NEWSLETTER

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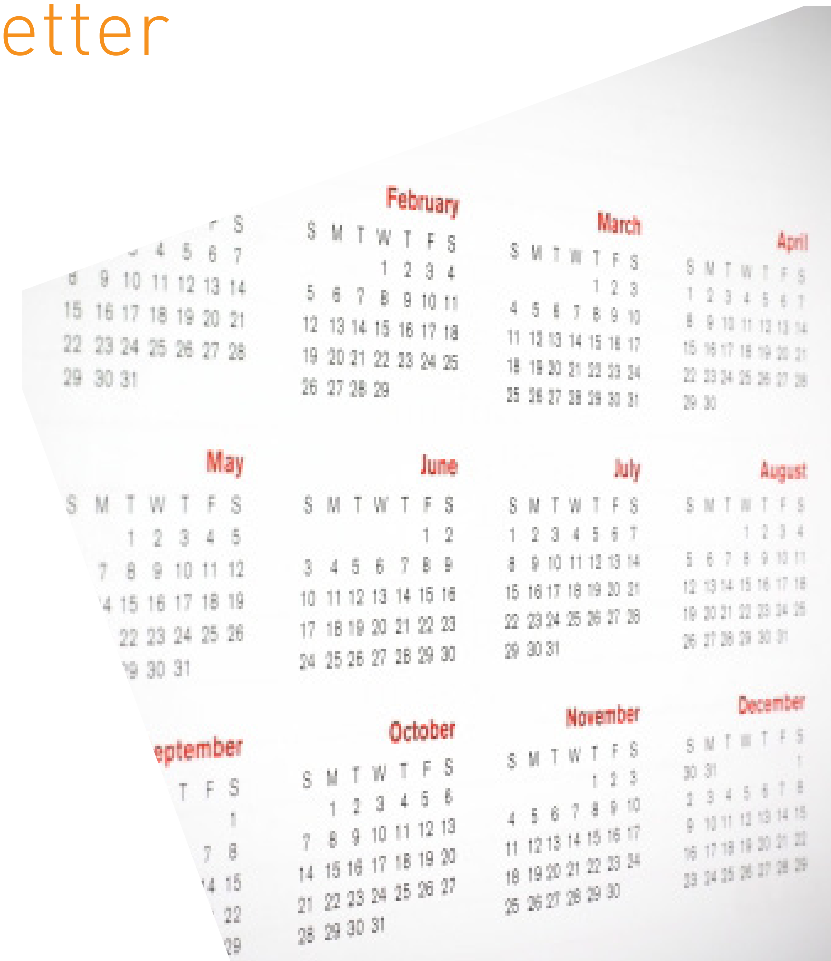
Corporate & Commercial Newsletter



Welcome to our December Corporate & Commercial newsletter

This quarter we have included news on:

- the *Personal Property Securities Act 2009* (Cth) and an update on registering your security interests
- *Crossmark Asia v Retail Adventures* and the effect of a 'retention of title' clause on unperfected goods
- incorporation of an exclusion clause by prior dealings and the decision of *La Rosa v Nudrill Pty Ltd*
- *Resource Capital Fund III LP v FCT*, which addressed various complex international tax issues, as well as approaches to valuing mining tenements and related assets
- the government's announcement that it will remove a licensing exemption that currently allows accountants to provide financial advice on self-managed superannuation funds (**SMSFs**) without an Australian Financial Services Licence (**AFSL**).

Please don't hesitate to contact us if you would like more information on any topic, whether covered in this newsletter or not. We hope you find the newsletter informative and useful.

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Personal Property Securities Act 2009 (Cth) (PPSA) – two year transition period ends on 31 January 2014

A secured party with a transitional security interest that is not registered on the Personal Property Securities Register (**PPSR**) should register that interest no later than 31 January 2014. This will ensure that the interest is perfected and preserve the priority of that interest.

For example, if you have an interest that arose prior to 30 January 2012 and was created under:

- a lease or hiring arrangement;
- a PPS lease (eg a lease of a car for more than 90 days or, for most other goods, for more than one year);
- a retention of title supply; or
- some commercial consignment arrangements,

then you will need to register your security interest if your arrangement with the grantor party is continuing and you want to preserve your right to reclaim your goods.

Contact: **Ian Sinclair**, Cornwall Stodart

The effect of a 'retention of title' clause on unperfected goods

Background

The New South Wales Supreme Court recently considered the relationship between a retention of title (**ROT**) clause and section 267 of the *Personal Property Securities Act 2009* (Cth) (**PPSA**).

In *Crossmark Asia v Retail Adventures Pty Ltd* [2-13] NSWC 55, the court found that despite goods being supplied on a ROT basis (generally, title in all goods supplied is retained until the purchase price is paid in full), if they have not been perfected on the Personal Property Securities Register (**PPSR**), they become the property of the customer immediately before either the customer becomes bankrupt or the company is wound up.

Case summary

Crossmark and Retail Adventures Pty Ltd (**RAPL**) had entered into two separate agreements regarding the sale and purchase of convection ovens and electric fans. A dispute then arose as to the terms of the supply agreements between the parties. On 26 September 2012, Crossmark demanded payment from RAPL prior to delivery of the goods, on the basis of RAPL's 'very high risk' credit rating. On receiving the demand RAPL cancelled all orders, which Crossmark accepted. On 26 October 2012, administrators were appointed to RAPL. During this time, Crossmark had failed to perfect its security interest in the goods in accordance with the PPSA requirements.

The court ultimately found in favour of Crossmark. The applicable terms on which the agreements were based were those set out in the signed agreements incorporating the ROT clause and not those in subsequent purchase orders. Additionally, the contracts had been properly terminated after shipment but before delivery. RAPL had no legal title in the goods at the time of its insolvency.

As a result, Crossmark was entitled to regain possession of the goods because both sale agreements had been terminated before RAPL had gone into administration. Accordingly, section 267 did not apply because there was no charge over the goods that could vest in RAPL.

Comment

The judgment emphasises the necessity for suppliers to be absolutely certain as to the terms of their supply agreements. If the court had accepted the terms provided by RAPL in the purchase orders as amending the signed agreements, the legal title in the goods would have vested in RAPL, leaving Crossmark as an unsecured creditor. Additionally, regardless of the presence of a ROT clause, if the goods have not been properly registered, legal title will pass to the purchasers immediately before their insolvency.

Consequently, the case highlights the need for suppliers to perfect their ROT goods by registering them under the PPSR. By doing so, suppliers avoid the potential to lose their security interest in the goods supplied under the ROT agreement or having to prove their retention of title in court.

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Incorporating exclusion clauses via prior dealings

Background

In *La Rosa v Nudrill Pty Ltd* the Western Australian Court of Appeal found that incorporating an exclusion clause on the back of an invoice was not sufficient notice to bind the parties, despite there being a long working relationship between them. At issue was whether the clause had been accepted and treated as contractual by the conduct of the parties.

Case summary

Mr La Rosa was contracted by Nudrill to transport a drill rig from Perth to Kalgoorlie. Towards the end of the journey the drill tipped off the back of the trailer, causing significant damage. Nudrill sued Mr La Rosa for damages as a result of Mr La Rosa's negligence. The trial judge awarded damages against Mr La Rosa, who appealed to the Western Australian Court of Appeal.

The usual practice between the parties had been to enter into an oral contract and on completion of the delivery, Mr La Rosa would invoice Nudrill. Mr La Rosa argued that as the result of their prior dealings, Nudrill should be taken to have accepted that any future services provided would be subject to the terms included on the back of the invoice. The court had to consider whether the contract was subject to the exclusion clause, therefore excluding Mr La Rosa for any damage or loss to property by act, default or negligence.

In coming to the decision, the court concluded that neither the timing of the notification of the clause nor the question of whether the exclusion clause was part of a past contract were determinative factors. Rather, it was the conduct of the parties that had not reflected the knowledge and acceptance of the term. The court explained that by receiving the invoice there was no proof that Nudrill accepted the terms of the exclusion clause. An invoice including terms after services are rendered cannot constitute contractual terms of an agreement. In this sense, it was too late for Nudrill to negotiate or refuse the terms of the contract. In addition, the circumstance in which Mr La Rosa provided the invoice, only after services had been performed, was indicative of the nature of the document – to demand payment for work completed, and not to add a 'last shot' to the existing terms.

In the end there was no evidence to suggest that Nudrill had in fact accepted the exclusion clause as part of the contract. Had Nudrill's attention been drawn to the back of the invoice, no doubt the result would have been different.

Comment

Regardless of the nature of the relationship between parties, it is necessary to include exclusion clauses within the main body of the contract or else by sending a document that contains or refers to the important terms and conditions, particularly in 'repeat contracts'. It is essential to make the other party aware of the existence of an exclusion clause, and to accept it as part of the contract.

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Case Note – *Resource Capital Fund III LP v FCT*

A recent decision of the Federal Court has addressed various complex international tax issues, as well as approaches to valuing mining tenements and related assets.

Of particular note was the fact that the court identified 'mining information' as a separate asset with a value distinct from that of the mining tenements to which it related. Even though the Commissioner has filed an appeal against the decision, the case may present planning opportunities for taxpayers, especially those in the extractive industries.

Facts

The case concerned a private equity fund, the Resource Capital Fund III LP (**Fund**), which established a limited partnership in the Cayman Islands. However, the Fund was managed in the United States, and had mainly United States resident investors.

In 2007 the Fund disposed of its investment in St Barbara Mines Ltd (**SBM**), an ASX listed goldminer, and crystallised a $52.25 million gain. Because neither the Fund nor its investors were Australian residents, the gain on disposal of the SBM shares could only be taxable in Australia if the shares were taxable Australian property. The Commissioner took the view that the shares were taxable Australian property, and assessed the Fund for the gain.

The critical issues before the court were:

a) whether the Australia/United States double tax agreement (**DTA**) prevented the Commissioner from assessing the Fund for the gain; and

b) if the Fund could be assessed, whether the shares in SBM were taxable Australian property.

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Did the DTA prevent the Commissioner from assessing the Fund for the gain?

Before addressing the specific question before it, the court made various observations on the interpretation of international tax treaties. It confirmed that such treaties should be interpreted by reference to international legal principles concerning treaty interpretation (rather than domestic statutory interpretation rules), and that such principles permitted reference to OECD commentaries on tax treaties. Although this is the generally accepted view of treaty interpretation, it had been questioned following a recent Federal Court decision[1], and comments made by the High Court in *Minister for Home Affairs v Zentai*[2].

Turning to the substantive issue in dispute, the court concluded that the DTA operated such that only the Fund's investors could be assessed for the gain, and that the Fund itself could not be assessed. The reason for this was that the relevant article of the DTA stated that only United States residents could be assessed for the gain. Although the Fund was treated as a company under Australia's domestic tax law, it was a fiscally transparent, 'flow through' entity for United States tax purposes. The OECD commentary expressed the view that this 'flow-through' treatment prevented the Fund from being a United States resident, and consequently it could not be assessed for the gain. The DTA operated such that only the Fund's investors who were United States residents could be assessed for the gain.

1 *Russell v Federal Commissioner of Taxation* (2011) 190 FCR 449

2 (2012) 289 CLR 644

Were the shares taxable Australian property?

The court's conclusion on the DTA point was sufficient for the Fund to be successful. However, the court went on to consider whether the SBM shares sold were taxable Australian property.

The Fund's shares in SBM could only have been taxable Australian property if the value of SBM's Australian real property assets exceeded the value of its non-real property assets. Both parties accepted that SBM's only Australian real property assets were its mining rights. The balance of its assets was not Australian real property assets. In light of this, one might have expected the resolution of this question to have involved a simple comparison of the values of SBM's assets. However, the court's decision demonstrates the complexities involved both in identifying the relevant assets, and in determining their market value.

The court rejected the Commissioner's argument that SBM's assets should be valued by reference to the company's entire value if sold as a going concern. It viewed such an approach as flawed because it did not reflect the value of SBM's specific assets, but rather the value of SBM in its entirety.

When assigning value to SBM's individual assets, the court confirmed that SBM's mining information should be identified and valued separately to its actual mining rights. In other words, the information and knowledge SBM had gained from its exploratory activities had a value separate to that of the mining rights to which the knowledge was applied. Although the mining rights were Australian real property, the mining information was not.

The court discussed valuation methodologies regarding SBM's various assets in considerable detail, analysing the approaches of different experts called to give evidence for the parties. One key message to take from this discussion is the method for valuing mining tenements. It used the discounted cash flows from SBM's mining operations as a starting point. It then subtracted the 'cost' of re-creating SBM's mining information and replacing its plant and equipment. The remaining amount was the market value of SBM's tenements. This approach leads to a lower value for the tenements, primarily because the cost of re-creating SBM's mining information was substantial.

Due to this, the court found that the value of SBM's non-real property assets exceeded that of its real property assets. Consequently, the Fund's gain could not be taxed even if the DTA did not apply.

Subsequent developments

As we have mentioned, the Commissioner has already filed an appeal against the decision. But, perhaps pre-empting the outcome of any appeal, the government announced a legislative measure as part of the 2013/14 Budget that will reverse aspects of the case. It will amend the test for determining whether an asset is taxable Australian property. Mining, quarrying or prospecting information, know-how and goodwill will be valued together with the mining rights to which they relate. In essence, this means that these assets will be treated as though they are real property assets for the purposes of the particular division.

Implications for taxpayers

Despite the government's announcement, the court's approach presents a number of planning opportunities around the valuation of mining assets. The approach could be particularly useful for landholder duty purposes. In most jurisdictions, duty is calculated by reference to the value of mining tenements, but not of any mining information. It may be possible to rely on this case to attribute a lower value to mining tenements and hence reduce a landholder duty liability.

A further opportunity relates to the acquisition of mining assets (tenements, information etc). Taxpayers undertaking such transactions could potentially allocate a higher proportion of a purchase price to mining information rather than mining tenements. The cost of mining information is likely to be immediately deductible rather than simply a depreciation deduction, so this strategy can accelerate tax deductions. We note that this strategy is not a new development; however, the court's decision arguably confirms the technical reasons behind its use.

We recommend that businesses undertaking mining acquisitions consider these strategies when negotiating transactions.

Contact: **Michael Kohn**, Cornwall Stodart

Accountants must obtain limited AFSL to advise on SMSFs

The government has announced it will remove a licensing exemption that currently allows accountants to provide financial advice on self-managed superannuation funds (**SMSFs**) without an Australian Financial Services Licence (**AFSL**). A new 'limited financial services licence' (**Limited AFSL**) that enables licensees to advise on, or deal in, SMSFs has been introduced to replace the exemption.

The government has given accountants three years to comply with the new licensing requirements or revise the scope of their business activities. From 1 July 2016, accountants must have either a Limited AFSL or an AFSL in order to advise clients on SMSFs. Among other things, the transitional arrangements lower the competency requirements for accountants who are members of specific professional organisations (**Recognised Accountants**).

Purpose of removing the exemption

Under the previous regime, Recognised Accountants were able to advise on the acquisition and disposal of an interest in an SMSF without an AFSL. However, the practical operation of this exemption resulted in various undesirable consequences for consumers. For example:

- Accountants were not required to adhere to the regulatory requirements imposed on other financial service providers (eg ongoing training obligations and maintenance of dispute resolution procedures).
- Accountants were not permitted to advise on certain matters incidental to SMSFs (eg investment strategies for SMSFs).

In order to enable accountants to provide more balanced commercial advice to their clients, the *Corporations Amendment Regulations 2013 (No 3)* (Cth) were introduced to streamline the licensing regime for limited categories of financial advice.

Who can apply for a Limited AFSL?

A Limited AFSL is not restricted to accountants and any person who satisfies the eligibility requirements may obtain a Limited AFSL. Recognised Accountants can take advantage of the lower competency requirements for obtaining a Limited AFSL during the transition period from 1 July 2013 to 30 June 2016. Corporations and partnerships can also apply for a Limited AFSL if they have Recognised Accountants who are responsible for and supervise the provision of financial advice (**Responsible Managers**) within their organisation.

What does a Limited AFSL cover?

Limited licensees may provide financial product advice on the following:

- SMSFs (eg making a recommendation to establish an SMSF, providing advice regarding contributions or pensions under a superannuation product).
- 'Class of product' advice (ie general advice regarding superannuation products, securities, simple managed

investment schemes, general insurance products, life risk insurance products and basic deposit products). A limited licensee must not make a specific recommendation that a person invest in a particular financial product (eg a term deposit product offered at a particular bank or institution).

- Arranging to deal in an interest in an SMSF (eg applying for, acquiring, issuing, varying or disposing of an interest in an SMSF).

Key date

Recognised Accountants (and entities that employ Recognised Accountants) should consider applying for a Limited AFSL prior to 30 June 2016 to take advantage of the transitional arrangements. These arrangements dispense with the requirement to demonstrate 'appropriate experience' in providing financial services of a type that will be authorised under the prospective Limited AFSL. Recognised Accountants who apply for a Limited AFSL after 1 July 2016 will be required to demonstrate a minimum of three years' experience (or make a written submission to ASIC), in addition to meeting the 'knowledge' (ie training or qualifications) conditions currently required pursuant to the transitional arrangements.

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Louise provides legal and strategic advice to clients on employment and industrial relations issues, including industrial disputes, enterprise bargaining, wrongful and unfair dismissals, EEO and occupational health and safety.

She has experience representing clients in the AHRC, Fair Work Australia, the VEOHRC, and federal and state courts. As well as advising and representing clients in employment, OHS and discrimination matters, Louise also conducts training seminars on issues of interest to clients.

In addition, Louise prepares employment-related documentation such as contracts, workplace policies and procedure manuals.

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