



Explanatory Memorandum

October 2009

Tax Office Compliance Program 2009/10

The Tax Office's Compliance Program for the 2009/10 income year, released in August 2009, sets out the key priorities and focus areas the Tax Office has highlighted for greater scrutiny.

Individuals

The Tax Office has highlighted the following specific compliance issues for individual taxpayers.

International dealings

Tax returns of individuals will be matched against information supplied by overseas revenue agencies and the Australian Transaction Reports and Analysis Centre (AUSTRAC) to identify unreported foreign income, including bank interest, dividends, pensions, salary and wages.

The Tax Office will also work closely with financial institutions to identify taxpayers who are involved in abusive tax haven-related arrangements.

Employees and work-related expenses

Work-related expenses continue to be a focus of the Tax Office for the 2009/10 income year. In particular, the Tax Office is focusing on the following areas:

- occupations with a pattern of large and/or rising claims;
- tax returns that do not fit the pattern of a particular occupation; and
- claims in tax returns lodged by tax agents that are outside the norm for their client base.

The Tax Office has identified the occupations listed below to be of interest:

- truck drivers;
- sales and marketing managers;
- sales representatives; and
- electricians.

According to the Tax Office, the most common incorrect claims by people in the above occupations include:

- insufficient documentation to support motor vehicle and travel expenses;
- claiming the living-away-from-home allowance when a claimant is not eligible;
- motor vehicle expenses on the basis that a taxpayer is carrying bulky equipment required for work; and
- home offices, mobile phone and internet expenses.

Investors

The Tax Office is concerned that investors may not be correctly reporting their capital gains and losses. To assist investors, the Tax Office will be sending educational letters advising them of their CGT obligations.

Tax returns of investors with investment products (eg managed funds and managed investment schemes) will be reviewed by the Tax Office to ensure deductions relating to the products claimed in the returns are allowable. The Tax Office has also expressed concern about products that have the following features:

- deductions for financing costs are brought forward, including prepayment of interest in the first year;
- non-arm's length financing, including non-recourse or limited recourse lending and uncommercial long interest-only periods;
- 'round-robin' payment arrangements;
- artificial reductions in risk exposure;
- generation of excessive franking credit entitlements in comparison with real income received.

Micro enterprises

The micro enterprises segment consists of businesses with an annual turnover of less than \$2 million and self-managed superannuation funds (SMSFs). Businesses in this segment operate through various structures including sole traders, companies, partnerships and trusts.

The headline issues the Tax Office have identified are:

- ***helping businesses stay on track*** — To assist businesses understand and meet their obligations, the Tax Office offers a range of services. These services include tax seminars and workshops and business assistance visits. The Tax Office also says its assistance services reflect its 'prevention is better than cure' approach to compliance. However, it also says it will respond firmly where businesses choose not to engage with the Tax Office or fail to meet promises to pay a tax liability.
- ***meeting employer obligations*** — The Tax Office says a key priority is for employers to meet their obligations (eg PAYG withholding).
- ***Superannuation guarantee*** — The Tax Office says that for the 2009/10 income year it will action over 20,000 employee complaints about unpaid superannuation guarantee contributions. In addition, a communication campaign aimed at increasing compliance in the road freight transport, automotive repair and electrical services industries will be conducted.
- ***cash economy*** — The cash economy remains a focus of the Tax Office.

The Tax Office has identified six specific compliance issues:

- ***international dealings***

The Tax Office will match data and information supplied by overseas revenue agencies and AUSTRAC with income tax returns to identify unreported foreign income. It will also match data from payment service providers to identify Australian residents involved in foreign transactions. It will also work with financial institutions to identify taxpayers involved in abusive tax haven-related arrangements.

- ***property transactions and shares***

In the area of property transactions, GST and CGT compliance risks have been identified. The specific GST issues are:

- unreported property sales;
- incorrect application of the margin scheme; and
- avoidance of GST obligations by not lodging activity statements or registering for GST.

The particular CGT issues are:

- sales of property;
- creation and attribution of capital losses; and
- correct use of the CGT small business concessions.

In the area of share transactions, the Tax Office is concerned that some taxpayers will treat their share losses on revenue account rather than on capital account to offset those losses against other income. The Tax Office will examine shares and correct accounting for CGT when taxpayers exit a business.

- ***Refund fraud***

The Tax Office says all claims for GST refunds and the research and development (R&D) tax offset will be subject to credibility checks. It will also examine risks stemming from misuse of tax return labels. It will also increase its scrutiny of trading stock reporting and company losses.

- ***Partnership and trust distributions***

The Tax Office is expanding its data matching to ensure distributions from partnerships and trusts are correctly disclosed in beneficiaries' tax returns.

- ***Dodgy schemes***

The Tax Office will focus on identifying the promotion of tax exploitation schemes and providing early warning to participants to highlight its concerns about specific schemes and arrangements. (Generally, the Tax Office will issue a Taxpayer Alert in which it will outline the tax issues that are of concern.)

The Tax Office says participants of tax exploitation schemes who come forward and who make full and true voluntary disclosures may receive significant reductions in penalties.

- ***Self-managed superannuation funds***

The Tax Office will focus on regulatory issues, such as loans, in-house assets, borrowings and non-arm's length transactions. According to the Tax Office, over 3,000 trustees of SMSFs will be contacted in relation to these issues. The timely lodgment of tax returns will also be a focus of the Tax Office. The Tax Office's active compliance activities will cover at least 10% of all new funds during the 2009/10 income year.

Another focus of the Tax Office is ensuring SMSFs satisfy the definition of an 'Australian superannuation fund' (see Thomson Reuters note* below). In particular, it says that trustees of SMSFs who travel and work overseas for extended periods of time need to ensure their SMSFs meets the definition.

The Tax Office will continue to pay attention to schemes designed to allow individuals to access their superannuation early. It says its responses to such schemes include freezing bank accounts, raising income tax assessments with penalties and referring the individuals and promoters for prosecution.

The Tax Office will monitor SMSF auditors to ensure they fulfil their role properly.

*** Note**

A superannuation fund will satisfy the definition of an 'Australian superannuation fund', which is contained in s 295-95 of ITAA 1997, if:

- the fund is established in Australia, or any of the fund is situated in Australia;
- the central management and control of the fund is ordinarily in Australia; and
- either the fund has no active member or at least 50% of the total market value of the fund's assets attributable to superannuation interests held by active members (the sum of the amounts that would be payable to or in respect of active members if they voluntarily ceased to be members) is attributable to superannuation interests held by active members who are Australian residents.

In Taxation Ruling TR 2008/9, the Tax Office explains the Commissioner's interpretation of the definition of an 'Australian superannuation fund'.

Small-to-medium enterprises

Small-to-medium enterprises (SMEs) are businesses with an annual turnover of between \$2 million and \$250 million. This sector includes highly wealthy people who, with their associates, effectively control \$30 million or more in net wealth.

The Tax Office says that, when conducting risk assessments and other compliance activities of SMEs, its focus is on the economic group (including related companies, super funds, trusts, partnerships and controlling individuals) rather than individual entities. It also looks at the transparency of business transactions between associated entities and their tax effects. For wealthy taxpayers, it takes a similar approach and profiles and assesses the risk of all groups associated with these people.

In its general income tax compliance activities for the sector over the coming year, the Tax Office says it will be developing and using new information collection and data matching tools to identify potential high risk taxpayers. It will also continue risk assessments for all taxpayers with turnovers between \$100 million and \$200 million, as well as initiate more than 300 new reviews of SMEs.

For the wealthy individuals component of the segment, the Tax Office says it will extend its compliance activities to look at individuals with a net wealth between \$5 million and \$30 million. It will also:

- focus on identifying and risk reviewing potential cases for audits;
- identify improper use of losses and tax outcomes from property development transactions that are inconsistent with economic outcomes;
- expand use of external data such as records of property sales and share transactions;
- undertake at least 120 audits and 420 reviews; and
- share more information with other jurisdictions to identify high-risk transactions.

Specific compliance issues in SME sector

The Tax Office has identified the following specific compliance issues.

Income tax and FBT compliance activities

The Tax Office will conduct 650 reviews and 370 audits of SMEs, focusing on compliance issues relating to income tax and FBT. It will also contact 2,000 SMEs to verify specific income tax and FBT issues.

The specific areas the Tax Office will examine include:

- **employer obligations** — The Tax Office plans to focus on the correct FBT treatment of motor vehicles. It will also focus on superannuation guarantee issues such as late payment and incorrect calculations. The Tax Office will increase support for small business employers to ensure they understand their superannuation guarantee obligations.
- **capital management** — The Tax Office will focus on business owners who use loans, payments and debt forgiveness to distribute private company profits to shareholders (or associates of the shareholders) without paying the correct amount of tax. It will also examine the relationship between private companies and trusts, particularly compliance with the untaxed private company distribution provisions.
- **CGT** — The Tax Office says it will seek to ensure CGT is correctly applied, with a particular focus on ensuring capital losses are not offset against income. Compliance activities include:
 - writing to taxpayers involved in developing properties, before they lodge their returns, to help them determine how to report their assessable income to ensure they correctly claim the CGT discount;
 - monitoring disposals of interests in taxable Australian property by foreign residents;
 - reviewing claims for rollover exemption and pre-CGT status on share disposals;
 - raising awareness through tax agents of the implications of issuing shares at a discount, triggering the general value-shifting integrity measures.
- **tax planning for business exits** — The Tax Office will examine business restructures with a focus on exit and succession-planning arrangements. The correct treatment of pre-CGT assets when a business is sold is also a focus of the Tax Office.

- **trusts** — The Tax Office will focus on increasing voluntary compliance of entities controlling or benefitting from trusts. It will also examine hybrid trusts and how the trusts are used to alter tax outcomes for some beneficiaries.
- **losses** — The correct application of the same business test is a key compliance concern of the Tax Office. It will also monitor other loss claims including foreign losses.
- **phoenix arrangements** — Attempts to evade tax through deliberate, systematic liquidation of related corporate trading entities remain a focus of the Tax Office.
- **international transactions** — The Tax Office intends to use internal and external data to verify the transactions and target high-risk transactions monitored by AUSTRAC. For the 2009/10 income year, the support and compliance activities will focus on:
 - foreign source income and deductions relating to cross-border transactions;
 - concealed assets and income;
 - ensuring foreign residents earning Australian income are meeting their obligations;
 - transfer pricing arrangements; and
 - thin capitalisations and correct application of safe harbour rules.

Goods and services tax

The GST compliance activities that the Tax Office plans to focus on include:

- **refund fraud** — All claims for GST refunds will be subject to credibility checks. The Tax Office will verify questionable claims through telephone interviews or field visits. It will also contact third parties to substantiate claims if required. It will also refer potential fraud cases to its investigations area.
- **property transaction audits** — The audits will focus on unreported sales, correct application of the margin scheme, and correct GST treatment of commercial and residential premises and retirement villages. The Tax Office says it will work more closely with the state revenue and land title offices to enable its data matching program to match sales data with business activity statements.
- **financial supplies** — The Tax Office will help taxpayers making financial supplies to understand their GST entitlements. It will also focus on correct GST treatment for:
 - initial public offers, capital raisings and share buy-backs;
 - costs incurred by credit card and charge card issuers, including acquisitions made under a loyalty reward program; and
 - securitisation and asset financing, including hire purchase.
- **cross-border transactions** — The Tax Office plans to examine material risks posed by:
 - businesses failing to correctly apply GST on supplies made to non-residents;
 - non-resident businesses that fail to correctly apply GST on supplies connected with Australia; and
 - registered businesses which fail to correctly apply GST on the acquisition of imported services.
- **refund claims under s 13 of the GST Transitional Act** — Refund claims for transactions made more than four years ago under this section will be reviewed.

The Tax Office will strengthen its information matching to identify unreported income and obligations by employers, investors and highly paid executives in public, private and foreign-owned companies.

The Tax Office will also expand its verification activities of remuneration payments for highly paid company directors and executives involving overseas accounts and incorrect reporting of shares and options received as part of their salaries.

Specific Advice for SMSFs

The Tax Office has released details on its new non-binding rulings program for self-managed superannuation funds (SMSFs).

SMSF advice

An SMSF advice sets out the Commissioner's opinion on the application of the *Superannuation Industry (Supervision) Act 1993* (SIS Act) and the *Superannuation Industry (Supervision) Regulations 1994* (SIS Regs) to SMSFs. The advice is provided in the form of:

- self-managed superannuation fund rulings;
- self-managed superannuation fund determinations;
- self-managed superannuation fund specific advice; or
- self-managed superannuation fund product rulings (see ***SMSF Product Rulings*** on page 8).

The Tax Office has released Law Administration Practice Statement PS LA 2009/5, in which it explains the forms of SMSF advice and guidance the Commissioner can provide.

Self-managed superannuation fund specific advice

Self-managed superannuation fund specific advice (SMSFSA) is a written expression of the Commissioner's opinion of how a provision of the SIS Act and/or SIS Regs apply to a particular transaction or arrangement that has been entered into or is being contemplated by the trustees of an SMSF.

The superannuation-related topics on which trustees of an SMSF can obtain specific advice include:

- investment rules, including:
 - investment in a company or unit trust;
 - acquisition of assets from related parties;
 - borrowing and charges;
 - in-house assets;
 - business real property;
- in-specie contributions/payments; and
- payment of benefits under a condition of release.

However, an application for an SMSFSA may be declined if:

- the SMSF has not yet been established;
- the trustees already have an SMSFSA on the particular transaction/arrangement and the application is considered unnecessary;
- the SMSF is, at the time of the request, the subject of a Tax Office audit relating to the particular transaction/arrangement raised in the application; or
- the particular transaction/arrangement relates to a 'reviewable decision' under s 10(1) of the SIS Act.

In addition, an application may be declined if the issue stated in the application relates to:

- the complying status of the SMSF;
- the trustee covenants;
- the residency status of the fund,

or if the trustees are asking the Commissioner to exercise his discretionary power.

It is important to note that the advice provided in an SMSFSA only applies to the SMSF named in relation to the particular transaction or arrangement stated in the application.

The Tax Office says an SMSFSA will only be provided if there is a precedential view of the relevant law or the particular transaction/arrangement raised in an application involves a straightforward application of the law.

Applying for an SMSFSA

An application for an SMSFSA must be submitted in writing and contain the information as required by the Tax Office. An application may be made by:

- the trustees of an SMSF;

- the fund's advisor;
- the legal personal representative of the fund; or
- the auditor of the SMSF acting under a duly-sighted letter of authority.

A standard application form (NAT 72441) is available on the Tax Office website at <www.ato.gov.au/businesses/content.asp?doc=/content/00207232.htm>. However, it is not mandatory to use the standard application form. A request for an SMSFSA will be considered by the Tax Office provided it is made in writing and contains all the necessary information. The necessary information includes:

- the fund details;
- the questions and issues to be considered by the Commissioner; and
- the facts describing the particular transaction or arrangement.

The Tax Office encourages trustees to provide a summary of research and analysis of the technical issues involved so their views on the particular transaction or arrangement can be considered in providing the SMSFSA. It is a requirement that the trustees make a full and true disclosure of all relevant facts in relation to the transaction or arrangement. The Tax Office says if the relevant facts are not fully and truly disclosed, the advice does not apply to the transaction or arrangement.

A tax agent may lodge an application via the Tax Agent Portal or the Business Portal.

The Tax Office says it aims to provide a response to an application for an SMSFSA within 28 days of receiving all the necessary information. If all the necessary information has not been supplied in the application, the Tax Office aims to contact the applicant within 14 days of receiving the application to ask for the information. If the application raises a complex matter that will take more than 28 days to resolve after receiving all the required information, the Tax Office aims to contact the applicant within 14 days of receiving all necessary information to negotiate an extended reply date.

Departure from an SMSFSA

The Tax Office says its basic administrative policy is to only depart from what is said in an SMSFSA if there are good and substantial reasons to consider the advice to be 'incorrect or inappropriate', such as where:

- there have been legislative changes since the advice was made that affect the basis for the advice;
- a tribunal or court decision has affected the interpretation of the law on which the advice is founded;
- commercial practice that provided the context for the advice has changed;
- the advice has been exploited in an abusive or unintended way; or
- the advice is no longer considered to be correct, because it is found on reconsideration to be based on or to express a view of the law that is wrong.

In the case of legislative change, the Tax Office says timing of a departure from previous advice or guidance will depend on the date of effect of the legislation, and would normally apply to transactions entered into after the date of effect, unless particular circumstances warranted another approach

Date of effect

An SMSFSA applies from the time when it is made.

Legal status of SMSFSA

An SMSFSA is not a private ruling for the purposes of Div 359 of Sch 1 to the *Taxation Administration Act 1953*. Therefore, an SMSFSA is not binding (legally or administratively) on the Commissioner and does not have the same review rights as a private ruling.

In addition, there are no formal review rights under the SIS Act or SIS Regs if the trustees of an SMSF are dissatisfied with an SMSFSA issued. However, the trustees may request the Commissioner take a 'second look' at the decision he had made. Furthermore, the Commissioner's decision not to issue an SMSFSA is not reviewable under the *Administrative Decisions (Judicial Review) Act 1977*.

- An SMSF that relies on an SMSFSA will remain responsible for its actions under the SIS Act or SIS Regs.

SMSF guidance

SMSF trustees and their advisors can also seek advice in the form of a non-binding SMSF guidance, which may be given in writing or orally, instead of having to apply for an SMSFSA.

The purposes of an SMSF guidance are to assist SMSF trustees to understand their obligations and entitlements under the SIS Act and SIS Regs administered by the Commissioner.

The Tax Office says oral guidance can only be provided on matters of a general, straightforward or simple nature. Where an SMSF trustee seeks assistance on a matter that is not of such characteristics, the Commissioner suggests that the trustee apply for an SMSFSA or written guidance. The Tax Office says this will ensure the trustee receives a properly considered opinion on the application of the law to the SMSF's circumstances.

According to the Tax Office, written guidance is usually provided if an SMSF trustee has enquired about the broad application of the law and has not provided specific details of the fund's circumstances. It says written guidance may take the form of a Tax Office publication, including:

- content on the Tax Office website;
- SMSF publications;
- published speeches, minutes of consultative forums, media releases and Decision Impact Statements;
- ATO Interpretative Decisions; and
- Law Administration Practice Statements (PS LAs).

Legal status of SMSF guidance

SMSF guidance is not legally or administratively binding on the Commissioner.

- An SMSF that relies on SMSF guidance will remain responsible for its actions under the SIS Act or SIS Regs.

SMSF product rulings

The Tax Office has released Self Managed Superannuation Funds Product Ruling SMSFPR 2009/1 in which it outlines the system of self-managed superannuation funds product rulings (SMSFPRs).

What is an SMSFPR?

An SMSFPR sets out the Commissioner's opinion (in his role as regulator of SMSFs) on the application of the SIS Act and SIS Regs to particular products where an SMSF is a potential investor.

The Commissioner will only provide advice on the precise scheme that is identified in an SMSFPR application. It is important to note that each SMSFPR is confined to its specific terms and it cannot be used as a precedent for similar schemes or for a future SMSFPR application regardless of how similar the facts of that application may be to an issued SMSFPR.

It is expected that SMSFPRs will usually be sought for products for which a product ruling is also sought on the tax issues. However, an SMSFPR differs from a product ruling in that it deals with:

- a product that is a scheme in which a number of SMSFs have entered into substantially the same contractual arrangements; and
- transactions with a common entity or group of entities in return for fees or other consideration.

The Tax Office states that an SMSFPR is only issued where the Commissioner and the applicant agree on all aspects of the advice. As a general proposition, the Commissioner says negative SMSFPRs or SMSFPRs expressing adverse views to that of the applicant are unlikely to be issued.

Each SMSFPR will also define the class of SMSFs to which the advice applies and set out those SMSFs, if any, which are specifically excluded. The ruling will also contain a statement that the advice will only apply to participants who are within the defined class of SMSFs entering the relevant scheme after the date of effect and within specific dates of a particular income year or years.

An SMSFPR will have no application to superannuation funds other than SMSFs (and former SMSFs where they remain regulated by the Commissioner).

Applying for an SMSF product ruling

Applicants for an SMSFPR are requested to complete an application form (Nat 72440) which is available on the Tax Office website at < www.ato.gov.au/businesses/content.asp?doc=/content/00207231.htm>.

Three copies of the completed form must be sent to the relevant 'SMSFPR contact' at the Tax Office (see **Further information** on page 10 of this explanatory memorandum).

An entity applying for an SMSFPR must also be able to sign and give the Commissioner each of the assurances required by the Tax Office's SMSFPR 'Agreement on terms of use' (see **Further information** on page 10).

However, the Tax Office says SMSFPRs will only be issued in respect of applications by, or on behalf of, an entity that is a principal of the scheme or is the implementer of the scheme. An SMSFPR will not be issued to either scheme participants (or potential scheme participants), or to brokers or similar entities whose business involves promoting or marketing the 'products' of other entities who are the implementers of the scheme being promoted or sold.

To ensure sufficient time to finalise the advice, the Tax Office encourages applicants to submit applications early in the financial year to which the proposed SMSFPR relates.

Proposed changes to a scheme

Where an implementer (promoter) of a scheme proposes to implement that scheme differently from the scheme set out in either their application, preliminary draft SMSFPR or a published SMSFPR, then applicants are instructed to notify the Tax Office in writing before the change occurs providing full details of the nature and extent of the change, the reason for the change and any implications that result from the change.

The Tax Office notes that any revision of arrangements or submission of additional material, whether requested by the Tax Office or not, will be treated as a fresh application, made at the time the revised or additional material is received. The Tax Office also warns that considerable delays can be caused by the frequent submission of additional or updated material.

Where a scheme is implemented differently from the details set out in the SMSFPR due to changes outside the implementer's control or knowledge, the Tax Office says the implementer should notify the Commissioner within 14 days of becoming aware of the difference in implementation.

Later legislative changes

Although each SMSFPR will deal with the SIS Act or SIS Regs enacted as at the time it is issued, later legislative amendments may impact on the ruling. If the later legislation expresses the same ideas as the original legislation and the outcomes are unaltered then the SMSFPR continues to apply, as issued. However, if the law changes the ideas expressed in the original legislation and the outcomes are altered then the later legislation takes precedence over the application of the advice and, to that extent, the advice will be superseded.

No assurance on commercial viability

The Tax Office warns that a SMSFPR provides no assurance that:

- the product is commercially viable;
- charges are reasonable or represent industry norms; or
- projected returns will be achieved or are reasonably based.

The Tax Office also reminds trustees of SMSFs to ensure that all of the SMSF's investments are in accordance with the SMSFs properly formulated investment strategy.

Date of effect

SMSF 2009/1 (not previously released in draft form) applies from 12 August 2009.

Legal status of SMSFPR

An SMSFPR is not legally or administratively binding on the Commissioner. However, if the Commissioner later takes the view that the law applies less favourably to SMSFs than a ruling indicates, the fact that the trustee acted in accordance with the ruling would be a relevant factor in the Commissioner's exercise of any discretion as to what, if any, action is to be taken.

- An SMSF that relies on an SMSFPR will remain responsible for its actions under the SIS Act or SIS Regs.

Further information

The Tax Office has released the following publications to assist trustees and their advisers:

SMSF specific advice:

- **Getting help with your self-managed super fund questions** — The three main ways taxpayers can get help from the Tax Office with their SMSF questions. See <www.ato.gov.au/businesses/content.asp?doc=/content/00206765.htm>.
- **How to apply for SMSF specific advice** — Explains the process for applying for an SMSF specific advice. See <www.ato.gov.au/businesses/content.asp?doc=/content/00206984.htm>.

SMSF product ruling advice:

- **Facts about self-managed super fund product ruling** — SMSFPR was introduced to provide certainty to SMSF trustees participating or potentially participating in a product. See <www.ato.gov.au/businesses/content.asp?doc=/content/00207279.htm>.
- **Important information for SMSF participants** — Provides information for SMSF participants in arrangements on which an SMSF product ruling has been published. See <www.ato.gov.au/businesses/content.asp?doc=/content/00207493.htm>.
- **Changes to a scheme or request to withdraw SMSFPR** — Provides information to applicants on how an SMSF product ruling applies if the arrangement differs from the product ruling. See <www.ato.gov.au/businesses/content.asp?doc=/content/00206432.htm>.
- **Contact numbers for SMSFPR** — A list of Tax Office contact officers for SMSF product rulings. See <www.ato.gov.au/businesses/content.asp?doc=/content/00206479.htm>.
- **Important information for intending applicants of SMSFPR** — Provides general information for intending applicants of an SMSF product ruling. See <www.ato.gov.au/businesses/content.asp?doc=/content/00207513.htm>.
- **Agreement on terms of use** — A template for agreement on SMSF product ruling 'terms of use'. See <www.ato.gov.au/businesses/content.asp?doc=/content/00206501.htm>.
- **Information required for SMSFPR application** — Provides an overview about what an SMSF product ruling is and how a product ruling is sought. See <www.ato.gov.au/businesses/content.asp?doc=/content/00206630.htm>.

SMSFs and Disposal of Shares

In ATO ID 2009/92, the Tax Office states that the exceptions contained in s 295-85 of ITAA 1997 do not apply where the trustee of a complying self-managed superannuation fund (SMSF) realises losses on the disposal of shares. Instead, the losses are to be calculated under the relevant CGT provisions. The Tax Office says, in line with the operation of s 295-85(2), any loss realised by the fund on the sale of the shares is determined under the CGT provisions — a loss on the sale of the shares cannot be claimed as a deduction under s 8-1 of ITAA 1997.

In 2007/08, a trustee bought shares in a gold mining company with the intention to hold the shares for a short period and make a profit when the shares were sold. In the fund's 2007/08 tax return, the trustee claimed a deduction under s 8-1 of ITAA 1997 for losses incurred in respect of mining shares sold during the income year on the basis that the shares were purchased for profit by resale and were not intended as a long-term investment.

Legislation

A complying superannuation fund (including an SMSF) is required to calculate gains or losses realised on the disposal of CGT assets owned by the fund just before the time of the relevant CGT event under the CGT rules: s 295-85 of ITAA 1997.

Specifically, the section states that the following provisions do not apply if a CGT event happens to a CGT asset owned by a complying superannuation fund:

- section 6-5 of ITAA 1997 (ordinary income);
- section 8-1 of ITAA 1997 (general deductions);
- section 15-15 of ITAA 1997 (income from profit-making undertaking or plan);
- section 25-40 of ITAA 1997 (loss from profit-making undertaking or plan);
- section 25A of ITAA 1936 (income from profit-making undertaking or scheme); and
- section 52 of ITAA 1936 (loss on property acquired for profit-making).

However, s 295-85(3) provides two exceptions. A complying superannuation fund is not subject to the operation of s 295-85 if:

- the capital gain or capital loss from a CGT event is attributable to currency exchange rate fluctuations; or
- the CGT asset is a:
 - debenture stock, bond, debenture, certificate of entitlement, bill of exchange, promissory note or other security;
 - deposit with a bank, building society or other financial institution;
 - loan (secured or unsecured);
 - contract under which the fund is liable to pay an amount regardless of whether the liability is secured or not.

Essentially, the section was a rewrite of former s 304 of ITAA 1936, which similarly operated to provide that the CGT provisions were the primary provisions for determining the gains and losses of CGT assets disposed of by complying superannuation funds. The Explanatory Memorandum accompanying Tax Laws Amendment (Simplified Superannuation) Bill 2006 stated at para 3.14 that 'the rewritten provisions of Div 295 do not change the law as it currently operates under Pt IX of ITAA 1936' (which relates to the taxation of superannuation and related business). Therefore, the definition of 'security' for the purposes of former s 304 remains relevant for s 295-85.

The Explanatory Memorandum which accompanied the Taxation Laws Amendment (Superannuation) Bill 1989 stated that 'shares do not fall within the definition of security for the purposes of s 304'. Accordingly, a disposal of shares does not qualify for the exceptions contained in s 295-85(3).

- The correct treatment of gains and losses from the disposal of shares is one of the focuses of the Tax Office for its 2009/10 Compliance Program. See *Tax Office Compliance Program 2009/10* on pages 1–5.

Victory for Sham Victim

The AAT has held that a taxpayer who was the victim of a sham was entitled to deduct interest and bank charges associated with loans obtained by the taxpayer to meet his obligations under a guarantee: *Re Willersdorf-Greene and FCT* [2009] AATA 649.

According to the evidence presented to the Tribunal, directors of Company X approached Mr W (the taxpayer) to secure an investor in a fuel scheme. Under the belief he would derive assessable income, the taxpayer approached Company Z. On the basis the taxpayer entered into a guarantee arrangement in which he secured repayments by means of a mortgage over his house Company Z extended a loan to Company X. However, Company X defaulted on the loan. The taxpayer then discovered that he had been the victim of a sham. Consequently, the taxpayer took out two loans secured against his property to fulfil the guarantee.

In the Tribunal's view, there was a connection between the taxpayer giving the guarantee and Company Z entering into the scheme. It said that without the taxpayer providing the guarantee, the investor would not

have invested in the fuel scheme. It also said that while the guarantee was called upon by the investor after the scheme was revealed as a sham, the claim had its foundation in the arrangements made for Company Z to invest in the scheme and for the taxpayer to gain or produce assessable income.

The Tribunal noted that the guarantee was initially a contingent liability to the taxpayer. However, it said that the guarantee was a liability the taxpayer accepted for the purpose of producing or gaining assessable income. It also said it made no difference that the taxpayer was not called upon to meet that liability until a date after there was no possibility of him ever deriving income under the scheme.

In conclusion, the Tribunal allowed the taxpayer's claim for deductions in relation to the interest and bank charges associated with the loans obtained to meet his obligations under the guarantee to Company Z.

Director Liable to Indemnify Commissioner

The NSW Supreme Court has held that payments made by a company to the Tax Office were voidable transactions pursuant to s 588FE of the *Corporations Act 2001* (see *Cooper v FCT* [2009] NSWSC 880). An affidavit made by the company's liquidator, asserting the company was insolvent at the time the payments were made, was not challenged by either the Commissioner or the taxpayer. Therefore, the Court was satisfied that the payments were made when the company was insolvent. Accordingly, the Court ordered the Commissioner to repay the company an amount of \$126,153 in accordance with s 588FF of the *Corporations Act*.

The Court was also satisfied a portion of the payments fell within the scope of s 588FGA of the *Corporations Act*. This section requires a director of a company to indemnify the Commissioner for certain payments (eg PAYG withholding payments) where a court makes an order under s 588FF against the Commissioner. While s 588FGB provides statutory defences for a director, the Court found that the taxpayer failed to establish the requirements for those defences. In doing so, the Court also held that the taxpayer, who was a director of the company at the time of the payments, was liable to indemnify the Commissioner for an amount of \$70,414.

The Corporations Act

Broadly, s 588FF gives a court the ability to set aside voidable transactions, which are prescribed in s 588FE, provided that the transaction was entered into within a particular time prior to the appointment of a company's liquidator.

Upon an application by a company's liquidator, a court may make one or more orders if it is satisfied that a transaction of the company is voidable because of s 588FE. These orders include:

- an order directing a person to pay to the company an amount equal to some or all of the money that the company has paid under the transaction;
- an order directing a person to transfer to the company property that the company has transferred;
- an order requiring a person to pay to the company an amount that fairly represents some or all of the benefit that the person has received because of the transaction; and
- an order releasing or discharging (wholly or partly) a debt incurred, or a security or guarantee given, by the company under or in connection with the transaction.

Where a court makes an order under s 588FF against the Commissioner, each person who was a director of a company when a payment was made may be liable to indemnify the Commissioner in respect of any loss or damage resulting from the order if the payment was of a type prescribed in s 588FGA(1). The prescribed payments include:

- a payment paid under a liability created by notice under s 222AHA of ITAA 1936; and
- a payment paid under Subdiv 16-B of the *Taxation Administration Act 1953* (which relates to PAYG withholding).

A director can rely on the statutory defences in s 588FGB, which are similar to the defences of insolvent trading contained in s 588H. It is important to note that the onus is upon the director to prove the defences in a court. These defences include:

- the director had reasonable grounds to expect, and did expect, that the company was solvent at the time of making a payment and would remain solvent even if it made the payment;

- the director had reasonable grounds to believe, and did believe, on the basis of information provided by a competent and reliable person that the company was solvent at the time of making a payment and would remain solvent even if it made the payment;
- the director, because of illness or for some other good reason, did not partake in the management of the company at the payment time; and
- the director had taken all reasonable steps to prevent the company from making the payment or there were no such steps the director could have taken.

In ascertaining whether the director took a reasonable course of action to prevent the payment, a court will consider a range of matters including (but not limited to):

- any action the director took to appoint an administrator for the company;
- when that action was taken; and
- the results of that action.