Example: A common example of an encumbrance is a mortgage secured against an investment property.

For INCOME TEST purposes, the GROSS market value of a financial investment is used to calculate deemed income

Act reference: SSAct section 1072 General meaning of ordinary income

Policy reference: The Guide 4.6.6.30 Encumbrances & Loans Against Assets.

The Tribunal found that there was no legislative basis for the statement that the gross market value of a financial investment must be used to calculate deemed income. This was not consistent with s.1072. The Tribunal found that this section relates to gross ordinary income and not the gross value of assets.

The Tribunal found that the margin loans could therefore be offset against the value of assets under s.1121(1), for the purpose of calculation of deemed income from those assets.

Formal decision

The AAT remitted the matter to the Department with directions that:

- the rate of newstart allowance payable to Mr Draper should be determined by not treating as ordinary income the dividend of $3992.67 he received from the company on 17 May 2001, which the Tribunal determined was an exempt lump sum;
- the secured margin loans used by Mr Draper to purchase shares and managed funds held at 5 September 2001 should be taken into account when valuing those assets in order to calculate deemed income pursuant to s.1076 of the Act.

[R.P.]

Age pension: whether attributable stakeholder; whether asset attribution less than 100%

GEIDANS and SECRETARY TO THE DFaCS (No. 2003/773)

Decided: 8 August 2003 by L. Savage Davis.

Background

Geidans established Geologics Pty Ltd ('the company') in the early 1970s and with his own funds, purchased the company's primary asset, an abandoned farm. Geidans cleared the land and renovated the house. His son Edgar, born in 1965, assisted him on the property from about the mid 1970s. Geidans received age pension from 1989 and in the early 1990s, moved to live in a shack on the property. He sold his Perth home in 1993, the proceeds being placed in the company's account. In 1995, he moved into a new house on the property. All farming activities had ceased on the property by the summer of 2002.

At the time the company was established, Geidans held an 'A' class Governing Director's share and 98 ordinary shares. He acquired a 'B' class share in 1987. His wife and four children held a share each, as well as his two sisters. In 1994, he transferred 98 shares to Edgar. In around May 2001, Geidans spoke to Edgar about 'bowing out'. Edgar and Geidans' daughter, Indra were prepared to take over and become co-directors. In October 2001, Geidans transferred his 'A' class share to Edgar, although supporting documents suggested it was transferred to Indra. Geidans disposed of his 'B' class share in early 2002.

In an email to Geidans dated 4 January 2002, Edgar commented 'if by keeping the company you'd be jeopardising your pension and that if the company was liquidated you'd receive your pension then the answer is clear! It must be dissolved. You should inform us if this is the case'.

Centrelink attributed 100% of the company's assets to Geidans, and as a consequence, his rate of age pension was reduced from January 2002.

The law

Section 1207N of the *Social Security Act 1991* '(the Act') requires a company to be a 'designated private company'. The assets can be attributed to an individual, as an attributable stakeholder, if either the control or source tests set out in s.1207Q(2) and (3) respectively are satisfied. Section 1207X provides:

> **1207X.(1)** For the purposes of this Part, if a company is a controlled private company in relation to an individual:
>
> (a) the individual is an ***attributable stakeholder*** of the company unless the Secretary otherwise determines; and
>
> (b) if the individual is an attributable stakeholder of the company-the individual's ***asset attribution percentage*** in relation to the company is:
>
> (i) 100%; or
>
> (ii) if the Secretary determines a lower percentage in relation to the individual and the company-that lower percentage; and
>
> ...

Section 1209E requires the Secretary to comply with the Attribution Principles when making a determination under s.1207X.

The issue

The AAT was required to decide if Geidans was an 'attributable stakeholder' and if so, whether 100% of the assets, or some other percentage, should be attributed to him.

Discussion

The AAT was satisfied the company was a 'designated private company' and that the 'A' class share was held by a family member who was an 'associate'. Pursuant to s.1207Q, Geidans satisfied the control test as the aggregate of direct voting interests held by his associates was 50% or more. Being satisfied the company was a 'controlled private company', Geidans was an attributable stakeholder unless deemed otherwise pursuant to s.1207X(1)(a).

The AAT turned its mind to the Attribution Principles and whether the effect of one or more circumstances provided a 'sufficient basis' to determine a person was not an attributable stakeholder. Principle 7(2)(c) required consideration of whether Geidans could '... reasonably be expected to exercise effective control'. Control was defined in s.1207A to include '... control as a result of, or by any means of, trusts, agreements, arrangements, understandings and practice, whether or not having legal or equitable force and whether or not based on legal or equitable rights'.

The AAT was satisfied that Geidans retained effective control. So confident was Geidans about the security in his home he handed over all his shares for minimal consideration. There was no

evidence the directors would attempt to remove him, and any attempt to sell without his agreement would most likely give rise to an equitable claim in terms of a constructive trust. Geidans continued to reside at the property and the email of 4 January 2002 provided further evidence of effective control. In considering Principle 8, the AAT found no evidence that anyone apart from Geidans had made financial contributions to the company. Ultimately, having regard to all the Principles, the AAT was not satisfied a sufficient basis existed to determine Geidans was not an attributable stakeholder.

Finally, the AAT considered the attribution percentage. Geidans submitted that there should be no attribution, but if attribution was necessary, 50% would be appropriate. The Departmental representative and Counsel for Geidans were not aware of any determinations that had been made of an asset attribution of less than 100%. The AAT stated:

> ... The Tribunal accepts that Mr Geidans has taken progressive steps to divest himself of legal control of the company. Notwithstanding this fact there is no evidence to show that the running of the company has been effectively transferred to anyone else, even if that is Mr Geidans' desire. The Tribunal accepts that as outlined in the letter from his GP Mr Geidans has a number of health conditions which would render him unable to do physical work on the property. However the property is no longer a working farm and there is no evidence that Edgar himself undertakes any regular work on the property. Mr Geidans lives on the property and he alone has the ongoing benefit of it to the extent he can. In the absence of Edgar being contactable or his whereabouts even being known, it is difficult at this time to envisage decisions being made about the property by Edgar alone or even in conjunction with his father. The Tribunal has heard that Indra, Mr Geidans' daughter, is a co-director but there was no evidence that she played any role other than having mail for the company forwarded to her. For these reasons I can find no basis at this time to justify the asset attribution percentage at less than 100%.

(Reasons, para. 45)

Formal decision

The AAT affirmed the decision under review.

[S.L.]

Assets: loan to a trust; whether trust continued to exist

SZMERLING and SECRETARY TO THE DFaCS (No. 2003/661)

Decided: 15 July 2003 by B.H. Pascoe.

Background

Mr and Mrs Szmerling were beneficiaries of the Rossim-Szmerling Family Trust ('the trust'). As at 30 June 2000, Mr and Mrs Szmerling were owed $618,797. Centrelink treated the loan as an asset, rejected Mr Szmerling's claim for age pension on 22 February 2001 and cancelled Mrs Szmerling's age pension. A debt was raised against Mrs Szmerling in the sum of $34,133.44 for the period 28 November 1996 to 27 March 2001.

Mr and Mrs Szmerling had been involved in a business operated by Rossim Nominees as Trustee of the trust. In 1986, they borrowed $150,000 from NAB for the business secured by a mortgage over their home. Rossim Nominees also borrowed $600,000 from Carrington Confirmers Pty Ltd ('Carrington'). This loan was secured by mortgage and personal guarantee. In 1990, the business collapsed and Mr and Mrs Szmerling sold their home. The $150,000 NAB loan was paid in full and the remaining sum of $290,000 was paid to Carrington. An amount of $708,433 was recorded as a loan to the trust following the sale of the home in 1990. Rossim Nominees was removed and replaced as trustee in 1993, and until 1998, the trust remained dormant.

The SSAT decided that the $290,000 paid to Carrington was paid pursuant to a personal guarantee and not an amount loaned to the trust to operate its business. The reduction, however, did not reduce the loan below the relevant asset threshold. The SSAT decided that the debt relating to the period 28 November 1996 to 15 November 1998, during which the trust was inactive, ought to be waived due to 'special circumstances'.

Subsequent to the SSAT decision, the accountants prepared amended financial statements and returns for the trust from 1991 to 2001. These showed a loan account from Mr and Mrs Szmerling of $596,743 as at 30 June 1991, but nil at 30 June 1992, and no further loan account thereafter. The statements were prepared on the basis that Carrington as mortgagee in possession on 10 September 1991 took possession of all of the remaining assets of the trust leaving no funds for unsecured creditors. Mr and Mrs Szmerling entered into Part X arrangements vesting their assets in a trustee pursuant to a composition with their creditors. Given the trust had no assets, the loan was irrecoverable and written off.

The issue

The issue for the Tribunal was whether the loan to the trust by Mr and Mrs Szmerling was, at all material times, an assessable asset.

Discussion

The AAT commented that the accountant had erroneously characterised the events in 1991 and 1992. The AAT held as incorrect the assumption that a trust had been established in 1974 and continued until this day as a legal entity. The Tribunal stated:

> ... In simple terms, a trust is not a legal entity; it is a relationship between a trustee and property. As a general proposition of law, any liabilities incurred by a trustee in carrying out the terms of the trust are personal liabilities of the trustee with a right of recovery out of the assets held in trust. If there is no property, there is no *trust*.

(Reasons, para. 8)

The AAT took the view that the trust ceased to exist by 30 June 1992:

> From the evidence, which I accept, the business carried on by the trustee had ceased prior to 30 June 1992, all property held in trust by the trustee was seized by the mortgagee in possession leaving no property in which the then trustee had any obligation. The trustee, being a company, was wound up. It is clear, in my view, that *the trust* had ceased to exist by 30 June 1992. Some years later, when a new business was commenced, the accountant sought to have the benefit of the losses incurred by that former trust offset against profits of the new business by treating it as a continuation of the same trust under a new trustee. This was not legally possible. At best, the new trustee agreed to hold new assets on the same terms of trust as contained in the original trust deed. However, it was a new trust. It appears, also, that the same process occurred again when another business was commenced with a new trustee following the failure of the second business.
>
> From the foregoing, the alleged loan account was, at least to the extent of monies advanced to the then trustee prior to September 1991, a loan to the then trustee. It could well be argued that, given the knowledge of and involvement in the trust by Mr and Mrs Szmerling, the right of recovery by them was limited to the property held in trust. However, the liability was that of the trustee company. The trustee ceased to hold any property in trust, was subsequently wound up, and the debt became ir-