DBA Butler Pty Ltd Lawyers

NEWS

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New laws open up investment in instalment warrants

Recent amendments to superannuation legislation have opened the door to a number of investment opportunities for SMSFs.

Subject to some limited exceptions, super funds have generally been prohibited from borrowing. Whether an investment in instalment warrants constitutes a breach of this prohibition has been a source of some uncertainty in recent years.

While the general prohibition will remain in force, recent amendments have provided an express exception to the prohibition. Explanatory material to the new legislation describes the exception as permitting investment in instalment warrants. However, the laws themselves do not expressly refer to instalment warrants and may possibly apply to a range of other investments by SMSFs.

The new laws took effect from 24 September 2007, while the ATO and APRA will continue to use their discretion in managing breaches prior to that date.

Requirements for satisfying the exception

Broadly, a trustee will not be prohibited from borrowing money if each of the following requirements are met:

- The money is or has been applied for the acquisition of an asset.
- The trustee would not be prohibited from investing in that asset directly. Therefore, the arrangement cannot be used to, eg, acquire an asset from a related party which is not business real property, or for any other investment which would otherwise breach superannuation law.
- The asset is held on trust so that the super fund's trustee acquires a beneficial interest in the asset.
- The super fund's trustee has a right to acquire legal ownership of the asset by making one or more payments (ie, instalment payments).
- The lender's rights against the super fund's trustee for a default on the borrowing or charges related to the borrowing (eg, interest) are limited in recourse to the underlying asset only.

Exception to the in-house asset rules

A new exception to the in-house asset rules has also been created as an instalment warrant typically gives rise to a trust relationship in respect of an underlying asset. An investment which would be an investment in a related trust, but which is also a borrowing that meets the requirements of the new borrowing exception (above), will not be an in-house asset of the fund.

However, this again requires that the asset itself would not be an in-house asset if the fund invested in it directly. The trust's property must also be limited to the asset being acquired.

Care is needed

Despite the potentially broad application of the new rules, trustees and advisers should not assume that a financial product or arrangement is covered by the new exception, even if it claims to be.

Whether an arrangement constitutes a borrowing and whether that borrowing satisfies the new exception depends on the detailed terms and conditions of the arrangement and this may not be ascertainable from a PDS alone. If there is any doubt, expert advice should be obtained beforehand.

The general prohibition on trustees from giving a charge (eg, a mortgage) over any asset of a super fund also remains in place. The ATO and APRA have indicated that a shareholder application (ie, the use of existing fund assets such as shares as initial payment for an instalment warrant) may breach the charging prohibition.

These new rules will be covered in detail at the next DBA Network seminar on 16 November (Melbourne) and 23 November (Sydney).

Online SMSF Deeds: the Risks

A recent case, *Legal Practice Board v Computer Accounting And Tax Pty Ltd* [2007] WASC 184, has highlighted the risks associated with non-lawyers (eg, accountants and financial planners) varying SMSF deeds especially via web.

Facts of case

A registered tax agent (Ms Frigger, who was not a lawyer) was running a business through a company structure. The business prepared a trust deed to establish a new SMSF. In order to do this, Ms Frigger had obtained a pro-forma trust deed from an

online legal document supplier. Ms Frigger merely inserted the names of the trustees of the fund in the pro-forma document. The relevant Legal Practice Act provided that a person must not engage in legal practice unless the person is a certificated legal practitioner (ie, a lawyer) with a current practising certificate.

The originating motion stated that the company was guilty of contempt of the Legal Practice Act.

The Court's Judgment

Ultimately, however, the proceeding against the adviser was dismissed due to a technicality. Namely, Ms Frigger was running the business through a corporation and the judge held the prohibition in the relevant provision on a 'person' engaging in legal practice in this case did not extend to a 'corporation' engaging in legal practice.

However, the case highlights that:

- By merely inserting names in the pro-forma document, the company had engaged in 'legal practice' as it had 'drawn or prepared a deed related to or dealing with an interest in real or personal estate'.
- If in bringing documents into existence a person exercises their mind as to what is the appropriate form of words to accommodate the particular case, then this can be regarded as drawing or preparing a legal document. A process of that kind goes beyond mechanical or clerical tasks and is of a kind required to be performed by a lawyer (eg, who is added as a party to a deed and what conditions must be satisfied in the variation clause).
- The fact that the deed was not executed nor had any property been transferred to the fund was not relevant. The drawing and provision of documents to the client constituted the provision of legal services.

It was not a defence that the pro-forma trust deed had been drafted by lawyers. Lawyer sign-off is often misrepresented by many suppliers as it implies a lawyer signs-off each document and the lawyer's professional indemnity is supporting the service when it is not.

Implications for practitioners

- Some online services encourage advisers to vary SMSF deeds over the web without highlighting the risks that it may breach the Legal Practice Acts of the relevant State/Territory and be subject to significant penalty.
- Most non-lawyer PI insurance excludes cover for services that a lawyer must undertake. Therefore, when an accountant, financial planner or consultant provides, eg, a new SMSF trust deed, they may void their PI insurance cover and find themselves exposed to claims.
- A non-lawyer obtaining SMSF deeds of variation without lawyer sign-off is very risky. Merely inserting names for a new SMSF trust deed has been held to be engaging in legal practice and tailoring a precedent for an SMSF deed of variation is far more risky. Accordingly, tailoring a new SMSF precedent or an SMSF deed of variation is engaging in legal practice. A deed of variation involves the user making decisions on legal questions such as 'Was the prior document correctly executed?' or 'Was the variation power complied with?'
- Just because lawyers have written the precedent that you obtain via a deed supplier does not mean that you have lawyer sign-off. As demonstrated in this recent case, the offending behaviour was entering the data to tailor the pro forma precedent (the identity of the party who drafted the precedent was not an issue).

Obtaining SMSF deeds from online deed suppliers exposes non-lawyers to significant risks. Before using online deed suppliers advisers need to carefully consider whether any upfront benefits are worth these risks.

DBA also works on many cases where deeds that have not been properly varied have resulted in substantial extra costs, extended litigation and delays. This is often the case upon death and divorce.

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