DBA Butler Pty Ltd Lawyers

NEWS

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Trust Cloning for SMSFs

The ATO has recently examined the ability to split a superannuation fund without incurring a capital gains tax ('CGT') liability in ATO Interpretative Decision ID 2005/176. However, the ATO have since indicated that extra criteria needs to be satisfied by an SMSF to rely on this strategy.

What is trust cloning?

Trust cloning involves setting up a trust that is identical to or is a 'clone' of the original trust so that assets may be transferred to the cloned trust without giving rise to a CGT liability.

Generally, a CGT liability arises when an asset is transferred to an existing trust. An exemption to this applies where an asset is transferred from one trust to another trust and the beneficiaries and terms of both trusts are the same. Thus, care should be given to the timing of any asset transfer and the membership of each fund. Normally, CGT of 10% would be payable on capital gains made by SMSFs on assets held for more than 12 months.

Why 'clone' an SMSF?

In the past, many SMSFs were set up as employer-sponsored funds in small to medium enterprises ('SME'). This meant that, eg, two business partners and their spouses were members of the one SMSF.

The four member limit on SMSFs means that these SMSFs provide limited planning opportunities for the members, particularly if they want to provide for their children to become members or ensure that the surviving spouse has a 50% control of the fund in the event of death of a member. Having separate funds for each family is also desirable where the business partners want to go their own way on the break-up of the business (which may or may not be on amicable terms).

A Typical SME SMSF

Take the example of John and Bob, two business partners who have been working together for 20 years. They are members of the same SMSF set up by the business entity (ie, the standard employer-sponsor of the business). Since setting up the fund, John and Bob have married and their spouses are now also members of the same SMSF. The SMSF has substantial holdings of commercial properties, units in unit trusts (dating pre-August 1999) and listed securities. Most of these assets have appreciated significantly.

John and Bob are now 60 years of age, and are looking at their superannuation and succession planning before retirement. John and Bob have two children each, and want to provide that on the death of their spouse, their children will be paid pensions from the SMSF. Therefore, the children will eventually need to become members of the SMSF.

As the SMSF can only have a maximum of four members, John and Bob have decided to split the assets in the SMSF and have their own SMSF.

So, how might John and Bob (and their spouses) go about separating their benefits in the SMSF and what are the issues to look out for?

The issues to watch out for

While CGT relief for trust cloning of family trusts has been available for some time, it has not been relied on as an alternative until the ATO's recent ID 2005/176 that applies this principle to a superannuation fund.

The example of John and Bob above illustrates one case where trust cloning relief from CGT liability is particularly attractive. Without CGT relief, the trustee of the SMSF would incur a significant CGT liability on the transfer of assets from the original SMSF to the new SMSF.

However, trust cloning for SMSFs is not as easy as simply setting up a new fund that is identical to the original fund in terms of the same trust deed and the same beneficiaries. There are a number of issues to cover, eg, ensuring all the correct documentation is attended to for CGT, GST (if applicable), ATO and superannuation purposes. There is also the need to examine relevant stamp duty provisions and the availability of any exemptions. The rules under the *Superannuation Industry (Supervision) Act 1993* (Cth) also need to be considered, such as:

- the prohibition against acquisition of assets from a related party of the fund;
- the in-house asset rules and whether the new SMSF will be able to access the transitional relief for units held in related trusts that were acquired prior to August 1999;
- retaining the eligible service period of the members in the existing SMSF and whether any other grandfathering relief in the new fund is placed in doubt, eg, defined benefit pension powers.

Following the release of ID 2005/176, the ATO have since stated that the members' interests in the assets of each fund must be maintained on an identical basis for the CGT exemption to apply to a cloned fund. The ATO has been asked to clarify the basis for this view as it is inconsistent with their prior publications.

New Tax Team

We are pleased to announce a recent addition to our tax team at DBA. Marco Saccotelli joins DBA with more than 10 years experience in the fields of taxation, business law, estate and business succession planning and has a masters in taxation law.

DBA has a unique tax practice which combines the expertise of lawyers who work on a range of tax issues relating to SME's, individuals, companies, superannuation funds and trusts. In particular, our tax team works extensively in a wide range of tax matters including CGT, restructuring, superannuation, deceased estates, stamp duty, land tax and preparing tax objections. Contact Daniel Butler, Marco Saccotelli or Andrea Comini for assistance on your taxation queries.

Latest Superannuation Publication

'*Superannuation and Estate Planning Strategies*' is now available. It is current up to July 2005 and contains the latest on pensions and other rapidly changing areas of superannuation. To order this publication, fill out the form below. *Superannuation and Estate Planning Strategies* covers the same material as chapter 7 of the *Wills, Estates & succession Planning Service*. To order the full Service, which includes '*Superannuation and Estate Planning Strategies*', along with 15 other chapters, go to www.dbabutler.com/index.php?p=WES.

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