Australian Government
Australian Taxation Office

Taxpayer Alert

TA 2009/8

Exploitation of 1999 superannuation transitional provisions to obtain taxation and regulatory benefits

The Taxation Office view on this arrangement is set out in the fact sheet In-house assets and transitional rules

FOI status: may be released

Taxpayer Alerts are intended to be an 'early warning' of significant new and emerging higher risk tax planning issues or arrangements that the Australian Taxation Office has under risk assessment, or where there are recurrences of arrangements that have been previously risk assessed .

Taxpayer Alerts will provide information that is in the interests of an open tax administration to taxpayers. Taxpayer Alerts are written principally for taxpayers and their advisers and they also serve to inform tax officers of new and emerging higher risk tax planning issues. Not all potential tax planning issues that the Tax Office has under risk assessment will be the subject of a Taxpayer Alert, and some arrangements that are the subject of a Taxpayer Alert may on further examination be found not to be of concern to the Tax Office. In these latter cases, the Taxpayer Alert will be withdrawn and a notification published which will be referenced to that Taxpayer Alert .

Taxpayer Alerts will give the title of the issue (which may be a scheme, arrangement or particular transaction), briefly describe the issue and will highlight the features which are of concern to the Tax Office. These issues will generally require more detailed analysis to provide the Tax Office view to taxpayers .

Taxpayers who have entered into or are contemplating entering into an arrangement similar to that described in this Taxpayer Alert might obtain their own advice or contact the Tax Office to seek guidance in relation to the income tax and superannuation regulatory issues covered in the Taxpayer Alert .

This Taxpayer Alert is issued under the authority of the Commissioner .

This Taxpayer Alert describes an arrangement that involves the transfer of benefits associated with the 1999 'transitional provisions' for self-managed superannuation funds (SMSFs) with pre-existing interests in unit trusts. The concern is that these arrangements may not satisfy the requirement that the pre 1999 SMSF has to be continuously maintained to provide retirement benefits to members both before and after its sale.

Context for the arrangement

Transitional provisions that expire on 30 June 2009 were put in place when the definition of 'in-house asset' in the superannuation laws was amended with effect from 11 August 1999 to include investments in a related trust. Amongst other things, these transitional provisions allow SMSFs up until 30 June 2009 to pay up on any partly paid shares and units, or make additional investments in a related entity, if that investment was acquired by 11 August 1999. Where in-house assets for an SMSF exceed 5% of the market value of the fund's assets, the trustee needs to rectify the breach (usually within 12 months) or the fund may be made non-complying[1] and the fund's trustee may be liable to civil penalties.

Description

This Alert applies to arrangements with features substantially equivalent to the following:

1.

An organiser ('the organiser') has in possession one or more inactive SMSFs registered before 11 August 1999 ('pre 1999 SMSF') that hold an interest in a related unit trust which was acquired before 11 August 1999 ('the interest' in 'the unit trust').

The pre 1999 SMSFs may be inactive because, while registered with a nominal contribution, they may not have:

- had any active members;
- received any subsequent contributions;
- made any investments; or
- been continuously maintained for providing superannuation benefits to members on retirement e.g. where the fund was established, or subsequently sold, for the purpose of making a profit.

2.

The organiser advertises the sale of a pre 1999 SMSF and the unit trust. Typically, the advertising material states that the arrangement qualifies under the transitional provisions and therefore provides taxation and superannuation regulatory benefits, including:

a. Allowing ownership of a residential property through the pre 1999 SMSF and gearing through a related unit trust, then leasing the property to a related party (e.g. a member of the SMSF), which would not otherwise be permitted for post 1999 SMSFs;

b. Deducting interest expense which may not be deductible to other parties (i.e. private or domestic expenses of a member of the SMSF, or expenses incurred in producing exempt income of the SMSF);

c. Reducing/avoiding potential capital gains tax through the lower taxes paid by the SMSF (i.e. on the property held through the unit trust), and;

d. Circumventing the superannuation regulatory restrictions (especially the in-house asset rules) that would result in the SMSF's income or capital gains being subject to higher rates of tax.

3.

The organiser may also allege that the arrangement is supported by a Tax Office view (such as ATOID 2002/388) without any qualification regarding materially different facts. This may mean that the arrangement does not qualify under the transitional provisions and that the advertised superannuation regulatory or taxation benefits would not be available.

4.

A taxpayer pays a fee to the organiser to effectively gain control of, or membership in, an inactive pre 1999 SMSF which holds the interest in the unit trust.

5.

The organiser then changes the control of the pre 1999 SMSF to the taxpayer by arranging for a change in the member(s) and trustee(s), or director(s) in the case of a

corporate trustee, and moves previous member(s) account balance(s) out of the SMSF.

6. The fund investment strategy of the pre 1999 SMSF may be updated to cover the fund's new investments (to meet other superannuation regulatory requirements).

7. To attempt to exploit the transitional provisions (and gain the advertised superannuation regulatory or taxation benefits), the new member(s) make contributions and/or rollover existing benefits held in complying superannuation fund(s) to the pre 1999 SMSF, which are then invested in the related unit trust. This investment may include paying up partly paid up units or applying the funds to existing units to facilitate the purchase of a property or land.

8. The organiser charges a substantial fee for establishing this arrangement, based upon the perceived commercial advantages of the advertised superannuation regulatory or taxation benefits.

Features which concern us

Superannuation regulatory issues

The ATO considers that arrangements of this type involve the following superannuation regulatory issues, being whether:

a. the inactive pre 1999 SMSF meets the definition of a superannuation fund at all times, i.e. both before and after the implementation of this arrangement;

b. the transitional provisions contained in sections 71A to 71F of the *Superannuation Industry Supervision Act 1993* (SIS Act) apply (e.g. due to the exit of the original member/s from the SMSF); and

c. section 85 of the SIS Act, which prohibits a fund from entering into any scheme to avoid the application of the in-house asset, has been breached.

Taxation issues

The ATO considers that arrangements of this type also involve the following taxation issues, being whether:

d. the interest expense incurred by the related unit trust is deductible under section 8-1 the *Income Tax Assessment Act 1997* (ITAA 1997);

e. any capital gains tax concessions for complying superannuation funds apply;

f. any fee or commission paid is allowable as a deduction by the Australian resident taxpayer for that income year;

g. the general anti-avoidance provisions in Part IVA of the *Income Tax Assessment Act 1936* (ITAA 1936) apply to the arrangement;

h. any fee or commission received by the organiser/s of this arrangement constitutes assessable income for the relevant income year; and

i.

any entity involved in the arrangement may be a promoter of a tax exploitation scheme for the purposes of Division 290 of Schedule 1 to the *Taxation Administration Act 1953* (TAA 1953).

The Australian Taxation Office is currently examining these arrangements.

Note 1
Base penalties of up to 75% of the tax avoided can apply where someone makes a false and misleading statement to the Commissioner. Reductions in base penalty will be available if the taxpayer makes a voluntary disclosure to the Tax Office. If you have any information about the current arrangement, phone us on 13 10 20. Tax agents wanting to provide information about people or companies who may be promoting arrangements covered by this alert should call the tax practitioner integrity service on 1800 639 745.

Note 2
Penalties of up to 5,000 penalty units for individuals, 25,000 penalty units for bodies corporate or up to twice the amount of consideration received or receivable may apply to promoters of tax exploitation schemes under Division 290 of Schedule 1 to the TAA 1953. The Commissioner can also apply to the Federal Court of Australia for restraining and performance injunctions against promoters where prohibited conduct has occurred, is occurring or is proposed.

Note 3
Where appropriate, section 167 of the ITAA 1936 may be used to determine the amount of taxable income upon which the taxpayer should be assessed, see Law Administration Practice Statements, PSLA 2007/7 and PSLA 2007/24.

Date of Issue: 17 April 2009

Date of Effect: 17 April 2009

[1]
Non-complying funds are subject to 45% tax rates on their income (and assets other than undeducted contributions in the year that the fund becomes non-complying).

Subject References:
Self-managed superannuation fund
Sole purpose
In-house assets
Unit trust

Legislative References:
Income Tax Assessment Act 1936
167
Pt IVA
Taxation Administration Act 1953
Division 290 of Schedule 1
Superannuation Industry (Supervision) Act 1993
71A
71A
71A
71A
71A
71F
Income Tax Assessment Act 1997
8-1
Superannuation Industry (Supervision) Regulations 1994
The Regulations

Related Practice Statements:
PS LA 2007/7
PS LA 2007/24

Other References

ATO ID 2002/388

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