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SMSF liable for double stamp duty on property acquisition

In a recent decision of the NSW Civil and Administrative Tribunal, the late substitution of a custody trustee has exposed a SMSF to double duty on its acquisition of a property.

FP Transitions Pty Ltd ('Transitions') entered into a contract in March 2015 to purchase a property for $610,000. The intention was that Transitions would, as a 'custody trustee', hold the property in trust for an SMSF under a limited recourse borrowing arrangement.

However, Transitions was rejected as custody trustee by the bank financing the purchase, which insisted that a non-trading corporate entity act as custodian. Therefore, Happy Days Property Pty Ltd ('Happy Days') was registered in April 2015 as a new company and appointed as custodian trustee.

In April 2015, the purchase of the property was completed in accordance with an undated transfer document. The transfer was stamped on a concessional basis at $10 under S.18(3) of the *Duties Act 1997*, while the contract was stamped with duty of $22,940. However, the NSW Office of State Revenue reassessed duty on the Transfer as being payable on an ad valorem basis (i.e., another $22,940), as it had concluded that S.18(3) did not apply.

The main question for the Tribunal was whether the transfer qualified for relief from double duty under S.18(3), having regard to the fact that the transfer of property was not made in conformity with the contract for the sale of the property (the 'non-conformity' here being the substitution of Happy Days for Transitions). It was noted in particular that S.18(3) requires that the purchaser and the transferee are related persons both when the agreement was entered into and at settlement.

The Tribunal decided that S.18(3) could not be satisfied, given that Happy Days did not exist at the time the agreement was entered into (in March 2015), and there was no submission or evidence that Happy Days could, before it was registered, be related to Transitions.

Refer *Happy Days Property Pty Ltd v Chief Commissioner of State Revenue* [2016] NSWCATAD 289

SMSF may own property as tenants in common with a related party

The superannuation legislation imposes many restrictions in relation to dealings between an SMSF and related parties. An investment by an SMSF in a related party or related trust is generally prohibited as an 'in-house asset', and an SMSF is generally prohibited from acquiring an asset from a related party. 'Related party' is defined broadly in the superannuation legislation, and includes (among others) the members of the SMSF, their relatives, some contributing employers, related companies, and related trusts.

However, S.71(1)(i) of the Superannuation Industry (Supervision) Act 1993 provides that property (including residential property) owned by an SMSF and a related party as tenants in common is not included as an in-house asset. Therefore, an SMSF may own property as tenants in common with a related party, provided that the other requirements of the superannuation legislation (such as the 'sole purpose test', the 'prudent person test', the 'arm's-length test', etc are complied with).

It is also important to note the following:

- the property must be owned by the SMSF (that is, the trustee of the SMSF) and the related party as **tenants in common**, rather than as joint tenants, and this should be noted on the title documents (such as a certificate of title);
- the property in question cannot be leased to, or used by, a related party, unless the property is business real property (that is, real estate used wholly and exclusively for business purposes);
- there must **not** be a mortgage or charge over any part of the property in question; and
- the ownership as tenants in common must be properly documented and administered (e.g., if rent money is received from property owned as tenants in common, then the rent money should be divided between the SMSF and the other party to reflect their respective interests in the property, and this should be properly documented).

It may be possible for the SMSF to subsequently acquire all or part of the interest of the related party in the property (although if the property is not business real property, then this may infringe the general prohibition against an SMSF acquiring an asset from a related party). Detailed advice should be sought in this regard as appropriate.

ATO offer to remit penalties extended: Personal services income and SMSFs

The ATO's offer to remit penalties regarding arrangements in which personal services income (PSI) is diverted to SMSFs has been extended from **31 January to 30 April 2017.**

Since April 2016, the ATO has been reviewing arrangements where individuals purport to divert PSI to an SMSF. As described in **Taxpayer Alert TA 2016/6**, these arrangements involve individuals (generally SMSF members around retirement age) performing services for a client without directly receiving any (or adequate) consideration for the services. The client instead remits the consideration for the services to a non-individual entity such as a company or trust. The income is then distributed from that entity to the individual's SMSF, purportedly as a return on an investment in the entity. The income is then treated by the SMSF as subject to concessional tax of 15% or as exempt current pension income.

The ATO's view is that such arrangements may be ineffective at alienating income so that the income remains assessable income of the individual, or it is PSI. Also, the amounts received by the SMSF may constitute non-arm's length income of the SMSF, subject to tax at 47%, and there are superannuation compliance issues to consider.

The ATO has acknowledged that people may not have had sufficient time to consider its voluntary disclosure offer with all the superannuation changes taking place (including the recently legislated superannuation reforms and review of non-arm's length LRBAs). Accordingly, as stated above, the ATO has now extended the due date to contact it in relation to TA 2016/6 from 31 January to 30 April 2017.

Individuals and trustees who are not currently subject to ATO compliance action, and who come forward before 30 April 2017, will have administrative penalties remitted in full. However, shortfall interest charges still apply.

The ATO anticipates that, where individuals and trustees come forward to work with it to resolve issues, in most cases the PSI distributed to the SMSF by the non-individual entity would be taxed to the individual at their marginal tax rate. The ATO says it will take the individual's co-operation into account when determining the final outcome, although issues affecting the SMSF will be addressed on a case-by-case basis.

Superannuation death benefits and transfer balance cap

The ATO has recently issued Draft Law Companion Guideline **LCG 2017/D3** to clarify how superannuation income streams that are superannuation death benefits will be treated under the transfer balance cap provisions.

Under recently enacted legislation, a transfer balance cap is imposed as from 1 July 2017 (which is $1.6 million for the 2018 income year) to limit the amount of capital individuals can transfer to the retirement phase to support superannuation income streams.

ADVICE

Where an individual exceeds their transfer balance cap (e.g., the total value of their retirement phase income streams exceeds $1.6 million indexed), their superannuation fund(s) will lose the entire pension exemption unless the excess amount (plus notional earnings) is rolled-back (commuted) to accumulation phase within a specified time frame. 'Excess transfer balance tax' is also imposed in respect of the excess amount plus a notional earnings amount.

Normally, the value of a superannuation income stream in the retirement phase is counted towards an individual's transfer balance cap at the time the pension commences to be payable to the individual. However, if an income stream commenced before 1 July 2017, the value of that income stream on 1 July 2017 will be counted towards their transfer balance cap (i.e., a credit in the individual's transfer balance account will arise, equal to the value of their pension, on 1 July 2017).

Where an individual receives a death benefit pension that is a **reversionary pension** (i.e., the pension has automatically reverted to them upon the death of a fund member), the ATO effectively confirms (in LCG 2017/D3) that their pension will also be counted towards the transfer balance cap (e.g., $1.6 million for the 2018 income year). However, their reversionary pension will **not count towards the cap** (i.e., a credit in the individual's transfer balance account will not arise) **until**:

- for a reversionary pension that commenced on or after 1 July 2017 – 12 months after the individual started to receive the reversionary pension; or
- for a reversionary pension that commenced before 1 July 2017 – the later of 1 July 2017 or 12 months after the pension first became payable to the individual.

The reason for the 12-month delay (especially for a reversionary pension commencing on or after 1 July 2017) is to give a reversionary beneficiary sufficient time to adjust their superannuation affairs (especially if the reversionary pension causes the individual to breach their transfer balance cap) before any consequences for breaching their cap take effect.

The amount that is counted towards a beneficiary's transfer balance cap (i.e., the credit that arises in the beneficiary's transfer balance account), for a **reversionary pension**, is equal to the value of the pension on the day the pension commences (or the value of the pension just before 1 July 2017, for a reversionary pension that commenced before this date).