Wentworth Lawyers
COMMERCIAL LAWYERS

SMSF'S: BREACHES, PENALTIES AND DEALING WITH THE ATO

The recent decision of *Deputy Commissioner of Taxation (Superannuation) v Graham Family Superannuation Pty Limited [2014] FCA 1101* provides some interesting insights into:-

1. breaches of the rules applying to Self-Managed Superannuation Funds ("SMSFs") under the *Superannuation Industry (Supervision) Act 1993* (the "Act");

2. the approach to penalties; and

3. the possible benefits of early and frank communications with the Australian Taxation Office (the "ATO").

Facts

Graham Family Superannuation Pty Limited was the trustee ("Trustee") of the Graham Family Superannuation Fund (the "Superfund"). Mr and Mrs Graham were both members of the Superfund and Directors of the Trustee.

Between 11 July 2008 and 30 June 2012, the Trustee made 80 loans to Mr and Mrs Graham. It was accepted the loans were in breach of the Act, mainly the sole purpose test (section 62), loans to members (section 65), in-house assets exceeding 5% (section 84) and non-arm's length transaction (section 109).

Further, between 8 July 2008 and 30 June 2012, the Superfund acquired a residential property and paid for furnishings which was leased to Mr and Mrs Graham's son. No rent was collected from the Lessee leaving an accumulated debt for rent of $60,762. Similarly, it was accepted that there were further breaches of the sole purpose test, in house assets exceeding 5% and non-arm's length terms and conditions rules.

In addition the Trustee on behalf of the Superfund acquired a caravan, stud cattle and motor vehicles for the Graham family's use at no charge.

The Trustee failed to lodge income tax returns on time. The tax return for the year ended 30 June 2008 was not lodged until March 2011. The tax returns for the years ended 30 June 2009, 2010 and 2011 had not been lodged by 30 June 2012.

The auditor of the Superfund filed an Auditor Contravention Report ("ACR") in respect of the 2008 tax return. Despite the Auditor advising the Trustee and Mr and Mrs Graham of the reasons for his ACR, further breaches of the rules pursuant to the Act occurred. The auditor filed a further ACR in respect of the years ended 30 June 2009, 2010 and 2011. The ATO embarked on an audit of the Superfund during which the Trustee and Mr and Mrs Graham engaged representation in discussions and disclosures to the ATO. As a result of the ATO's audit Mr and Mrs Graham were disqualified from being Trustees or responsible officers of corporate trustees of a superannuation entity. However, the ATO did not declare the Superfund non-complying as Mr and Mrs Graham had repaid the Superfund from other assets. The result being that the net assets of the Superfund were not taxed at 45%. Further, Mr and Mrs Graham *"retained the benefits of their interests in the Superfund undiminished by a penalty assessment for non-compliance."*

As a result of the discussions between the Trustee, Mr and Mrs Graham and the ATO, an agreed Statement of Facts including agreed proposed penalties were presented to the Court. Whilst the Court acknowledged that such an approach assists the administration of justice, neither Mr nor Mrs Graham was required to appear in Court and were therefore not cross examined. It appears that Mr and Mrs Graham were not in attendance in Court.

The Superfund was wound up on 29 September 2013.

The Court accepted the agreed Statement of Facts and the proposed penalties. The penalties order by the Court totalled $40,000 plus costs of $10,000. The penalties were payable: Mr Graham $30,000, Mrs Graham $10,000 with the award of costs to be paid equally.

The Court observed:-

"A statutory maximum penalty of $220,000 applies to each contravention (2,000 penalty units of $110 each). Although, as the applicant [ATO] submitted the offences are serious ones they fall well short of a worst possible case. The second and third respondents [Mr and Mrs Graham] have shown remorse, they have made early admissions, they have co-operated with the Commissioner, they have remedied their conduct. A penalty should not be imposed which is "crushing", at the same time, the penalty should serve as a deterrent and mark the courts acceptance of the need to enforce the regulatory scheme."

Observations

The penalty regime has been amended with effect from 1 July 2014 enabling the ATO to impose administrative penalties but can still apply for Court imposed penalties. In Graham's decision the ATO was at that time required to apply to the Court for the imposition of penalties.

The Court provides some interesting observations on the calculation of penalties where there are multiple breaches which presumably will still have application under the new penalty regime.

The Court also accepted that Mrs Graham acted under the influence of Mr Graham and was effectively a "silent" Director and therefore the difference in penalties. This makes an interesting contrast to some decisions dealing with director's duties and insolvent trading under the Corporations Act.

Lessons

It is difficult to escape the conclusion that in the event of significant and/or repeated breaches of taxation acts, a full and frank disclosure and discussion with the ATO has advantages. Notwithstanding the courts detailed consideration on the imposition of penalties and the appropriateness of penalties in the circumstances, the penalties may have been considerably worse for the Superfund and Mr and Mrs Graham.

Date Published: 2 March 2015

Victor Hamit
Wentworth Lawyers Pty Ltd
Level 40
140 William Street
MELBOURNE VIC 3000

Tel: +61 (3) 9607 8380
Mobile (Aust.): 0408 590 706

Email: vhamit@wentworthlawyers.com.au
Website**:** www.wentworthlawyers.com.au