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December 2007 Newsletter

This newsletter deals with insolvency law, the ability of trustee of self-managed superannuation fund to borrow monies to acquire property and the terms of property law access and easements.

INSOLVENCY LAW INTERPRETATION OF CHAPTER 5 OF THE CORPORATIONS ACT 2001

The first of three steps in a raft of amendments to Chapter 5 of the *Corporations Act 2001 (Act)* (the first such amendments since the 1993 Harmer Report Amendments) commence on **1 January 2008** and can be summarised as follows:

- **Voluntary Administrations** - These account for approximately 1/3 of all corporate insolvencies in Australia. New Zealand will also shortly introduce the voluntary administration process.
- **Deadlines for Meetings** - The time limits for holding the first creditors meetings will be extended from 5 business days to 8 business days. The convening period for the second creditors' meeting will change from 21 to 20 business days with the meeting to be conducted before or after 5 business days of the convening period. The maximum time the second creditors' meeting can be adjourned will be reduced from 60 days to 45 days. The term Business Days has also been introduced into the Act. The changes are designed to allow more time to conduct financial investigations by administrators and creditor involvement in the process whilst maintaining the legislative aim for a rapid process
- **Rights of Secured Creditors** - The administrator will be entitled to obtain an injunction from the Courts to restrain a charge-holder who 'proposes' to enforce a charge. The new term "propose" is undefined and is likely to be the subject of Court review.
- **Liens** - The administrator will be entitled to sell property the subject of a lien, pledge or retention of title clause. If the administrator sells the property the subject of the lien, pledge or ROT clause, he will have to retain the funds derived from the sale to preserve the creditor's rights.

The lienee will be entitled to retain possession of the property but will only be able to sell property the subject of the lien with the consent of an administrator or Court.

- **Guarantees** - The creditor voting in favour of the DOCA preserves liability under a guarantee.
- **Employee Entitlements** - Employees are afforded a priority for recovery of certain employee entitlements above unsecured creditors. There is no change to the employee entitlements. Any DOCA proposing to vary that priority will require the consent from all employees who attend and vote at a separate meeting of employees. If such consent is not forthcoming, the proponee or administrator will need to go to Court to seek an order to vary the priority that is granted to the employees.
- **Shareholders** - Deed administrators will be able to sell shares in the company with the consent of the shareholders or with the leave of the Court. The Court will only grant leave if satisfied the proposed sale does not prejudice the rights of the shareholders.
- **Prospectus** - The administrator will only be able to provide a statement of all information known to him or her of the merits of the share offer but this will not be a prospectus. The exemption will only apply where the prospectus does not require the accepting creditors to contribute any further consideration.
- **Liquidation post DOCA** - The creditors of pre DOCA and post liquidation creditors will be treated uniformly.
- **Creditors Voluntary Winding Up** - These have reduced in number as more time, legal and accounting input is required. The changes are proposed to streamline the process. However, the involvement of members has been retained. In administration process, members have no say.

- **Priorities** - There will be a \$2,000 cap priority for outstanding superannuation guarantee charges and anything above that will be an unsecured debt.
- **Asset Pooling in a Winding Up of a Group** - The group assets will be pooled and treated as one company. Creditors will also be treated as creditors of the group as though it is one company. The creditors will be required to approve pooling by a 75% by value and 50% by number majority voting in favour. This will not affect rights of secured creditors. Each company in the group will be liable for the debts of the other companies in the group.

Voluntary pooling occurs where a liquidator makes a pooling determination in writing and this is sent to all unsecured creditors in the group who then vote at a meeting. Court ordered pooling could occur if the Court finds it is just and equitable to do so.

- **Voidable Preferences** - Recovered either 3 years from the relation back date or 1 year after the appointment of a liquidator where there has been an extended period of administration.

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SUPERANNUATION

ABILITY OF TRUSTEE OF SELF-MANAGED SUPERANNUATION FUND ("SMSF") TO BORROW MONIES TO ACQUIRE PROPERTY

1. Background

Prior to the amendments that had effect from 24 September 2007, Section 67 of the *Superannuation Industry (Supervision) Act ("SIS")* prohibited the trustee of a SMSF from borrowing monies. If it was desired to borrow monies to purchase property, this could be achieved by the trustee of the SMSF subscribing for units in a unit trust where:

- the unit trust was not a "related trust" so that, arguably, the trustee of the unit trust could purchase the property and use the property as collateral security for a borrowing; or
- the unit trust was a "related trust" that was a "non-g geared unit trust", with a related party subscribing for units in the unit trust and using other collateral security for the related party's borrowing.

With the amendments to Section 67, the trustee of the SMSF can now gear the purchase of property without establishing a unit trust provided the requirements of subsection 67(4A) are satisfied.

2. Borrowing in terms of subsection 67(4A)

The heading to subsection 67(4A) is "Exception – instalment warrants". However, this heading is misleading as a borrowing can take place in terms of that subsection without constituting an "instalment warrant" (as commonly understood).

In terms of the purchase of property, the following can take place:

- the trustee of the SMSF can borrow monies to purchase property, as long as the purchase of such property is not prohibited under *SIS*. For example, the trustee of the SMSF can borrow monies to purchase "business real property" from a "related party";
- however, the property purchased is not held by the trustee of the SMSF but, rather, held by an entity on trust for the trustee of the SMSF. The entity that holds the asset on trust for the trustee of the SMSF can be a "related party";
- the trustee of the SMSF has the right to acquire legal ownership of the property by making one or more payments after acquiring the beneficial interest;
- the lender's rights against the trustee of the SMSF are limited to rights in respect of the property acquired i.e. the lender only has limited recourse to the property acquired, and no recourse against the other assets held by the trustee of the SMSF.

There is also scope under subsection 67(4A) for the original property to be disposed of and substituted by a replacement property. Amendments made to the definition of "in house asset" in Section 71 ensure, notwithstanding the fact the trustee of the SMSF has an interest in a "related trust", that the interest is not an "in-house asset".

3. Possible transactions

Transactions that can now be entered into include:

- member of SMSF borrows money from a financial institution on a full recourse basis and on-lends the money to trustee of SMSF on a limited recourse basis, complying with subsection 67(4A);
- "related party" with available funds lends money to trustee of the SMSF under subsection 67(4A);
- company with large accumulated profits lends monies to trustee of SMSF, the terms of the loan satisfying the requirements of both subsection 67(4A) of *SIS* and Division 7A of the *Income Tax Assessment Act 1936*;

- trustee of SMSF acquires "business real property" from "related party", utilising vendor finance that satisfies the requirements of subsection 67(4A).

Transactions involving "related parties" are of particular interest as such loans are not subject to the "non-concessional contribution cap" which applies to contributions made by members to the trustee of the SMSF.

We will, undoubtedly, over the next calendar year, see an expansion of geared arrangements involving trustees of SMSFs as advisors apply their minds to the opportunities.

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PROPERTY LAW

TERMS OF ACCESS AND EASEMENTS

Westfield Management Limited v Perpetual Trustee Co Limited [2007] HCA 45

This case involved a right of way granted under a building known as "Glasshouse" which benefited Skygarden. Westfield bought the adjoining Skygarden, Imperial Arcade and Centrepoint, and it wished to use the right of way for access to all 3 properties. Perpetual, as owner of the Glasshouse, objected.

In delivering its judgment, the High Court considered the terms of the easement, and the relevance of any extrinsic evidence. The reasons for the judgment may be summarised as follows:

- The Court considered the wording of the easement and concluded that the easement allows only the passing to and from Skygarden and not across the Skygarden land and on to further property. If it had been intended to go across the Skygarden land then the words "*and across*" would also have been included.
- The Court then considered the construction of the words "*for all purposes*". Westfield argued that this wording compassed the purpose of accessing Skygarden and continuing on to a further property from there. After consideration of the authorities, the Court concluded that in order for the rights granted to Skygarden under the easement to be fully enjoyed, it is not necessary that those using the right of carriage be at liberty to pass beyond Skygarden to other land. To do so would be in excess of the rights conferred under the easement.

- The Court then considered the conditions of the easement. There was no provision in relation to costs of repairs caused by those utilising the easement to pass across and beyond Skygarden. There was also no provision for insurance against loss or damage by any owners of land beyond Skygarden or for public risk insurance for the uses, which Westfield contemplated beyond the boundary of Skygarden.
- The Court concluded that extrinsic evidence is only admissible to make sense of that which the Register of the Land Titles Office identifies by the terms or expressions found in the instrument creating the easement, such as, for example, surveying terms and abbreviations appearing on plans. It would be inconsistent with the definitive nature of the Land Titles Register to expect third parties to look beyond the Register for extrinsic material to establish facts or circumstances that exist at the time of creation of the registered dealing.

The case highlights the need for a purchaser of land (whether or not in the Sydney CBD) to carefully review the terms of access prior to making the purchase and subsequent plans for redevelopment.

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*The partners and staff at Parry Carroll,
Lawyers wish you a happy Christmas and
prosperous New Year*

*The office will remain open other than for
public holidays*