

## January 2010 Newsletter

*This newsletter deals with the issue of trusts and unpaid present entitlements and employment awards that apply from 1 January 2010.*

### TRUSTS

#### THE ISSUE OF UNPAID PRESENT ENTITLEMENTS

##### 1. Introduction

An unpaid present entitlement arises where a beneficiary is presently entitled to income of a trust but has not been paid that entitlement. The beneficiary has the right to request payment of its entitlement to income at any time, with the beneficiary being assessed on its share of the net income of the trust in accordance to its entitlement to income of the trust.

Prior to the Australian Taxation Office's ("ATO") recent rulings, the generally accepted view is that where:

- the trustee of a superannuation fund is presently entitled to income of a unit trust which has not been paid, that unpaid present entitlement does not cause an "in-house asset" to arise in terms of subsection 71(1) of the *Superannuation Industry (Supervision) Act* ("SIS"); and
- other than in the specific circumstances outlined in subdivision EA of Division 7A of the *Income Tax Assessment Act 1936* ("*Tax Act 1936*"), the unpaid present entitlement of a corporate beneficiary of a discretionary trust does not cause a Division 7A problem to arise in relation to that unpaid present entitlement.

However, following the release of:

- Self Managed Superannuation Fund Ruling SMSFR 2009/3; and
- Draft Taxation Ruling TR2009/D8,

it appears that the ATO is having a closer look as to whether an unpaid present entitlement can

cause an "in-house asset" to occur (in terms of subsection 71(1) of *SIS*) or a deemed dividend to occur in terms of Section 109D of the *Tax Act 1936*.

##### 2. Unpaid present entitlement in a superannuation context

The usual context in which the trustee of a superannuation fund will have an unpaid present entitlement is in relation to the trustee of the superannuation fund holding units in a unit trust which entitles the trustee of the superannuation fund to income of the unit trust to which it has not been paid.

Subsection 71(1) of *SIS* defines an "in-house asset" to include a "loan" to a "related party".

Subsection 10(1) defines "loan" as including:

*...the provision of credit or any other form of financial accommodation whether or not enforceable, or intended to be enforceable by legal proceedings.*

What the ATO states in SMSFR 2009/3 is that, in certain circumstances, the trustee of a superannuation fund not demanding payment of the income to which it is entitled to can be "financial accommodation" and, therefore, a "loan". In a rather chilling statement, the ATO states that where the trustee of a superannuation fund has not received income distributions due to insufficient cash, this may be evidence of an arrangement for the provision of "financial accommodation" by the trustee of the superannuation fund (paragraph 102 of SMSFR 2009/3).

In practice, the failure of the trustee of a superannuation fund to seek payment of an unpaid present entitlement is not because there is an

intention to financially assist the trustee of the unit trust but, rather, because the trustee of a superannuation fund that has an entitlement to income of the trust can call up that entitlement at any time. When so called, the trustee of the unit trust is compelled to pay the unpaid present entitlement. The definition of “loan” in Section 10 of SIS infers that there must be some positive act by the trustee of the superannuation fund in providing some sort of assistance: the mere inactivity of the trustee of the superannuation fund in demanding payment is not such a positive act.

In summary, though we are put on notice by the ATO that they may consider, in certain circumstances, that an unpaid present entitlement is an “in-house asset”, there is some doubt whether such an “in-house asset” arises.

### 3. Discretionary trusts

In TR2009/D8, the ATO indicates that an unpaid present entitlement of a corporate beneficiary of a discretionary trust can, in certain circumstances, be considered a loan by the company to the trustee of the discretionary trust. In a rather chilling statement, the ATO has stated that a loan comes into existence where there is a “consensual agreement” between the corporate beneficiary and the trustee of the discretionary trust with a consensual agreement arising where (paragraph 18):

*the private company authorises (including by acquiescing with knowledge) the continued use by the main trust of funds representing the private company’s UPE for trust purposes by not calling for:*

- *payment of that UPE; or*
- *investment of the funds representing the UPE for the private company’s absolute benefit (and no benefit accruing to the main trust from the use of those funds).*

In the situation where the corporate beneficiary does not require the trustee of the trust to pay the unpaid present entitlement and does not require the trustee to enter into a loan agreement, it is difficult to see how a loan agreement has been entered into between the company and the trustee. In terms of Section 109D, the question arises whether the mere inactivity of the corporate

beneficiary amounts to a “loan”. In this regard, subsection 109D(3) defines “loan” to include “a provision of credit or any other form of financial accommodation” and *a transaction (whatever its terms or form) which in substance affects a loan of money.*

Where a corporate beneficiary has simply not demanded payment of its unpaid present entitlement from the trustee of the discretionary trust, there is some difficulty in stating that the corporate beneficiary has provided “financial accommodation”.

In summary, though we are put on notice by the ATO that they may consider, in certain circumstances that an unpaid present entitlement is a “loan”, there is some doubt whether a corporate beneficiary can be said to have made a “loan” to the trustee of a discretionary trust where the corporate beneficiary does not demand payment of its unpaid present entitlement.

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## EMPLOYMENT LAW

### AWARDS

All States (except Western Australia) have given power to the Commonwealth from 1 January 2010 to allow National Employment Standards to apply. The National Employment Standards apply to all business, including sole traders and partnerships.

Since July 2009, the Australian Industrial Relations Commission has made a raft of comprehensive Modern Awards, covering areas where businesses may not be expecting an award – including the Professional Employees Award 2010 (which covers engineering, science and communications and information technology), and the Miscellaneous Award 2010, which (with some exceptions) covers almost anybody not covered by another award.

One obligation that appears in the awards is an obligation to make each applicable award, together with a complete copy of the National Employment Standards, available to all employees covered by the award, on a noticeboard or on an electronic information

system (whichever is more accessible to the effected employees). For many of the awards this applies from 1 January 2010. This is in addition to the requirement to provide employees with a copy of the Fair Work Information Statement that has been prepared by Fair Work Australia.

Employers should check what awards apply to their employees, and ensure that the salaries and conditions of employees meet the minimum requirements of the applicable award. Additionally, there may be a need to take additional steps, including:

- making flexibility agreements with employees to deal with things such as work schedules that do not fit within the narrow requirements of the award; and

- where employees are paid significantly above the rate set out in the award, and are not paid overtime rates, notifying employees that their salary has been set to take into account the requirement to work overtime.

In each case, there are strict requirements that must be complied with.

Employees who are on a base salary (not including superannuation, commissions, bonuses or fringe benefits) in excess of \$108,300 per year, may not be covered by any award. This amount will be indexed each financial year.

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