

# Superannuation Funds and Borrowings: The new way to grow your super!

Richard Horvath – Manager, Taxation & Business Services

*As part of our ongoing client seminar program, Lowe Lippmann Chartered Accountants recently hosted a presentation by Daniel Butler of DBA Butler, SMSF Lawyers on the new laws on borrowings in superannuation funds. For the benefit of those who were unable to attend this presentation, the following article briefly outlines the changes.*

*If you would like a copy of the notes from the presentation, please call us on 9525 3777 and we will send them to you. The notes are also available on our website at [www.lowelippmann.com.au](http://www.lowelippmann.com.au).*

Until recently, super funds were strictly prohibited from borrowing except in very limited circumstances. In September 2007, new laws were enacted to enable super funds to 'borrow' by way of investment in an instalment warrant.

An instalment warrant is a derivative – an instrument that 'derives' its value from an underlying asset. This is an important characteristic of the borrowing structure in that the super fund indirectly invests in an asset by actually investing in an instalment warrant. Once the borrowing is fully repaid, by paying the final instalment, the super fund has the right to take legal ownership of the underlying asset.

There are a number of conditions that must be met in order for the borrowing to be allowable:

- The asset acquired must be held in trust (that is, not directly by the super fund).
- The asset must be one that super funds are ordinarily permitted to acquire. For example, super funds are not allowed to acquire residential property from members.
- The super fund would have a right, not an obligation, to acquire legal (direct) ownership of the asset on paying the final instalment.

- The borrowing must be limited recourse. That is, if a super fund is unable to meet its repayment obligations under the terms of the loan, the lender should have no recourse in recovering the outstanding loan balance, other than retaining the underlying asset. This feature is designed to protect the other assets of the super fund.

Any asset would therefore need to be acquired by a nominee and held in trust for the benefit of the super fund. The super fund would pay the first instalment (say, the deposit on a property purchase) and borrow the balance from a lender to fund the acquisition. In the same way as holders of Telstra Instalment Warrants received dividend income from their investment, the super fund would be entitled to receive rental income.

While the borrowing arrangement must be very carefully structured in order to satisfy each of the conditions of the provisions, there is actually no condition on who the 'lender' must be. This could enable families to effectively lend money to their super fund from another entity within their family group. With the superannuation contribution limits introduced under the Simplified Superannuation measures, this could be a way of injecting additional funds into super.

Anyone considering a super fund borrowing to acquire an asset must first think carefully about the potential risks and ramifications. It is vitally important that where trustees are considering the acquisition of an asset by way of super fund borrowing that they contact a partner at Lowe Lippmann before any decision is made.

# Fringe Benefits Tax

As the Fringe Benefits Tax year ended on 31 March, now is the time for employers to gather information for the completion of the 2008 FBT return. A checklist has been sent to our clients to help identify any benefits that have been provided to employees that may fall within the FBT regime. If you have not received a checklist, please contact your partner at Lowe Lippmann and one will be sent to you.

The following article highlights some of the problem areas of FBT.

## Business-Owned cars and FBT

The Australian Taxation Office (ATO) has undertaken a project to review business-owned cars and FBT lodgements. Selected employers are being sent a questionnaire requesting information about cars owned by the business in the last two years. Should answers to the questionnaire reveal an FBT liability, we would encourage voluntary disclosure.

Three of the areas of concern to the ATO are:

1. Logbooks do not provide sufficient information about the car's use;
2. Substantial business use for a car is claimed, but the car is garaged at an employee's residence and there is no record in the logbook of business travel; and
3. The treatment of employee contributions for income tax and GST purposes.

An employer using the operating-cost method to calculate the taxable value of a car fringe benefit needs to ensure that the following details are recorded in the logbook for each business journey:

- the date on which the journey began and on which it ended;
- the odometer readings at the start and end of each journey;
- the kilometres travelled; and
- the specific purpose of the journey.

Car users should also be aware of FBT obligations that may arise under the 'home garaging rule'. In most instances, a car garaged at an employee's home is considered to be available for private use and automatically subject to FBT.

## Reportable Fringe Benefits

If an employee's individual fringe benefit amount in this FBT year (1 April 2007 to 31 March 2008) is more than \$2,000, the Reportable Fringe Benefits Amount must be included on the employee's Payment Summary for the tax year ending 30 June 2008.

The Reportable Fringe Benefit Amount is the grossed-up value of the employee's fringe benefit amount, and is calculated by multiplying the fringe benefit amount by 1.8692.

The Reportable Fringe Benefits Amount is not included in the employee's assessable income, but is used to determine the employee's entitlement to, or liability for, the following:

- Medicare levy surcharge
- Mature age worker tax offset
- Deduction for personal superannuation contributions
- Tax offset for eligible spouse superannuation contributions
- Super co-contribution
- Higher Education Loan Programme (HELP) repayments
- Child support payments
- Entitlement to certain income-tested government benefits

The Reportable Fringe Benefit Amount will also be taken into account in the income tests for the family tax benefit, the child care benefit and the parental income test for youth allowance. However, these tests will only include the non-grossed-up value of the fringe benefits.

In preparing your FBT return for the year ended 31 March 2008, we will be in a position to advise which amounts are reportable on your employees' PAYG Payment Summaries for the 2007/08 year.

## Entertainment Fringe Benefits

In entertaining business clients, often employees are also included. Whilst the costs of entertaining clients are neither income tax deductible nor subject to FBT, the opposite is generally the case with employees.

Entertainment fringe benefits take many forms, and can include any or all of the following:

- Business lunches with clients
- Birthday parties
- Christmas parties
- Golf days
- Product release functions
- Gym memberships
- Celebrations for achieving sales targets
- Farewell functions
- Reward and recognition functions
- Memberships to sporting clubs
- Anniversary dinners

Certain exemptions from FBT may be available where the benefit provided is infrequent or of low cost.

For assistance with determining your potential liability to FBT, contact one of the Lowe Lippmann Business Services partners. Details of each Partner and their area of expertise are included on the last page of this Newsletter.

# Personal Services Income – Are You Conducting a Business?

David McDonald – Manager, Taxation & Business Services

*As an independent contractor you would consider yourself to be conducting a business. But does the Australian Taxation Office (ATO)? Does it matter?*

Income earned mainly as a reward for an individual's personal effort or skills is that individual's personal services income (PSI). The PSI regime was introduced on 1st July 2000 and has been designed to ensure that income meeting the above definition is assessed to the individual, irrespective of the entity invoicing for the services.

The provisions of the PSI regime are not relevant if it can be demonstrated that a business is being conducted, possibly allowing additional deductions to be claimed, as well as providing for income to be shared between family members or related entities, and hence for income tax to be paid at lower rates.

For it to be considered that a business is being conducted, **one** of the following **two** tests must be satisfied:

- The Results Test
- The 80% Rule

The **Results Test** may be satisfied if the contractor is engaged to produce a specific result and is liable for the cost of rectifying any defects. Daily pay rates, and the practice of extending contracts until the specific task is achieved, will often lead to the results test not being passed.

Under the **80% Rule**, if **less** than 80% of your income is derived from one client during an income year, you will be considered to be conducting a business, provided one of the following three tests is also satisfied:

**Employment Test** – requires at least 20% of the principal work (not clerical or administrative work) to be conducted by someone other than the main contractor. This can be your spouse or other relative, if they perform the required services.

**Business Premises Test** – the premises from which the business is conducted must be separate from the contractor's home if this test is to be satisfied.

**Unrelated Clients Test** – requires income to be earned from two or more non-associated sources in a given year. This is the test most likely to be satisfied by contractors. It also requires the contracts to be obtained due to the contractor making offers to the public at large, or to a section of the public. This area is relatively untested, but is unlikely to be satisfied by obtaining several contracts through the one agent.

## **ATO Determination**

If you are unable to meet any of the above tests in an income year due to unusual circumstances applying to that particular year, a determination may be requested from the ATO to ascertain if, in its view, you are operating a business.

The tax benefits of demonstrating that you are conducting a business are significant. As the PSI regime is a relatively complex area of taxation law, we recommend that you seek our advice in considering its application to your particular circumstances.

# Director's Personal Liability

Julie Seow – Manager, Corporate Reconstructions & Insolvency

From 1 July 2000, a payer's obligation to pay withheld amounts to the Commissioner of Taxation (Commissioner) specifically includes amounts withheld under the PAYG withholding system.

Directors can incur a personal liability to pay the unpaid amount of a company's liability if a company fails to meet its obligations. Company directors, including new directors, are obligated to ensure that a company either meets its remittance provision obligations, or goes promptly into voluntary administration or liquidation.

The Commissioner is required to give a director 14 days notice before recovering this penalty. A director has, within the 14 days, to either:

- pay the liability;
- come to an agreement with the ATO relating to the liability;
- place the company under voluntary administration; or
- put the company in liquidation.

Directors of companies are automatically **personally** liable to pay if their company has not paid by the due date. Their personal liability commences on the day after the due date for payment.

## *Contravention of Payment Agreements*

If a company contravenes a payment agreement, a director becomes liable to pay a penalty equal to the balance payable under the agreement.

There is no requirement for the Commissioner to send notice of a penalty for breach of a payment agreement prior to the institution of recovery proceedings.

If the company is not able to discharge its liability either by payment of the unremitted amounts or by a payment agreement with the ATO, it may wish to consider voluntary administration or winding up the company.

## **Voluntary Administration – Part 5.3A of the Corporations Act 2001**

Part 5.3A of the Corporations Act 2001 deals with the administration of a company's affairs with a view to executing a deed of company arrangement.

The object of this Part is to provide for the business, property and affairs of the insolvent company to be administered in a way that:

- a) maximizes the chances of the company, or as much as possible of its business, continuing in existence; or
- b) if it is not possible for the company or its business to continue in existence – results in a better return for the company's creditors and members than would result from an immediate winding up of the company.

The administration of a company begins when an administrator of a company is appointed.

A company may, by writing, appoint an administrator\* of the company if the board of directors has resolved to the effect that:

- a) in the opinion of the directors voting for the resolution, the company is insolvent, or is likely to become insolvent at some future time; and
- b) an administrator of the company should be appointed.

(\*An administrator appointed under this Part must be a registered liquidator.)

A first meeting of creditors must be held within 8 business days after the administration begins.

A deed of company arrangement, proposed by the directors and accepted by the creditors at a second meeting of creditors, must be executed by both the company and the administrator within 15 days of the second meeting.

The company is then subject to the deed of company arrangement (deed) until the provisions of the deed are fully met.

## **Winding Up of the Company**

A company may be wound up voluntarily if the company so resolves by special resolution of members of the company.

Generally, at least 21 days' notice must be given of a meeting of a company's members. If sufficient members agree then a shorter notice period may apply. The company must call two meetings:

- 1) A meeting of members to vote on the special resolution to wind up the company and an ordinary resolution to appoint the liquidator; and
- 2) A meeting of creditors.

The meeting of creditors must be held within 11 days after the special resolution to wind up the company has been passed by the company's members. At least 7 days' notice must be given to creditors.

Should you wish to discuss this further, please contact Lowe Lippmann's Corporate Reconstruction and Insolvency division, which provides the following services:

- voluntary administration
- voluntary liquidation
- court liquidation
- receivership
- consulting
- forensic and investigative accounting and
- litigation and support

# Land Tax Update

David McDonald – Manager, Taxation & Business Services

A recent announcement by the Victorian Government has brought the structuring of land and property holdings in Victoria back into sharp focus.

Land tax is a state-based tax imposed on an individual's or an entity's Victorian landholdings. The tax is charged on an increasing scale whereby the higher the value of your cumulative landholdings, the higher the marginal rate of land tax applicable, up to 2.5% per annum for holdings in excess of \$2.7 million. There is also a surcharge payable (up to 0.375%) for land held through a trust structure. There are some exceptions to land tax, primarily your principal residence.

In recent years Victorian property values have increased significantly and to grant some land tax relief, the Victorian Government imposed a cap to limit the single year increase in your land tax liability to no more than 50%. If, for example, your liability was \$10,000 in 2006 it could be no more than \$15,000 in 2007.

This cap was removed with effect from 31 December 2007. With the ever-increasing property prices in Victoria (it was widely reported that Melbourne residential property rose by more than 25% in 2007 alone), this could have a substantial impact on future Land Tax assessments, as shown in the following example:

Jim purchased a property in 2006 with a land value of \$500,000. His Land Tax Assessment for 2006 was \$800. With a 25% increase in land value, Jim's 2007 Land Tax would have been \$1,305 but was limited by the cap to a 50% increase, being \$1,200. Jim's property increased in value by a further 25% (up to \$781,250) in 2008 and, despite reduced land tax rates, Jim's 2008 assessment amounted to \$2,086. With no capping available in 2008, the 2008 Land Tax Assessment represents a two-year increase of \$1,286 or 160%.

Coupled with the current environment of increasing interest rates, inflationary pressures, and the fact that in some cases there is no recovery of land tax available from the tenant, the overall return available from your property investments may be significantly eroded.

It may be possible to manage your land tax liability by carefully restructuring your existing (or new) land holdings. New opportunities such as superannuation fund borrowings (see related article in this edition) could allow you to split current land holdings amongst different legal owners. In any proposed structuring/restructuring, other taxes such as Stamp Duty, Capital Gains Tax and GST may be applicable and must be carefully considered.

Please contact a Partner at Lowe Lippmann to discuss the most effective methods of structuring your current or future investments.

# Lowe Lippmann Turns 60!



**Joseph Franck**  
Partner  
Taxation &  
Business Services



**Philip Behr**  
Partner  
Audit and Taxation &  
Business Services



**Brian Rudy**  
Partner  
Taxation &  
Business Services

Lowe Lippmann is proud to say that today our Practice continues to grow from its humble beginnings in January 1948, when it was first established by Kurt Lippmann and Robert Lowe. Mr Lippmann and Mr Lowe opened an office in Collins Street, Melbourne as a two-man partnership and today Lowe Lippmann Chartered Accountants has a staff complement of 77 members. Together with Lowe Lippmann Financial Services, Lowe Lippmann is now a team of 90.

Our clients represent a broad range of industries, and vary in size from individual employees and investors, to companies with an annual turnover in excess of \$100 million.

The success of Lowe Lippmann can be gauged by our total commitment to pursuing our clients' interests in a positive, professional and energetic manner. Ultimately our success is measured by our clients' success.

## Our Commitment – Vision with Tradition

Our clients are entitled to outstanding service.

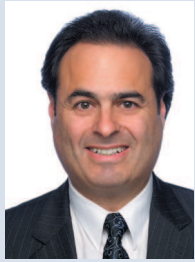
We have achieved our success by consistently delivering results through innovative and effective solutions for our clients. We recognize that our future is inextricably bound to theirs.

In a rapidly changing world, businesses must adapt to survive. We believe that our clients are entitled to the best that modern accountancy has to offer.

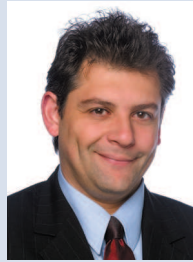
We are proud to offer many traditional services whilst continually evaluating and implementing the latest advances in technology and procedures.

In lieu of client cards and gifts at the end of 2007, Lowe Lippmann donated to the Paediatric Intensive Care Unit of the Royal Children's Hospital. The PICU Foundation matched our donation and purchased a Flow Probe. The Flow Probe controls and monitors the flow of blood for patients with an infectious disease. Lowe Lippmann is proud to support the PICU.

Today, Lowe Lippmann Chartered Accountants consists of twelve Partners, each a specialist in their field.



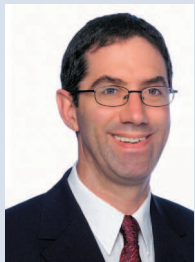
**Mark Saltzman**  
Partner  
Taxation &  
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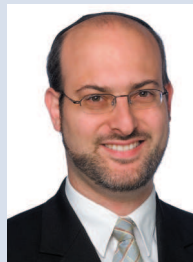
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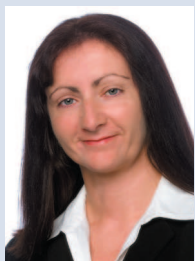
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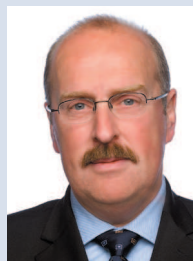
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### Disclaimer

The information contained in this publication is intended as general commentary and should not be regarded as advice. Should you require specific advice on any of the topics or areas discussed, please contact your Accountant.