

### Funds borrowing - beware the personal guarantee

The relatively new Section 67(4A) is extremely useful for some funds who are undertaking investment purchases utilising the provisions. But, some of the Section 67(4A) products promoted by some major banks do not actually comply with section 67(4A)! In *Taxpayer Alert TA 2008/5*, the Australian Taxation Office stated that security taken by a lender which exceeds the requirements of section 67(4A) - for example, the giving of a personal guarantee by a fund member or a related party, breaches the provisions of the Section itself. The ATO is due shortly to release a Draft Ruling on the issue. It is a sure bet that the Draft Ruling will cause the major banks to reduce their lending in this area given the virtual certainty of the ATO Ruling that the taking of personal guarantees from fund members and related parties breaches the Section.

We have dealt with a large number of Section 67(4A) transactions and those involving the major banks, invariably involve the provision of personal guarantees of fund trustees or, directors of corporate fund trustees who inevitably, are fund members. Simply, the legislation states that a lender's recourse is limited against a fund trustee to the asset acquired by the security trustee and the subject of the lending arrangement and, no other form of security.

Having got that far, a little more needs to be learned about Section 67(4A). The Section is prescriptive only in relation to a lender's rights against a fund trustee. Section 67(4A) does not limit a lender taking extra security from a party other than a fund trustee. So why the fuss then - why can't a fund member provide a personal guarantee? In its *Taxpayers Alert*, the ATO did not spell out the reasons why a member, trustee or director of a corporate trustee cannot provide a personal guarantee in favour of a lender. The reasons are twofold:

Firstly, by virtue of most fund trust deeds (and the common law), a trustee is generally entitled to an indemnity from fund assets as a consequence of incurring loss and damage in a trustee capacity. Thus, if as both a member and trustee (or director of a corporate trustee), a member suffers loss and damage as a consequence of a trustee's default in lending arrangements, there is a right of indemnity by the member against the trust (a fund) and the trustee. In other words, a security or right of action exists against a fund trustee which exceeds recourse to the asset itself which is the subject of a Section 67(4A) transaction.

Secondly, as a general proposition, the law of guarantee gives a guarantor rights of subrogation against a principal (a borrower) where a lender recovers pursuant to a personal guarantee. In Section 67(4A) transactions, the borrower must be a fund trustee. Thus, if a fund trustee defaults, it is possible that a member has recourse against a trustee. It follows that such recourse is other than the asset subject to the Section 67(4A) transaction.

We have a very comprehensive package available to advisers in relation to Section 67(4A) transactions in respect of which, our fees are sensibly balanced against many others we have seen. Our documents deal with both of the problems highlighted by the ATO and discussed above.

### SGC & Contractors

A recent Administrative Appeals Tribunal decision highlights the difficulties faced by the engagement of contractors and a principal's liability for SGC contributions. In *AAT Case [2008] AATA 869, Re Weston and FCT*, the principal engaged a number of foreign workers (with temporary visas) for the purpose of harvesting an agricultural crop. Payments were made by the principal to each contractor on a per kilogram basis. The taxpayer principal argued that he was not liable to make SGC contributions as his 'contractors' were engaged by a head contractor to whom all payments for the contractors were made. The AAT disagreed with the taxpayer principal's view and declared that the 'contractors' were properly of the nature of casual labour and thereby, SGC contributions were properly payable on the piece work payments made to each contractor.

### Binding Death Benefit Nominations and Self-Managed Funds

At last the issue is resolved by the ATO in the manner we've always known about. *Draft Self Managed Funds Determination 2008/D1* states that a self-managed fund may accept a Binding Death Benefit Nomination from a member provided a fund's trust deed permits the making of such a Nomination which need not necessarily accord with the prescriptive requirements of Regulation 6.17A. Our self-managed fund Trust Deeds permit Binding Death Benefit Nominations and in appropriate circumstances, alleviate the requirement for renewal of the Nomination every three years.

## Early release scheme involves criminal charges

There has been an unfortunate proliferation of early release schemes whereby the unsuspecting are obtaining early release of benefits in breach of the cashing restrictions. Invariably, these schemes involve the scheme promoters receiving a percentage of the benefits released (more often than not) from self-managed funds. In one case, *ASIC v Kassongo* (District Court Sydney, 12 September 2008), ASIC alleged that the promoter retained in excess of \$600,000 of member's benefits by way of commissions which were channelled to his own self-managed fund. The matter is the first criminal prosecution against a trustee of a self-managed fund.

## Redundancy Payments

*Draft Taxation Ruling TR 2008/D6* sets out for the first time, the ATO's view as to the requirements which need to be satisfied in order to consider a redundancy payment as a genuine redundancy payment to qualify for taxation concessions under Division 83-175 of the ITAA 1997. In order to qualify for concessional tax treatment, the payment must be made as a consequence of termination of employment (dismissal) attributable to redundancy. The ATO suggests that six elements must be present in order for a genuine redundancy payment to exist:

- The payment must be received as a consequence of termination;
- The employee must be dismissed from employment;
- The dismissal must be caused by redundancy;
- The redundancy must be genuine;
- The employee must be less than 65 years of age; and
- The payment must not be in lieu of superannuation benefits.

## Bonuses count as ordinary time earnings for SGC purposes

In *AAT Case [2008] AATA 762, Re Prushka Fast Debt Recovery Pty Ltd and FCT*, the Administrative Appeals Tribunal has found that bonuses paid to employees were accrued during ordinary hours of work and therefore formed part of employees' salary and wages. Accordingly, the Tribunal found that the bonuses attracted the SGC contribution and the Commissioner was correct in imposing an SGC Shortfall Charge.

## Rulings and Determinations worth reading

There have been a large number of Rulings and Determinations issued by the ATO since our last Newsletter which impact on superannuation funds. The following (non-exhaustive) list details those which we consider to be of greatest interest. Copies of any of publications may be obtained from the ATO's website.

*Self Managed Superannuation Funds Determination SMSFD 2008/1*: An increase in the number of unit holders in a trust may cause a fund to have in-house assets.

*Self Managed Superannuation Funds Determination SMSFD 2008/2*: Determination of the market value ratio of in-house assets cannot be at cost but, must be to current market valuation at the time of calculation.

*Decision Impact Statement re IRG Technical Services Pty Ltd & Anor v DCT*: Who is an employee and who is a contractor - the ATO's views following the IRG Case.

*Self Managed Superannuation Fund Ruling SMSFR 2008/1*: Financial assistance to fund members.

*Self Managed Superannuation Fund Ruling SMSFR 2008/2*: The sole purpose test and incidental benefits.

*Draft Self Managed Superannuation Funds Ruling SMSFR 2008/D1*: Unpaid trust distributions to a fund may contravene the SIS Act and constitute a loan by a fund.

*Draft Self Managed Superannuation Funds Ruling SMSFR 2008/D2*: Contributions of assets in specie to a fund by a related party may contravene Section 66 of SIS.

*Draft Self Managed Superannuation Funds Ruling SMSFR 2008/D3*: What the ATO considers is "business real property".

*Draft Taxation Ruling TR 2008/D5*: What is an Australian superannuation fund and the residency rules in relation to funds.

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