

ATO OUTLINES KEY COMPLIANCE RISKS FOR SMSF'S

At the SMSF Professionals' Association of Australia (SPAA) conference in Brisbane on 12 March 2008
Tax Commissioner Michael D'Ascenzo has outlined the compliance areas for SMSF's, in particular:

New established SMSF - The ATO said it is looking closely at newly-registered SMSF's and their trustees to ascertain whether they have sufficient knowledge to meet their obligations. Currently the ATO has been sending a information questionnaire to trustees of new SMSF's.

Approved auditors - The ATO says it will undertake 900 audits and reviews of individual approved auditors of SMSF's in 2007-08.

Auditor contravention report - The ATO said a revised auditor contravention report (ACR) will also be available from 1 July 2008 which will switch to events-based reporting rather than being legislation-based.

Loans of 80% or more of assets - The ATO is undertaking 550 reviews of funds that reported loans of 80% or more of assets. In these cases the Commissioner has been looking to whom the loan was made, was it an arm's length transaction, and were market interest rates charged?

In-house asset grandfathering - The in-house asset transitional arrangements end on 30 June 2009 for re-investments of certain dividend and trust distributions.

Trustee declarations - New trustees are required to sign a declaration no later than 21 days after becoming a trustee or a director stating that they understand their duties as trustees of a SMSF or a corporate trustee.

Excess contributions - the ATO has identified a substantial number of cases where it appears that the \$1m transitional contribution cap has been exceeded and the relevant trustees have not come forward.

NEW COMPETENCY REQUIREMENTS FOR SMSF AUDITORS

The accounting professional bodies have released a new set of competency requirements for approved auditors of self-managed superannuation funds (SMSFs). The requirements will be mandatory for members of CPA Australia, the Institute of Chartered Accountants in Australia (ICAA) and the National Institute of Accountants (NIA) auditing SMSFs for financial years commencing on or after 1 July 2008.

Members will be required to complete a course in the audit of SMSFs prior to commencing in the area of SMSF audit. They will also need to complete at least 30 hours of ongoing professional development activity in each rolling 3-year period.

NEW SMSF ANNUAL RETURN

The ATO says that when reporting for the 2007-08 financial year onwards, SMSF's will have only one return to complete, i.e., the income tax return and regulatory return will be merged with the member contributions statement resulting in the requirement to lodge only an annual return for SMSF's.

The ATO will be asking trustees ongoing disclosure questions, including, whether:

- the SMSF had/has financial involvement with related parties
- the SMSF has lent money to members or their family
- investments have been undertaken on an arm's length basis
- the SMSF has allowed members access to assets and money before retirement

NEW SMSF ANNUAL RETURN *continued*

- the trustees have paid themselves for their services
- non-cash contributions (known as "in-specie" contributions) have been made to the SMSF
- any of the fund's trustees have become disqualified during the year
- the SMSF has engaged in activities of selling goods and/or services
- all assets are appropriately secured through appropriate documentation as owned by the SMSF
- the approved auditor has provided services other than auditing the fund to the SMSF.

Argyle Comment:

Advisors need to 'warn' and educate clients on the many issues that impact in superannuation and with respect to SMSF's. Even the basic issues must be considered and the clients equipped with the capacity to answer these basic issues.

PROPERTY WITH SHED QUALIFIES FOR CGT MAIN RESIDENCE EXEMPTION RE.RE SUMMERS AND FCT

A taxpayer who occupied a shed on her land for 4 months after the contract to build a house on the land fell through has been successful in obtaining a partial main residence exemption on the basis that the shed qualified as her home.

The AAT accepted that the taxpayer had made the shed her home despite the fact she had only moved her bed into the premises (albeit mains water and a toilet were connected to the shed). It took into account her prior history of occupying rented premises in a similar manner, and her working and social habits that, among other things, involved her working 14-hour days, showering at her work premises and always buying meals.

The tribunal found that the taxpayer could not apply the concession in s 118-150 of the ITAA 1997 for building a house on vacant land in order to obtain a full main residence exemption as she did not occupy the shed as soon as practicable after its completion as required under the section.

In calculating the partial exemption, the AAT accepted that she was entitled to use the absence concession under s 118-145 from the time she moved out of the shed until its sale.

Argyle Comment:

It may represent the extremes of what constitutes a home, but it is now clear that the CGT free home really is where the heart is.

OSR - DEADLINE FOR LAND UNIT TRUST EXTENDED

The Office of State Revenue NSW has announced that the NSW Treasurer has authorised "Act of Grace Payments" on a case-by-case basis for unit trusts that were unable to meet the 31 December 2007 deadline to become fixed trusts. The OSR said this relief will only be provided if a trust deed is changed to become a fixed trust by 30 June 2008.

The OSR says you must show that there were reasons beyond your control that prevented you from restructuring to a fixed trust by the original deadline of 31 December 2007.

If you qualify for relief, Acts of Grace payments may be provided for the 2006, 2007 and 2008 land tax years, and for transfer duty arising from restructuring your trust. You should note that the OSR relief does not assist any possible CGT consequences arising from a potential resettlement.

Argyle Comment:

This has got to be the last opportunity to rectify a trust that otherwise causes land tax. Advisors should alert all property owning clients to this final once only amnesty.

65 YEAR OLD WOMAN JAILED FROM DATA-MATCHING EXERCISE

A 65-year-old woman who used a false identity to steal more than \$100,000 in Centrelink payments has been sentenced to 24 months in prison in Sydney. The woman, from Sydney's inner-west, received a Widow Allowance and Age Pension in her real name between December 1998 and February 2007 whilst also working under a false name. Centrelink uncovered the fraud after a data-matching exercise with the ATO.

The Minister said the woman, who pleaded guilty, will be eligible for parole after serving 9 months in prison. She was also ordered by the court to repay Centrelink the outstanding debt of \$99,870.

SMALL BUSINESS CGT CONCESSIONS ASSET NOT AN ACTIVE ASSET - NOT USED BY A CGT AFFILIATE AAT Case [2008] AATA 176, Re Stephens and FCT

The AAT has confirmed a decision of the ATO that an asset owned by a family trust did not qualify as an active asset, even though it was used in the legal firm in which one of the controllers of the trust was a principal. This was because the legal firm did not qualify as a 'small business CGT affiliate' of the trust in the circumstances.

Facts

The taxpayer was a beneficiary of the Stephens Family trust. She was also one of the co-directors of the corporate trustee. Her husband was the other director. He was one of 7 principals in a legal firm. In 1998, the family trusts of 6 of the principals in the firm jointly purchased the business premises for the legal firm. In 2003, the premises were sold and each the Stephens Family trust made a capital gain of \$116,500 from the sale of its interest. The taxpayer claimed the 50% reduction under the CGT small business concession in respect of the gain on the basis that the interest in the premises was an active asset of the trust as it had been used by a 'small business CGT affiliate' (the legal firm) in carrying on its business. The Commissioner denied the taxpayer's claim for the reduction, arguing that the legal firm was not an affiliate as it did not 'act, or could not reasonably be expected to act, in accordance with Mr and Ms Stephen's directions or wishes, or in concert with them'.

Decision

The AAT agreed that the Stephens Family trust's interest in the business premises was not an active asset because there was no evidence to support the claim that the legal firm was an 'affiliate' of the trust in terms of the requirement of the relevant definition.

The AAT noted Mr Stephens was only one of 7 principals in the firm. The AAT held that it was not sufficient to show that Mr and Ms Stephens directed or influenced the way in which the firm used the *CGT asset* (ie the premises). It had to be shown that the firm acted in accordance with their direction or wishes in the way it carried on its *business*, which it could not.

Note

In relation to CGT events occurring from 1 July 2007, the concept of 'small business CGT affiliate' was replaced by the concept of 'affiliate' which is defined as an 'individual or a company that acts, or could reasonably be expected to act, in accordance with the taxpayers directions or wishes, or in concert with taxpayer, in relation to the affairs of the business of the individual or company' (s 328-130(1)). The new definition specifically provides that an 'affiliate' can only be an individual or company.

Argyle Comment:

Once again this case reinforces the need for proper and solid business structuring to cater for the various tax concessions that are available to small (and not so small) business.

TAX COMMISSIONER'S UPDATE ON COMPLIANCE ISSUES

Speaking at the TIA National Convention on 13 March 2008, the Tax Commissioner provided an update on the headline compliance issues for 2007-08. The Commissioner's speech is available on the ATO Website

TAX COMMISSIONER'S UPDATE ON COMPLIANCE ISSUES continued**International tax risks**

The Commissioner indicated that the ATO is stepping up its compliance activity against taxpayers with undeclared income in overseas bank accounts or using overseas credit cards and warned that time is running out for taxpayers with hidden income offshore to come forward and make voluntary disclosures to access the penalty concessions.

ATO alert - Liechtenstein accounts

The Commissioner provided an update on international action on Liechtenstein accounts, announcing the Taxpayer Alert TA 2008/2. He warned that ongoing investigations may include unannounced visits to taxpayers with suspected links to Liechtenstein or other tax havens, and where necessary, he will be raising default assessments with significant penalties, and/or considering criminal sanctions.

Project Wickenby

The Commissioner indicated that voluntary compliance of people identified through Project Wickenby has increased by some 49%. He noted that Wickenby has 20 criminal investigations underway, 9 by the Australian Crime Commission, 9 by the AFP and 2 by ASIC, and that the ATO has completed 168 audits and raised assessments in 124 cases. He also indicated that ATO is also currently auditing a further 353 cases.

High wealth individuals

The Commissioner stated that additional resources have greatly increased the probability of a tax risk being detected for high wealth individuals. There are currently 58 audits of high wealth individuals in progress and 103 risk assessments have been completed under the 2007-08 compliance program.

High income individuals

The ATO is reviewing executives remunerated in excess of \$1m. Around 22% of those reviewed, have received a questionnaire seeking an explanation as to possible discrepancies.

UNCOMMERCIAL USE OF TRUSTS, DEDUCTIONS, INCOME AND SMSF'S

Taxpayer Alert TA 2008/3 - Uncommercial use of trusts - describes a non-arm's length arrangement under which taxpayers use borrowed funds to acquire an interest, such as units, in a certain type of trust, which uses the funds to purchase income-producing property. The ATO says the arrangement seeks to provide income tax deductions to the taxpayers for all of their interest payments and other borrowing costs. The ATO view is that the arrangement does not provide a sufficient connection between the expenditure and the production of future income and/or capital gains, which may be distributed to other beneficiaries of the trust, who may have a lower tax rate

The ATO is not concerned about all "discretionary", or "hybrid" trust arrangements, but negatively geared trust arrangements which involve the taxpayer incurring interest expenses or borrowing costs where all or a proportion of the borrowed funds could be used for the benefit of the beneficiaries, or where the taxpayer's interest in the trust could be brought to an end before their costs of investment have been recouped".

Taxpayer Alert TA 2008/4 - Self-managed superannuation funds deriving income from certain uncommercial trusts - describes a non-arm's length arrangement under which a self-managed superannuation fund (SMSF) derives income through a direct or indirect interest in a closely-held trust. Previously this type of income was considered special income. Now the reference is made to non-arms length income. Such income is taxed at 45% instead of 15%. The Commissioner has warned that the compliance status of the fund may also be effected where special income is distributed to a SMSF.

DIV 7A - NEW BROCHURE FROM THE ATO, PLUS AMNESTY REMINDER

The ATO has released a new information brochure entitled "*Division 7A - Separating your personal and company money*" **NAT 71938-02.2008**. As well as the booklet for taxpayers, the ATO has also provided sample letters to clients that explain the recent amendments to Division 7A.

DIV 7A - NEW BROCHURE FROM THE ATO, PLUS AMNESTY REMINDER *continued*

The letters explain the Commissioner's new discretions under the law and the one-off opportunity available to business owners until 30 June 2008 to self-correct past mistakes regarding payments and loans from their private companies, and to avoid penalties under Div 7A, without applying for the Commissioner's discretion.

Certain conditions must be met. The offer applies to situations where honest mistakes and inadvertent omissions have been made in respect of the 2001-02 to 2006-07 income years.

Taxpayers who don't meet the conditions, can apply to the ATO in writing to disregard errors at any time. If taxpayers meet the conditions to correct the error themselves, and do not self correct by 30 June 2008, they will have to apply to the ATO in writing to disregard the error.

**TAX LAWS AMENDMENT (2008 MEASURES NO 2) BILL 2008
SUPER GUARANTEE RELIEF FOR LATE PAYMENTS**

The Bill which was introduced in the House of Representatives on 20 March 2008 contains, among other amendments, measures amending the *Superannuation Guarantee (Administration) Act 1992* (SGAA) to extend the period within which an employer can make a contribution after the quarterly due date and still be eligible to use the late payment offset to reduce their superannuation guarantee (SG) charge liability.

The changes are designed to reduce the incidence of employers having to potentially pay the same amount twice, once when they make a late contribution to the employee's fund and again when they are assessed with an SG charge for making the contribution late.

The amended late payment offset will be available to employers who, have made a contribution for an employee after the due date for the quarter, have an outstanding SG charge for the employee for that quarter and elect, in the approved form, to use the offset.

The late contribution can only be offset against an SG charge which relates to the same quarter and to the same employee.

The SG charge and late payment offset are *not tax deductible* to the employer, therefore employers still have a strong incentive to continue making their SG quarterly payments on time. The amendments will take effect from the date of Royal Assent.

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