



**TECHNICAL COMMITTEE MEETING**

**MINUTES OF MEETING HELD ON 7 APRIL 2011 AT 11.30 a.m. EST**

**BY TELEPHONE CONFERENCE**

**Present:**

Rob Jeremiah, (RJ) Harwood Andrews Lawyers (Chair)  
Claire Malone (CM) Harwood Andrews Lawyers (taking minutes)  
Philip Broderick, (PB) DLA Phillips Fox  
Carmel Riordan, (CR) Carmel Riordan Lawyers  
Kevin Sudlow (KS) Multiport  
Darren Kingdon (DK) Plan Wealth

**Apologies:**

Larisa Moran (KPMG)  
Chris Hocking  
Steven Skoglund (Davidsons)  
Teresa Parletta (Superfund Accounting Services)  
Barbie Chiro (WWSA)

**1. Welcome:**

Rob Jeremiah opened the meeting at 11.30 a.m. AEST.

**2. Report on technical issues discussed at National Tax Liaison Group (NTLG) Superannuation technical Sub-Group meeting held on 21 March 2011:**

**2.1 Cases considered in the litigation update:**

RJ noted that quite a few cases were considered in the litigation update and he had selected several key decisions for discussion:

**2.1.1 *Allen's Asphalt Staff Superannuation Fund v Cmr of Taxation* [2010] FCA 1276**

This was a non-arm's length income case involving distributions from a non-fixed trust to a fixed trust which were then distributed to a superannuation fund who held units in the fixed trust. The income derived by the fund was found to be non-arm's length income.

It was noted by the Committee members that this was probably the correct outcome but some of the reasoning of Collier J is questionable, including some commentary about what amounts to the derivation of income. The decision is being appealed to the Full Federal Court. It is expected that the outcome will not change but it will be interesting to see how the Full Court addresses Collier J's reasoning.

**2.1.2 *Player v Cmr of Taxation* [2011] AATA 35**

In this decision the AAT examined whether the payment of \$355,000 by a superannuation fund to a member was an ETP or a roll-over. The Tribunal found that this was an ETP because it was not a payment from one complying superannuation fund to another. Consequently the amount was a contribution when it was paid by the member to a second

fund and the member became liable for excess contributions tax. This case is also now on appeal.

It was noted by Committee members that it appears that there is not much doubt that the amount in this case was an ETP.

### **2.1.3 *Dolevski v Hodpick Pty Ltd* [2011] FCA 54**

A key aspect of this case was whether it was reasonable for the trustees, who had breached ss 62, 84 and 109 of the *Superannuation Industry (Supervision) Act 1993 (SISA)* in making certain loans, to rely on advice provided by a former tax agent and whether the defences in ss 323(2) (contravention due to a reasonable mistake or reasonable reliance on information supplied by another person) and 221(2) (where a person has acted honestly and ought fairly to be excused) were available.

The Federal Court found that it was reasonable to rely on advice provided by the former tax agent and the trustees had no reason to doubt the reliability of that advice. It was also noted in the judgment that these issues involved matters in respect of which the taxpayers had little experience. In respect of further loans which the tax agent had not specifically provided advice about, the trustees could claim the "reasonable mistake" defence because, as a result of the tax agent initially providing advice about a first loan, the trustees operated under a genuine but mistaken belief that it was legally and commercially appropriate to make further loans.

The defences were found not to be available in respect of the breach of the in-house asset rules because, in the circumstances, the contravention was due to ignorance of the state of affairs that gave rise to the obligation (ie, that the market value ratio of the fund's in-house assets exceeded 5% at the end of an income year) or possibly the obligation itself and not due to a reasonable mistake or reasonable reliance on information provided by another person.

However, the Court found that the defence in s 221(2) was available to the extent that s 323(2) did not apply because the trustees had acted honestly. The defence was available even though they did not read the fund's trust deed and did not seek advice about all of the loans. The Court noted that the defence in s 221(2) may be available even where a contravention is serious.

The Committee noted that this is a significant decision because it demonstrates that there is potentially considerable scope for these defences to apply where trustees have breached the SISA. In particular, incorrect advice from an adviser could effectively be a defence to some breaches. It was noted by the committee that this is in contrast to the penalty provisions for tax shortfalls and that the approach of the ATO in taxation matters is that receiving incorrect professional advice is no excuse and that taxpayers should simply take action against their advisers in such situations.

### **2.1.4 *Roy Morgan Research Pty Ltd v Federal Cmr of Taxation* [2010] FCAFC 52**

It was noted that this case, in which the Full Federal Court rejected the taxpayer's argument that superannuation guarantee charge is not a tax and has no constitutional basis, was to be appealed and heard in the High Court at the end of March 2011. It was noted that the outcome is not yet known and no judgment has been published.

### **2.1.5 ZDDD v Cmr of Taxation [2011] AATA 3**

This involved breaches of ss 109, 65 and 62 and whether the Commissioner's decision to issue a notice of non-compliance should be set aside. The Tribunal agreed with the Commissioner that the trustee's offer of an enforceable undertaking should not be accepted because it did not seek to rectify the contraventions or put the fund in the position it should have been in but for the contraventions (for example, the undertaking did not take into account that if the fund's money had been invested in arm's length investments, the value of those investments would have increased over time and the fund should be given credit for these increases). There was also no evidence that the trustee's proposal was financially viable.

### **2.1.6 Cmr of Taxation v Newton [2010] FCA 1440**

In this decision that Federal Court agreed with the Commissioner that the AAT had erred in interpreting s 12(11) of the SG Act (ie, whether work is wholly or principally of a domestic or private nature). It was noted that this has now been appealed to the Full Federal Court.

### **2.1.7 An Employee v Federal Cmr of Taxation [2010] AATA 912**

This decision examined whether a payment by an employer under a deed of settlement with an employee was an ETP. The employee had commenced legal action on the basis that (amongst other claims) he suffered a stress disorder due to bullying in his workplace. The Tribunal found that because there was no admission of liability by the former employer, the payment under the settlement could not be "for, or in respect of, personal injury" and was therefore an ETP.

## **2.2 Leasing part of a fund asset and the business real property test**

Where land owned by a superannuation fund is used for multiple purposes under multiple lease arrangements (some for business use and others non-business), the ATO has confirmed that the land will not be business real property (**BRP**) because it is the whole of the land owned by the fund that must be used wholly and exclusively in business. The in-house assets exception in s 71(1)(g) therefore will not apply and the fund will have an in-house asset. (However, the ATO confirms that the part of the land that is leased to a related party will constitute the fund's in-house asset, consistent with the ATO's view in paragraphs 124 and 125 of SMSFR 2009/4.)

At the NTLG it was noted that the ATO's comments in SMSFR 2009/1 that the "underlying" land must be used wholly and exclusively in business is a reference to the land underlying the relevant entity's interest in the land (ie, the owner, being the trustee of the fund, who has a freehold interest). It is therefore the whole of the land that is relevant. These comments had possibly been misinterpreted to refer to the interest in land of the lessee (ie, their leasehold interest). However, the ATO confirmed that it is the owner and not the lessee who is the relevant entity for the purposes of s 71(1)(g).

The Committee agreed that this is the correct application of the law. It was also noted that the only scenario in which partial residential use of a property could meet the BRP test was possibly where a person must reside on the premises in connection with a business (eg, an employee who is on call 24 hours a day and must reside on-site).

### **2.3 In specie payments from a superannuation income stream**

At the NTLG the question was raised as to whether payments from a superannuation income stream which are superannuation lump sums (rather than superannuation income stream benefits) can be paid in specie rather than in cash and, if so, whether there is any minimum payment from an account-based pension that must be paid in cash.

The ATO responded only by saying that these issues will be addressed in an upcoming ruling which is due to be released on 29 June 2011.

Several Committee members stated that they expect the ATO will follow the view in APRA Circular No.I.C.2 that pension payments can only be made in cash. The committee briefly questioned whether the regulations should be amended to allow in specie payments but it was resolved that the Committee await the ATO's ruling before considering this further.

### **2.4 Tax savings amount for anti-detriment deduction**

The ATO has confirmed its view regarding the anti-detriment deduction provisions in s 295-485 of the Income Tax Assessment Act 1997 (ITAA 97) that if a trustee pays only a part of a deceased member's death benefit as a lump sum, the "tax saving amount" (and therefore the anti-detriment deduction) is effectively pro-rated.

The Committee had not considered this in detail but it was noted initially that this appears to be a reasonable approach. It was also noted by the Committee that the ATO's recent statement will not affect how the tax saving amount is calculated (ie, before pro-rating) and that either the audit method or the method in ATO ID 2007/219 could be used.

It was resolved to consider this further after the example provided by the ATO is circulated. [A numerical example has been attached to these minutes as "Annexure A". This is similar to the example provided by the ATO in the NTLG minutes, but uses different figures.]

### **2.5 Recontribution strategies involving untaxed elements**

A question was raised by a NTLG member in September 2010 regarding recontribution strategies involving untaxed elements and the member was asked to provide a detailed example of such a strategy. The NTLG revisited this at the recent meeting after an example was provided.

The hypothetical example involved a public sector superannuation scheme (PSSS) and the member's benefits therefore included an untaxed element. The strategy involved non-concessional contributions being made by the member prior to the member receiving a lump sum. It was suggested that this had the effect of increasing the tax free component pursuant to s 307-150 of the ITAA 97.

The ATO responded only that the strategy does not operate as suggested because benefits paid from a PSSS that represent contributions paid to the scheme as well as contributions from some other source are preserved as two separate interests. The benefit payment is therefore taken to be two separate lump sums. The non-concessional contributions made by the member would not form part of the interest that includes the untaxed element and therefore s 307-150 would not have any effect. The ATO therefore had no comment about Part IVA.

The Committee commented on recontributions strategies more generally. It was noted that the ATO has previously said that where members are over 60 years and benefits are all tax-free, it is difficult to identify any tax benefit for the

purposes of Part IVA. (Even when death benefits are ultimately paid to adult children who will pay tax on the taxable component, it is difficult to identify with certainty the tax benefit.) It was noted by the Committee that in other scenarios (eg, if a member is under 60 years) a once-off recontribution should not be of concern, although a more systematic recontribution strategy (eg, one that is implemented annually) might potentially be of concern.

3. **Sections 67A and 67B**

RJ updated the Committee that the ATO is preparing a ruling on sections 67A and 67B of the SISA. The timing on this ruling is not yet known. The ATO says this is of the highest priority and RJ understands that considerable ATO resources are being deployed.

The ruling will cover the meaning of "single acquirable asset", improvements to property and the nature of a trust relationship (specifically, whether a "bare trust" can exist).

RJ understands that the ATO might be willing to take a favourable approach to "improvements" in the case of properties destroyed by natural disaster, but noted that it does not appear to be possible under the current legislation to distinguish between developments that are undertaken for different purposes (eg, purely voluntary development versus reconstruction after a disaster). RJ also understands that the ATO might not be willing to accept SISFA's view regarding "bare trusts" and, if so, it will be interesting how they address the associated practical and taxation consequences if the holding trust is not a "bare trust".

RJ has also provided the ATO with promotional material from a property strategy group that outlines a concerning approach to SMSF borrowing. The strategy described appears to be both aggressive from a tax viewpoint and non-SIS compliant. This has been provided as an example of the concerning advice being provided to SMSFs about borrowing. RJ is meeting with the ATO and will suggest the ATO take steps to discourage these practices.

4. **Excess contributions tax (ECT) – the doctrine of mistake**

RJ briefly discussed two responses to ECT objections he has received on behalf of his clients. The ATO has rejected the taxpayers' arguments which relied on the doctrine of mistake. If successful, these would have had the result that the contributions in question were void because they were made under a mistake. In RJ's view, the ATO has possibly misunderstood the doctrine, the principles of *David Securities* and in particular the concept of 'voluntariness'.

RJ had been waiting for the ATO's response for some time and the two responses received might indicate that the ATO has now formed a view internally. Other taxpayers might also receive responses soon if they have relied on similar arguments.

RJ's clients will not be seeking any further review because of cost constraints. However, it would be useful for a taxpayer to contest this issue in the courts because the ATO appears to be unmoved on arguments about the doctrine of mistake.

5. **Conversion to a regulation 13.22C compliant trust**

It was agreed that the Committee should proceed with preparing a submission about conversion to a regulation 13.22C compliant trust. Although RJ agrees with the ATO's technical view (as outlined at the September 2010 NTLG meeting), it was noted that there is an alternative technical view and also strong policy reasons for allowing all funds with pre-August 1999 investments to rely on the regulation 13.22C in-house assets exception to now make further investments.

It was agreed that the submission should also be forwarded to the SISFA policy committee with a suggestion they forward it to Treasury.

**6. SMSF return amendment request**

A request had made by SISFA that the SMSF return be amended to cater for situations where part of a contribution made in June of one income year is allocated within 28 days of the end of the month (ie, in July of the following income year). The present format of the return does not recognise such allocations and could result in an ECT liability being imposed if it appears all of a contribution is "made" in the month of June.

The ATO has responded that this is not a matter for the ATO but they have referred it to the appropriate body for consideration.

**7. Report from SMSF Working Group meeting of 5 April 2011**

RJ reported that the SMSF Working Group had met to discuss competency requirements for SMSF auditors. It has been confirmed that there will be an exam set for auditors and that all professional bodies will have an opportunity to provide input for the setting of the exam. (RJ noted that when this was discussed at the SISFA Victorian Chapter Meeting of 4 April 2011, several attendees were of the opinion that setting any kind of exam might not be an appropriate measure. However, it is now understood that an exam will definitely be introduced.) There will be a transitional period for auditors who complete at least 20 audits in 2011-12; these auditors will have a 12 month period in which to sit the exam.

There will also generally be a minimum number of audit hours and number of audits that must be completed. It has been noted that of the current auditor population, only 12% would meet the proposed new minimum standards. It is therefore expected that these measures will generate significant discussion once they are made public.

The Committee agreed that auditors undertaking a very low number of audits (eg, less than 5 per year) should not be able to audit SMSFs. However, the proposed new measures will need to be carefully implemented. In particular, RJ will mention to the ATO that in his experience (eg, in setting specialist accreditation exams for the Law Institute of Victoria) sitting an exam is a daunting prospect for many professionals and it is important that otherwise capable persons are not deterred from becoming or continuing to work as SMSF auditors.

**8. Other business**

The Committee discussed several items in the minutes of the last Committee meeting and noted that item 3.4 of "other business" had been resolved. It was agreed that:

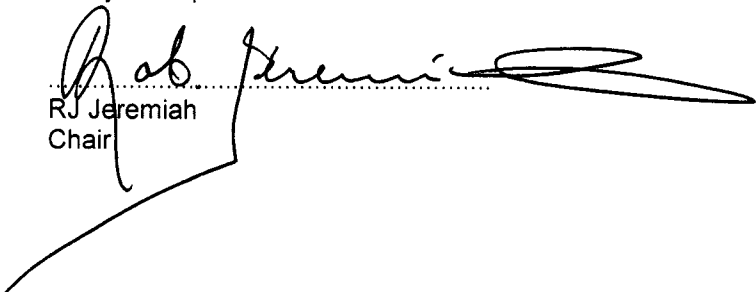
- All Committee members would revisit DK's emails regarding pension reversion in situations other than the death of a pensioner (item 3.1 of those minutes).
- PB would report back at the next meeting several issues in relation to allocations from reserves (item 3.5 of those minutes).

It was also noted that DK has recently prepared a submission on behalf of SISFA regarding the \$500,000 maximum benefits limit proposed by the Government in order to qualify for the higher concessional contributions cap.

It was agreed that the next Committee meeting should be held in three to four weeks time in May 2011. Patricia Close would be in contact shortly to arrange this.

**9. Close**

RJ closed the meeting at approximately 12.55pm AEST.

  
RJ Jeremiah  
Chair

### Annexure A

**Application of s 295-485 where part of a death benefit is paid as a lump sum. (Based on the example provided by the ATO in NTLG minutes of 21 March 2011.)**

- Sally passes away with total member benefits in her fund of \$170,000.
- For simplicity, it is assumed that this represents \$200,000 made as concessional contributions, less the 15% tax incurred by the trustee on those contributions. (Earnings and capital growth have been ignored.)
- The trustee proposes to pay her death benefit as follows:
  - A lump sum of \$20,000; and
  - A pension with the remaining balance (\$150,000).

The "tax saving amount" (TSA) is calculated as follows.

- If the full amount of Sally's \$170,000 benefit had been paid as a lump sum, then pursuant to s 295-485(1) the trustee would have needed to increase the lump sum by \$30,000 in order for the lump sum to represent what the trustee could have paid had no contributions tax been payable (ie, \$200,000). The TSA would therefore be \$30,000 in this event.
- However, because only \$20,000 of her benefit is paid as a lump sum, the TSA needs to be pro-rated as follows:

$$\$30,000 \times (\$20,000/\$170,000) = \$3,529$$

- The trustee must therefore pay a total lump sum of  $\$20,000 + \$3,529 = \$23,529$ .
- In applying the formula in s 295-485(3), the deduction available is as follows:

$$\$3,529 \div 15\% = \$23,529$$

(Note, figures are rounded in this example.)