THIRTEEN WENTWORTH SELBORNE

Self Managed Superannuation Fund Tax Landscape

A paper presented by Denis Barlin
Legalwise Seminars
"SMSF's: Property, Death and Taxes"
Monday, 30 March 2015

Denis Barlin
Barrister
13 Wentworth Selborne Chambers
174-180 Phillip Street
SYDNEY NSW 2000

All references in this paper are to:

- The *Income Tax Assessment Act 1936* (Cth) (**'the 1936 Act'**);
- The *Income Tax Assessment Act 1997* (Cth) (**'the 1997 Act'**);
- The *Superannuation Industry (Supervision) Act 1993* (Cth) (**'the SIS Act'**); and
- The *Superannuation Industry (Supervision) Regulations 1994* (Cth) (**'the SIS Regulations'**).

1 Superannuation contributions caps 4
Concessional contributions caps 5
Non-concessional contributions cap 5
Non-concessional bring-forward cap 5
Other Super thresholds 5
2 Deductions for personal superannuation contributions 6
3 Division 293 of the *1997 Act* surcharge 7
4 Taxation death benefits paid to "dependents" 8
Superannuation lump sum benefits 8
Superannuation income stream benefits 9
Benefit paid from element untaxed from the Fund 9
5 Taxation death benefits paid to "non-dependents" 9
6 Section 35 of the *Succession Act 2006 (NSW)* 10
7 Excess contributions - *Taxation and Superannuation Laws Amendment (2014 Measures No. 7) Bill 2014* 11
8 Gearing in superannuation funds 12
Prohibition against borrowing in superannuation funds 13
The legal relationships required to obtain the borrowing carve-out 16
9 Estate planning and superannuation 20
What is a 'death benefit'? 20
Payment of death benefits 20
Timing of payment of death benefits 21
Lump sum payments 21
Income streams 22
Who is a dependent? 22
Interdependency relationship 23
Life insurance and superannuation funds 24
Binding nominations in the context of self-managed superannuation fund 25
10 Superannuation proceeds trusts 29
11 Superannuation and Stamp Duties 29
Transfer as a result of change in superannuation membership 30
Transfer to a self managed superannuation fund 31
Transfer of property to trustees or custodians of superannuation funds 32
12 *Ioppolo & Anor v Conti & Anor* [2015] WASCA 45 32
13 *Deputy Federal Commissioner of Tax (Superannuation) v Graham Family Superannuation Pty Ltd & Ors* [2014] SCA 1101 (Buchanan J) 39
14 *Olesen v Early Sunshine Pty Ltd* [2015] FCA 12 42

1 Superannuation contributions caps

1.1 From 1 July 2007, contributions for which a deduction is allowed are referred to as a 'concessional contributions'. Concessional contributions, whether made by the member or an employer, are included in the assessable income of the superannuation fund. Undeducted contributions are referred to as 'non-concessional contributions'.

1.2 Generally speaking, concessional contributions are either employer contributions and deductible personal superannuation contributions that are included in the assessable income in the recipient's superannuation fund.

1.3 Self-employed or substantially self-employed persons may be entitled to a deduction for contributions into a complying superannuation fund or an RSA. Generally speaking, being substantially self-employed means that the individual earns less than 10% of their income in a year from employment-related activities. If the individual satisfies the deduction conditions, then there is no limit on the amount of deductible contributions that may be made. However, excess contributions tax may be imposed if the contributions exceed the contributions cap for the year.

1.4 That is, despite the full deductibility of 'concessional contributions' to the contributor, there are limits on the amount of concessional contributions that can benefit from concessional treatment when paid to the fund (i.e. subject to 15% tax when contributed into the fund and potentially 0% when paid from the fund as a superannuation benefit). Concessional contributions which exceed the cap are subject to excess concessional contributions tax of 31.5%.

1.5 Similarly, excess contributions tax at 46% is imposed on non-concessional (i.e. undeducted) contributions where those contributions exceed the relevant cap amount for the year. It should be noted that non-concessional contributions are subject to no tax when contributed into a superannuation fund, and may be subject to no tax when paid out as a superannuation benefit.

Contribution caps for the financial year ended 2014/2015:

Type of contribution	Age requirement	Cap amounts	Tax on contributions over the caps
Concessional	Less than 50 years old	$30,000	31.5% (plus 15% which is already paid by the fund) AND Amounts over the concessional cap count towards the non-concessional contribution cap
	49 years old or more (on 30 June 2013)	$35,000	As above
Non-	65 years old or more (to contribute you must satisfy	$180,000 (can bring forward 3	46.5%

concessional	certain criteria)	years)	
	Less than 65 years old	$180 (cannot bring forward 3-year period)	46.5%

1.6 The Commissioner of Taxation has announced the superannuation rates and thresholds to apply in respect of the 2014/15 financial year.

Concessional contributions caps

1.7 The concessional contributions cap has increased to $30,000 for 2014/15, up from $25,000.

1.8 The special concessional contributions cap for older people remains at $35,000, but will apply to anyone aged 49 or over on 30 June 2013.

1.8 Concessional contributions include employer contributions (including contributions made under a salary sacrifice arrangement); and personal contributions claimed as a tax deduction by a self-employed person.

Non-concessional contributions cap

1.9 The non-concessional contributions cap has increased to $180,000, up from $150,000.

1.10 Non-concessional contributions include personal contributions for which you do not claim an income tax deduction.

Non-concessional bring-forward cap

1.11 The bring-forward non-concessional cap has increased to $540,000, up from $450,000.

1.12 People aged less than 65 years on 1 July in a financial year may be able to make non-concessional contributions of up to three times their non-concessional contributions cap over a three year period - this is known as the “bring forward” rule.

1.13 The bring-forward cap is three times the non-concessional contributions cap of the first year. If you brought forward your contributions in 2014/15, it would be 3 x $180,000 = $540,000.

1.14 To maximise non-concessional contributions, the $150,000 contribution could have been made in the 2013/14 year and $540,000 of contributions after 1 July 2014. However, care should be taken however, to ensure that the $150,000 cap in this financial year is not accidently exceeded, triggering the ‘bring forward’ provisions as the consequences can be serious.

Other Super thresholds

1.15 Capital Gains Small Business contributions cap – increased to $1,355,000 from $1,315,000

1.16 Low rate tax cap – increased to $185,000 from $180,000. For people aged less than 60 years old who are retired and wish to draw a lump sum from super, this is the amount that can be withdrawn at 0% tax; amounts thereafter are taxed at 15% plus the Medicare levy.

1.17 Account-based pension drawdown rates – no change.

1.18 Maximum SG contributions base – increased to $49,430 from $48,040 per quarter.

1.19 Government Co-Contribution lower threshold – increased to $34,488, up from $33,516. (This is the threshold above which the maximum co-contribution amount of $500 begins to taper.)

1.20 Government Co-Contribution higher threshold – increased to $49,488, up from $48,516. This is the threshold above which the co-contribution will not be paid.

1.21 Low income superannuation contribution – $37,000 income threshold is not indexed. (The Federal Government has introduced legislation which, if passed by the Senate, will abolish this co-contribution in respect of 2013/14 and subsequent financial years.)

2 Deductions for personal superannuation contributions

2.1 From 1 July 2007, individual taxpayers have been entitled to a deduction for personal superannuation contributions if the conditions in Subdivision 290-C of the *1997 Act* are satisfied. Before 1 July 2007, the conditions relating to the deductibility of personal superannuation contributions were contained in the (former) section 82AAS and 82AAT of the *Income Tax Assessment Act 1936 (Cth)*.

2.2 From the income tax year ended 30 June 2008, there have been no limits on the amount of the deduction, as age-based limits that applied pre-30 June 2008 have been abolished. However, taxpayers may be liable to excess contributions tax if the deductible contributions made for or by the taxpayer in the year exceeded the concessional contributions cap. Section 290-10 of the *1997 Act* provides that a taxpayer cannot deduct an amount paid as a contribution to a complying superannuation fund except as provided by Division 290 of the 1997 Act. Further, subdivision 290-C of the *1997 Act* does not apply to a contribution that is:

- A roll-over superannuation benefit, a superannuation lump sum that is paid from a foreign superannuation fund, or an amount transferred from a scheme that has never been, an Australian superannuation fund or a foreign superannuation fund (section 290-5 of the *1997 Act*);
- A directed termination payment paid into a superannuation plan by an employer under transitional arrangements that apply until 30 June 2012. See *Income Tax (Transitional Provisions) Act 1997* at section 290-10.
- Section 290-150(2) of the *1997 Act* provides that a taxpayer is eligible for a deduction for its personal superannuation contributions if section 290-155, 290-160 (if applicable), 290-165 and 290-170 of the 1997 Act is satisfied.
- Subsection 290-150(3) of the *1997 Act* provides that the deduction is allowable for the income year in which the contribution is made.

2.3 Broadly speaking, a personal superannuation contribution is deductible if the contributions are made to a complying superannuation fund (or a Retirement Savings Account (RSA) for the purposes of providing superannuation benefits for the taxpayer, even if the benefits are payable to the taxpayer’s “SIS dependence” (as defined in the *SIS Act*).

2.4 Further, the conditions in sections 290-160, 290-165 and 290-170 of the 1997 Act (if applicable) must also be satisfied, being:

- If the taxpayer holds an office of appointment, performs functions or duties, engages in work or does acts or things, and this results in the taxpayer being treated as an "employee" for superannuation guarantee purposes in the year that the contribution is made, then less than 10% of the total of the taxpayer's assessable income and reportable fringe benefits for the income year, must be attributable to those activities. This is the "maximum earnings as an employee" contained in section 290-160 of the 1997 Act;

- Section 290-165 of the 1997 Act creates an "age-related" space condition – if the taxpayer is under the age of 18 at the end of the income year in which the contribution is made, the taxpayer must have derived income in the year from carrying on a business or from employment-related activities;

- Subsection 290-165(2), being another "age-related" condition – the contribution must be made by the 28th day after the month in which the taxpayer turns 75;

- Section 290-170 of the *1997 Act* – notice requirements – the taxpayer must notify the fund, trustee or RSA provider in writing that he or she intends to claim the deduction and the trustee or RSA provider must acknowledge receipt of the notice.

2.5 Subsection 290-150(4) of the *1997 Act* provides that if the contribution is the CGT exempt amount arising from the disposal of an active asset of a small business pursuant to Division 152 of the 1997 Act, and the contributor is under the age of 55, the contribution is not deductable to the extent that it is trivial to the exempt capital gain.

3 Division 293 of the *1997 Act* surcharge

3.1 Division 293 of the 1997 Act contains an additional rate of 15% over tax on individuals whose income and relevantly concessionally taxed superannuation contributions (referred to as low tax contributions) is more than $300,000 per year.

3.2 Income for Division 293 tax purposes includes taxable income, reportable fringe benefits, reportable superannuation contributions and total net investment losses. A member's low tax contributions includes employer and member "before tax" contributions and notional employer contributions for defined benefit members. A member's low tax contributions do not include non-concessional contributions and concessional contributions that are subject to excess concessional contributions tax or refunded excess contributions that are disregarded by the Commissioner of Taxation for the purposes of the excess contributions tax.

3.3 If applicable to a member, tax pursuant to Division 293 is applies to the lower of:

- member's low tax contributions; and
- the sum of the member's income for surcharge purposes (less reportable superannuation contributions and low tax contributions above the $300,000 threshold).

3.4 Division 293 of the 1997 Act subjects an individual to additional tax if the sum of their "income for surcharge purposes" and their concessional contributions for the year exceeds $300,000.

3.5 If an individual's income for surcharge purposes is less than $300,000, but the inclusion of the relevant concessional contributions pushes them over the $300,000 threshold, Division 293 tax applies to the part of the contributions that is in excess of the threshold.

4 Taxation death benefits paid to "dependents"

Superannuation lump sum benefits

4.1 Section 302-5 of the *1997 Act* provides that:

> *A superannuation lump sum that you received because of the death of a person of whom you are a death benefit dependent is not assessable income and is not except income.*

4.2 This is whether the lump sum is paid from an "element taxed" or an "element un-taxed" in the Fund.

4.3 The SIS Regulation 6.21(2)(b) of the SIS Regulations provides that where a death benefit is paid in the form on an annuity or pension to a child of a Deceased member, it must be cashed as a lump sum no later than when the child reaches 25 years of age unless the child has a permanent disability.

4.4 Section 303 of the 1997 Act provides that:

> *"(1) A superannuation lump sum that you received from a complying superannuation plan is not assessable income and is not exempt income if:*
> *(a) superannuation lump sum arises from the commutation of a superannuation income stream; and*
> *(b) any of these conditions are satisfied:*
> *(i) you are under 25 and you received a superannuation lump sum;*
> *(ii) the commutation takes place because you turned 25;*
> *(iii) you are permanently disabled when you received the superannuation lump sum; and*
> *(c) you had received one or more superannuation income stream benefits from the superannuation income stream before the commutation because of the death of a person of whom you are a death benefit dependent.*
> *(2) Subsection (1) applies despite Divisions 301 and 302.*

Superannuation income stream benefits

4.5 The taxation of superannuation income stream death benefits which are paid to a dependent will depend on whether they are paid from an "element taxed", or an "element untaxed" from the fund.

4.6 Pursuant to section 302-65 of the 1997, a superannuation income stream death benefit paid to a dependent from an "element taxed" in a fund is tax-free if:

- the recipient (i.e. the dependent) is aged at least 60 when the benefit is received; or
- the deceased was aged at least 60 when the deceased died.

4.7 Pursuant to sections 302-70 and 302-75 of the 1997 Act, a superannuation income stream death benefit if taxed as follows where both the dependent and the deceased are aged over 60 at the time of death:

- the tax-free component of the income stream is tax-free (section 302-70 of the 1997 Act);
- the taxable component is assessable income, but the dependent is entitled to a tax offset equal to 15% of the taxable component (section 302-75 of the 1997 Act); and
- when the recipient turned 60, the income stream is tax-free.

Benefit paid from element untaxed from the Fund

4.8 In the event that the taxable component of a superannuation income stream death benefit paid to a dependent includes "element untaxed" in the Fund, the taxation of the "element untaxed" in a Fund depends on the age of the deceased:

- in the event that the deceased or the dependent was aged at least 60, the dependent is entitled to an offset of 10% of the element untaxed in the fund;
- if neither the dependent or the Deceased were aged 60, the "element untaxed" in the Fund is included in the dependent's assessable income and taxed at ordinary rates (see all of sections 302-80, 302-85 and 302-90 of the 1997 Act.

5 Taxation death benefits paid to "non-dependents"

5.1 Regulation 6.21(2A) of the SIS Regulations provides that a person who is not a "dependent" of the deceased is not able to receive a superannuation income stream benefit.

5.2 Broadly speaking, a superannuation death benefit paid to a non-dependent is treated as follows:

- Section 302-140 of the 1997 Act provides that the "tax free component" is not subject to tax.
- Section 302-145 of the 1997 Act provides that the taxable component is included in the assessable income, with the tax offset to ensure that:
  - the rate of tax on the element taxed in the fund does not exceed 15%; and
  - the rate of tax on the element untaxed in the fund does not exceed 30%.

6 Section 35 of the *Succession Act 2006 (NSW)*

6.1 Section 35 of the *Succession Act 2006 (NSW)* may have unintended taxation consequences in the event that a death benefit is paid through an estate.

6.2 Regulation 6.21 of the *Superannuation Industry (Supervision) Regulations 2004 (Cth)* (SIS Regulations) provides that *"... a member's benefits in a regulated superannuation fund must be cashed as soon as practicable after the member dies."* The form in which a benefit may be cashed is provided for in regulation 6.21(2) of the SIS Regulations, which includes a single lump sum (or an interim lump sum or one or more pensions).

6.3 Regulation 6.22 (2) of the SIS Regulations provides that a death benefit may be paid to either:

- the members legal personal representative;
- one or more of the member's dependents.

6.4 That is, a death benefit, being a lump sum, may be paid to a member's legal personal representative, which means it is in effect paid into the estate. Of course, it is not automatically the case that a death benefit forms part of the estate (see for example *McFadden v Public Trustee for Victoria* [1981] 1 NSWLR 15).

6.5 However, if a death benefit is paid into an estate then section 35 of the *Succession Act* needs to be considered. That section provides:

> *(1) If a disposition of property is made to a person who dies within 30 days of after the testator's death, or, if that or another person for survival appears in the Will, or, if that or another period for survival appears in the Will, the Will is to take effect as if the person had died immediately before the Testator; or*
> *(2) This section does not apply if a contrary intention appears in the Will;*
> *(3) A general requirement or condition that a beneficiary survive the testator does not indicate contrary intention for the purpose of this section.*

6.6 Section 35 of the *Succession Act* comes into play when considering whether the final recipient of the death benefit (or parts of the death benefit) are death benefit dependents. Section 302-10 of the 1997 Act provides that:

> *(1) This section applies to you if:*
>
> *(a) You are the trustee of a deceased estate; and*
> *(b) You receive a superannuation death benefit in your capacity as trustee.*
>
> *(2) To the extent that one or more beneficiaries of the estate who were death benefit dependents of the deceased have benefited or may be expected to benefit, from the superannuation death benefit:*
>
> *(a) the benefit is treated as if it had been paid to you as a person who was a death benefits dependent of the deceased; and*
> *(b) the benefit is taken to be income to which no beneficiary is presently entitled.*

> *(3) To the extent that one or more beneficiaries of the estate who were not death benefits dependents of a deceased have benefited or may be expected to benefit, from the superannuation death benefit:*
>
> *(a) the benefit is treated as if it had been paid to you as a person who was not a death benefits dependent of the deceased; and*
> *(b) the benefit is taken to be income to which no beneficiary is presently entitled.*

6.7 That is, if a superannuation death benefit is paid to an estate, then the executor of that estate needs to determine whether the ultimate recipient of the death benefit is a "death benefits dependent" or not. If the ultimate recipient is not a death benefit dependent, then the taxable component (taxed element) (being the concessional contributions of the deceased member) is subject to tax at 16.5%. Alternatively, if the actual or expected recipient of the death benefit dependent is a "death benefit dependent", then the death benefit will be tax free.

6.8 For example, if in the deceased's Will, the whole of the estate goes to the deceased's spouse, (who is a "death benefit dependent"), then any death benefit paid by a trustee of a superannuation fund into the estate should not be subject to tax. This is because the death benefit will, (or at least is expected to) be paid to the spouse (the death benefit dependent).

6.9 However, in the event that section 35 of the *Succession Act* is not displaced, and the spouse is deemed to have predeceased the deceased on the basis of section 35 (for example if section 35 has not been displaced, and the surviving spouse does not survive the predeceasing spouse by 30 days), then it cannot be said that it is expected that the surviving spouse will receive the superannuation death benefit.

6.10 However, if section 35 is displaced in the Will (for example, if the Will specifically says that section 35 of the *Succession Act* does not apply), and the surviving spouse does not survive the former spouse by 30 days, then subject to the period in which the death benefit is within an unadministered estate, it may just be that it is expected that the surviving spouse does benefit, or that it goes to the surviving spouses estate and dealt with that way (that is tax free).

7 Excess contributions - *Taxation and Superannuation Laws Amendment (2014 Measures No. 7) Bill 2014*

7.1 The *Taxation and Superannuation Laws Amendment (2014 Measures No.7) Bill 2014* has been passed without amendment and awaits Royal Assent. Broadly speaking, the Bill does three things:

- Contains measures which affect:
  (a) excess non-concessional contributions;
  (b) superannuation fund mergers;
  (c) provides minor miscellaneous tax and superannuation amendments.

7.2 In relation to excess non-concessional contributions, the Bill provides that an individual who has non-concessional contributions in excess of their cap, can elect to release an amount which is:

- equal to those excess contributions; plus

- 85% of the associated earnings amount for those contributions from their superannuation.

7.3 All of the associated earnings amount is to be included in the individual's assessable income in the year the excess contribution arose and is taxed at the individual's marginal tax rate.

7.4 The individual will be entitled to a non-refundable tax offset equal to 15% of the associated earnings amount that is included in their assessable income.

7.5 Currently, tax is applied in relation to excess non-concessional contributions. The tax benefit received on the excess contribution is not subject to tax. Further, the tax is applied at the top marginal tax rate regardless of the individual's marginal tax rate. The same treatment applies irrespective of whether a breach of the cap is intentional or inadvertent.

7.6 The proposed amendments to the excess non-concessional contributions were announced in the 2014-15 Federal Budget and also the Assistant Treasurer's Media Release entitled "Superannuation Excess Contributions Tax" date 13 May 2014.

7.7 Excess non-concessional contributions tax will not be imposed on an excess contribution to the extent that they are released from superannuation, or where the value of an individual's remaining superannuation interest in nil. However, excess non-concessional contributions tax will still be imposed on excess non-concessional contributions that remain in a superannuation fund.

7.8 The measure provides for a process that addresses inadvertent breaches of contributions caps where the error would result in a disproportionate penalty.

7.9 The measure applies from the income tax year ended 30 June 2014 and later financial years. The measures are retrospective, and they ensure that no taxpayer need face a disproportionate penalty for exceeding their excess non-concessional contribution cap after the date of the announcement (being 13 May 2014).

8 Gearing in superannuation funds

8.1 On 3 November 2006, the Minister for Revenue and Assistant Treasurer, the Hon. Peter Dutton, M.P. in Press Release No. 078 ('**the Press Release**') announced that instalment warrants contain an element of borrowing, and are therefore a prohibited investment for superannuation funds. This is notwithstanding longstanding practice and that '*Over a number of years instalment warrants have been marketed to superannuation funds — particularly to self managed superannuation funds (SMSFs).*'[1]

[1] See also paragraph 3.6 of the Explanatory Memorandum.

8.2 Further, both the Australian Prudential Regulation Authority and the Australian Taxation Office (collectively '**the Regulator**'), both being the regulators of the superannuation industry, had previously formed the view that instalment warrants did not involve a 'borrowing'.

8.3 Indeed, the Regulator had issued guidelines as to what constitutes a borrowing for the purposes of section 67 of the SIS Act. The Regulator, in Superannuation Circular No II.D.4 entitled *Borrowing by superannuation entities* ('**the Borrowings Circular**'), considered that not all liabilities incurred by a superannuation fund would be a 'borrowing'. As an example, the Regulator at paragraph 16 of the Borrowings Circular distinguished between 'borrowings' and other debts:

> *'… in general ... a borrowing involves receiving a payment from someone in the context of a lender/borrower relationship on the basis that it will be repaid. A transaction that gives rise to a debtor/creditor relationship does not necessarily give rise to a lender/borrower relationship and hence does not necessarily represent a borrowing for the purpose of the restriction.'*

8.4 Further, the Regulator, at paragraph 17 of the Borrowings Circular, provided examples of borrowings, which includes a loan (whether secured or unsecured) and a bank overdraft (in normal circumstances). However, at paragraph 19 of the Borrowings Circular, the Regulator considered that the following would not be a borrowing:

> *'… amounts paid on behalf of, or owed by, regulated superannuation funds … [that include] … the purchase by a trustee of property where ownership of the property passes to the trustee before the instalments are finalised. Under this example, an investment in **endowment warrants or instalment receipts** may not be considered borrowing. It is necessary to check the obligations that lie with the purchaser to meet the instalment(s), as these determine whether the investment is a borrowing. Where the **remaining instalment(s) is not "compulsory"** and the **warrant / receipt holder receives the value of the warrant / receipt (less handling or sales costs)** on "default", APRA considers the warrant / receipt does not constitute a borrowing.'* [emphasis added]

8.5 Further, the Regulator at paragraph 6 of the Borrowings Circular gives examples of endowment warrants and instalment warrants as not involving borrowings by a Fund. The Regulator reiterated the views that it expressed in the Borrowings Circular regarding instalment warrants in the *Guidelines on Instalment Warrants for Superannuation Trustees* ('**Guidelines**'):

> *'… prohibition on borrowing was developed before many currently available geared products had been developed … The regulators had previously taken the view that a superannuation fund investment in an instalment warrant **may not** constitute a borrowing under section of the SIS Act.'* [emphasis added]

<u>Prohibition against borrowing in superannuation funds</u>

8.6 Notwithstanding the change in the Government's view as announced in the Press Release, the *Tax Laws Amendment (2007 Measures No 4) Bill 2007* (Cth) ('**the Bill'**) amended the SIS Act so as to ensure that investments in instalment warrants do not breach the prohibition against trustees of regulated superannuation funds from borrowing. Subsection 67(1) of the SIS Act expressed the prohibition, by providing that:

'… a trustee of a regulated superannuation fund must not

(a) borrow money; or

(b) maintain an existing borrowing of money.'

8.7 However, there are a number of exceptions to the prohibition contained in subsection 67(1) of the SIS Act, which includes (as a result of the enactment of the Bill) the former subsection 67(4A) of the SIS Act. Subsection 67(4A) of the SIS Act was repealed by *Superannuation Industry (Supervision) Amendment Act* 2010 which commenced on 7 July 2010. The former subsection 67(4A) was replaced by sections 67A and 67B.

8.8 Sections 67A of the SIS Act provide:

'(1) Subsection 67(1) does not prohibit a trustee of a regulated superannuation fund (the RSF trustee) from borrowing money, or maintaining a borrowing of money, under an arrangement under which:

(a) the money is or has been applied for the acquisition of a single acquirable asset, including:

(i) expenses incurred in connection with the borrowing or acquisition, or in maintaining or repairing the acquirable asset (but not expenses incurred in improving the acquirable asset); and

Example: Conveyancing fees, stamp duty, brokerage or loan establishment costs.

(ii) money applied to refinance a borrowing (including any accrued interest on a borrowing) to which this subsection applied (including because of section 67B) in relation to the single acquirable asset (and no other acquirable asset); and

(b) the acquirable asset is held on trust so that the RSF trustee acquires a beneficial interest in the acquirable asset; and

(c) the RSF trustee has a right to acquire legal ownership of the acquirable asset by making one or more payments after acquiring the beneficial interest; and

(d) the rights of the lender or any other person against the RSF trustee for, in connection with, or as a result of, (whether directly or indirectly) default on:

(i) the borrowing; or

(ii) the sum of the borrowing and charges related to the borrowing;

are limited to rights relating to the acquirable asset; and

Example: Any right of a person to be indemnified by the RSF trustee because of a personal guarantee given by that person in favour of the lender is limited to rights relating to the acquirable asset.

(e) if, under the arrangement, the RSF trustee has a right relating to the acquirable asset (other than a right described in paragraph (c))--the rights of the lender or any other person against the RSF trustee for, in connection with, or as a result of, (whether directly or indirectly) the RSF trustee's exercise of the RSF trustee's right are limited to rights relating to the acquirable asset; and

(f) the acquirable asset is not subject to any charge (including a mortgage, lien or other encumbrance) except as provided for in paragraph (d) or (e).'

8.9 Further, sections 67B of the SIS Act deals with replacement assets.

8.10 A summary of the key features of the former subsection 67(4A) of the SIS Act is provided in paragraph 1.5 of the Explanatory Memorandum for the *Superannuation Industry (Supervision) Amendment Act* 2010:

> *'Schedule 1 of this Bill amends the Act to make sure that superannuation fund assets are protected in the event of a default on a limited recourse borrowing arrangement by ensuring that:*

- *the recourse of the lender and of any other person against the superannuation fund trustee for default on the borrowing is limited to rights relating to the acquirable asset;*
- *the asset within the arrangement can only be replaced in prescribed circumstances that arise from owning the original asset; and*
- *the borrowing is referable and identifiable only over a single asset (excluding money) or in prescribed circumstances, a collection of assets which are identical and are treated as a single asset.*

8.11 A comparison of the key features of the new sections 67A and 67B with the former subsection 67(4A) of the SIS Act is also provided in the Explanatory Memorandum:

New law	Current law
Explicitly defines the interpretation of acquirable asset in the singular.	While the Act refers to 'asset' in the singular, it is possible to interpret asset in the plural.
Ensures that the recourse of the lender or of any other person against the superannuation fund trustee for default on the borrowing is limited to rights relating to the acquirable asset.	The Act limits the rights over the original asset in terms of the direct lender and associated borrowing only.
Limits borrowing arrangements to a single asset or a collection of identical assets together treated as a single asset.	Allows borrowing arrangements over multiple assets which may permit the lender to choose which assets are sold in the event of a default on the loan.
Clearly defines circumstances under which assets can be replaced.	Allows arrangements where the asset subject to the borrowing can be replaced at the

	discretion of the trustee or the lender.

<u>The legal relationships required to obtain the borrowing carve-out</u>

8.12 It is essential to consider the legal relationships that arise when seeking to avail oneself of the borrowing carve-out in sections 67A and 67B of the SIS Act. The provisions require the following conditions to be satisfied:

Condition	Description
One	A trustee of a superannuation fund borrows money (or indeed maintains a borrowing of money).
Two	The asset that has been acquired by the borrowed money.
Three	The asset that has been acquired is held on trust so that the trustee of the superannuation fund has a 'beneficial interest' in the asset.
Four	The trustee of the superannuation fund has an option (i.e. a right to acquire) the 'legal ownership' by making further (instalment) payments.
Five	The right of the lender is limited in recourse – to the asset acquired and held by the trustee.
Six	If, under the arrangement, the trustee of a superannuation fund has a right relating to the asset (other than a right to acquire the underlying asset) – the rights of the lender against the trustee of the superannuation fund are limited to rights relating asset.

8.13 That is:

- The trustee of the superannuation fund borrows to acquire the underlying asset (i.e., the '**Investor**');
- The trustee of the superannuation fund needs to have the 'beneficial interest' in the underlying asset;
- The underlying asset is held on trust (indeed – bare trust) for the benefit of the trustee of the superannuation fund (held by a '**Security Trustee**');
- The trustee of the superannuation fund has an option to acquire the underlying asset after paying the loan amount;
- The lender's rights with respect to the borrowing are limited in recourse, to the underlying asset;

- Any rights that the trustee of a superannuation fund has to the underlying asset (except the option to acquire) may be subrogated in the lender, but only to the extent that the rights apply to the underlying asset.

8.14 The Security Trustee needs to hold the legal title in the underlying property. The Security Trustee acts as a 'bare trustee' with respect to the underlying property, as the Security Trustee does no more (under the trust relationship) than hold the legal title in the underlying property. It is also essential from a taxation perspective (see discussion below) that the relationship as between the Security Trustee and the Investor with respect to the underlying property is a 'bare trust' - i.e. the Investor is 'absolutely entitled' to the underlying asset and the Security Trustee has no active duty with respect to the underlying asset.

8.15 There are a number of contractual relationships that need to be established. A lender / borrower relationship needs to be established as between the lender and the Investor. Under that relationship, the Security Trustee is prohibited from dealing with the underlying asset on behalf of the Investor, unless the Security Trustee is required to do something which involves the discharge of the loan (for example):

- the lender exercises a power of sale with respect to the underlying asset;
- the Investor pays the outstanding amount and the legal title in the underlying asset transferred to the Investor; or
- the Investor wants to dispose of the underlying asset and repay the outstanding loan.

8.16 It needs to be ensured that the only right that the lender has (including with respect to the repayment of the loan) is limited to the underlying asset. None of the other assets of the Investor can be at risk. As a result, all of the Investor, the Security Trustee and the lender need to enter into a contractual relationship.

8.17 Further, and in some situations, the Security Trustee may be granted a power of attorney by the Investor with respect to the underlying asset, until the borrowing is discharged and the legal title is transferred to the Investor.

8.18 The Investor needs to be able to acquire the legal title in the underlying property at any time.

8.19 Product Ruling PR 2005/96 entitled *Income tax: tax consequences of investing in ABN AMRO Rolling Instalment Warrants IZY Series 2005 Product Disclosure Statement – Cash Applicants and Secondary Market Purchasers* (withdrawn) ('**PR 2005/96**')[2] outlines the arrangements and the participants involved in the particular warrant product. Paragraphs 18 to 20 of PR 2005/96 outline the participants in the product:

> *'18. ABN AMRO …* [i.e. the financier] *… is the Issuer of the ABN AMRO IZY Rolling Instalments. ABN AMRO is also the provider of the Loans to Investors to fund the acquisition of the Underlying Parcel …* [i.e. the asset to be held subject to the warrant arrangement] ….

[2] Paragraph 20 of PR 2005/96 provides that the '*… Investors may be individuals, companies, trusts or superannuation funds*'.

19. ABNED Nominees Pty Limited … [i.e. the 'bare' trustee in the warrant relationship] … holds the legal title to the Underlying Parcel as Security Trustee and as nominee for the Investor.

20. The Investors may be individuals, companies, trusts or superannuation funds.'

8.20 Sub-paragraph 17(b) of PR 2005/96 provides that:

> *'Under a Cash Application, a Cash Applicant …* [e.g. a trustee of a superannuation fund] *… pays the First Payment …* [i.e. the initial 'instalment'] *… and draws down the Loan made by ABN AMRO …* [i.e. the financier]. *The First Payment and the Loan Amount is applied toward the purchase of the Underlying Parcel …* [i.e. the asset to be held subject to the warrant arrangement] *… , payment of the First Interest Amount and payment of the Capital Protection Fee and Borrowing Fee (if any).*
>
> *ABN AMRO …* [i.e. the financier] *… purchases the Underlying Parcel …* [i.e. the asset to be held subject to the warrant arrangement] *… in the name of the Security Trustee …* [i.e. the 'bare' trustee in the warrant relationship] *… for the benefit of the Cash Applicant …* [e.g. a trustee of a superannuation trust] *… and takes a security interest over the Underlying Parcel …* [the asset to be held subject to the warrant arrangement] *…'.*

8.21 Further, at sub-paragraph 17(e) of PR 2005/96:

> *'… repayment of the Loan will be secured by a mortgage over the Underlying Parcel …* [i.e. the asset to be held subject to the warrant arrangement] *… Legal title to the Underlying Parcel will be held by the Security Trustee …* [i.e. the 'bare' trustee in the warrant relationship] *… on trust for the Investor. Each trust and each Underlying Parcel to which it relates will be kept as a separate trust and there will be no pooling of interests of property to which the trust relates'.*

8.22 Product Ruling PR 2005/40 entitled *Income tax: tax consequences of investing in Macquarie Regular Instalment Warrants IMF Series 2004 Product Disclosure Statement - cash applicants and on-market purchasers* (withdrawn) ('**PR 2005/40'**) discusses the relationships and obligations that arise under that specific product. It is observed at paragraph 16(d) of PR 2005/40 that:

> *'… under a Cash Application, the Cash Applicant* … [e.g. a trustee of a superannuation fund] *… pays the varying First Payment …* [i.e. the initial 'instalment']*. Macquarie …* [i.e. the financier] *… lends the Completion Payment amount (which is the current Loan Amount) to the Cash Applicant and takes a security interest over the Underlying Share …* [i.e. the asset to be held subject to the warrant arrangement] *… . Proceeds of the Loan and the First Payment from the Cash Applicant are applied toward the purchase of the Underlying Share, prepayment of interest to Macquarie and the payment of borrowing fees to Macquarie. Macquarie buys the underlying share in the name of the Security Trustee* [i.e. the '*bare'* trustee in the warrant relationship]. *The Macquarie IMF instalment is issued in the name of the cash Applicant.'*

8.23 Sub-paragraph 16(f) of PR 2005/40 provides that:

> *'… repayment of the Loan will be secured by a mortgage over the Underlying Share which will be held by the Security Trustee as trustee for the Holder. Each trust and*

each Underlying Share to which it relates will be kept as a separate trust and there will be no pooling of interests or property to which the trust relates.'

8.24 The 'Loan' in the warrant arrangement described in PR 2005/40 is described in paragraph 16(g):

> *'the Loan is provided on a limited recourse basis such that Macquarie's right to repayment of the Loan is limited to the amount it can obtain by enforcing its right in respect of the Mortgaged Property'.*

8.25 Product Ruling PR 2006/5 entitled *Income tax: tax consequences of investing in Westpac 'SWB' Series Self-Funding Instalments - 2005 Product Disclosure Statement - cash applicants and on-market purchasers (withdrawn)* ('**PR 2006/5'**)[3] is another example. Paragraphs 16 to 18 of PR 2006/5 describe the participants involved in the product:

> *'16. Westpac …* [i.e. the financier] *… is the Issuer of the Westpac SWB Instalments and is also the provider of the Loans to Holders …* [e.g. a trustee of a superannuation fund] *… to fund the acquisition of the Underlying Parcel …* [i.e. asset to be held subject to the warrant relationship].
>
> *17. Westpac Custodian Nominees Limited* ... [i.e. the 'bare' trustee in the warrant relationship] *…, as Security Trustee, holds the legal title to each Underlying Parcel for each Holder.*
>
> *18. The Holders may be individuals, companies, trusts or superannuation funds'.*

8.26 Sub-paragraph 15(a) of PR 2006/5:

> *'Westpac SWB Instalments …* [i.e. the warrant] *… are a leveraged investment under which a Holder …* [e.g. a trustee of a superannuation fund] *… acquires a beneficial interest in shares and/or stapled securities listed on the ASX and/or units in certain listed trusts (Security) …* [i.e. asset to be held subject to the warrant relationship] *… using a limited recourse Loan made by Westpac …* [i.e. the financier]*. Where the Security includes a stapled security, the stapled security comprises shares and/or units that are jointly listed for quotation on the ASX. The Security, together with any Accretions, is referred to as the 'Underlying Parcel'.*

8.27 Sub-paragraph 15(g) of PR 2006/5:

> *'… repayment of the Loan is secured by a mortgage over the Underlying Parcel. Legal title to the Underlying Parcel is held by the Security Trustee* ... [i.e. the 'bare' trustee in the warrant relationship] *… on trust for the Holder. Each Underlying Parcel is held on a Separate Trust and there is no pooling of interests or property to which the trust relates …'.*

8.28 Subparagraph 15(i) of PR 2006/5:

> *'… the Loan is provided on a limited recourse basis so that if the Holder does not make the Completion Payment, Westpac's right to repayment is limited to the proceeds which it can obtain from enforcing its Security Interest over the Underlying*

[3] Paragraph 18 of PR 2006/5 provides that the '… Holders may be individuals, companies, trusts or superannuation funds'.

Parcel. If the Holder provides a Completion Notice to Westpac, however, Westpac is entitled to recover the Completion Payment from the Holder in full …'.

9 Estate planning and superannuation

9.1 A member's interest in a superannuation fund does not automatically form part of their estate. However, in the context of estate planning and superannuation, there are a number of considerations, including:

- when benefits must be paid;
- who can receive the benefits;
- in what form should those benefits be taken; and
- the taxation implications for the beneficiaries.

<u>What is a 'death benefit'?</u>

9.2 Regulation 6.21 of the SIS Regulations provides that a trustee of a regulated superannuation fund is required to cash a member's benefit as soon as practicable after a member's death. Except if there is an effective death benefit nomination, the superannuation fund's trustee has a discretion as to which dependants it should distribute a deceased's benefits.

9.3 The term 'superannuation death benefit' is defined in section 307-5 of the 1997 Act. Amongst other things, item 1 of column 3 in that section defines a 'superannuation death benefit as '*A payment to you from a superannuation fund, after another person's death, because the other person was a fund member.*'

9.4 Section 307-10 of the 1997 Act sets out the payments which are not considered 'superannuation death benefits'.

<u>Payment of death benefits</u>

9.5 A payment from a superannuation fund in consequence of the death or a member can be paid either:

1. directly to a beneficiary; or
2. to the executor of the deceased's estate or a trustee of a testamentary trust, with the amounts then paid to a beneficiary as a distribution from the estate or the trust.

9.6 Broadly speaking, upon death a member's superannuation interest is transferred from the member's fund, being a 'death benefit'. Subject to the terms of the particular trust deed of the superannuation fund, the transfer may be effected by either a lump sum payment, an income stream, or both.

9.2 Regulation 6.21(2) of the SIS Regulations provides that a lump sum must not be paid in more than two instalments.

9.8 Further, there are limitations with respect to the payment of income streams.

Timing of payment of death benefits

9.9 Regulation 6.21(1) of the SIS Regulations provides that '*… a member's benefits in a regulated superannuation fund must be cashed as soon as practicable after the member dies.*' That is, there is no prescribed time in which a death benefit must be paid. All that is required is that the payment must be made as soon as practicable after death.

Lump sum payments

9.10 Section 302-60 of the 1997 Act provides that lump sum payments received by a dependant of the deceased is tax free. The amount is treated as non-assessable non-exempt income.

9.11 However, if a lump sum is paid to a non-dependant, then the tax free component will not be subject to tax (see section 302-140 of the 1997 Act), but the taxable component of the lump sum is included in the recipient's assessable income and subject to tax at marginal rates. Section 302-145 of the 1997 Act provides for a tax offset mechanism, that ensures that the rate of tax on the tax free component does not exceed 30% (plus Medicare levy), whereas the rate of tax on the tax free component does not exceed 15% (plus Medicare levy).

Superannuation lump sum death benefit	Dependent	Non-dependent	
		Taxed element	Untaxed element
Tax free component	Tax free	Tax free	Tax free
Taxable component	Tax free	15%	30%

9.12 The possible methods of transfer of a member's interest upon death depend on the character of the recipient, with the possibilities being:

Recipient	Permitted benefit
Spouse	Either or both a lump sum and/or income stream
Dependent children under the age of 18	Either or both a lump sum and/or income stream. However, income stream must cease at 25.
Non-dependent children over the age of 18	Lump sum
Dependent children between 18 and 25	Either or both a lump sum and/or income stream. However, income stream must cease at 25.
Dependent child over the age of 25	Lump sum
Dependent grandchildren	Either or both a lump sum and/or income stream
Non-dependent grandchildren	Lump sum (made via estate)

Non-dependent (i.e. not child or spouse)	Lump sum (made via the estate)
Estate	Lump sum

Income streams

9.13 Section 302-65 of the 1997 Act provides that a superannuation income stream is tax free if either the deceased or the dependant is aged at least 60 as at the time of death.

9.14 If a superannuation income stream is paid to a dependant upon death, and neither the deceased or the dependant are aged at least 60 at the time of death, then:

- that part of the income stream which is the ***tax free component*** is tax free;
- that part of the income stream which is paid from a ***taxed component*** is assessable income for the dependent. The dependent is entitled to a tax offset which is equal to 15% of the element taxed in the fund. The income stream becomes tax free when the recipient turns 60 years of age;
- that part of the income stream which is paid from an ***untaxed component*** is assessable income for the dependent. The dependent will receive a tax offset of only 10%, but only when they attain the age of 60.

9.15 A non-dependent is unable to receive a superannuation income stream. Such income streams must be commuted, and paid to the non-dependant as a lump sum.

Who is a dependent?

9.16 The term 'dependent' for taxation purposes is defined in section 302-195 of the 1997 Act. Subsection 302-195 of the 1997 Act provides that:

> *'(1) A **death benefits dependant**, of a person who has died, is:*
>
> *(a) the deceased person's spouse or former spouse; or*
>
> *(b) the deceased person's child, aged less than 18; or*
>
> *(c) any other person with whom the deceased person had an interdependency relationship under section 302-200 just before he or she died; or*
>
> *(d) any other person who was a dependant of the deceased person just before he or she died. '*

9.17 That is, a 'death benefit dependant' with respect to a deceased includes:

- the deceased's spouse;
- the deceased's former spouse;

- the deceased's child, provided that at the time of death the child is under the age of 18;
- a person with whom the deceased had an 'interdependency relationship' just before the deceased died;
- any other person who was a 'dependant' of the deceased just before the death of the deceased; and
- under section 302-195 of the 1997 Act, a death benefits dependant also includes a person who receives a superannuation pension or annuity if the annuity or pension commenced before 1 July 2007 as a result of the death of another person.

<u>Interdependency relationship</u>

9.18 The term 'interdependency relationship' for the purposes of paragraph 302-195(1)(c) of the 1997 Act is provided for in section 302-200 of the 1997 Act:

> ***'What is an interdependency relationship?***
>
> *(1) Two persons (whether or not related by family) have an* ***interdependency relationship*** *under this section if:*
>
> *(a) they have a close personal relationship; and*
>
> *(b) they live together; and*
>
> *(c) one or each of them provides the other with financial support; and*
>
> *(d) one or each of them provides the other with domestic support and personal care.*
>
> *(2) In addition, 2 persons (whether or not related by family) also have an* ***interdependency relationship*** *under this section if:*
>
> *(a) they have a close personal relationship; and*
>
> *(b) they do not satisfy one or more of the requirements of an interdependency relationship mentioned in paragraphs (1)(b), (c) and (d); and*
>
> *(c) the reason they do not satisfy those requirements is that either or both of them suffer from a physical, intellectual or psychiatric disability.*
>
> *(3) The regulations may specify:*
>
> *(a) matters that are, or are not, to be taken into account in determining under subsection (1) or (2) whether 2 persons have an* ***interdependency relationship*** *under this section; and*
>
> *(b) circumstances in which 2 persons have, or do not have, an* ***interdependency relationship*** *under this section.'*

9.20 That is, two individuals have an independency relationship if they satisfy ***all*** of the following conditions (see section 302-200 of the 1997 Act):

- they have a close personal relationship;
- they live together;
- one or each of them provides the other with financial support; and
- one or each of them provides the other with domestic support and personal care.

Life insurance and superannuation funds

9.21 An important part of a financial plan is life insurance. Generally speaking, a life insurance payout can:

1. form part of the deceased's estate;
2. be directed to a specific beneficiary; or
3. be paid to the policy owner.

9.22 The purpose of life insurance is to provide a lump sum benefit upon death of the life insurer. Life insurance which is 'term insurance' is guaranteed to be renewable (i.e. the policy cannot be changed) whilst the premiums continue to be paid. Such a policy can be held within a superannuation fund, with the result that upon death of the individual insured, the proceeds are paid to the fund. This has the result of increasing the death benefit payable.

9.23 Upon death, the proceeds of life insurance policies held by the superannuation fund are paid directly to the fund (as the policy owner). The proceeds are allocated to the member's fund as a taxable component.

9.24 The death benefit is paid tax free as a lump sum to a death benefit dependent. However, such a payment made to a non-financial dependant will be taxable (with no low rate threshold for the taxable component.

9.25 The taxable component paid from insurance proceeds may be either a taxed component or an untaxed component. A higher rate of tax is payable on an untaxed component received by a non-death benefit dependent. If:

- the superannuation fund **has not** claimed a tax deduction for the premiums paid for the insurance policy, then the ***taxable component*** is a ***taxed component***; and
- the superannuation fund **has** claimed a tax deduction for the premiums paid for the insurance policy, then the ***taxable component*** is an ***untaxed component***.

9.26 Further, in the year that a death benefit is made, the trustee can choose to claim a deduction for the future service period of that member instead of claiming a tax deduction for the premium paid on the insurance policy. This strategy will only be beneficial if the fund is in accumulation (i.e. tax paying) phase, and not income phase.

<u>Binding nominations in the context of self-managed superannuation fund</u>

9.27 Section 59 of the SIS Act provides that:

> *'(1) Subject to subsection (1A), the governing rules of a superannuation entity other than a self managed superannuation fund must not permit a discretion under those rules that is exercisable by a person other than a trustee of the entity to be exercised unless:*
>
> *(a) those rules require the consent of the trustee, or the trustees, of the entity to the exercise of that discretion; or*
>
> *(b) if the entity is an employer-sponsored fund:*
>
> *(i) the exercise of the discretion relates to the contributions that an employer-sponsor will, after the discretion is exercised, be required or permitted to pay to the fund; or*
>
> *(ii) the exercise of the discretion relates solely to a decision to terminate the fund; or*
>
> *(iii) the circumstances in which the discretion was exercised are covered by regulations made for the purposes of this subparagraph.*
>
> *(1A) Despite subsection (1), the governing rules of a superannuation entity may, subject to a trustee of the entity complying with any conditions contained in the regulations, permit a member of the entity, by notice given to a trustee of the entity in accordance with the regulations, to require a trustee of the entity to provide any benefits in respect of the member on or after the member's death to a person or persons mentioned in the notice, being the legal personal representative or a dependant or dependants of the member.*
>
> *(2) If the governing rules of a superannuation entity are inconsistent with subsection (1), that subsection prevails, and the governing rules are, to the extent of the inconsistency, invalid.'*

9.28 Further, section 31 of the SIS Act provides that regulations may be made so as to provide operating standards for superannuation fund. Relevantly, Regulation 6.17A of the *Superannuation Industry (Supervision) Regulations 1993* (Cth) provides that:

> ***'6.17A Payment of benefit on or after death of member (Act, s 59 (1A))***
>
> *(1) For subsections 31(1) and 32(1) of the Act, the standard set out in subregulation (4) is applicable to the operation of regulated superannuation funds and approved deposit funds.*
>
> *(2) For subsection 59(1A) of the Act, the governing rules of a fund may permit a member of the fund to require the trustee to provide any benefits in respect of the member, on or after the death of the member, to the legal personal*

representative or a dependant of the member if the trustee gives to the member information under subregulation (3).

(3) The trustee must give to the member information that the trustee reasonably believes the member reasonably needs for the purpose of understanding the right of that member to require the trustee to provide the benefits.

(4) Subject to subregulation (4A), and regulations 6.17B, 7A.17 and 7A.18, if the governing rules of a fund permit a member of the fund to require the trustee to provide any benefits in accordance with subregulation (2), the trustee must pay a benefit in respect of the member, on or after the death of the member, to the person or persons mentioned in a notice given to the trustee by the member if:

(a) the person, or each of the persons, mentioned in the notice is the legal personal representative or a dependant of the member; and

(b) the proportion of the benefit that will be paid to that person, or to each of those persons, is certain or readily ascertainable from the notice; and

(c) the notice is in accordance with subregulation (6); and

(d) the notice is in effect.

(4A) The trustee is not required to comply with subregulation (4) if the trustee:

(a) is subject to a court order that has the effect of restraining or prohibiting the trustee from paying a benefit in respect of the member in accordance with a notice of the kind described in that subregulation; or

(b) is aware that the member of the fund is subject to a court order that:

(i) requires the member to amend or revoke a notice of that kind that the member has given the trustee; or

(ii) has the effect of restraining or prohibiting the member from giving a notice of that kind.

(5) A member who gives notice under subregulation (4) may:

(a) confirm the notice by giving to the trustee a written notice, signed, and dated, by the member, to that effect; or

(b) amend, or revoke, the notice by giving to the trustee notice, in accordance with subregulation (6), of the amendment or revocation.

(6) For paragraphs (4) (c) and (5) (b), the notice:

(a) must be in writing; and

> (b) *must be signed, and dated, by the member in the presence of 2 witnesses, being persons:*
>
> > (i) *each of whom has turned 18; and*
> >
> > (ii) *neither of whom is a person mentioned in the notice; and*
>
> (c) *must contain a declaration signed, and dated, by the witnesses stating that the notice was signed by the member in their presence.*
>
> (7) *Unless sooner revoked by the member, a notice under subregulation (4) ceases to have effect:*
>
> > (a) *at the end of the period of 3 years after the day it was first signed, or last confirmed or amended, by the member; or*
> >
> > (b) *if the governing rules of the fund fix a shorter period — at the end of that period.'*

9.29 However, in Self Managed Superannuation Funds SMSFD 2008/3, entitled *Self Managed Superannuation Funds: is there any restriction in the Superannuation Industry (Supervision) legislation on a self managed superannuation fund trustee accepting from a member a binding nomination of the recipients of any benefits payable in the event of the member's death?*, the Commissioner of Taxation observed that:

> *'Section 59 of the Superannuation Industry (Supervision) Act 1993 (SISA) and regulation 6.17A of the Superannuation Industry (Supervision) Regulations 1994 (SISR) do not apply to self managed superannuation funds (SMSFs). This means that the governing rules of an SMSF may permit members to make death benefit nominations that are binding on the trustee, whether or not in circumstances that accord with the rules in regulation 6.17A of the SISR.*
>
> *2. However, a death benefit nomination is not binding on the trustee to the extent that it nominates a person who cannot receive a benefit in accordance with the operating standards in the SISR. The relevant operating standards are mentioned in Appendix 1 of this Determination.'*

9.30 As a result, before a death benefit nomination is made, regard should be given to the particular constituent documents for the fund so as to determine what (if any) death benefit nominations can be made. In the event that the constituent documents are silent on the matter, then no nomination can be made.

9.31 Further, if the constituent documents provide that binding death benefit nominations may be made under the SIS Act, and because the relevant binding death benefit rules in the SIS Act do not apply to self-managed superannuation funds, such a provision will not allow a member to make such nominations.

9.32 It should be noted that the jurisdiction of the Superannuation Complaints Tribunal does not extend to decisions made by trustees of self-managed superannuation funds or certain public sector superannuation schemes. As a result, self-managed superannuation funds are a valuable mechanism to ensure that a death benefit is paid as directed by the deceased member.

9.33 Further, because death benefits are not dealt with under a will, legal challenges can be greatly reduced by directing payments from a self-managed superannuation fund upon death directly to a person specified by the deceased, as opposed to having such payments directed to the estate of the deceased.

9.34 However, it should also be noted that if the decision as to who will receive the death benefit is made by the remaining trustee(s) of the self-managed superannuation fund, the death benefit may be paid in a way which is contrary to the deceased member's wishes. Consideration should be given to the decision in *Katz v Grossman* [2005] NSWSC 934, which according to the first sentence of the judgement was: '*…a contest between a brother and a sister over the control of a superannuation trust fund established at the behest of their late father Ervin Katz. The assets of the fund exceed $1 million.*'

9.35 *Katz v Grossman* is authority for the proposition that in the event that binding directions are not provided to the trustee of a self-managed superannuation fund, then the trustee of a fund has complete discretion with respect to dealings with superannuation benefits. Such discretion includes the trustee providing the benefits to themselves, notwithstanding that they are not dependants of the deceased.

9.36 Ervin Katz was a member of the E. Katz Employees Trust Fund, which was a self-managed superannuation fund. Both Mr Katz and his daughter, Linda Ann Grossman were trustees of the self-managed superannuation fund. Mr Katz had made a non-binding nomination, in which he expressed the desire for his death benefit to be divided equally amongst his daughter (the co-trustee) and his son.

9.37 However, following the death of Mr Katz, Mrs Grossman appointed her husband as a co-trustee. The trustees then resolved to pay the whole of Mr Katz's death benefit to Mrs Grossman.

9.38 Mr Katz's son took action in the New South Wales Supreme Court arguing that:

- Mr Katz had not validly appointed Mrs Grossman as a trustee; and that
- Mrs Grossman was not validly appointed as a member.

9.39 With respect to the first issue, after reviewing the terms of the superannuation fund's deed, the relevant documentation and consideration of the *Trustee Act 1925* (NSW) , Smart AJ held that Ms Grossman had been validly appointed. As a result, Mrs Grossman's decisions were held to be valid, which included the payment of the death benefit referable to Mr Katz's interest in the fund to herself.

9.40 With respect to the issue of whether Mrs Grossman was validly appointed as a member of the fund, Smart AJ considered that because the fund's deed required an appointment as a member to be effective the trustee had to consent to it, as there was no documentary evidence which showed that the trustee had consented to Mrs Grossman becoming a member, it was held that Mrs Grossman was not a member of the fund.

9.50 As a result, in order to ensure that the wishes of a member with respect to the payment of their interest in a self-managed superannuation fund occurs, either a binding death benefit nomination should be executed, or there should be a trust deed direction which provides for such wishes.

10 Superannuation proceeds trusts

10.1 Division 6AA of the 1936 Act discourages 'income splitting' by means of diversion of income to children to take advantage of the tax-free threshold and progressive tax rates. Broadly speaking, the provisions apply a 45% tax rate on unearned income of minors. Such income includes certain distributions from trusts.

10.2 However, Division 6AA of the 1936 Act does not apply to certain 'excepted trust income'. Such trust income includes that from a 'superannuation proceeds trust'. That is, superannuation proceeds trusts may be established by the transfer of property from a superannuation fund, as a result of the death of a person, to a trustee of a trust which will hold the property for the benefit of a child.

10.3 Paragraph 102AG(2)(c)(v) of the 1936 Act provides that:

> *'(2) Subject to this section, an amount included in the assessable income of a trust estate is excepted trust income in relation to a beneficiary of the trust estate to the extent to which the amount:*
>
> *...*
>
> *(c) is derived by the trustee of the trust estate from the investment of any property transferred to the trustee for the benefit of the beneficiary:*
>
> *...*
>
> *(v) directly as the result of the death of a person and out of a provident, benefit, superannuation or retirement fund;'*

10.4 The terms of the trust must provide for the beneficial acquisition of trust property by the beneficiary upon the termination of the trust.

10.5 Although death benefits do not generally form part of an estate, generally speaking, superannuation proceeds trusts are established under the terms of a will. Such a transfer may be ensured via a binding death benefit nomination.

10.6 The Commissioner in ATO ID 2001/751 accepts even where a superannuation death benefit is paid to a trustee, apart from the estate (e.g. so as to satisfy the superannuation cashing rules, to an adult child of the deceased), in order to assess whether the superannuation death benefit tax concessions apply, one should look through the trust to the underlying beneficial ownership of the trust.

10.7 This would be the situation if the beneficiaries of such a trust were minor children of the deceased.

11 Superannuation and Stamp Duties

11.1 Consideration should also be given to the stamp duty exemption in relation to superannuation funds under the Duties Act in relation to business real property.

<u>Transfer as a result of change in superannuation membership</u>

11.2 Section 61 of the Duties Act provides for an exemption in respect of transfers of property in connection with persons changing superannuation fund. On application of the exemption, the duty chargeable on a relevant transfer is ad valorem duty or $500, whichever is the lesser (see subsection 61(2)).

11.3 Relevantly, subsection 61(1) of the Duties Act provides:

> *'(1) This section applies to a relevant transfer that occurs in connection with a person:*
>
> *(a) ceasing to be a member of, or otherwise ceasing to be entitled to benefits in respect of, a superannuation fund that is a complying superannuation fund or was a complying superannuation fund within the period of 12 months before the transfer was made, and*
>
> *(b) becoming a member of, or otherwise becoming entitled to benefits in respect of, another superannuation fund that is also a complying superannuation fund or will, in the opinion of the trustees of both funds concerned, be a complying superannuation fund within 12 months after the transfer is made.'*

11.4 A 'relevant transfer' is set out in subsection 62(1A) to be:

> *'(a) a transfer of, or an agreement to transfer, dutiable property from a trustee of a superannuation fund, or a custodian of the trustee, to the trustee of another superannuation fund, or to a custodian of the trustee of another superannuation fund,*
>
> *(b) a transfer of, or an agreement to transfer, dutiable property from a trustee of a superannuation fund to a custodian of the trustee, or from a custodian of the trustee of a superannuation fund to the trustee,*
>
> *(c) a transfer of, or an agreement to transfer, marketable securities from a trustee of a pooled superannuation trust, made in exchange for a redemption of units in the trust, to the trustee of a superannuation fund, or a custodian of the trustee of a superannuation fund,*
>
> *(c1) a transfer of, or an agreement to transfer, marketable securities from the trustee of a superannuation fund, or a custodian of the trustee of a superannuation fund, made in exchange for the issue of units in a pooled superannuation trust, to a trustee of the pooled superannuation trust,*
>
> *(d) a transfer of, or an agreement to transfer, marketable securities from a life company or custodian for a life company to the trustee of a superannuation fund or a custodian of the trustee of a superannuation fund if the transfer is made in consideration of the surrender or termination, by the trustee of the superannuation fund of which the person has ceased to be a member, of a policy of life insurance issued by the life company.'*

11.15 It is noted that the exemption in section 61 is available to complying superannuation funds whilst the exemption in section 62A is only available to self managed superannuation funds.

<u>Transfer to a self managed superannuation fund</u>

11.16 Section 62A of the Duties Act provides for nominal duty to be paid on a transfer to the trustee or the custodian of the trustee of a self-managed superannuation fund ('**SMSF**'):

> *'**62A Transfers to self managed superannuation funds***
>
> *(1) Duty of $50 is chargeable on a transfer of, or an agreement to transfer, dutiable property from a person (the transferor) to the trustee of a self managed superannuation fund but only if:*
>
> *(a) the transferor is the only member of the superannuation fund or the property is to be held by the trustee solely for the benefit of the transferor, and*
>
> *(b) the property is to be used solely for the purpose of providing a retirement benefit to the transferor.*
>
> *(2) Property held by the trustee of a superannuation fund is held solely for the benefit of the transferor if:*
>
> *(a) the property is held specifically for the benefit of the transferor, as a member of the superannuation fund, and*
>
> *(b) the property (or proceeds of sale of the property) cannot be pooled with property held for another member of the superannuation fund, and*
>
> *(c) no other member of the superannuation fund can obtain an interest in the property (or the proceeds of sale of the property).*
>
> *(3) Duty of $500 is chargeable on a transfer of, or an agreement to transfer, dutiable property from a person (the **transferor**) to the custodian of the trustee of a self managed superannuation fund but only if:*
>
> *(a) the transferor is the only member of the superannuation fund, or*
>
> *(b) the property is to be used solely for the purpose of providing a retirement benefit to the transferor.*
>
> *(4) This section does not apply in respect of a transfer of, or an agreement to transfer, dutiable property if, as a result of the transfer, the superannuation fund will cease to be a complying superannuation fund.'*

11.17 In particular, subsection 62A(3) was inserted by the *State Revenue Legislation Further* Amendment *Act* 2010 (NSW) which had effect from 1 January 2011.

11.18 The insertion of subsection 62A(3) means that a person may transfer NSW dutiable property to the custodian of a SMSF if the transferor is the only member of the fund, or the property is to be

used solely for the purpose of providing a retirement benefit to the transferor (see also subsection 62A(2)).

11.19 The property could then be held on a gearing arrangement pursuant to section 67A of the SIS Act. Section 67A of the SIS Act requires that the legal title of the property is to be held on trust so that the trustee of the SMSF acquires a beneficial interest in the property. As a result, and pursuant to both section 67A of the SIS Act and the security trust, the registered proprietor of the property (and therefore the 'transferee' disclosed on the transfer) will be the bare trustee / custodian.

11.20 The security trust deed will be subject to nominal ($50) duty pursuant to subsection 55(1) of the Duties Act, which provides that:

> *'Duty of $50 is chargeable in respect of:*
>
> *(a) a declaration of trust made by an apparent purchaser in respect of indentified dutiable property:*
>
> *(i) vested in the apparent purchaser upon trust for the real purchaser who provided the money for the purchase of the dutiable property, or*
>
> *(ii) to be vested in the apparent purchaser upon trust for the real purchaser, if the Chief Commissioner is satisfied that the money for the purchaser of the dutiable property has or will be provided by the real purchaser ...'*

11.21 Paragraph 55(1A) of the Duties Act further provides that:

> *'For the purposes of subsection (1), money provided by a person other than the real purchaser is taken to have been provided by the real purchaser if the Chief Commissioner is satisfied that the money was provided as a loan and has or will be repaid by the real purchaser.'*

11.22 That is, under the gearing arrangement, the mere registered proprietor / bare trustee / custodian (i.e., the 'apparent purchaser' pursuant to section 55 of the Duties Act) of the property will hold the property for the 'real purchaser', being the SMSF trustee.

Transfer of property to trustees or custodians of superannuation funds

11.23 Section 62 of the Duties Act provides an exemption for a transfer or an agreement to transfer dutiable property between trustees and custodians of superannuation funds or pooled superannuation trusts where there is no change in the beneficial ownership of the property.

11.24 On application of the exemption, the duty chargeable on a dutiable transaction is ad valorem duty or $500, whichever is the lesser (see subsection 62(3)), or if the transfer relates to marketable securities, the duty of $10.

12 *Ioppolo & Anor v Conti & Anor* [2015] WASCA 45

12.1 In *<u>Ioppolo & Anor v Conti & Anor</u>* [2015] WASCA 45, the Western Australian Court of Appeal (Martin CJ, Buss JA and Beech J) confirmed that upon the death of a member of a self-managed superannuation fund, the *<u>Superannuation Industry (Supervision) Act 1993</u>* (**SIS Act**) permitted, but did not require the executor of the deceased member's estate to be appointed as a trustee of the SMSF. Of concern was section 17A of the SIS Act, which provides that:

> *Subsection 17A(1) of the SIS Act contains the "basic conditions" that need to be satisfied for funds other than single member funds, in order to be a self-managed super fund. Subsection 17A(2) of the SIS Act contains for the "basic conditions" for single member funds so as to meet the definition of a "self-managed superannuation fund".*

12.2 Subsection 17A(1) of the SIS Act provides:

> *(1) Subject to this section, a superannuation fund, other than a fund with only one member, is a* ***self managed superannuation fund*** *if and only if it satisfies the following conditions:*
>
> *(a) it has fewer than 5 members;*
>
> *(b) if the trustees of the fund are individuals--each individual trustee of the fund is a member of the fund;*
>
> *(c) if the trustee of the fund is a body corporate--each director of the body corporate is a member of the fund;*
>
> *(d) each member of the fund:*
>
> *(i) is a trustee of the fund; or*
> *(ii) if the trustee of the fund is a body corporate--is a director of the body corporate;*
>
> *(e) no member of the fund is an employee of another member of the fund, unless the members concerned are relatives;*
>
> *(f) no trustee of the fund receives any remuneration from the fund or from any person for any duties or services performed by the trustee in relation to the fund;*
>
> *(g) if the trustee of the fund is a body corporate--no director of the body corporate receives any remuneration from the fund or from any person (including the body corporate) for any duties or services performed by the director in relation to the fund.*

11.3 Subsection 17A(2) of the SIS Act provides:

*(2) Subject to this section, a superannuation fund with only one member is a **self managed superannuation fund** if and only if:*

(a) if the trustee of the fund is a body corporate:

(i) the member is the sole director of the body corporate; or
(ii) the member is one of only 2 directors of the body corporate, and the member and the other director are relatives; or
(iii) the member is one of only 2 directors of the body corporate, and the member is not an employee of the other director; and

(b) if the trustees of the fund are individuals:

(i) the member is one of only 2 trustees, of whom one is the member and the other is a relative of the member; or
(ii) the member is one of only 2 trustees, and the member is not an employee of the other trustee; and

(c) no trustee of the fund receives any remuneration from the fund or from any person for any duties or services performed by the trustee in relation to the fund;

(d) if the trustee of the fund is a body corporate--no director of the body corporate receives any remuneration from the fund or from any person (including the body corporate) for any duties or services performed by the director in relation to the fund.

11.4 However, whilst subsections 17A(1) and (2) of the SIS provide that members of a self-managed super fund must also be trustees, or directors of corporate trustees, subsection 17A(3) provides that certain other persons may be trustees, by providing that:

(3) A superannuation fund does not fail to satisfy the conditions specified in subsection (1) or (2) by reason only that:

(a) a member of the fund has died and the legal personal representative of the member is a trustee of the fund or a director of a body corporate that is the trustee of the fund, in place of the member, during the period:

(i) beginning when the member of the fund died; and
(ii) ending when death benefits commence to be payable in respect of the member of the fund; or

(b) the legal personal representative of a member of the fund is a trustee of the fund or a director of a body corporate that is the trustee of the fund, in place of the member, during any period when:

(i) the member of the fund is under a legal disability; or
(ii) the legal personal representative has an enduring power of attorney in respect of the member of the fund; or

(c) if a member of the fund is under a legal disability because of age and does not have a legal personal representative:

(i) the parent or guardian of the member is a trustee of the fund in place of the member; or
(ii) if the trustee of the fund is a body corporate--the parent or guardian of the member is a director of the body corporate in place of the member; or

(d) an appointment under section 134 of an acting trustee of the fund is in force.

11.5 Circumstances in which entity that does not satisfy basic conditions remains a self managed superannuation fund.

11.6 The term "legal personal representative" for the purposes of subsection 17A(3) of the SIS Act is defined in section 10 of the SIS Act as:

> *... means the executor of the Will or administrator of the estate of a Deceased person, the trustee of the estate of a person under a legal disability or a person who holds an enduring power of attorney granted by a person.*

11.7 *Ioppolo v Conti* is authority for the proposition that the SIS Act permits, but does not require, the executor of a deceased member's estate to be appointed as a trustee of a self-managed super fund.

11.8 The broad facts in *Ioppolo v Conti* were that:

- Mrs Francesca Conti and Mr Augusto Conti established the "Conti Superannuation Fund" in 1992.
- The Conti Superannuation Fund was established pursuant to the terms of a trust deed.
- Pursuant to the trust deed, Mr and Mrs Conti were the Fund's trustees and members.
- The trustee mandated that the Fund was to be conducted pursuant to the terms of the SIS Act, so as to obtain favourable tax treatment which was given to complying superannuation funds.
- Since the establishment of the Fund (in 2002), Mr and Mrs Conti made contributions to the Fund. Those contributions were recorded in the accounts of the Fund as standing to the benefit of their respective member accounts.
- Mrs Conti passed away on 5 August 2010.
- On 28 October 2010, probate of Mrs Conti's Will was granted to her son and daughter, them being the executors of the late Mrs Conti's estate.
- Mrs Conti's son and daughter (who are the executors) were issue from a previous marriage of Mrs Conti (that is, they were not Mr Conti's biological children).
- On 3 February 2011, Mr Conti (in his capacity as trustee of the Fund) determined that the benefit standing to the account of his wife were to be paid to him rather than to any of her children. Mr Conti did this after obtaining legal advice.
- After making the determination, Mr Conti elected to take the benefit in the form of a pension, with the pension being paid to him out of the assets of the Fund.

- On 4 February 2011, Mr Conti resigned as a trustee of the Fund and Augusto Investments Pty Ltd was appointed the trustee of the Fund.
- Agusto Investments Pty Ltd was a company which Mr Conti was a sole director.

11.9 The executors commenced proceedings claiming:

- As a trustee of the Fund, Mr Conti was required pursuant to section 17A of the SIS Act to appoint one of them to act as a trustee of the Fund in place of the late Mrs Conti.
- Until such an appointment was made, Mr Conti had no power to deal with the interest that the late Mrs Conti had in the Fund in his capacity as trustee of the Fund.
- The executives contended that Mr Conti's determination to confer the interest of the late Mrs Conti to himself was void, and that Mr Conti had acted in bad faith in making the determination by preferring his own interest to the interest of Mrs Conti's children.

11.10 The Western Australian Court of Appeal dismissed the executor's claims, and upheld the decision at first instance (see *Ioppolo & Hesford v Conti* [2013] WASC 389).

11.11 Martin CJ at [71] considered that there were no words in subsection 17A(3) of the SIS Act which mandated the appointment of a legal personal representative to be a trustee, or a director of a corporate trustee of a self-managed superannuation fund. It was observed at [71] that:

> *Significantly, however, there are no words in s17A(3), or any inference of legislative intension to be drawn from the operation or effect of the subsection viewed in the context of the section or in the context of the SIS Act as a whole, to suggest that a fund is obliged to utilise the opportunities for compliance provided by the subsection either within any particular time, or at all, if there are other means by which the fund can be brought into compliance. Nor is there anything in the language in of the subsection or any inference of legislative intent to be drawn from the effect of the subsection viewed in the context of the section or the SIS Act as a whole to suggest that any constraint is placed upon the powers of the trustee unless and until the opportunities for compliance provided by the subsection are utilised.*

11.12 The other provisions in s17A(3) are, as the executors rightly concede, permissive rather than mandatory. There is no sufficient basis to construe par(a) of s17A(3) differently. Rather, Martin CJ at [72] observed that:

> *To the contrary, a consideration of other provisions of the SIS Act compels the conclusion that s17A(3) should be construed in accordance with its natural and ordinary meaning – that is, as providing opportunities for compliance with the other requirements of the section which might, or might not, be taken up. As I have noted, pt 6 of the SIS Act contains a number of provisions with respect to the governing rules of superannuation*

> *entities and includes s52 which contains a number of specific convents to which trustees have regulated funds are subject. If it had been the intention of the legislature to impose obligations upon trustees for the protection of the interests which beneficiaries or dependents of deceased members may have in the benefit standing to the account of a deceased member, Part 6 of the Act would have been the obvious place in which to provide such obligations, rather than in s17A which stipulates the conditions which must be met in order for a regulated fund to achieve the tax concessions which attend satisfaction of those conditions.*

11.13 The Western Australian Court of Appeal also rejected the executor's claim that Mr Conti had acted in bad faith in making the determination that the late Mrs Conti's interest in the Fund should be conferred on him. In the context of the burden of proof, Martin CJ at [81] observed of the lack of discharge of the burden that:

> *As it is the executors who assert that Mr Conti did not exercise a discretion conferred upon him as trustee of the Fund in a bone fide manner, they carry the burden of proving that assertions on the balance of probabilities. They have made no attempt to discharge that burden other than by asserting that an inference is to be drawn as to Mr Conti's reasons from the terms of the letter of advice received from Norton & Smailes. No attempt was made to adduce evidence as to the respective financial positions of Mrs Conti's children, as compared to Mr Conti, and Mr Conti was not cross-examined on his Affidavit. If and to the extent that Mrs Conti's wishes were relevant to the exercise of the discretion, as the Master pointed out, the evidence with respect to her wishes was equivocal, given the terms of the Will are inconsistent with binding beneficiary nomination forms which she executed both before and after her Will. It is therefore impossible to draw an inference of lack of bona fides from, for example, an assertive failure to take into account the clear and unequivocal wishes of a deceased. It was open to Mr Conti to consider that the subsequent execution of the binding nomination meant that the expression of intension in the Will had been superseded, and was no longer worthy of weight as an expression of the intention of the deceased member as to what should happen on her death.*

11.14 The Western Australian Court of Appeal noted that the Deceased had made binding beneficiaries nomination forms, which had both lapsed. Those nomination forms nominated Mr Conti as the recipient of a death benefit from the Fund. Martin CJ at [74] considered that:

> *There is a cogent argument to the effect that the beneficiary nomination form is executed by Mrs Conti, although deprived of their characteristic as being binding beneficiary nominations by the lapse of time, nevertheless, satisfied the requirement of identifying a person nominated by her as a person she wished to receive her benefit in the event of her death, which is an apt way of describing the role of a Nominated Dependent.*

11.15 As a result, Martin CJ considered that (given the lapsed nomination forms) the only way that the executors could succeed in their argument of lack of bona fides was to demonstrate that the *"... Mr Conti, in his capacity as trustee, failed to address the question of whether it would be inequitable or inappropriate to pay the benefit to himself..."* ([75]).

11.16 However, Martin CJ considered that that question did not need to be resolved as there was no evidence capable of sustaining the conclusion that the exercise of the discretion miscarried ([76]).

11.17 Martin CJ at [77] observed that:

> *In the course of presenting oral argument on these issues, Senior Counsel for the executors advanced a nuanced position not previously evident in either the pleadings, the proceedings before the Master, the grounds of appeal or the written submissions in support of those grounds. It was asserted that it should be concluded that there was in fact no exercise of discretion by the trustee, but rather, Mr Conti simply determined that he should have the benefit of Mrs Conti's interests in the Fund for himself. Assuming, for the sake of argument, that it is open, notwithstanding the way in which the case was conducted before the Master, it is difficult to see how this proposition adds anything to the executors' fundamental argument, which is to the effect that it should be concluded the exercise of the trustee's discretion miscarried because he did not give full and proper consideration to the competing interests of the prospective beneficiaries as required by the principle enunciated in Karger v Paul as developed by the High Court in Finch v Telstra Super Pty Ltd. But whichever way the argument is presented, it must fail on the evidence.*

11.18 Martin CJ observed that Mr Conti's evidence advanced a series of propositions, which was based on information that he received in advice from solicitors. These propositions included that the executors (in their capacity as children of the deceased) only have a right to be considered by the trustee in the exercise of the discretion of who to pay out any death benefit ([79]).

11.19 The executor's argument (which was not accepted) was that Mr Conti acted pursuant to the legal advice, but excluding that portion of the advice which refers to the right of Mrs Conti's children to be considered in the exercise of the trustee's discretion. The Court considered that *"there is simply no basis in evidence for drawing any inference to that effect"* ([80]).

11.20 It was also noted that there was a clause in the trust deed which provides that a trustee may exercise a power or a right even where there is a conflict of interest, provided that the power of right is exercised in a bona fide manner. There was no argument that that particular provision was offended.

13 *Deputy Federal Commissioner of Tax (Superannuation) v Graham Family Superannuation Pty Ltd & Ors* [2014] SCA 1101 (Buchanan J)

13.1 The Federal Court in *Deputy Federal Commissioner of Tax (Superannuation) v Graham Family Superannuation Pty Ltd & Ors* [2014] SCA 1101 (Graham's Case) endorsed pecuniary penalties and costs totalling $50,000 which were imposed on a husband and wife who are members of a self-managed super fund for contravention of provisions of the SIS Act.

13.2 The broad facts were:

- The First Respondent was a corporate trustee of the Graham Family Superannuation Fund. The Fund was established in October 20, 2006.
- The Second and Third Respondents were the directors of the trustee, and members of the Fund.
- In July 2007 there was a roll-over of $216,047 from another fund which had the wife's superannuation benefits.
- In August 2007 further amount of $273,113 was rolled over into the Fund from another superannuation fund, on account of the husband's member benefits.
- Between July 2008 and June 2012, the Respondents caused the Fund to make 80 loans to the husband and wife which total $134,418.
- The loans were made without the authorisation of the governing rules of the Fund.
- The monies were expended by the husband and wife on a caravan, stud cattle for private purposes, two motor vehicles for their adult sons, and other unspecified (private) purposes.
- The Fund's principal asset was a residential property. It was fully furnished, and leased to one of the sons of the husband and wife. There was no rent in fact paid in relation to that occupancy.
- There are also some non-contravening loans, so that by June 2012, the loan account of the Fund stood at approximately $260,064 (which included both contravening and non-contravening loans).
- In relation to the 80 loans and the leasing of the residential property (without collecting rent) the following provisions of the SIS Act were said to have been contravened:

  - Section 62 of the SIS Act – because the Fund was no maintained solely for one or more of the purposes contained in subsection 62(1) of the SIS Act;
  - Section 65 of the SIS Act – because money was lent using the assets of the Fund to the husband and wife members;
  - Section 84 of the SIS Act – because there was a failure to take all reasonable steps to ensure that the in-house asset provisions contained in Part 8 of the SIS Act were complied with. Rather, there were loans made to members of the Fund which caused the market value ratio of the Fund's in-house assets to exceed 5%, and there was also a failure to prepare a plan setting out steps to ensure that the 5% limit would not be continued to be breached;
  - Section 109 of the SIS Act – this provision was contravened because investments were made in their capacity as trustee in circumstances where the

trustee and the other parties to those transactions failed to deal with each other at arm's length.

- The parties accepted that the husband played a dominant role in the management of Fund. The wife relied on the judgement of the husband. As a result, it was accepted that he husband would have higher penalties imposed.
- The parties agreed to the basic facts, the legal obligations and the nature extent of the contraventions. They also agreed to the declarations which should be made by the Court, and the pecuniary penalties which should be imposed and the costs which should be assessed.
- Buchanan J at [3] considered that whilst there was an agreement, the Court was still required to independently assess whether the penalties proposed fall within an acceptable range (having regard to the circumstances:

> *The fact and extent of the agreement of the parties has avoided, I have no doubt, a considerable drain on the resources of the Court. No doubt the discussions have proceeded by reference, on each side, to principles and general regulatory objectives (in the case of the applicant) or personal interest (in the case of the second and third respondents) which do not reflect a commonality of purpose. For that reason alone, some examination of the proposed orders is appropriate and necessary. Moreover, it is accepted doctrine in this Court that the Court has an independent role in assessing whether penalties proposed (even jointly) by parties fall within an acceptable range, having regard to the particular circumstances of the case.*

13.3 Buchanan J agreed with the principles of the Full Federal Court in *Minister for Industry, Tourism & Resources v Mobil Oil Australia Pty Ltd* [2004] FCAFC 72 in relation to agreed penalties to be imposed. The general principles are:

- It is the responsibility of the Court to determine the appropriate penalty to be imposed in respect of contraventions of statute;
- Determining the quantum of penalty is not an exact science. It is within a permissible range that the Courts have acknowledged that a particular figure cannot necessarily be said to be more appropriate than another;
- There is a public interest in promoting settlement of litigation, particularly where it is likely to be lengthy. As a result, a regulator and contravener reaching agreement may present to the Court a statement of facts and opinion as to the effect of those facts, together with joint submissions as to the appropriate penalty to be imposed.
- The view of a regulator (being a specialist body) is relevant, but not determinative in considering the question of penalty. In particular, the views of the regulator are matters within its expertise will usually be given greater weight that its views on more "subjective matters".
- In determining whether the proposed penalty is appropriate, the Court will examine all relevant circumstances of the case.
- In determining whether the proposed penalty is appropriate, the Court will examine all relevant circumstances of the case. Where the parties have put

forward an agreed statement of facts, the Court may act on that statement if it is appropriate to do so.

- Where the parties have jointly proposed a penalty, it will not be useful to investigate whether the Court would have arrived at that precise figure in the absence of agreement. Rather, the question is whether the figure is, in the Court's view, appropriate in the circumstances of the case. In answering that question, the Court will not reject the agreed figure simply because it would have been disposed to select some other figure. It will be appropriate if within the permissible range.

13.4 Buchanan also observed the following principles:

- The Court, if it considers that the evidence or information before it is inadequate to form a view as to whether the penalty proposed is appropriate, it may request the parties to provide additional evidence or verify the information provided. Without such further information, the Court may not be satisfied that the proposed penalty is within in the range.
- If there is an absence of a contradictor, which inhibits the Court in performing its duties, the Court may seek the assistance of an amicus curiae or of an individual body prepared to act as an intervener.
- If the Court is disposed not to impose a penalty proposed by the parties, it may be appropriate, depending on the circumstances of each of them to be given the opportunity to withdraw consent to the proposed orders and for the matter to proceed as a contested hearing.

13.5 Buchanan J at [18] considered that the contraventions were very serious, and that they fell into two broad categories, being:

- The making of 80 contravening loans to members for a period of four years for a wide variety of private purposes;
- The lease of the Fund's principal asset (being residential premises) to the son of the members and a failure to collect rent.

13.6 Buchanan J accepted the Commissioner's submissions as to how multiple contraventions should be considered. At [35] Buchanan J considered *the "... principles about how to deal with multiple contraventions, including the significant of a course of conduct and the applicant's application of the "totality" principle, and the factors which Courts frequently take into account when fixing a penalty, including the central purpose of deterrence."*

13.7 Further, Buchanan K at [36]-[37] accepted the Commissioner's submissions that penalties should not be imposed for a breach of each provision. Rather, the proper way to approach the matter was to have:

- A separate and single penalty assessed and imposed for each contravention relating to the lease of a residential premises to the son (being contraventions of sections 62, 84 and 109 of the SIS Act);
- A single penalty assessment imposed on a "course of conduct" basis for the making of the 80 loans.

13.8 Whilst there were multiple separate contraventions for each of the loans, being contraventions of sections 62, 65, 84 and 109 of the SIS Act, the circumstances of the case were such that it was appropriate to impose one penalty for each course of conduct.

13.9 Buchanan J at [38] observed that:

> *A statutory maximum penalty of $220,000 applies to each contravention (2,000 penalty units of $110 each). Although, as the applicants submitted, the events are serious ones they fall well of a worse possible case. The second and third respondents have shown remorse, they have made early admissions, they have co-operated with the Commissioner. They have remedied their conduct. A penalty should not be imposed which is "crushing". At the same time, the penalty should serve as a deterrent and mark the Court's acceptance of the need to enforce a regulatory scheme.*

13.10 The Court endorsed the penalties and costs agreed by the parties – that is, that the husband paid a total penalty of $30,000 ($21,000 and $9,000), and that the wife paid a total penalty of $10,000 ($7,000 and $3,000).

13.11 Further, the Court agreed that each of the husband and wife should be responsible for half the agreed costs at $10,000.

14 *Olesen v Early Sunshine Pty Ltd* [2015] FCA 12

14.1 Foster J delivered the decision in *Olesen v Early Sunshine Pty Ltd* [2015] FCA 12, which involved multiple contraventions of the SIS Act for which the Federal Court was asked to make declarations and impose certain penalties.

14.2 Broadly speaking, the facts were:

- Early Sunshine was a trustee of a self-managed super fund.
- Early Sunshine Pty Ltd had three directors, who were all members of the Fund.
- The members of the Fund were also directors of a company known as George MacDonald & Sons Pty Ltd, which is a company that carried on a freight trucking business (Freight Truck Co).
- Freight Truck Co experienced some financial distress, and as a result, Early Sunshine Pty Ltd lent an amount of $553,568 to Freight Truck Co during a 4 year period beginning 2007 and ending 2011.
- In total, there was some 71 discreet loans made to Freight Truck Co.
- A small loan was also made to Vertu Pty Ltd, which is a company controlled by one of the members.
- All of the loans were ultimately repaid.
- The Commissioner and the respondents all agreed that the trustee of the Fund had contravened:
    - Section 62(1) of the SIS Act, being the sole purpose test, on the basis that loans were made to two related companies;

- Subsection 84(1) of the SIS Act, being the in-house asset rules, as not all reasonable steps were taken to ensure that the in-house asset requirements were complied with (as a result of the loans which were made to the two related companies that exceeded the relevant limits; and
- Subsection 109(1) of the SIS Act, failing to deal with entity at arm's length's – as a result of the lending of the money to Freight Truck Co on terms more favourable to Freight Truck Co than would have been arm's length (that is the loans were interest free.

14.3 The parties had agreed on the facts, and also the penalties. The agreed penalties were that each director would pay a penalty of $13,000 and $5,000 of the Commissioner's costs in brining the case. That is, there was a total of $39,000 in penalties and $15,000 in costs.

14.4 The Court had to consider whether the agreed penalties were appropriate. Foster J at [37] observed that:

> *When first informed of the quantum of the pecuniary penalties which the parties have agreed, I initially felt that the quantum of those penalties was insufficient. However, upon more mature reflection and having regard to all of the relevant circumstances, I formed the view that the quantum of those penalties was appropriate.*

14.5 Foster J outlined the tension as between the nature of the contraventions (i.e. their seriousness, and repetitive nature), as compared to the lack of loss of capital and the cooperation that the members gave the Commissioner, by observing at [31] – [33] that:

> *31. There is no doubt that the contraventions in the present case were serious when viewed from a regulatory perspective. As submitted by the parties, they were deliberate, repetitive and took place over a period of 4 years. There were numerous separate contraventions. The assets of the fund were clearly put at risk by being lent to a business which was under financial stress.*
>
> *32. However, it must be remembered that, in the end, the Fund did not suffer any loss of capital. The foregone interest income was not significant. In addition, all the respondents admitted all the contraventions which were ultimately pressed by the Commissioner and co-operated fully with the Commissioner both at the investigation stage and in the proceeding. Also, the Fund has now been wound up and the members' balances have now been transferred to a public fund which should ensure that they are satisfactorily protected.*
>
> *33. Each of the individual respondents has taken full responsibility for their involvement in the contraventions and expressed remorse and contrition for their conduct.*