 3 9603 3573
Senior Associate
jerome.tse@hallandwilcox.com.au

Tax education - for the thinking tax professional

We use preparatory questions to ensure real employee participation and the development of essential issue flagging skills.

You choose the pitch & the focus.

A few time slots (monthly or each second month) are still available throughout 2007 in each state but on limited days & times.

For further information

See our website www.taxmatrix.com.au / Call 03 9820 0082 / email taxmatrix@taxmatrix.com.au

PRIVACY STATEMENT: Please tell us if you do not wish to receive this publication in the future. You may contact us by calling our Privacy Officer on +613 9603 3555 or emailing information@hallandwilcox.com.au.

IMPORTANT: This is not advice. Readers should not act solely on the basis of the material contained in this newsletter. Items herein are general comments only and do not constitute or convey advice per se. Changes in legislation may occur quickly. We recommend that our formal advice be sought before acting in any of the areas covered in this newsletter. © Copyright 2006.