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NSW MINI BUDGET ANNOUNCEMENTS

On 11 November 2008, the NSW Treasurer Hon. Eric Roozendaal MLC introduced various measures aimed at correcting the deficit in the NSW Budget. These measures include:

1. A land tax rate of 2% - to apply to land tax payers with total taxable land holdings above \$2.25m from 1 July 2009. Land holding below the threshold will remain subject to the 1.6% rate. The threshold is to be indexed in line with the existing land tax threshold and the exemptions for principal place of residence and rural properties will remain;
2. A landholder model replacing the land rich duty. The model is meant to eliminate the need for complex valuations and calculations regarding the proportion of assets represented by land and provide increased tax harmonisation between NSW and other jurisdictions that use the landholder model. The important point to note is that under the new landholder provisions, the 60% test will no longer apply, whereas under the current rules both a threshold test and a percentage test applied in respect of the acquisition and disposal of such interests. These provisions are not set to commence until 1 July 2009;
3. Increase in nominal stamp duties - trust settlements will be assessed at \$500 as opposed to the \$200. Other nominal duties will increase from \$2.00 and \$10.00 to \$10.00 and \$50.00 for documents. These increases are set to take effect from 1 January 2009;
4. Deferral of the abolition of duties on mortgages, business loans, unquoted marketable securities and transfer duty on non-land business assets until 1 July 2012;
5. Increasing coal royalty rates from 1 January 2009 as follows:
 - (a) open cut mining will increase to 8.2% (from 7%);
 - (b) underground mining will increase to 7.2% (from 6%); and
 - (c) deep underground mining from 5% to 6.2%.
6. New Home Buyers Supplement a NSW New Home Buyers Supplement of \$3,000 will be added to the existing First Home Owner Grant of \$7,000 for eligible applicants building a new home or buying a newly constructed home. \$3,000 Supplement will be available for 12 months (11 November 2008 to 10 November 2009 inclusive). This additional to the \$14,000 Commonwealth's First Home Owner Boost scheme. Eligible applicants building or buying a newly constructed home will be eligible to receive a total of \$24,000; and
7. Subject to Commonwealth Government approval, the First Home Owner Grant Scheme and New Home Buyers Supplement will be limited from 1 July 2009 to first homes valued under \$750,000.
8. Parking Levies will be increased from 1 July 2009 as follows:
 - (a) from \$950 to \$2,000 a year per off-street, non residential parking space in the Sydney, North Sydney and Milsons Point business districts and
 - (b) from \$470 to \$710 a year in the business areas of St Leonards, Chatswood, Parramatta and Bondi Junction.

Existing exemptions will remain in place and the levy will continue to be indexed in line with the Sydney CPI.
9. Payroll tax cuts remain

The Treasurer has confirmed that the payroll tax cuts announced in the 2008-09 NSW Budget would remain, in particular, the State Revenue and Other Legislation Amendment (Budget) Act 2008 (NSW) which was assented to on 30 June 2008 amended the Payroll Tax Act 2007 (NSW) so that:

NSW MINI BUDGET ANNOUNCEMENTS

continued

- (a) the payroll tax rate of 6% will be reduced to 5.75% from 1 January 2009, to 5.65% from 1 January 2010 and to 5.5% from 1 January 2011;
- (b) the tax-free threshold will be indexed annually in line with increases in the Sydney CPI; and
- (c) special arrangements would apply in the 3 financial years over which the reduction in tax rate would be phased in.

BILL TO REGULATE THE PROVISION OF TAX AGENT SERVICES

On 13 November 2008, the Assistant Treasurer, Chris Bowen MP, introduced the Tax Agent Services Bill 2008 into the Parliament.

The Bill seeks to reform the registration and regulation of entities providing tax agent services for a fee. The Assistant Treasurer outlined that *"Reform in this area is long overdue. An updated regulatory regime that is appropriate for the modern tax environment has been on the drawing board for almost 15 years."* The Bill follows an exposure draft Bill and EM released for public consultation in mid-2008.

Key measures of the Bill include:

A national Tax Practitioners Board

A single national Tax Practitioners Board is proposed to replace the existing state-based Tax Agents' Boards. The Board is to be an independent statutory body, with its key functions being the registration and regulation of tax agents and Business Activity Statement (BAS) agents as well as certain powers to ensure that unregistered entities are not holding themselves out as registered. It will have the power to investigate matters and impose sanctions where appropriate.

Registration requirements

Tax Agent Services providers and BAS services providers (for a fee or other reward) advertising the provision of such services, or holding out as being registered, will be required to register with the Board. The new type of registration will be that for those providing BAS services for a fee or other reward. Tax Agent registration will remain broadly the same.

BAS agents will not be required to demonstrate the same degree of formal education and relevant experience as tax agents. Entities that specialise in a particular area of the taxation laws or that only provide a type of tax agent service will be eligible to register, with scope to operate in their specialty.

A Code of Professional Conduct

The existing scheme of offences and criminal penalties will be replaced by civil penalties and injunctions, which are more appropriate where the conduct being sanctioned is not serious enough to warrant a criminal conviction or imprisonment.

Civil Penalties

The Board may apply to the Federal Court for a civil penalty order in certain circumstances or for an injunction to prevent or compel certain conduct, particularly where:

- (a) an unregistered entity provides a tax agent service or BAS services for a fee or other reward; or
- (b) a registered agent makes a false or misleading statement, employs or uses the services of an entity whose registration has been terminated due to misconduct, or signs a declaration in relation to a document prepared by an entity that is not qualified to prepare that document and was not appropriately supervised.

Section 251M - Removed

The Bill removes the existing statutory negligence provision found in section 251M of the ITAA 1936 which currently reads as follows:

"If, through the negligence of a registered tax agent... a taxpayer becomes liable to pay a fine or other penalty, the general interest charge under a provision of this Act, or to pay shortfall interest charge, the registered tax agent, or the person, as the case may be, shall be liable to pay to the taxpayer the amount of that fine or other penalty, additional tax, general interest charge or shortfall interest charge, and that amount may be sued for and recovered by the taxpayer in any court of competent jurisdiction."

BILL TO REGULATE THE PROVISION OF TAX AGENT SERVICES

continued

Safe harbours for taxpayers from certain administrative penalties

There will be two safe harbours for taxpayers who engage a tax agent or BAS agent. They will exempt taxpayers from liability for administrative penalties for making a false or misleading statements resulting in shortfalls where they demonstrate they have taken reasonable care by engaging a tax agent or BAS agent and giving all relevant taxation information to the agent.

Taxpayers where they fail to lodge a document on time and in the approved form, in circumstances where a tax agent or BAS agent has been engaged and has been provided with all necessary information to enable lodgement or provision to the Commissioner on time and in the approved form.

The safe harbours do not apply where the taxpayer or agent has intentionally disregarded a taxation law or has been reckless as to the operation of a taxation law.

AUASB GUIDANCE STATEMENT GS 009 - AUDITING SELF MANAGED SUPER FUNDS

The Auditing and Assurance Standards Board (AUASB) has issued Guidance Statement GS 009 Auditing Self Managed Superannuation Funds. It replaces the 2004 and 2005 Audit Guidance documents. The document is aimed at providing auditors with a greater awareness and understanding of their responsibilities when conducting audits of SMSFs.

Merran Kelsall, Chairman of the AUASB, said the Guidance Statement will help improve the quality of audits conducted for SMSFs by identifying, clarifying and summarising the existing responsibilities of auditors.

The document explains that it seeks to assist auditors on matters which the auditor should consider when planning, conducting and reporting on the financial and compliance audits of an SMSF.

The document deals with a whole range of issues including, trustees responsibilities, auditors responsibilities, as well as a whole raft of other considerations to be taken in to account by Auditors of Self Managed Superannuation Funds.

Importantly whilst the document does not extend the responsibilities of auditors beyond those which are imposed by the various pieces of legislation and regulations, it provides guidance and clarity and many issues which auditors would generally be required to consider.

DRAFT TAXATION DETERMINATION TD 2008/D16 - DEDUCTIBILITY OF INTEREST

The Australian Taxation Office has released Draft Taxation Determination TD 2008/D16 which follows a series of private binding rulings as well as the Taxpayer Alert released earlier this year, TA 2008/3. Both papers essentially deal with arrangements involving the deductibility of interest in connection with a loan used to fund the acquisition of an interest in a hybrid trust.

Draft taxation determination TD 2008/D16 follows Taxpayer Alerts TA 2008/3 and TA 2008/4, which were issued on 26 March 2008. These taxpayer alerts outlined ATO concerns about certain uncommercial trust arrangements. In many of the trust arrangements the ATO has examined:

- (a) the taxpayer's entitlement to trust income is determined by the exercise of the trustee's discretion, rather than by the rights attaching to the units – meaning that the interest is not deductible, or
- (b) the taxpayer's entitlement to trust income and/or capital is disproportionately small compared to their contribution to the trust – meaning that the interest is not deductible in full and some apportionment of the interest deduction would be required.

The Draft TD, released on 19 November 2008, provides that interest on a loan used to settle moneys on trust to benefit the borrower and others cannot be deducted in full under s 8-1 of the ITAA 1997. The ATO explains that the interest can only be deducted to the extent to which the taxpayer has used the borrowed moneys to gain or produce assessable income of the taxpayer.

DRAFT TAXATION DETERMINATION TD 2008/D16 - DEDUCTIBILITY OF INTEREST

continued

The Commissioner explains that interest will not be deductible to the extent the taxpayer has used the borrowed moneys for the purpose of benefiting persons other than the taxpayer. The ATO explains that an apportionment of interest will be required.

The ATO explains that arrangements which display some or all of the following features are of particular interest:

- (a) The taxpayer arranges for the establishment of a trust. The trustee of the trust is either the taxpayer, or is controlled by the taxpayer and/or associates of the taxpayer.
- (b) The beneficiaries of the trust are the taxpayer and his or her associates (the other beneficiaries). The other beneficiaries are members of the taxpayer's family, and/or entities which the taxpayer and/or the taxpayer's associates control; they do not usually contribute any capital to the trust, nor do they provide money or property to the taxpayer.
- (c) The taxpayer borrows money at interest and settles it on the trust. The trustee issues units to the taxpayer. The units carry particular rights to trust income and/or capital.
- (d) The trustee uses the money in (c) to purchase one or more income producing assets. Typically, the assets comprise real estate or shares.
- (e) The trust deed and/or the trustee acting under authority of the trust deed determines how much of the income of the trust is available for distribution to beneficiaries.
- (f) The taxpayer's units do not give the taxpayer an entitlement to all of the benefits which may reasonably be expected to be produced by the asset(s) in (d). Alternatively, an objective implication to be drawn from the trust deed is that the taxpayer cannot reasonably expect to receive all such benefits.
- (g) Units may:
 - (i) carry no entitlement to share in realised capital gains of the trust;
 - (ii) carry no entitlement to share in anything other than realised capital gains of the trust;
 - (iii) carry an entitlement to share only in part of the income of the trust; or
 - (iv) be redeemable, at trustee's discretion, for an amount which fails to reflect the taxpayer's contribution to the trust (for example the cost of the units or their market value, where such value reflects the limited nature of the rights which the units carry).
- (h) For a number of income years, the amounts included in the taxpayer's assessable income because of his or her unit holding are significantly less than the interest expense on the borrowing. The taxpayer claims that the interest expense is deductible in full under s 8-1 of the ITAA 1997.

The Commissioner also explains in his draft determination that *"if a taxpayer was entitled to an unapportioned deduction of interest, the Commissioner may consider whether Part IVA of the ITAA 1936 applies to the facts of the particular case. If the Commissioner concluded, based upon the facts of a particular case, that there was a scheme entered into for the sole or dominant purpose of obtaining a tax benefit, the Commissioner may determine that the whole or part of the deduction is not allowable to the taxpayer."*

Advisors should also note that following the release of Draft TD 2008/D16, the ATO has further advised that it is currently examining the conduct of entities involved in marketing these arrangements and that in a number of cases it is considering, or is in the process of taking, action against them under the promoter penalty laws.

It is extremely important that advisors review the affairs of clients in circumstances contemplated by the draft determination and the Taxpayer Alert and appropriately consider as well as document the reasoning and nature of any interest expenditure incurred by relevant persons. Advisors should also ensure that their conduct with respect to the use of such investment vehicles does not fall within the type of conduct contemplated by the promoter penalty laws.

ATO DATA MATCHING PROJECT - THOROUGHBRED RACEHORSES

The ATO has announced that its current thoroughbred data matching project is seeking to identify taxpayers with large interests in thoroughbred racehorses. Information will be sourced from the auctioneers William Inglis and Son Ltd and Magic Millions.

ATO DATA MATCHING PROJECT - THOROUGHBRED RACEHORSES

continued

The Australian Taxation Office (the Tax Office) will request and collect details pertaining to horse trainers, owners, jockeys, stable-hands and track-riders from the Stakes Payment System of the New South Wales Thoroughbred racing Board.

These details will reflect data captured in respect of the 2003-04 and 2004-05 financial years. These details will be electronically matched with certain sections of Tax Office data holdings to identify non-compliance with lodgment and payment obligations under taxation law. Records relating to individuals, partnerships, companies and trusts will be matched.

FAIR WORK BILL 2008

On 25 November 2008, the Minister for Workplace Relations Julia Gillard introduced the Federal Government's new laws which will dismantle Work Choices legislation, which she says will create a fairer system for both workers and employers.

The Fair Work Bill covers all workers under unfair dismissal laws, establishes Fair Work Australia, legislates for "good faith" collective bargaining and does not differentiate between a union or non-union agreement.

The Minister explained that the Bill establishes Fair Work Australia which will facilitate and approve collective bargaining agreements, adjust minimum wages and deal with unfair dismissal claims and workplace disputes.

It is intended that Fair Work Australia (FWA) replace six other existing bodies, including the Australian Industrial Relations Commission, the Australian Fair Pay Commission, the Workplace Ombudsman and the Australian Building and Construction Commission. If an employer refuses to take part in bargaining, FWA can order them to take part if it finds that a majority of employees want to collectively bargain.

In summary, the measures contained in the Bill establish:

- (a) a safety net applicable to all employees (guaranteed things such as maximum weekly hours of work, right to request flexible working arrangements, parental leave and related entitlements),
- (b) introducing new awards and national minimum wage orders that apply to award-free employees,
- (c) a new institutional framework for the administration of the new workplace relations system comprising an independent statutory body with a range of functions and powers (including facilitating collective bargaining, approving enterprise agreements, adjusting minimum wages and award conditions and dealing with unfair dismissal claims), as well as the creation of a Fair Work Ombudsman,
- (d) framework for dealing with terms and conditions of employment where there is a transfer of business that intends to balance the protection of employees' terms and conditions of employment and the interests of employers in running their enterprises efficiently.
- (e) streamlined and simple general protections dealing with workplace and industrial rights, including the rights to freedom of association and protection against discrimination, unlawful termination and sham arrangements.
- (f) unfair dismissal protections for employees under a flexible and informal process, with an emphasis on re-instatement and a Fair Dismissal Code for small businesses.
- (g) default right for employers to stand down employees in defined circumstances.

In addition to a number of other measures, the 10 National Employment Standards which include such provisions as a 38-hour week, four weeks' annual leave and a right to request flexible working arrangements are included in the package.

FEATURE ARTICLE - HOW WELL DO YOU YOUR COVENANTS MR & MRS TRUSTEE

Sub-section 52(1) of the Superannuation Industry (Supervision) Act, i.e., the SIS Act, effectively deems all the covenants set out in sub-section 52(2) of the SIS Act to be included in governing rules of a super fund if those rules do not contain covenants to the effect of each of the section 52(2) covenants.

FEATURE ARTICLE - HOW WELL DO YOU YOUR COVENANTS MR & MRS TRUSTEE

continued

Those covenants which all trustees of super funds are deemed to have entered into are as follows:

- (a) to act honestly in all matters concerning the entity;
- (b) to exercise, in relation to all matters affecting the entity, the same degree of care, skill and diligence as an ordinary prudent person would exercise in dealing with property of another for whom the person felt morally bound to provide;
- (c) to ensure that the trustee's duties and powers are performed and exercised in the best interests of the beneficiaries;
- (d) to keep the money and other assets of the entity separate from any money and assets, respectively:
 - (i) that are held by the trustee personally; or
 - (ii) that are money or assets, as the case may be, of a standard employer-sponsor, or an associate of a standard employer-sponsor, of the entity;
- (e) not to enter into any contract, or do anything else, that would prevent the trustee from, or hinder the trustee in, properly performing or exercising the trustee's functions and powers;
- (f) to formulate and give effect to an investment strategy that has regard to the whole of the circumstances of the entity including, but not limited to, the following:
 - (i) the risk involved in making, holding and realising, and the likely return from, the entity's investments having regard to its objectives and its expected cash flow requirements;
 - (ii) the composition of the entity's investments as a whole including the extent to which the investments are diverse or involve the entity in being exposed to risks from inadequate diversification;
 - (iii) the liquidity of the entity's investments having regard to its expected cash flow requirements;
 - (iv) the ability of the entity to discharge its existing and prospective liabilities;
- (g) if there are any reserves of the entity--to formulate and to give effect to a strategy for their prudential management, consistent with the entity's investment strategy and its capacity to discharge its liabilities (whether actual or contingent) as and when they fall due;
- (h) to allow a beneficiary access to any prescribed information or any prescribed documents

Given sub-section 52(1) deems all the covenants set out in sub-section 52(2) to be contained in the governing rules of superannuation funds if they are not already contained in the deed or rules, it is not for SIS purposes necessary to set out each covenant.

But, it is a common law duty of a trustee to acquaint itself with the terms of the trust, as well as to act impartially between all the beneficiaries. For this reason, SIS covenants should be in the rules or deed of the fund to ensure that trustees are aware of them. Most trustees do not know what is deemed to be included in the rules or deed of a fund by virtue of the SIS Act, and so specific reference is the better approach.

The best interest covenant, which is set out in sub-section 52(2)(c) of the SIS Act provides that each trustee of a superannuation entity covenants to ensure that the trustee's duties and powers are performed and exercised in the best interest of the beneficiaries. The term 'best interest of the beneficiaries', is taken to mean the best interest of all the beneficiaries. Let's look at a practical example.

A married couple John and Mary who separated just under a year ago, are trustees, members and joint signatories of the Joma Superannuation Fund. Over the last 12 months Mary has refused to allow John to sell down shares in the fund in his anticipation of the share market crash. As a result John who just went into Pension mode 12 months ago has now been unable to pay the pension he anticipated paying himself as the member balances have dropped by about 70% from when the time he intended to sell the shares. ***What issues arise with respect to the SIS Covenants?***

Section 55 of the SIS Act sets out the consequences for a contravention of a covenant contained (i.e., set out in the governing rules of a superfund) or taken to be contained in the governing rules of a superfund.

The section provides that a person who suffers loss or damage as a result of conduct of another person that was engaged in, in contravention of a covenant, may recover the amount of the loss or damage by action against that other person involved in the contravention. The section sets out that recovery action may be commenced at any time within 6 years after the day on which the action arose.

FEATURE ARTICLE - HOW WELL DO YOU YOUR COVENANTS MR & MRS TRUSTEE

continued

A defence to an action for loss or damage suffered as a result of an investment decision, is that the investment decision was made in accordance with a complying investment strategy. The term investment decision does not only relate to a decision to acquire an asset, but it also includes a decision to retain or dispose of an asset.

In the case of *Dunstone v Irving* [2000] VSC 488 in the Supreme Court of Victoria, Justice Hanson was asked to consider a trustee's failure to transfer a member's \$1.365 million benefit from a self-managed superannuation fund. In that case the plaintiff and the defendant were involved in a joint business venture and were the sole members and trustees of the superfund. As a result of a dispute regarding the amount of the plaintiff's entitlements, the defendant, acting in the capacity as trustee, refused to sign a cheque for the claimed amount, or for any other amount.

The court determined that the plaintiff was entitled to the amount claimed, and ordered the defendant to do all things necessary to transfer the entitlement. More importantly though, the court also held that the plaintiff was entitled to damages under section 55 of the SIS Act, at approximately \$250,000 for the loss suffered as a result of the defendant's breaches of his obligations as trustee.

The loss was calculated on the basis of expert accounting evidence that set out the amount the plaintiff's payment would have been worth if he had invested the amount that he should have been paid in a balanced fund, in accordance with his most likely investment choice.

Problematic Arrangements:

- Separated Couples involved in a family law dispute
- Family members arguing over investment decisions (*particularly in context of falling market*)
- Blended families and deceased estates dealing with SMSF interests
- Trustee's '*taking care of the investment side of things*' for all members

For further information or enquiries please contact any member of the Argyle Lawyers Pty Limited Taxation & Superannuation Team.

Contact Details

Phone + 61 2 8263 6622 (direct)
Fax + 61 2 8263 6633
Email pbobbin@argylelawyers.com.au
Mobile 0408 111 831
1983 Bachelor of Commerce (Accounting & Finance Systems)
 Bachelor of Laws University of New South Wales
1998 Master of Taxation (distinction) University Western Sydney
 Fellow of the Taxation Institute of Australia

**GEORGE SAMARAS - SOLICITOR****Contact Details**

Phone + 61 2 8263 6628 (direct)
Fax + 61 2 8263 6633
Email gsamaras@argylelawyers.com.au
Mobile 0407-003-010
2003 Bachelor of Laws /Bachelor of Commerce (Acc)
 Studying Master of Laws
 Member Young Lawyers Business Law Committee
 Fellow of the Taxation Institute of Australia
 Member of TIA Membership Committee
 Regular chair and presenter in professional forums

**DANIEL HAWRYLUK - SOLICITOR****Contact Details**

Phone + 61 2 8263 6637 (direct)
Fax + 61 2 8263 6633
Email dhawryluk@argylelawyers.com.au
Mobile 0413 555 222
2002 Bachelor of Social Science / Bachelor of Laws University of Western Sydney
2006 Masters of Taxation University of New South Wales

**MARY FERIZIS - SOLICITOR****Contact Details**

Phone + 61 2 8263 6646 (direct)
Fax + 61 2 8263 6633
Email mferizis@argylelawyers.com.au
Mobile 0416 025 019
1999 Bachelor of Arts Sydney University
2003 Bachelor of Law University of Technology, Sydney
2004 Admitted to the Supreme Court of New South Wales
2008 Diploma in Financial Planning - Kaplan

