

SEPTEMBER 2008

A year ago, the major area of change from an estate planning perspective had been superannuation – the consequences of the extensive changes are still becoming apparent. Now the major area of change is family law and the far reaching changes proposed for de facto relationships. Together with trust issues, these two diverse areas of law are the focus of this edition.

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## Insurance within Superannuation

The types of insurance that can be owned by superannuation funds are:

- Life insurance;
- Total and Permanent Disablement (“TPD”) insurance;
- Income Protection insurance; and
- Trauma insurance.

Should you be advising your clients to hold any of these forms of insurance via superannuation? There are a number of factors to be considered for each of these types of insurance before deciding whether a superannuation fund is an appropriate vehicle for ownership. Some of these factors include:

- Deductibility of premiums; and
- Estate planning considerations

### **Deductibility of Premiums**

One of the main reasons that ownership of insurance in superannuation is common is because the premiums are tax deductible where they may not otherwise be under other forms of ownership.

Deductions apply for premiums paid by a complying superannuation fund for life and TPD insurance. These premiums are not deductible to individuals.

A deduction is also available for premiums in relation to income protection insurance (ie, benefits payable under an income stream because of the person’s temporary inability to engage in gainful employment). Premiums for this type of insurance were only previously deductible if the income stream was payable for a period of no longer than two years. This meant superannuation funds did not generally provide benefits exceeding two years. This differed from individual ownership.

The Australian Taxation Office issued Tax Determination TD2007/3 where it stated that “deductions are allowable....for premiums on insurance policies where income payments may be made to members of that fund pursuant to such a policy during periods of temporary disability which last longer than two years”. The determination further states that the benefits payable under the terms of the insurance policy must comply with the requirements of the *Superannuation Industry (Supervision) Act 1993* (Cth). This determination refers to section 279 of the *Income Tax Assessment Act 1936* which is now found as section 295-460 of the *Income Tax Assessment Act 1997* (Cth) (‘ITAA 1997’).

There is no prohibition on superannuation funds holding trauma insurance however, it is rarely so held. This is because the premiums are not tax deductible, there are issues as to whether the sole purpose

test is able to be met and more importantly, there may be issues in a member accessing the proceeds of the policy. For example, the insurance company may pay the proceeds to the superannuation fund, however the member may not be able to satisfy one of the conditions of release in Schedule 1 of the *Superannuation Industry (Supervision) Regulations 1994* (Cth).

### ***Estate Planning Considerations***

With the removal of Reasonable Benefits Limits (RBLs), this has led to an increasing amount of life insurance held in superannuation. Notwithstanding the RBL removal, a client's objectives in relation to who they want to benefit on their death and their potential beneficiaries may influence the decision on whether holding life insurance in superannuation is appropriate.

If a fund has claimed a tax deduction in respect of an insurance premium, the death benefit will generally include an element untaxed in the fund which is part of the taxable component. This is because the deductibility of the premiums results in no contributions tax having been paid on this part of the benefit. The untaxed element of a death benefit is calculated in accordance with section 307-290 of the ITAA 1997.

Lump sum death benefits paid to persons who are death benefits dependants (ie, spouse, children under 18, a person who was in an interdependency relationship with the deceased or financially dependent on them) are received tax-free whether they comprise the taxable or tax-free component. They are not assessable income or exempt income.

Where, however death benefits are paid to non-death benefits dependants (eg, children over 18 who cannot satisfy financial dependency or an interdependency relationship), the tax-free component will be tax-free and the tax on the taxable component will depend on whether the benefit comprises the element taxed in the fund, the element untaxed in the fund or both. We may be all aware that the element taxed in the fund entitles an offset so that the rate of tax on this component is 15% (plus Medicare levy). However, not all may be aware that the element untaxed in the fund is taxed at 30% plus Medicare.

This article does not cover in detail the tax treatment of the untaxed element of the fund where a death benefit is paid as a pension. However, in brief, a tax offset equal to 10% of the element untaxed in the fund is available where either the deceased died over 60 or the recipient is 60 years or over and is a death benefits dependant. There is no tax offset if the deceased died under 60 and the death benefits dependant is also under 60.

Whilst the tax deductibility to the superannuation fund may be of attraction, there are considerations which may factor into the decision. Therefore the decision to hold insurance via superannuation should not be made without the advice of advisors.

## **SMSF Warning – Criminal Charges for Breach of Sole Purpose Test**

With the increase in popularity of Self Managed Superannuation Funds over recent years, it is no real surprise that a case has arisen involving criminal charges brought by ASIC against a trustee of a self-managed fund under the *Superannuation Industry Supervision Act*, and this may well be the first of many. In the case of Mr Atan Ona Kassongo, he has been charged with dishonestly failing to ensure that a SMSF met the sole purpose test of the Kassongo Superannuation Fund, following allegations by ASIC that he used the Fund to facilitate early superannuation distributions to numerous other superannuants, retaining over \$600,000 commission for himself in the process. The case returns to the Downing Centre Local Court on 19 August.

*Louise Barbaro*  
Lawyer

## De Facto Couples & Property Disputes

The Victorian Government has recently enacted the *Relationships Act 2008* which provides that if a same or different gender de facto couple separates, and they have:

- been together for at least two years; or
- had a child together (even if they have not lived together); or
- signed the Relationships Register;

then either party can apply for spousal maintenance and a property settlement. This means their rights will be very similar to the rights of married couples. This is where the "shotgun marriage" comes into play because if a child is conceived after a "one night stand", then both parties are treated as if they are married when considering their financial entitlements. This legislation is due to commence operation on 1 December 2008.

Therefore couples that have been living together for at least two years, or for less if they have a child together, need to be aware that the financially weaker party will now have rights that they previously did not.

To use a stereotypical example, if a wealthy man and a young woman with no earning capacity have a child together, she will very likely have an entitlement to spousal maintenance for her own support. This is likely to be for a minimum of three years or until the child goes to school - although this entitlement would cut out if she entered another relationship.

It is expected that the Commonwealth Government will enact similar legislation expected to take effect next year, even though traditionally, the property disputes of de facto couples has been a matter for the States and Territories. This will mean that these relationships will be dealt with by the Family Court under the *Family Law Act*. The entitlements of the financially weaker person will be potentially even broader than under the Victorian *Relationships Act*. For example, the State legislation does not confer super splitting powers, unlike the *Family Law Act*.

If it is not intended that these issues be left to the discretion of the Family Court, we recommend that the couple enter into a financial agreement, setting out how assets are to be divided if the relationship ends. The agreement can be specifically tailored to suit the couple's circumstances and give effect to their particular objectives. Each party is required to obtain independent legal advice. **It is most important that the "wealthy" client is warned of the risks of any casual liaison, brought about by this legislation.**

If you would like to discuss these issues, please contact one of our experienced lawyers in family law.

*Suhanya Ponniah*  
Lawyer

and

*Stephen Winspear*  
Principal, Family Law  
Accredited Specialist Family Law

## Parent to Child Loans – In the Best Interests of You and Your Children

Superannuation laws, rising house prices and relationship breakdowns mean that many parents need to consider how they can help their children financially. In this article we consider some of the key things that parents and children should consider before parents lend financial assistance to their children.

### **Family Law, Bankruptcy and Estate Planning Considerations**

In the context of a relationship breakdown, a failure to correctly document a parent to child loan can have severe consequences for both the parent and the child as highlighted below:

- A gift made by a parent to their child could be attacked as an asset of the relationship to be divided between the child and their spouse or partner.
- Federal and State Courts have the ability to view a parent to child loan as a resource of the child to be taken into account when the Court divides the other assets. Generally speaking, the more commercial in nature the terms of the loan, the more likely the Court will be to view the loan as neither an asset of the relationship nor a financial resource of the child
- In a bankruptcy context, failing to take security over the child's assets may mean that other creditors get paid before the parent.

From an estate planning point of view, although loan agreements will usually state that the loan is repayable on death, perhaps the following should be considered:

- Whether the parent would forgive the debt in their Will and compensate their other children accordingly.
- What the parent would do if the child passes away before their parent, potentially leaving a spouse/partner and/or children who are unable to repay the loan. Having security over the child's asset(s) would give the parent flexibility to recall the loan immediately or at a later date.
- Similarly, if the loan was invested in the child's superannuation fund, the parent may find it hard to obtain repayment unless they have security over the child's asset(s) such as real estate.

### **What To Do?**

Where there is a risk of the child going bankrupt or suffering a relationship breakdown or where the parent requires flexibility in the case of either the parent or child passing away, the following options should be considered:

- Loans should be acknowledged by both the child and their spouse/partner (preferably the child and their spouse/partner should enter into a Binding Financial Agreement (rather like a pre-nuptial agreement)) and at least annually the child should make repayments of the principal or pay interest.
- The parent should consider taking security over the loan, such as a charge over real estate.
- Review your estate planning documents to ensure that they put into effect your intentions in relation to the loan.
- Alert your executors and attorneys to the existence of the loan and your decision concerning whether the loan is to be forgiven or repaid.
- Always seek specific taxation advice before entering into a loan agreement.
- Remember, if there is a dispute in the future, it will generally be the parent who has to prove that the loan was not a gift. An appropriately drafted loan agreement can help resolve disputes and help to prevent them from occurring.

*Edward Skilton*  
*Estate Planning Superannuation & Structuring*

## Family Trust Elections

The previous Government foreshadowed that many of the changes made in relation to family trust elections over the recent years would be modified or reversed subsequent to any change of government. As announced by the current Government in the May Budget 2008, whilst there will be changes to the definition of “family”, these changes will not be as severe as predicted. The most significant change will be that the family group will no longer extend to the descendants of the nephews, nieces and grandchildren of the Test Individual.

The Bill to enact the *Tax Laws Amendment (2008 Measures No. 4) Act 2008* which will change the definition of family (among other things) is currently before the Commonwealth Parliament. These amendments are set to apply to the 2008/09 tax year and subsequent years.

Once enacted, the definition of family will include:

- (a) the Test Individual;
- (b) the parents, grandparents, children, grandchildren, siblings, nephews and nieces of the Test Individual or their spouse;
- (c) the spouse of the Test Individual; and
- (d) any spouses of the parents, grandparents, children, grandchildren, siblings, nephews and nieces listed in paragraph (b).

The legislation in relation to Widows, Widowers and former spouses remains unchanged and these individuals will continue to be members of the family group. Also unchanged is the definition of “children” which includes adopted, step and ex-nuptial children and the definition of “spouse” which includes de-facto spouses.

*Jennifer Jackson*  
Lawyer

## The Not-So-Special Disability Trust

In September 2006, parents of children with severe disabilities in Australia hurraed the introduction of the much-heralded ‘Special Disability Trust’ which enabled a beneficiary suffering from a severe disability to benefit from \$500,000 (indexed – now \$532,000) exempt from means testing for Centrelink purposes. The establishment of the trust would, in many cases, enable the beneficiary to retain pension benefits and the health care card where it would otherwise be lost on the basis of the means test.

18 months on from the celebrated introduction of the Special Disability Trust, less than 50 have been established nationwide, and the lack of enthusiasm for what was supposed to be the new “hot item” for sufferers of severe disabilities is currently the subject of a Senate enquiry. It seems that, on closer examination, the terms of the trusts are not so “special” after all, and families of those in receipt of the disability pension are arguing for the introduction of some significant changes to the terms and the taxation treatment of the trusts in order to make them more attractive to the ‘everyday’ user.

### ***What’s So ‘Special’ About Them?***

There are a number of areas in which the Special Disability Trust could be improved to be made truly ‘special’. These include:

- Re-evaluation of the eligibility requirements to enable people suffering from severe mental illnesses (such as schizophrenia and bipolar disorder) to become eligible even if they are temporarily able to work in unsupported employment;

- Removal of some of the 'Special-ly' restrictive expenditure provisions.  
Once funds have been contributed to a Special Disability Trust, they cannot be moved out of the trust other than to pay for the 'reasonable care and accommodation' expenses of the principal beneficiary. Where a person with a severe disability has very minimal care or accommodation costs, potential donors are often reluctant to restrict the funds in this manner.

The expenditure must take place in Australia, and cannot be made to a family member of the principal beneficiary. Family members frequently act as the primary care providers, and often a child with a severe disability will continue to live with their parents until the parents have passed away or entered a retirement facility themselves. There is no real incentive to establish the trust while those family members are able to continue to assist.

- 'Special' Tax Treatment. Currently there are no income tax concessions for a Special Disability Trust, no Capital Gains Tax concessions, stringent rules for Stamp Duty exemptions/concessions (which do not apply in all States), and penalty land tax rates (where property is owned by the trust) in certain States.

If the parents of an adult child with a disability have their assets held primarily in Superannuation and their family home, the assets are in a far more tax-effective environment than the 'Special' Disability Trust can offer. There is very little incentive to transfer assets from a tax-friendly environment to the Special Disability Trust which may cause substantial losses due to high taxation levels on unexpended income and does not offer any capital gains tax or land tax concessions.

### ***In Conclusion***

There is clearly room for improvement in the realm of the Special Disability Trust. However, despite the restrictions and issues, it does serve a useful purpose in certain cases, particularly in the estate planning and Will for parents of children with severe disabilities. We await the results of the Senate enquiry with anticipation and hope for a positive outcome which will result in a Special Disability Trust that truly earns its' name.

*Rohani Bixler*  
Lawyer

## **Queen St & Mornington Offices & MOORESLEGAL EPSS Personnel**

Our Senior **EPSS** Lawyer **Krista Fitzgerald** has returned from maternity leave and will be working in our Box Hill office every Monday and Thursday.

**MOORESLEGAL** now have 3 Victorian locations available for client meetings, ie the full service Box Hill office (at which all staff spend either all or at least part of each week and to which all telephone calls, mail and faxes should be made or sent) and our serviced offices at 10/350 Queen St, Melbourne and 12/1140 Nepean Highway, Mornington.

Appointments can be arranged at our Queen St office with **Allan Swan, Jennifer Dixon, Louise Barbaro, Suhanya Ponniah, Edward Skilton** and **Jennifer Jackson**.

Appointments can be arranged at our Mornington office with **Rohani Bixler, Allan Swan** and **Andrew Simpson**.

The current **EPSS** team is as follows:

**Principals:**

**Allan Swan, Jennifer Dixon, Andrew Simpson and Philip Curtis** (who will return from long service leave in March 2009).

**Senior Lawyer:**

**Krista Fitzgerald**

**Lawyers:**

**Louise Barbaro, Suhanya Ponniah, Jennifer Jackson, Edward Skilton and Rohani Bixler.**

**Administrative Assistants:**

**Sarah Parker, Diane King, Rachael James, Rachael Barnewall and Kathryn Skilton.**

**Other MOORESLEGAL Private Client Services Contacts:**

- **Property:** Andrew Boer, Peter Loftus and Andrew Sudholz.
- **Family Law:** Stephen Winspear and Peter Szabo.
- **Executive Employment:** Frances Anderson and Peter Andrew.
- **Elder Law (and Estate Administration and Litigation):** Andrew Simpson and Anna Hacker.

For information regarding each of these areas and the commercial and other legal services offered by **MOORESLEGAL**, see [www.mooreslegal.com.au](http://www.mooreslegal.com.au).  
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