



# ***TR 2008/D5 - Income tax: meaning of 'Australian superannuation fund' in subsection 295-95(2) of the Income Tax Assessment Act 1997***

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## Draft Taxation Ruling

# Income tax: meaning of ‘Australian superannuation fund’ in subsection 295-95(2) of the *Income Tax Assessment Act 1997*

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## What this Ruling is about

1. This Ruling sets out the Commissioner’s interpretation of the definition of ‘Australian superannuation fund’ in subsection 295-95(2) of the *Income Tax Assessment Act 1997* (ITAA 1997). The definition of ‘Australian superannuation fund’ is relevant in determining whether a superannuation fund is a ‘complying superannuation fund’ for the purposes of the *Superannuation Industry (Supervision) Act 1993* (SISA). Superannuation funds that are complying superannuation funds are eligible for concessional tax treatment.

2. There are three tests that a fund must satisfy in order to be treated as an ‘Australian superannuation fund’ as defined in subsection 295-95(2) of the ITAA 1997. While this Ruling discusses all three tests contained in subsection 295-95(2), the particular focus of the Ruling will be a consideration of the ‘central management and control’ test. The definition of ‘Australian superannuation fund’ is applicable from 1 July 2007.

3. This ruling applies to funds that are 'superannuation funds' as defined in section 10 of the SISA.<sup>1</sup> It is otherwise beyond the scope of the Ruling to discuss the meaning of 'superannuation fund'.

4. This Ruling will not explore in any detail the meaning of the terms 'superannuation interests',<sup>2</sup> 'Australian resident'<sup>3</sup> and 'foreign resident' which appear in the definition of 'Australian superannuation fund'.

5. The question of whether a trustee can delegate their duties and powers as trustee of the superannuation fund and any flow on consequences from such a delegation is a separate question to determining who in fact is exercising the CM&C of the fund and where the CM&C of the fund is in fact located. It is beyond the scope of this draft Ruling to consider the issue of whether a trustee can in fact delegate their duties.

6. All references in this ruling are to the ITAA 1997 unless otherwise stated.

## **Class of entity/arrangement**

7. The class of entities to which this Ruling applies are superannuation funds that seek to be Australian superannuation funds.

## **Ruling**

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8. Subsection 295-95(2) of the ITAA 1997 provides that:

A \*superannuation fund is an 'Australian superannuation fund' at a time, and for the income year in which that time occurs, if:

- (a) the fund was established in Australia, or any asset of the fund is situated in Australia at that time; and
- (b) at that time, the central management and control of the fund is ordinarily in Australia; and

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<sup>1</sup> Subsection 995-1(1) of the ITAA 1997 states that 'superannuation fund' has the meaning given by section 10 of the SISA. That is, the fund is an indefinitely continuing fund and is a provident, benefit, superannuation or retirement fund or is otherwise a public sector superannuation scheme.

<sup>2</sup> For further information on the concept of 'superannuation interest', refer to the fact sheet 'How many superannuation interests does a member of a superannuation fund have in their fund?' which is located at [www.ato.gov.au/super](http://www.ato.gov.au/super).

<sup>3</sup> A number of other taxation rulings issued by the Commissioner discuss the meaning of 'Australian resident' in relation to individuals. See Taxation Rulings IT 2615 Income tax: Medicare Levy – test for Australian residency – payable by Australians living overseas and by visitors to Australia; IT 2650 Income tax: Residency – permanent place of abode outside Australia; IT 2681 Income tax: residency status of business migrants and Taxation Ruling TR 98/17 Income tax: residency status of individuals entering Australia.

- (c) at that time either the fund had no member covered by subsection (3) (an **active member**) or at least 50% of:
  - (i) the total \*market value of the fund's assets attributable to \*superannuation interests held by active members; or
  - (ii) the sum of the amounts that would be payable to or in respect of active members if they voluntarily ceased to be members;

is attributable to superannuation interests held by active members who are Australian residents.

9. Subsection 295-95(3) of the ITAA 1997 provides the meaning of 'active member' for the purposes of paragraph 295-95(2)(c) of the ITAA 1997. The concept of 'active member' is further discussed at paragraphs 63 to 65 of this draft Ruling.

10. Therefore, there are three tests that a superannuation fund must satisfy at the same time if it is to be an Australian superannuation fund as defined in subsection 295-95(2) of the ITAA 1997. If a fund fails to satisfy any one of the tests at that particular time, it is not an Australian superannuation fund at that time, even if it satisfies the other two tests. If the fund has satisfied all three tests at the same time in the income year, it is an Australian superannuation fund for the entire income year in which that time occurs.

#### **First test – fund established in Australia or any asset of the fund is situated in Australia**

11. The first test that must be satisfied is that the fund was established in Australia, or any asset of the fund is situated in Australia at the relevant time (paragraph 295-95(2)(a) of the ITAA 1997). The requirements in the first test must be read disjunctively such that the first test will be satisfied if the superannuation fund is or was established in Australia *or* at a particular time any asset of the fund is situated in Australia.

#### ***Whether superannuation fund established in Australia***

12. A superannuation fund is established in Australia if the initial contribution made to establish the fund is paid to and accepted by the trustee or trustees of the fund in Australia.

13. The establishment of the fund requirement in paragraph 295-95(2)(a) of the ITAA 1997 is a once and for all requirement. That is, once it is determined that a fund was established in Australia, it will satisfy the first test at all relevant times. The fact that no asset of the fund is situated in Australia does not affect this conclusion.

## ***Whether any asset of the fund is situated in Australia***

14. If a superannuation fund was not established in Australia, it will satisfy the test in paragraph 295-95(2)(a) of the ITAA 1997 if at least one asset of the fund is situated in Australia at the relevant time.

15. The location of an asset is determined by reference to the type of asset and the common law rules established by the courts for assets of that kind. These rules are discussed at paragraphs 88 to 92 of this draft Ruling.

16. If a fund that was not established in Australia ceases to have an asset in Australia at a particular time, it will fail the first test and the fund will not be an Australian superannuation fund at that time.

### *Example 1: location of shares acquired by a superannuation fund*

17. *The HB Superannuation Fund, a fund established outside Australia, acquires shares in a company incorporated in Australia. A replaceable rule in the Corporations Act 2001 – section 1072F – makes provision for a transfer of shares to be registered on the register of members before it can be regarded as an effective transfer at law. The register of members is kept in Australia. The shares in the company are therefore located in Australia.*<sup>4</sup>

## **Second test – central management and control of the fund ‘ordinarily’ in Australia**

18. The second test requires that, at a particular time, the central management and control (CM&C) of the fund is ordinarily in Australia – paragraph 295-95(2)(b) of the ITAA 1997.

### ***What is the nature of CM&C of a superannuation fund?***

19. The CM&C of a superannuation fund involves a focus on the who, when and where of the strategic and high level decision making processes and activities of the fund. In the context of the operations of a superannuation fund, the strategic and high level decision making processes includes the performance of the following duties and activities:

- formulating the investment strategy for the fund;
- reviewing and updating or varying the fund's investment strategy as well as monitoring and reviewing the performance of the fund's investments;
- if the fund has reserves – the formulation of a strategy for their prudential management; and

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<sup>4</sup> See paragraph 91 of this draft Ruling for an explanation of the rules that apply to determine the *situs* of shares in a company.

- determining how the assets of the fund are to be used to fund member benefits.

20. In the majority of cases, the other principal areas of operation of a superannuation fund, such as the acceptance of contributions, the actual investment of the fund's assets, the fulfilment of administrative duties and the preservation, payment and portability of benefits are not of a strategic or high level nature to constitute CM&C. Rather, these activities form part of the day-to-day or productive side of the fund's operations.

### ***Who exercises the CM&C of a superannuation fund?***

21. Establishing who is exercising the CM&C of a superannuation fund is a question of fact to be determined with reference to the circumstances of each case. While it is the trustee of the fund which has the legal responsibility or duty to exercise the CM&C of a superannuation fund, the mere duty to exercise CM&C does not, of itself, constitute CM&C. If the trustee in fact performs the high level duties and activities of the fund, they will be exercising the CM&C of the fund in practice.

22. There may be situations where a person other than the trustee is exercising the CM&C of the fund. If a person other than the trustee of the fund independently and without any influence from the trustee performs those duties and activities that constitute the CM&C of the fund, that person is exercising the CM&C of the fund.

23. If the trustee uses an investment manager to carry out part or all of the investment management function, this does not mean that the investment manager is in any sense exercising the CM&C of the fund.

### ***Trustee acting on external advice***

24. The trustee of a fund may seek external advice relating to the performance of their high level duties and activities. Provided that the trustee makes the actual high level decisions for the fund, the circumstance that the trustee acts on such advice does not affect the fact that the trustee is exercising the CM&C of the fund.

### ***Location of the CM&C of the fund***

25. The location of the CM&C of the fund is determined by where the high level and strategic decisions of the fund are made and high level duties and activities are performed.

***When is the CM&C of the fund ‘ordinarily’ in Australia?***

26. Whether the CM&C of a fund is ordinarily in Australia at a particular time is to be determined by the relevant facts and circumstances of each case. It involves determining whether, in the ordinary course of events, the CM&C of the fund is regularly, usually or customarily exercised in Australia. There must be some element of continuity or permanence if the CM&C of the fund is to be regarded as being ‘ordinarily’ in Australia. If the CM&C of the fund is being temporarily exercised outside Australia, this will not prevent the CM&C of the fund being ‘ordinarily’ in Australia at a particular time.

***CM&C – temporary absences***

27. Subsection 295-95(4) of the ITAA 1997 states that, to avoid doubt, the CM&C of a superannuation fund is ordinarily in Australia at a time even if that CM&C is temporarily outside Australia for a period of not more than 2 years. The effect of subsection 295-95(4) is to provide one set of circumstances in which the CM&C of a fund will be taken to be ‘ordinarily’ in Australia at a time for the purposes of paragraph 295-95(2)(b) of the ITAA 1997 (that is, it operates as a ‘safe harbour’ rule).

28. Subsection 295-95(4) of the ITAA 1997 does not otherwise restrict the meaning of ‘ordinarily’ so that the CM&C of the fund can only be outside Australia for a period of 2 years or less. If the CM&C of the fund is outside Australia for a period *greater* than 2 years, the fund will satisfy the CM&C test if it satisfies the ‘ordinarily’ requirement in paragraph 295-95(2)(b) of the ITAA 1997.

29. While the CM&C of a fund can be outside Australia for a period greater than 2 years, the period of absence of the CM&C must still be *temporary*. Furthermore, if the CM&C of the fund is not temporarily outside Australia, it will not be ‘ordinarily’ in Australia at a time even if the period of absence of the CM&C is 2 years or less.

30. The CM&C of a fund will be ‘temporarily’ outside Australia if the person or persons who exercise the CM&C of the fund are outside Australia for a relatively short period of time. The duration of the absence must either be defined in advance or related (both in intention and fact) to the fulfilment of a specific, passing purpose. Whether a period of absence is considered to be relatively short involves considerations of questions of degree which must be decided by reference to the circumstances of each particular case.

31. Whether an absence is temporary must be determined objectively by reference to all the relevant facts and circumstances on a ‘real time’ basis. That is, it cannot be established in retrospect.

**Division of CM&C**

32. In those situations where there are an equal number of trustees both in Australia and overseas who *equally* participate in the exercise of the CM&C of the fund, the CM&C of the fund will ordinarily be in Australia within the meaning of paragraph 295-95(2)(b) of the ITAA 1997, even though the CM&C of the fund is also ordinarily being exercised overseas. It is considered that such a situation would be rare.

*Example 2 – nature of CM&C of a superannuation fund*

33. *Tim and Toni are the trustees and members of the T&T Superannuation Fund, a self managed superannuation fund (SMSF). The investment strategy of the fund, which was formulated after advice from a superannuation consultant, is expressed via asset allocation ranges with associated benchmarks against which performance may be measured. Tim and Toni also establish a policy for intended actions should an asset or asset class diverge from benchmark expectations. They also consider whether or not investments will be made on a passive (indexed) or an actively managed basis and they review these decisions annually.*

34. *The formulation of the investment strategy for the fund with the associated performance benchmarks, the establishment of a policy for corrective action should the performance of an investment diverge from benchmark expectations, the decision whether investments will be made on a passive or active basis and the annual review of these decisions all constitute strategic or high level decisions and actions. Since Tim and Toni make these decisions and perform these activities, they are exercising the CM&C of the fund.*

*Example 3 – nature of CM&C of a superannuation fund*

35. *The Lepanto Superannuation Fund, which is an SMSF, has a corporate trustee, Lepanto Pty Ltd. Edmond and his wife Amanda and their son Anthony are the members of the fund and directors of the corporate trustee. In July 2009, Edmond, Amanda and Anthony travel to the USA for 2 years to further the business interests of Lepanto Pty Ltd. Whilst they are overseas, the fund's accountant in Australia lodges the income tax and regulatory return for the fund and ensures that the fund's financial statements and accounts and its compliance with the SISA are audited. However, Edmond, Amanda and Anthony review and monitor the performance of the fund's investments as well as review and update the investment strategy for the fund.*

36. *In these circumstances, the CM&C of the Lepanto Superannuation Fund is being exercised by the trustee directors of the fund as they are performing those activities and duties that constitute CM&C. The activities of the accountant in meeting the fund's lodgement and administrative obligations do not constitute CM&C.*

*Example 4 – using a financial adviser when determining investment strategy of fund*

37. John and Jacqueline, the trustees of a newly established SMSF, the ‘Camelot Superannuation Fund’, have been drafting an investment strategy for their fund and have decided they will seek professional advice before finalising the strategy. They meet with a financial adviser and provide the following information:

- when they would like to retire;
- their ability to make further contributions between now and the time when they would like to retire;
- how much they would like to have as their retirement income; and
- their own preferences for investments and risk and ideas they have come up with from their own research.

38. From this information the financial adviser helps the trustees determine the annual return needed by the fund and suggests alternate asset allocation strategies depending on their flexibility around retirement dates and the level of annual contributions they make.

39. The trustees consider the adviser’s suggestions and decide to finalise their investment strategy at a meeting before putting the strategy into effect.

40. Since John and Jacqueline set the investment strategy for the fund, they are exercising the CM&C of the fund. The fact that they act on advice in formulating the strategy does not affect this conclusion and, in the context of the facts, it cannot be said that the financial adviser is participating in the high level decision making of the fund.

*Example 5(a) – person other than trustee exercising CM&C whilst the trustees are overseas*

41. Henry and Eleanor are the trustees of their SMSF, the ‘Plantagenet Family Superannuation Fund’ which was established in Australia. The members of the Plantagenet Family Superannuation Fund are Henry and Eleanor.

42. On 29 September 2009, Henry and Eleanor travel to France to take up management of Eleanor’s family business interests in Europe. They do not have an expected return date although they do intend to return to Australia at some point in the future. They take their children with them to France, and they move into Eleanor’s family home. The children are enrolled in local schools in France. Henry and Eleanor return to Australia permanently on 22 September 2011.

43. *Prior to moving overseas, Henry and Eleanor arrange for Richard to perform the duties and activities that constitute the CM&C of the fund. Such activities include reviewing and monitoring the performance of the fund's investments, re-balancing the investment portfolio and altering the fund's investment strategy.<sup>5</sup> During Henry and Eleanor's absence from Australia, Richard undertakes these activities without reference to Henry and Eleanor. Furthermore, Henry and Eleanor did not participate in any of these high level decision making activities whilst overseas.*

44. *In these circumstances, the CM&C of the Plantagenet Family Superannuation Fund continues to be ordinarily in Australia (by virtue of Richard exercising the CM&C in Australia) within the meaning of paragraph 295-95(2)(b) of the ITAA 1997 at all times during Henry and Eleanor's absence from Australia. At no stage do Henry and Eleanor participate in the CM&C of the fund during their absence from Australia.*

*Example 5(b) – trustee exercising CM&C whilst the trustees are overseas despite arranging for another person to perform their duties*

45. *Assume the same facts as that of Example 5(a), except that Richard is required to obtain Henry and Eleanor's approval before he alters the investment strategy for the fund or re-balances the fund's investment portfolio. He is also required to provide a report every 6 months to Henry and Eleanor regarding the performance of the fund's investments.*

46. *In this situation, the CM&C of the fund is not being exercised by Richard because Henry and Eleanor are in effect exercising the CM&C of the fund whilst they are overseas.*

*Example 6 – CM&C of the fund is 'ordinarily' in Australia*

47. *Simon and his wife Donna are the trustees and members of their SMSF which was established in Australia. They have an established home in Australia but also decide to establish a second home in an overseas country. The couple and their family spend approximately 6 months at the overseas home and the rest of the year at the Australian home. The majority of trustee meetings are held in Australia at which the high level decisions in respect of the fund are made. The CM&C of the fund is only occasionally exercised in the overseas country.*

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<sup>5</sup> As trustees of the fund, Henry and Eleanor may still be held liable for acts undertaken by Richard. As noted above, the question of whether or not a trustee can delegate their duties and powers and the flow on consequences of such a delegation is a separate question to determining who in fact is exercising the CM&C of the fund and where the CM&C of the fund is in fact located. That issue is beyond the scope of this Ruling.

48. *In this situation, the CM&C of the fund is regularly, usually or customarily exercised in Australia and is only being casually or intermittently exercised overseas. Therefore, the CM&C of the fund is 'ordinarily' in Australia within the meaning of paragraph 295-95(2)(b) of the ITAA 1997 at all times.*

*Example 7(a) – trustees of the fund are outside Australia for a period greater than 2 years yet the CM&C of the fund is still 'ordinarily' in Australia*

49. *Joseph and his wife Marian are the trustees and members of their SMSF 'The J&M Superannuation Fund'. The J&M Superannuation Fund was established in Australia in August 2006. Joseph and Marian exercise the CM&C of the fund at meetings of the trustees at their home in Sydney.*

50. *Joseph, who is a chartered accountant, was seconded to his employer's London office on 1 July 2008 for a period of 2 years. It was always the intention of both Joseph and his employer that the duration of his secondment would actually be 2 years and that Joseph would return to working in Australia at the expiration of that period. However, due to unforeseen business pressures, Joseph was required to remain in London for an extra 3 months.*

51. *His wife accompanied Joseph for the duration of his secondment. They rented out the family home in Australia via their real estate agent and lived in a furnished house in London which was provided by Joseph's employer. Both Joseph and Marian continued to maintain bank accounts and private health insurance cover in Australia during the period of Joseph's secondment. They travelled back to Australia for a holiday during the Christmas 2009 period.*

52. *During the period of Joseph's secondment, the CM&C of the J&M Superannuation Fund was exercised at trustee meetings at the house in London.*

53. *In these circumstances, it is considered that the CM&C of the fund remains ordinarily in Australia during the period of Joseph's secondment as the trustees' absence from Australia was temporary. The factors that support this conclusion include the facts that Joseph and Marian intended to return to Australia at the expiration of Joseph's 2 year period of secondment and never abandoned that intention. The entire period of the absence, including the additional three months, was related to the fulfilment of a specific purpose. They did not establish a home outside Australia. They continued to maintain their home and other assets in Australia which indicates a durability of association with Australia. Accordingly, the CM&C of the J&M Superannuation Fund remained ordinarily in Australia within the meaning of paragraph 295-95(2)(b) of the ITAA 1997 during the period that the trustees were in London.*

*Example 7(b) – change of intention*

54. Assume the same facts as in Example 7(a) except that Joseph abandons his intention to return to Australia at the expiration of the 2 years and continues to work in the London office of his employer on an indefinite basis. After 3 months however, Joseph and his wife return to Australia because of the illness of Joseph's parents.

55. In this situation, the first 2 years of the trustees' absence from Australia is a for a defined (temporary) period during which the trustees maintained their intention to return to Australia. However, from the time, that is. at the end of the 2 year secondment period, that the intention of the trustees changed so that they decided to remain overseas indefinitely, their absence ceased to be temporary. Therefore, it could not be said that the CM&C of the fund was ordinarily in Australia within the meaning of paragraph 295-95(2)(b) of the ITAA 1997 during the 3 months prior to the trustees' return to Australia.

*Example 8(a) – trustees are outside Australia for a period greater than 2 years but the CM&C of the fund is not 'ordinarily' in Australia*

56. Luke and Olivia are the members and trustees of an SMSF. On 22 August 2008 they travel to an overseas country for an extended working holiday. They do not have an expected return date although they do intend to return to Australia at some point in the future. They exercise the CM&C of the fund whilst overseas.

57. They have been renting a home in Australia for several years and on leaving Australia, they do not renew this lease. They sell larger items of furniture and give some smaller items they do not wish to take with them to Olivia's parents who have a home in Western Australia. They sell their cars. Apart from personal bank accounts and their interests in the SMSF, they do not have any assets in Australia. Whilst overseas, they live in rented accommodation. They eventually return to Australia 2½ years later.

58. Because the trustees' absence from Australia is greater than 2 years, subsection 295-95(4) of the ITAA 1997 has no application in determining whether the CM&C of the fund remains 'ordinarily in Australia. To determine whether the CM&C of the fund remained 'ordinarily' in Australia in these circumstances, it is necessary to consider whether the trustees' absence from Australia was temporary.

59. The test for establishing whether the CM&C of the SMSF is 'temporarily' outside Australia must be applied at the relevant time during the year, that is, the test is a 'real time' test. Hence, the test should be applied at the time Luke and Olivia move overseas. The factors in this case that are relevant in determining whether the trustees' absence from Australia is temporary or not include: the indefinite nature of Luke and Olivia's absence from Australia, their length of stay in the overseas country and the fact that they divested themselves of the majority of their assets in Australia.

*Based on these factors, Luke and Olivia's absence from Australia is not a temporary absence. Therefore, in these circumstances, the CM&C of the fund is not 'ordinarily' in Australia within the meaning of paragraph 295-95(2)(b) of the ITAA 1997 at any time during the period of the trustees' absence from Australia.*

*Example 8(b) – trustees are outside Australia for a period less than 2 years but the CM&C of the fund is not 'ordinarily' in Australia*

60. Assume the same facts as in Example 8(a) except that Luke and Olivia return to Australia after 18 months due to the ill health of Olivia's parents. In view of the fact that Luke and Olivia moved overseas with the intention of remaining there indefinitely, their absence would still not be temporary even though it in fact turned out to be of a relatively limited duration. This is because the CM&C test is not applied in retrospect or, in other words, with the benefit of hindsight. Therefore, even though the trustees' absence from Australia was actually less than 2 years, the CM&C of the fund is not 'ordinarily' in Australia within the meaning of paragraph 295-95(2)(b) of the ITAA 1997 at any time as their absence from Australia was not temporary.

### **Third test – the 'active member' test**

61. The third test that must be satisfied is the 'active member' test (paragraph 295-95(2)(c) of the ITAA 1997). The 'active member' test is satisfied if, at the relevant time:

- the fund has no 'active member'; or
- at least 50% of the total market value of the fund's assets attributable to superannuation interests held by active members is attributable to superannuation interests held by active members who are Australian residents (subparagraph 295-95(2)(c)(i) of the ITAA 1997); or
- at least 50% of the sum of the amounts that would be payable to or in respect of active members if they voluntarily ceased to be members is attributable to superannuation interests held by active members who are Australian residents (subparagraph 295-95(2)(c)(ii) of the ITAA 1997).

62. A fund with an active member can apply either method in subparagraphs 295-95(2)(c)(i) and (ii) of the ITAA 1997 to determine whether it satisfies the active member test.

63. The definition of 'active member' is contained in subsection 295-95(3) of the ITAA 1997. A member is an active member of a superannuation fund at a particular time if the member is a contributor to the fund at that time (paragraph 295-95(3)(a) of the ITAA 1997) or is an individual on whose behalf contributions have been made (paragraph 295-95(3)(b) of the ITAA 1997).

64. However, a member of a fund is not an active member of the fund at the relevant time under paragraph 295-95(3)(b) of the ITAA 1997 if:

- they are a foreign resident (subparagraph 295-95(3)(b)(i) of the ITAA 1997); and
- they are not a contributor at that time (subparagraph 295-95(3)(b)(ii) of the ITAA 1997); and
- the only contributions made to the fund on their behalf since they became a foreign resident were made in respect of a time when they were an Australian resident (subparagraph 295-95(3)(b)(iii) of the ITAA 1997).

65. A member of a fund will also be an active member if the member's employer is on a 'contributions holiday'. The meaning of 'contributions holiday' is explained at paragraph 179 of this draft Ruling.

66. The term 'contributor' in the definition of active member is not defined. Therefore, it is to be given its ordinary meaning subject to the context in which it appears. The concept of a 'contributor' within the context of the active member test is directed at establishing the status of a member as a contributor at a particular point in time, not on the specific act of contributing. In establishing that status, reference must be had to the circumstances of each case, including a reference to the member's intention to make further contributions to the fund. The status of the member as a 'contributor' continues over the relevant period of time until the member decides to cease making contributions. When a member ceases to be a contributor is a question of fact to be determined with reference to the circumstances of each case.

*Example 9 – not an active member*

67. *Ally, who is the single member of her SMSF goes overseas on a holiday in July 2009 for an indefinite period of time. She ceases being an Australian resident in July 2011. Before travelling overseas, Ally worked as a fitness instructor at the local health & fitness centre. Her employer failed to make any superannuation contributions in respect of the period of work performed by Ally in the quarter prior to her departure (April to June 2009). In August 2012, Ally's former employer pays the superannuation guarantee charge to the Tax Office which then distributes the shortfall component of the charge to Ally's SMSF in September 2012. Ally makes no personal contributions to her SMSF during her absence from Australia.*

68. *As Ally is not a resident of Australia from July 2011 and the contribution, that is the shortfall component of the superannuation guarantee charge was made to the SMSF on her behalf in respect of the April-June 2009 period when she was a resident, Ally does not become an active member because of the contribution.*

*Example 10 – whether member of fund ‘contributor’ to the fund at a particular time<sup>6</sup>*

69. *Isabella, one of two members/trustees of an SMSF, has been making personal contributions to the fund on a monthly basis since the fund was established on 1 July 2007. Isabella makes these regular contributions through an automatic deduction from her bank account. On 1 July 2010, Isabella departs Australia for a 2 year working holiday in Spain. She returns to Australia on 30 June 2012.*

70. *Before her departure from Australia, Isabella decided that she would not make any personal contributions to the SMSF during her period of absence from Australia. She therefore instructs her bank to stop the regular transfer of funds to her SMSF. She makes no further contributions to the SMSF until her return to Australia.*

71. *In these circumstances, Isabella is a ‘contributor’ to the fund within the meaning of subsection 295-95(3) of the ITAA 1997 throughout the entire period from 1 July 2007 to 30 June 2010. As evidenced by her instruction to her bank to stop the regular transfers, she ceased to be a ‘contributor’ to the fund from 1 July 2010. Since Isabella made no further contributions until her return to Australia, she ceased to be a ‘contributor’ to the fund from that time until her return to Australia.*

## **Date of effect**

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72. It is proposed that when the final Ruling is issued, it will apply both before and after its date of issue. However, the final Ruling will not apply to taxpayers to the extent that it conflicts with the terms of settlement of a dispute agreed to before the date of issue of the final Ruling (see paragraphs 75 and 76 of Taxation Ruling TR 2006/10).

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**Commissioner of Taxation**

4 June 2008

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<sup>6</sup> See paragraphs 172 to 176 of this draft Ruling for an explanation of the meaning of ‘contributor’ and whether a member of a fund is a ‘contributor’ to the fund at a particular time in the context of subsection 295-95(3) of the ITAA 1997.

## Appendix 1 – Explanation

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**❶** *This Appendix is provided as information to help you understand how the Commissioner’s preliminary view has been reached. It does not form part of the proposed binding public ruling.*

### Legislative context and background

73. For a superannuation fund to qualify for concessional tax treatment for income tax purposes, it must be a ‘complying superannuation fund’ within the meaning of the SISA. To be a complying superannuation fund in relation to a year of income, the fund must, amongst other things, be a ‘resident regulated superannuation fund’ at all times during the year of income when it was in existence. A ‘resident regulated superannuation fund’ means a regulated superannuation fund that is an ‘Australian superannuation fund’ within the meaning of the ITAA 1997.<sup>7</sup>

74. Further, only a superannuation fund that is an Australian superannuation fund can deduct amounts incurred in obtaining all (assessable and non-assessable) contributions made to the fund.<sup>8</sup>

75. The definition of ‘Australian superannuation fund’ in subsection 295-95(2) was inserted into the ITAA 1997 by the *Tax Laws Amendment (Simplified Superannuation) Act 2007*. It replaced the definition of ‘resident superannuation fund’ in former section 6E of the *Income Tax Assessment Act 1936* (ITAA 1936) with application from 1 July 2007. The policy intention of the amendment was to simplify the scope of the fund residency definition and give effect to a minor policy change in respect of the application of the central management and control test.<sup>9</sup>

76. For income tax purposes, a fund does not need to satisfy the definition of Australian superannuation fund in subsection 295-95(2) of the ITAA 1997 at all times in an income year to be an Australian superannuation fund for the income year. Provided that a fund satisfies the definition of ‘Australian superannuation fund’ at any time during the income year, it will be an Australian superannuation fund for the income year in which that time occurs.

77. The consequences of being an Australian superannuation fund in relation to an income year is that the fund must include in its assessable income, the ordinary and statutory income the fund derived from all sources, whether in or outside Australia, during the income year. If the fund is a complying superannuation fund in relation to the year of income, this income will be taxed concessionally, that is at 15%. If the fund is non-complying, the income will be taxed at the highest marginal tax rate, that is 45%.

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<sup>7</sup> Section 10 of the SISA.

<sup>8</sup> Subsection 295-95(1) of the ITAA 1997.

<sup>9</sup> Paragraph 3.91 of the Explanatory Memorandum to the Tax Laws Amendment (Simplified Superannuation) Bill 2006.

## **Superannuation fund established in Australia or any asset of the fund situated in Australia at the relevant time**

78. The first test that a superannuation fund must satisfy to be an 'Australian superannuation fund' at a time is that the fund was either established in Australia, or any asset of the fund is situated in Australia at the relevant time – paragraph 295-95(2)(a) of the ITAA 1997.

### ***When will a superannuation fund be established in Australia?***

79. To determine when a superannuation fund will be established in Australia, it is first necessary to consider the elements required to bring a superannuation fund into existence. *The Australian Oxford Dictionary* defines 'establish' as '1. set up or consolidate...on a permanent basis...'

80. The key elements required to bring a superannuation fund into existence are that the trust deed for the fund is signed and executed *and* money paid or other property is transferred to the trustee or trustees of the fund as an initial contribution that is to be held on trust for the beneficiaries (members) of the fund.

81. Case law provides support for the view that both of those requirements must be satisfied before a superannuation fund will be established. In *JD Mahoney v. FCT*<sup>10</sup> (*JD Mahoney*), a case in which the High Court was required to decide whether the appellant fund was being applied for the purpose for which it was established, that is to benefit employees,<sup>11</sup> Owen J stated:<sup>12</sup>

In order to succeed the appellants must in the first place show that a fund was established. That, it seems to me, they have done by producing the deed of the trust and proving that £500 was paid by the company to the trustees to be dealt by them in accordance with the trusts declared in the deed.

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<sup>10</sup> (1965) 13 ATD 519.

<sup>11</sup> If the fund was being applied for the purpose for which it was established, the fund's income for the relevant year was exempt from income tax.

<sup>12</sup> (1965) 13 ATD 519 at 525.

82. In *Walstern Pty Ltd v. FCT*<sup>13</sup> (*Walstern*), Hill J made the following observations in the context of deciding whether a deduction was allowable to a company for a contribution made to a non-complying superannuation fund under former section 82AAE of the ITAA 1936:<sup>14</sup>

There is an argument...that there could be no 'fund' in the year of income unless at the time the contribution was made there was actually money or other property held in trust or otherwise subject to legal requirements of a kind which would make the fund a provident benefit superannuation or retirement fund. In *Scott v. FC of T* (No 2) (1966) 40 ALJR 265 Windeyer J at 351, expressed the view...that 'fund' in the context of 'superannuation fund' ordinarily meant 'money (or investments) set aside and invested, the surplus income therefrom being capitalised.' **For present purposes, the point is the need for 'money' or 'other property' to constitute a fund.**

...

Prima facie it may be that where there is what may be referred to as a master fund to which separate contributions are to be made, which contributions are to be kept separate from other contributions, it might suffice if there was any contribution at all made which could bring about the result that there was a fund...The evidence does not permit me to say whether at the time the original contribution was made to the ATC Fund by Walstern the trustees in fact held property upon trust in the master fund. **Mere signature of a trust deed, without assets held in trust would not create a fund** (emphasis added).

83. In the House of Lords decision in *British Insulated & Helsby Cables v. Atherton*<sup>15</sup> (*British Insulated & Helsby Cables*), where it was held that an initial contribution to establish a superannuation fund to benefit employees was not deductible because it was capital, Viscount Cave LC stated the following:

The payment of £31,784, which is the subject of dispute, was made, not merely as a gift or bonus to the older servants of the appellant company, but (as the deed shows) to 'form a nucleus' of the pension fund which it was desired to create; and it is a fair inference from the terms of the deed and from the Commissioners' findings that **without this contribution the fund might not have come into existence at all.**

The object and effect of the payment of this large sum was to enable the company to establish the pension fund and to offer to all its existing and future employees a sure provision for their old age, and so to obtain for the company the substantial and lasting advantage of being in a position throughout its business life to secure and retain the services of a contented and efficient staff (emphasis added).

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<sup>13</sup> (2003) 138 FCR 1.

<sup>14</sup> (2003) 138 FCR 1 at 15. In making these comments, Hill J referred to the view of Owen J in *JD Mahoney* as to when a fund will be established.

<sup>15</sup> [1926] AC 205.

84. The views expressed in *JD Mahoney, Walstern* and *British Insulated & Helsby Cables* reflect the principles of the general law of trusts as to when a trust will be created.<sup>16</sup> As most superannuation funds are trusts, these principles will be applicable in determining when a superannuation fund will be established.<sup>17</sup>

85. However, there appears to be no case law which provides guidance on the location of the establishment of a superannuation fund. Notwithstanding this, it is considered that a superannuation fund will be established *in Australia* when the initial contribution that establishes the fund is paid to and accepted by the trustee in Australia.<sup>18</sup> It is not necessary that the deed for the fund is signed and executed in Australia. Whether the initial contribution to establish the fund occurred in Australia is a question of fact which is determined by reference to the circumstances of each case.

86. If there is a situation where the initial contribution to establish the fund occurred *outside* Australia, notwithstanding that one or more of the signatories executed the deed in Australia, the fund will not be established *in Australia*.

87. The establishment of a fund is a once off event. The requirements in paragraph 295-95(2)(a) of the ITAA 1997 must therefore be read disjunctively such that once it is determined that a fund was established in Australia then it will satisfy the first test in paragraph 295-95(2)(a) at all relevant times. If it is determined that the fund was not established in Australia, then the alternative requirement in paragraph 295-95(2)(a), namely location of the assets of the fund, must be considered.

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<sup>16</sup> According to these principles, before a valid trust is created there must be certainty on three matters:

- (1) certainty of intention to create a trust;
- (2) certainty as to the property that is the subject matter of the trust; and
- (3) certainty as to the objects (beneficiaries) of the trust.

<sup>17</sup> The courts have expressed the view that unless the trustee legislation or the rules governing the trust provide to the contrary, the principles of the general law of trusts applies to superannuation funds. See, for example, *Cowan v. Scargill* [1985] Ch 270 at 292; [1984] 2 All ER 750 at 764 and *Lock v. Westpac Banking Corporation* (1991) 25 NSWLR 593 at 609-610.

<sup>18</sup> Those superannuation schemes that are established by or under the law of the Commonwealth, or of a State or Territory – see paragraph (a) of the definition of ‘public sector superannuation scheme’ in section 10 of the SISA - are established in Australia.

**Location of the assets of the fund**

88. If a fund was not established in Australia, it will satisfy paragraph 295-95(2)(a) of the ITAA 1997 if any asset of the fund is situated in Australia at the relevant time. 'Asset' is not defined in the ITAA 1997 and hence should be given its ordinary meaning in the context in which it appears.<sup>19</sup> According to the *Butterworths Australian Legal Dictionary*, an asset is:

An item, whether tangible or intangible, having economic value to its owner which, if not already in the form of money, can be converted into money to the owner's benefit.

89. The courts have formulated a number of common law tests to determine the site or location of a particular asset for various purposes (including for taxation purposes). These rules are most often discussed in a private international law or conflict of laws context.<sup>20</sup> The application of these common law tests can raise complex questions of fact and law.

90. As noted by Nygh and Davies in their text, *Conflict of Laws in Australia*,<sup>21</sup> while the rules for determining the location or *situs* of an asset is not the same for all the various purposes for which it is important to determine an asset's *situs*, for many, and perhaps even most, kinds of property the rules may well be the same, whatever the purpose for which the *situs* is sought to be established. For example, the learned authors state that it is not possible to argue that land or tangible assets have a location other than the place where they physically are.<sup>22</sup>

91. While it is not possible to deal with every type of asset that may be relevant to superannuation funds, the general common law rules established by the courts for determining the site or location of particular types of assets are as follows:

- *land* – land and interests in land are situate in the place where the land lies.<sup>23</sup>

<sup>19</sup> Relevantly, the word 'asset' is defined in section 10 of the SISA to mean any form of property, including money.

<sup>20</sup> See for example, Collins, L 2006, *Dicey, Morris and Collins on The Conflict of Laws*, 14<sup>th</sup> edn, Sweet & Maxwell, London; Mortensen, RG 2006, *Private International Law in Australia*, LexisNexis Butterworths, Australia; Nygh, PE and Davies, M 2002, *Conflict of Laws in Australia*, 7<sup>th</sup> edn, LexisNexis Butterworths, Australia.

<sup>21</sup> Nygh, PE and Davies, M 2002, *Conflict of Laws in Australia*, 7<sup>th</sup> edn, LexisNexis Butterworths, Australia, p.586

<sup>22</sup> Nygh, PE and Davies, M 2002, *Conflict of Laws in Australia*, 7<sup>th</sup> edn, LexisNexis Butterworths, Australia, p.586

<sup>23</sup> *Haque v. Haque (No 2)* (1965) 114 CLR 98 at 136, per Windeyer J.

- *shares* – the basic principle for identifying the location of shares in a company is that they are situate where, according to the law of the place where the company was incorporated, the shares can be dealt with effectively as between the owner for the time being and the company.<sup>24</sup> The law of the place of incorporation of the company decides how shares in the company may be transferred. If they may be transferred only by registration on a particular register, they will be regarded as situate at the place where the register is kept.<sup>25</sup>
- *beneficial interests under a trust* – if the beneficiary is given a beneficial interest in the trust property then their interest in the trust is located in the country where the trust property is situated.<sup>26</sup> If the beneficiary is merely given a right of action against the trustees then his interest under the trust is located where the action may be brought, that is at the trustees' place of residence.<sup>27</sup>
- *simple contract debts* – the general rule applicable to debts is that they are deemed to be situate where the debtor resides.<sup>28</sup> This will apply irrespective of the location of the documentary evidence recording the debt.<sup>29</sup>
- *specialties* (such as a policy of insurance) – a debt created by deed (a 'specialty') has been held to be located where the deed itself is to be found because, by reason of the deed itself, the debt is taken to have some tangible existence.<sup>30</sup>
- *bank accounts* – a bank account is a debt being a single chose in action.<sup>31</sup> The bank is the relevant debtor in the relationship.<sup>32</sup> The rules that apply to determine the location of debts would therefore apply to bank accounts.

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<sup>24</sup> Collins, L 2006, *Dicey, Morris and Collins on the Conflict of Laws*, 14<sup>th</sup> edn, Sweet & Maxwell, London, p.1125.

<sup>25</sup> *Attorney-General v. Higgins* (1857) 2 H & N 339; *Brassard v. Smith* [1922] 1 AC 215.

<sup>26</sup> See *Re Berchtold* [1923] 1 Ch 192; *Philipson-Stow v. Inland Revenue Commissioners* [1961] AC 727 at 762.

<sup>27</sup> Collins, L 2006, *Dicey, Morris and Collins on The Conflict of Laws*, 14<sup>th</sup> edn, Sweet & Maxwell, London, p.1127.

<sup>28</sup> *Attorney-General v. Bouwens* (1838) 4 M & W 171 at 191; 150 ER 1390 at 1398; *English Scottish & Australian Bank Ltd v. IRC* [1932] AC 238; [1931] All ER Rep 212; *Haque v. Haque (No.2)* (1965) 114 CLR 98 at 137, per Windeyer J.

<sup>29</sup> *Sutherland v. Administrator of German Property* [1934] 1 KB 423.

<sup>30</sup> *Shaw v. R* (1895) 21 VLR 338; 1 ALR 122; *Haque v. Haque (No.2)* (1965) 114 CLR 98 at 137, per Windeyer J.

<sup>31</sup> *Joachimson v. Swiss Bank Corporation* [1921] 3 KB 110 at 127.

<sup>32</sup> *Foley v. Hill* [1843-1860] All ER 16.

- *negotiable instruments and securities transferable by delivery* – for taxation purposes, bonds, bills of exchange and other securities which can be validly and effectively transferred by delivery with or without endorsement are situate in the country where the paper representing the security is itself from time to time found.<sup>33</sup>
- *leases* – the general rule for land applies to any leasehold interest in land.<sup>34</sup> It is deemed to be situate in the place where the land over which the lease is held, lies.<sup>35</sup>
- *chattels* (such as artwork, jewellery etcetera) – in the same way that land is situate where it lies, so chattels are situate in the place where they happen to be at the relevant time.<sup>36</sup>

92. It is a question of fact in each case whether or not these rules are satisfied.

### **The central management and control test**

93. The second test and one of the key requirements that a superannuation fund must satisfy to be an ‘Australian superannuation fund’ at a particular time is that the CM&C of the fund is ordinarily in Australia – paragraph 295-95(2)(b) of the ITAA 1997.

94. To determine the location of the CM&C of a fund at a point in time, it is necessary to consider what constitutes the CM&C of a fund and who it is that exercises the CM&C of a fund.

### ***Meaning of ‘central management and control’ in the context of a superannuation fund***

95. The phrase ‘central management and control’ is not defined in the ITAA 1997. Therefore, the term must be given its common law meaning in the context in which the term appears. In this case, the operations of a superannuation fund form part of that context, using the word ‘context’ in its widest sense.<sup>37</sup>

<sup>33</sup> *Attorney-General v. Bouwens* (1838) 4 M & W 171; 150 ER 1390.

<sup>34</sup> Mortensen, RG 2006, *Private International Law in Australia*, LexisNexis Butterworths, Australia, p.449.

<sup>35</sup> *Attorney-General v. Bouwens* (1838) 4 M & W 171 at 191; 150 ER 1390 at 1398.

<sup>36</sup> *Haque v. Haque (No.2)* (1965) 114 CLR 98 at 136, per Windeyer J.

<sup>37</sup> *CIC Insurance Ltd v. Bankstown Football Club Ltd* (1997) 187 CLR 384.

96. The term ‘central management and control’ was developed by the courts as the common law rule for determining the residence of a company. As Lord Loreburn LC stated in *De Beers Consolidated Mines Ltd v. Howe*<sup>38</sup> (*De Beers*):

In applying the concept of residence to a company, we ought, I think, to proceed as nearly as we can upon an analogy of an individual. A company cannot eat or sleep, but it can keep house and do business. We ought, therefore, to see where it really keeps house and does business...a company resides for purposes of income tax where its real business is carried on. I regard that as the true rule, and the real business is carried on where the central management and control actually abides.

97. Since the House of Lords decision in *De Beers*, there has been a number of cases, both in the United Kingdom and Australia, which have discussed the application of the CM&C test in relation to companies. However, there is no case law which has discussed the meaning of CM&C in the context of superannuation funds.

98. Notwithstanding this, it is considered that, despite the differences between companies and superannuation funds, when the duties of the trustee of a superannuation fund and the nature of a fund’s operations and activities are taken into account, particularly the trustee’s duties in relation to the fund’s investment activities, the principles expressed in cases dealing with the operation of the CM&C test in relation to companies are capable of application to determine the meaning of CM&C as it relates to superannuation funds.

99. In *Koitaki Para Rubber Estates Ltd v. FCT*<sup>39</sup> (*Koitaki*), Williams J stated that in relation to determining the residence of a company:<sup>40</sup>

the crucial test is to ascertain where the real business of the company is carried on, not in the sense of where it trades but in the sense of from where its operations are *controlled and directed*. It is the place of personal control over and not of the physical operations of the business which counts (emphasis added).

Hence, the CM&C of a company comprises the management and control decisions made at the highest levels in the company. Such an analysis focuses on who makes those strategic decisions and when and where those decisions are made.

100. Like companies, determining the CM&C of a superannuation fund involves a focus on the who, when and where of the strategic and high level decision making of the fund.

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<sup>38</sup> [1906] AC 455 at 458.

<sup>39</sup> (1941) 64 CLR 241; (1941) 6 ATD 82.

<sup>40</sup> (1941) 64 CLR 241 at 248; (1941) 6 ATD 82 at 89.

101. In the context of the operations of a superannuation fund, the strategic and high level decision making of the fund includes the performance of the following duties and activities:

- formulating the investment strategy for the fund;<sup>41</sup>
- reviewing and updating or altering the investment strategy of the fund as well as monitoring and reviewing the performance of the fund's investments;<sup>42</sup>
- if the fund has reserves<sup>43</sup> – the formulation of a strategy for their prudential management;<sup>44</sup> and
- determining how the assets of the fund are used to fund member benefits, for example the decision to segregate certain fund assets to support superannuation income stream benefits.

102. In the majority of cases, the other principal areas of operation of a superannuation fund, such as the acceptance of contributions, the actual investment of the fund's assets, the fulfilment of administrative duties<sup>45</sup> and the preservation, payment and portability of benefits are not of a strategic or high level nature to constitute CM&C. Rather these activities form part of the day-to-day or productive side of the operations of a superannuation fund.

103. Furthermore, in accepting contributions, paying benefits and in the fulfilment of administrative obligations, the prudential requirements in SISA, the governing rules of the fund and other legislative requirements are merely being complied with. As emphasised by the courts in the context of companies, compliance with statutory requirements is not, of itself, sufficient to constitute CM&C but rather is a matter to be taken into account in determining where the CM&C is located. In *Egyptian Delta Land and Investment Company Ltd v. Todd*,<sup>46</sup> the House of Lords held that a company, which was incorporated in England and did nothing in that country beyond fulfilling its statutory requirements, was not a resident of England as its CM&C was in Egypt.

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<sup>41</sup> An investment strategy is a plan or policy adopted by the fund for investing the fund's assets to achieve the fund's investment objectives. A fund can have more than one investment strategy. The duty to formulate an investment strategy is contained in paragraph 52(2)(f) of the SISA.

<sup>42</sup> There is a requirement in each of the state and territory trustee Acts that the performance of a trust's investments, individually and as a whole, are to be reviewed at least once on an annual basis. Since the majority of superannuation funds are trusts, this rule would also apply to superannuation funds.

<sup>43</sup> Where permitted by the trust deed, reserves may be maintained by a fund for the purpose of smoothing investment returns to members.

<sup>44</sup> The requirement to formulate a reserving strategy where a fund maintains reserves is set out in paragraph 52(2)(g) of the SISA.

<sup>45</sup> Such as lodging the regulatory and income tax return for the fund, the preparation of financial statements, the audit of the fund and record-keeping.

<sup>46</sup> [1929] AC 1.

***Who exercises the CM&C of the fund?***

104. As mentioned above, the majority of superannuation funds operate under a trust structure. According to the general law of trusts, a trust is not a legal person but rather is a collection of rights, duties and powers arising from the relationship to property held by the trustee for the benefit of beneficiaries.<sup>47</sup> Therefore, it is the trustee which is the legal person to that relationship.<sup>48</sup> Since the legal responsibility for operating and managing the fund, including the responsibility for performing the high level duties and actions mentioned in paragraph 101 of this draft Ruling rests solely with the trustee, it is the trustee of the fund which has the legal obligation for exercising the CM&C of a fund.

105. In the context of companies, the courts have held that the possession of the mere 'legal right or power to exercise CM&C' is not, of itself, sufficient to constitute the CM&C of the company.<sup>49</sup> Rather, the focus has been on whether that right or power has been exercised in practice. This is a question of fact. As emphasised by Lord Loreburn LC in *De Beers*:<sup>50</sup>

This is a pure question of fact, to be determined, not according to the construction of this or that regulation or bye-law, but upon a scrutiny of the course of business or trading.

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<sup>47</sup> Trusts and superannuation funds are given statutory status as entities in themselves under subsection 960-100(1) of the ITAA 1997. See also the definition of 'superannuation entity' in section 10 of the SISA.

<sup>48</sup> To be a regulated superannuation fund within the meaning of the SISA, a superannuation fund must have a trustee – subsection 19(2) of the SISA. The trustee of the fund can be an individual, a group of individuals or a corporate trustee. A 'trustee' for the purposes of the SISA is defined in section 10 of that Act.

<sup>49</sup> *Mitchell v. Egyptian Hotels Ltd* [1915] AC 1022 at 1041, per Lord Sumner. See also *Egyptian Delta Land and Investment Company Ltd v. Todd* [1929] AC 1 where it was considered that the mere existence of the capacity for ultimate control was not sufficient to constitute CM&C where the control was not exercised in practice.

<sup>50</sup> [1906] AC 455 at 458.

106. In *Unit Construction Co Ltd v. Bullock (Inspector of Taxes)*<sup>51</sup> (*Unit Construction*), the House of Lords held that the CM&C of African subsidiaries of a United Kingdom parent company was not exercised by its board even though the board possessed the legal power to exercise CM&C under the company's constitution. Rather, the court concluded that it was in fact the board of directors of the parent company in London that had exercised the real management and control of the African subsidiary.<sup>52</sup> In reaching this conclusion, the House of Lords followed the approach laid down in *De Beers*. In the context of the facts in *Unit Construction*, Viscount Simonds stated:<sup>53</sup>

Nothing can be more factual and concrete than the acts of management which enable a court to find as a fact that central management and control is exercised in one country or another. It does not in any way alter their character that, in greater or less degree, they are irregular or unauthorised or unlawful. The business is not the less managed in London because it ought to be managed in Kenya. Its residence is determined by the solid facts, not by the terms of its constitution however imperative.

107. Therefore, the focus has been on where the high level and strategic decisions that comprise the CM&C of the company have in fact been made. Such an analysis necessarily must focus on who in fact is making those decisions.

108. In the context of superannuation funds, this same principle applies in that the trustee's duty or responsibility to carry out or perform those activities that constitute CM&C does not, of itself, amount to CM&C. It is only by performing those high level duties and activities that the trustee will be exercising the CM&C in practice.<sup>54</sup> There also may be situations where a person other than the trustee is exercising the CM&C of the fund.

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<sup>51</sup> [1959] 3 All ER 831.

<sup>52</sup> In that case, the directors of the African subsidiaries 'stood aside' from their directorial duties and never purported to function as a board of management.

<sup>53</sup> [1960] AC 351 at 362-363.

<sup>54</sup> Since duties are imperative, that is, they compel or prohibit a trustee from acting in a certain way, the failure to fulfil a duty prima facie renders the trustee liable for breach of trust. Further, the requirements under the SISA should be considered when undertaking such a course of action.

***Delegation of trustee's duties and powers***

109. Where the trustee of a fund delegates their duties<sup>55</sup> to another person, the delegate will be exercising the CM&C of the fund if they independently and without influence from the trustee, perform those duties and activities that constitute CM&C of the superannuation fund. This is because, as was stated above, the location of the CM&C of the fund will be where the relevant high level and strategic actions that comprise the CM&C of the fund are in fact performed.

110. However, if the trustee continues to participate in the high level decision making and activities of the fund by reviewing or considering the decisions and actions of the delegate before deciding whether any further or different action is required then it cannot be said that the delegate is exercising the CM&C of the fund. The decision in *BW Noble Ltd v. Mitchell*<sup>56</sup> (*BW Noble*) illustrates this principle.

111. In *BW Noble*, full management and control of the business of the company registered in England was vested in the board of directors in London by the company's articles of association, with powers of delegation. The board of directors exercised that power by executing a power of attorney granting one of the directors of the board, full power to carry on the company's business in France. The French attorney sent some reports on the progress of the business to the directors in London, and on one or two occasions received the agreement of the board to his proposals. It was held that the CM&C of the company remained with the board of directors in London and had not been shifted to France under the power of attorney. Relevantly, Rowlatt J stated:<sup>57</sup>

...in my judgment that power of attorney did not and could not, consistently with the Articles, and did not by its tenor, divest the Board in London of their authority; it did not make an independent plenipotentiary who could do what he liked until the power of attorney was determined. It seems to me that although he held the power of attorney, the Directors at any moment could have said to him: 'Well, we do not think under your power you ought to do this; we decide that it shall not be done, although you might have done it under your power of attorney if we had not told you to the contrary'.

112. Similarly, despite the intention to delegate the trustee's duties, the trustee may continue to make the high level decisions in respect of the fund and instruct the delegate to implement those decisions. Or alternatively, the trustee may continue to make those decisions and perform those duties and activities that constitute CM&C themselves. In these situations, the CM&C of the fund would remain with the trustee and would be located where the trustee makes those decisions.

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<sup>55</sup> Whether the trustee can in fact delegate their duties and any flow on consequences of such a delegation is a separate issue from determining who in fact is exercising CM&C and where the CM&C of the fund is in fact located. It is beyond the scope of this ruling to consider such issues.

<sup>56</sup> (1926) 11 TC 372.

<sup>57</sup> (1926) 11 TC 372 at 410.

***Delegation of the investment management function***

113. The trustee of a superannuation fund will often appoint an investment manager to invest the assets of the fund, consistent with the investment strategy of the fund, on behalf of the trustee. Importantly, the investment manager is subject to a prudential requirement under SISA to periodically provide information to the trustee of the fund regarding the making of, and return on those investments and to provide such information as is necessary to enable the trustee to assess the capability of the investment manager to manage the investments of the fund.<sup>58</sup>

114. The delegation of the investment management function to an investment manager does not mean however that the investment manager is exercising the CM&C of the fund in any sense. This is because the trustee is still controlling the general affairs of the fund by ensuring that the investments of the fund are consistent with the investment strategy of the fund and by monitoring and evaluating the performance of the investment manager. Further, the actions of the investment manager in investing the assets of the fund in accordance with the fund's investment strategy can be likened to the day-to-day or 'productive' side of the operations of the fund rather than to the strategic or high level decision making activities of the fund, which, as noted, includes the setting of the investment strategy of the fund and the monitoring of the performance of the fund's investments.

115. This view is consistent with the decision of Dixon J in *Koitaki*. The company in *Koitaki*, which was incorporated in Sydney, owned rubber plantations in Papua. The plantations were managed by an officer of the company who acted under a power of attorney by which the company authorised him to manage, carry on and conduct the company's property, affairs and business. The officer sent weekly reports of the working of the plantations to the chairman of directors in Sydney which is where the directors of the company resided and met. He also periodically sent to the manager of the company in Sydney for presentation to the directors, reports concerning the running of the plantations and the yield of rubber.

116. Dixon J's decision, which was affirmed by the Full High Court on appeal, was that the company was not a resident of Papua as the company's central management and control was not there exercised, despite the responsibilities of the attorney. His Honour stated that the responsibility of the attorney was confined to the production and shipment of rubber and did not extend to the control of the general or corporate affairs of the company or to matters of policy and finance.<sup>59</sup> The matters of policy and finance were matters which in fact formed part of the CM&C of the company as distinct from the day to day management of the production and shipment of rubber. The fact that the performance of the attorney was being monitored from Sydney was also an important consideration in the decision of Dixon J.

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<sup>58</sup> Section 102 of the SISA.

<sup>59</sup> (1940) CLR 15 at 18; (1940) 6 ATD 42 at 45.

***Trustee acting on external advice***

117. The trustee of a fund may seek external advice relating to the performance of their high level duties and activities. Provided that the trustee makes the actual decisions for the fund, the circumstance that the trustee acts on such advice does not affect the fact that the trustee is exercising the CM&C of the fund. This view is supported by the decision of Gibbs J at first instance in *Esquire Nominees Ltd v. FC of T (Esquire Nominees)*.<sup>60</sup>

118. In *Esquire Nominees*, his Honour stated that even if it was accepted that the decision makers of the appellant company did what the company's advisers told them to do, it did not necessarily follow that the control and management of the company's affairs lay with the advisers. He acknowledged the possibility that the advisers in *Esquire Nominees* exerted strong influence on the company directors but found that even though the advisers had power to exert influence on the company directors, that power of itself did not amount to the advisers exercising control and management of the company. He also considered that had the advisers instructed the company's directors to 'do something which they considered improper or inadvisable' that he did not believe that the directors would have acted on the instruction. He decided, on the facts of *Esquire Nominees*, that the company directors were the high level decision makers.

***Location of the CM&C of the fund***

119. The place from where the CM&C of the fund is exercised is a question of fact<sup>61</sup> to be determined in light of all the relevant facts and circumstances. The location of the CM&C of the fund is intertwined with identifying who it is that is exercising the CM&C of the fund.

120. In the case of a fund with an individual trustee who also exercises the CM&C of the fund, the place where the trustee performs the high level duties and activities that constitute CM&C will determine the location of the CM&C of the fund.

121. Equally, in the case of a fund with a group of individual trustees or a corporate trustee, the place where the trustees (or directors of the corporate trustee) meet will determine where the CM&C of the fund is located, provided that the CM&C of the fund is exercised at those meetings.<sup>62</sup> If the CM&C of the fund is not exercised at the meeting of trustees, it will be located where the high level decisions and activities are made and carried out.

<sup>60</sup> (1973) 129 CLR 177; 72 ATC 4076; (1972) 3 ATR 105.

<sup>61</sup> *Unit Construction Co Ltd (Inspector of Taxes) v. Bullock* (1959) 3 All ER 831 at 839, per Lord Radcliffe.

<sup>62</sup> In determining where the CM&C of a company is located, the common law places significant weight on the place where the board of directors meet. For example, *De Beers and Koitaki*. However, the courts have also held that the place where the board meets is not necessarily conclusive of the location of CM&C: Lord Radcliffe in *Unit Construction*.

122. If the CM&C of the fund is being exercised by a person other than the trustee, the place where the person performs the high level duties and activities in relation to the fund will determine the location of the CM&C of the fund (subject to the principles set out in paragraphs 109 to 112 of this draft Ruling).

123. Where trustee meetings are conducted via electronic facilities (rather than physical attendance), the focus is on where the participants contributing to the high level decisions and activities are located rather than where the electronic facilities are based. The fact that a majority of the trustees regularly participate in meetings from a jurisdiction other than Australia would support a conclusion that the CM&C of the fund is not located in Australia.

124. The residency status of those who exercise the CM&C of the fund does not of itself determine the location of the CM&C but may indicate the place where the CM&C of the fund is likely to be located.<sup>63</sup>

#### **When is the central management and control of a superannuation fund ‘ordinarily’ in Australia?**

125. Paragraph 295-95(2)(b) of the ITAA 1997 requires the CM&C of the superannuation fund to be ‘ordinarily’ in Australia at the relevant time. The word ‘ordinarily’ is not defined. Therefore, consistent with modern principles of statutory interpretation,<sup>64</sup> it takes on its ordinary or common law meaning subject to the context in which it appears and the purpose or object underlying paragraph 295-95(2)(b).

126. ‘Ordinarily’ is defined in *The Australian Oxford Dictionary* by reference to the term ‘ordinary’. ‘Ordinary’ is defined as ‘1. a regular, normal, customary, usual (*in the ordinary course of events*)...’

127. A number of authorities, both in Australia and the United Kingdom, have considered the meaning of the phrase ‘ordinarily resident’ in statutory contexts such as bankruptcy and income tax. These cases are relevant in determining where the CM&C of a superannuation fund is ordinarily located because they provide an explanation of the meaning of the term ‘ordinarily’ in resolving questions relating to residency.

<sup>63</sup> *John Hood and Company Ltd v. Magee* (1918) 7 TC 327.

<sup>64</sup> For example, as expressed in section 15AA of the *Acts Interpretation Act 1901* and in such cases as *CIC Insurance Ltd v. Bankstown Football Club* (1997) 187 CLR 384; *Newcastle City Council v. GIO General Ltd* (1997) 191 CLR 85 and *HP Mercantile Pty Ltd v. Commissioner of Taxation* (2005) 143 FCR 553.

128. In *Re Vassis; Ex parte Leung*<sup>65</sup> (*Re Vassis*), one of the questions under consideration was whether the debtor, who had departed Australia to Greece for two years before returning, was 'ordinarily resident' in Australia within the meaning of subparagraph 43(1)(b)(i) of the *Bankruptcy Act 1966* (Bankruptcy Act) during a period after his departure. Burchett J made the following comment in relation to the meaning of the expression 'ordinarily resident':<sup>66</sup>

The question where a person is ordinarily resident is a question of fact...It is obviously not to be answered, in respect of any particular time, by asking where that person was then *resident*. Otherwise, the word 'ordinarily' would have no meaning. But even the unqualified concept of residence is not tied to the accidents of a day; for, as Viscount Sumner said in *IRC v. Lysaght* [1928] AC 234 at 245: 'One thinks of a man's settled and usual place of abode as his residence'. At the same time, His Lordship pointed out that 'in many cases in ordinary speech one residence at a time is the underlying assumption and, though a man may be the occupier of two houses, he is thought of as only resident in the one he lives in at the time in question'. In s 43 of the Bankruptcy Act, the phrase is not 'resident in Australia', but 'ordinarily resident in Australia'...In such a context, it must convey the former of the meanings which I have quoted from Viscount Sumner's speech rather than the latter. **If a man's home is in Australia, a mere temporary absence will not prevent his being 'ordinarily resident in Australia'** It is a question of fact and degree at what point a temporary absence might, if sufficiently prolonged, prevent its being proper to continue to regard him as ordinarily resident in Australia (emphasis added).

129. On the basis of the evidence, His Honour held that the debtor was 'ordinarily resident' in Australia, both at the time that he departed from Australia, and throughout the period of his departure until his return. Therefore, the journey overseas was no more than a temporary interruption of his ordinary residence in Australia.

130. In *Re Taylor; Ex parte Natwest Australia Bank Limited (Re Taylor)*<sup>67</sup> Lockhart J also considered the meaning of the expression 'ordinarily resident' in the context of subparagraph 43(1)(b)(i) of the Bankruptcy Act. The issue in that case was whether the debtor was 'ordinarily resident' in Australia at the time when he committed an act of bankruptcy.

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<sup>65</sup> (1986) 9 FCR 518.

<sup>66</sup> (1986) 9 FCR 518 at 524-525.

<sup>67</sup> (1992) 37 FCR 194.

131. In the three years prior to committing the act of bankruptcy, the debtor travelled frequently from Australia to various countries throughout the world for business reasons and the duration of each absence from Australia ranged from 30 days to 5 months. Subject to one exception, the debtor described himself as an Australian resident either leaving or returning to Australia as the case may be. In considering whether the debtor was 'ordinarily resident' in Australia at the time of committing the act of bankruptcy, Lockhart J stated:<sup>68</sup>

I shall not attempt to give any comprehensive definition of the word 'resident'. It has no technical or special meaning for the purposes of the Act. Nor do the words 'ordinarily resident' have any such technical or special meaning. They are ordinary English words. Whether a debtor is ordinarily resident in Australia is a question of fact and degree.

...

To say that a person is ordinarily resident in Australia must mean something more than he is resident of Australia. **The word 'ordinarily' connotes a comparison, a measure of degree.** A person may have more than one residence, but he is not ordinarily resident in each of them. The question must be determined for the purposes of s.43 of the Act at a particular time. One must ask the question whether at that time the person was ordinarily resident in Australia. The concept of 'ordinary residence' for the purposes of the Act, in my opinion, connotes a place where in the ordinary course of a person's life he regularly or customarily lives. There must be some element of permanence, to be contrasted with a place where he stays only casually or intermittently. The expression 'ordinarily resident in' connotes some habit of life, and is to be contrasted with temporary or occasional residence...The concept of ordinarily resident cannot be stated in definite terms; each case must be determined on its facts and after taking into account all relevant matters...(emphasis added).

On the basis of the facts of the case, Lockhart J concluded that the debtor was ordinarily resident in Australia at the time he committed the act of bankruptcy.<sup>69</sup>

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<sup>68</sup> 37 FCR 194 at 197-198.

<sup>69</sup> The decision of Lockhart J was affirmed by the Full Federal Court on appeal in *Taylor v. Natwest Australia Bank Ltd* (Unreported, Full Federal Court, Wilcox, Burchett and Foster JJ, 16 October 1992).

132. In both *Re Taylor* and *Re Vassis*, reference was made to the House of Lords decision in *Levene v. IRC*<sup>70</sup> (*Levene*). One of the questions raised in *Levene* was whether the appellant was entitled to an exemption from income tax on War Loan interest under the *Income Tax Act 1918 (UK)* as a person not 'ordinarily resident' in the United Kingdom. In finding that the appellant was 'ordinarily resident' in the United Kingdom for the purposes of the Act, Viscount Cave L.C. stated:<sup>71</sup>

The suggestion that in order to determine whether a man ordinarily resides in this country you must count the days which he spends here and those which he spends elsewhere, and that it is only if in any year the former are more numerous than the latter that he can be held to be ordinarily resident here, appears to me to be without substance. The expression 'ordinary residence' is found in the *Income Tax Act of 1806* and occurs again and again in the later Income Tax Acts, where it is contrasted with usual or occasional or temporary residence; **and I think that it connotes residence in a place with some degree of continuity and apart from accidental or temporary absences** (emphasis added).

133. Accordingly, in terms of paragraph 295-95(2)(b) of the ITAA 1997, establishing whether the CM&C of a superannuation fund is 'ordinarily' in Australia at a particular time is a question of fact and degree. It involves determining whether, in the ordinary course of events, the CM&C of the fund is regularly, usually or customarily exercised in Australia. There must be some element of continuity or permanence if the CM&C of the fund is to be regarded as being 'ordinarily' in Australia. If the CM&C of the fund is only casually or intermittently exercised in Australia, then the CM&C of the fund will not 'ordinarily' be in Australia.

134. However, if the CM&C of the fund is being temporarily exercised outside Australia, this will not prevent the CM&C of the fund being 'ordinarily' in Australia at a particular time, provided that the CM&C of the fund is regularly or usually exercised in Australia.

### **Central management and control – temporary absences**

135. Subsection 295-95(4) of the ITAA 1997 states that, to avoid doubt, the CM&C of a superannuation fund is ordinarily in Australia at a time even if that CM&C is temporarily outside Australia for a period of not more than 2 years.

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<sup>70</sup> [1928] All ER Rep 746.

<sup>71</sup> [1928] All ER Rep 746 at 750.

136. Subsection 295-95(4) was inserted into the ITAA 1997 by the *Superannuation Legislation Amendment (Simplification) Act 2007*. Its purpose is to operate as a 'safe harbour' provision for funds (mainly SMSFs) whose trustees are temporarily outside Australia for 2 years or less and who exercise the CM&C of the fund outside Australia during that period. As outlined in the Explanatory Memorandum (EM) to the Superannuation Legislation Amendment (Simplification) Bill 2007 at paragraph 3.8:

To provide certainty to trustees of superannuation funds, especially trustees of self-managed superannuation funds (for whom the old 'two-year temporary absence rule' was mainly directed), a provision is inserted into the definition of 'Australian superannuation fund', which explains that a superannuation fund is considered ordinarily in Australia even if the central management and control is temporarily outside Australia, where it is for a period of less than two years.

137. The effect of subsection 295-95(4) of the ITAA 1997 is to provide one set of circumstances in which the CM&C of the fund will be taken to be ordinarily in Australia at a time for the purposes of paragraph 295-95(2)(b) of the ITAA 1997. However, the provision is not of itself an exhaustive list or set of circumstances which would satisfy the requirements of paragraph 295-95(2)(b). Apart from operating as a 'safe harbour rule', it does not otherwise restrict or limit the meaning of 'ordinarily' in paragraph 295-95(2)(b) so that the CM&C of the fund can only be outside Australia for a period of 2 years or less. As noted in paragraph 133 of this draft Ruling, whether the CM&C of the fund is 'ordinarily' in Australia at a particular time is a question of fact and degree.

138. Absences of more than 2 years will need to be taken into account in the context of determining if, as a matter of fact and degree, the CM&C of the fund is still 'ordinarily' located in Australia. Put another way, if the CM&C of the fund is outside Australia for a period greater than 2 years, the fund will satisfy paragraph 295-95(2)(b) of the ITAA 1997 if it satisfies the 'ordinarily' requirement. An example of such a situation was provided in the EM to the Tax Laws Amendment (Simplified Superannuation) Bill 2006:

#### **Example 3.1**

A married couple are trustees of their self-managed superannuation fund that was established in 2001. In July 2007 the husband accepts a two year employment contract to work for an overseas government, intending to return to Australia after the contract is fulfilled. His wife joins him for the term of his contract. They make no contributions to the fund after leaving Australia.

In these circumstances it is accepted that the central management and control of the self-managed superannuation fund is ordinarily in Australia and the self-managed superannuation fund will be treated as an Australian superannuation fund. If the husband's employment contract was continually extended so that the couple remained overseas for a period considerably in excess of two years, central management and control of the self-managed superannuation fund would not ordinarily be in Australia and the self-managed superannuation fund would not be treated as an Australian superannuation fund.

139. While the CM&C of the fund can be outside Australia for a period greater than 2 years such that subsection 295-95(4) of the ITAA 1997 does not apply, it is clear from the context in which the term ‘ordinarily’ appears that the period of absence of the CM&C from Australia must be ‘temporary’. This view is also supported by the purpose or object underlying paragraph 295-95(2)(b) of the ITAA 1997 as disclosed in the EM to the Tax Laws Amendment (Simplified Superannuation) Bill 2006. In explaining the changes to the operation of the CM&C test from the way it previously operated, the EM states:<sup>72</sup>

The definition of Australian superannuation fund does not use this alternative test [the two-year temporary absence rule]. It deals with **temporary absences of trustees** by requiring that the central management and control of the fund *ordinarily* be in Australia. Satisfying the current two-year temporary absence rule described above...would normally satisfy the *ordinarily* requirement (emphasis added).

140. From this, it follows that if the CM&C of a fund is not temporarily outside Australia, it will not be ordinarily in Australia at a time within the meaning of paragraph 295-95(2)(b) of the ITAA 1997 even if the period of absence is 2 years or less.

#### **When is the central management and control of a fund ‘temporarily’ outside of Australia for the purposes of subsection 295-95(4)**

141. The word ‘temporarily’ in subsection 295-95(4) of the ITAA 1997 is not defined in the ITAA 1997. Therefore, it takes on its ordinary meaning subject to the context in which it appears.

142. The ordinary meaning of ‘temporarily’ is derived from the word ‘temporary’. *The Australian Oxford Dictionary* defines the word ‘temporary’ as lasting or meant to last only for a limited time.

143. While there is no case law which has considered the meaning of ‘temporarily’ in subsection 295-95(4) of the ITAA 1997, a number of cases have considered whether a person’s absence from Australia was ‘temporary’ for the purposes of social security legislation. These cases are relevant in the context of subsection 295-95(4), particularly in cases involving SMSFs, because it is the trustee of the fund (whether individual trustees or trustee directors of a corporate trustee) that normally exercises the CM&C of the fund. The cases are also relevant because they consider the meaning of ‘temporary’ in the context of residence.

144. In *Hafza v. Director-General of Social Security (Hafza)*,<sup>73</sup> Wilcox J considered whether the taxpayer’s absence from Australia was ‘temporary’ for the purposes of subsection 103(1) of the *Social Services Act 1947*. That section provided that child endowment was not payable to a person outside Australia unless that person’s usual place of residence was in Australia or the person’s absence from Australia was temporary only.

<sup>72</sup> At paragraph 3.93

<sup>73</sup> (1985) 60 ALR 674.

145. The taxpayer in *Hafza* travelled from Australia to Lebanon with her husband and children in April 1978 for a visit which was intended to last for three months. The family however did not return to Australia until June 1982. Upon her return, the taxpayer sought payment of child endowment for the period of absence from Australia on the basis that her absence was temporary only and that she did not cease to have her usual place of residence in Australia.

146. Wilcox J stated the following in relation to the meaning of the word 'temporary':<sup>74</sup>

...I think that the adjective 'temporary' was used to denote an absence that was, **both in intention and in fact**, limited to the fulfillment of a passing purpose. The purpose might be of a business or professional nature; it might be for a holiday or for compassionate or family reasons. But, whatever the purpose, it seems to me to be implied in the concept of 'temporary' absence that the absence will be relatively short and that its duration will be either defined in advance or be related to the fulfillment of a specific, passing purpose. If, for example, a businessman travels overseas for a period of three months to engage in sales discussions, intending always to return to his usual home in Australia and in fact returning at the end of that period, there is no difficulty about describing his absence as 'temporary'. If that same person moves himself and his family to an overseas location, intending to remain there indefinitely in pursuit of business orders, his absence would not properly be described as 'temporary'; and I think that this is so even if, after two months for family or personal reasons, he decides to abandon his overseas home and return to Australia. Under such circumstances the absence from Australia would have turned out to be of limited duration, but it would not have been in fulfilment of a passing need.

The intention to return to Australia at the expiration of a particular time -- being, in recognition of the word 'passing', relatively short -- will normally be a feature of an absence which...may properly be described as temporary. There may, however, be exceptions. A person may travel overseas to fulfil a particular purpose which is expected to occupy a relatively short time, the exact extent of which is not known in advance and with the intention thereafter of returning to Australia. An example would be to undertake a particular journey or to attend the bed of a sick relative. I see no problem about describing such an absence as a 'temporary' absence from Australia because it is a short term absence to fulfil a particular purpose.

I think that it follows from my view as to the meaning of the word 'temporary' that the intention of the absentee is of considerable importance; indeed, it will often be decisive. If the businessman on his world sales tour should decide to abandon his plan to return to Australia at the expiration of three months and to remain indefinitely in New York, his absence from Australia will cease to be a temporary absence. It will become an indefinite absence, notwithstanding that it may turn out not to be a permanent absence. Similarly, if an endowee, who has left Australia upon a compassionate visit to a sick relative, should decide indefinitely to stay on at the relative's home after the completion of that purpose, the absence will cease to be temporary notwithstanding an intention eventually to return to Australia. (emphasis added)

<sup>74</sup> (1985) 60 ALR 674 at 682-683.

147. On the basis of the facts of the case, His Honour held that the taxpayer's absence, from the time her husband commenced employment in Lebanon (which was sometime in 1979) was not a temporary absence. Some of the important factors that supported this conclusion included the facts that the taxpayer and her husband had no assets in Australia, did not hold return air tickets, that they resided with the taxpayer's husband's family in Lebanon, that the children attended the local school in Lebanon and that the taxpayer's husband engaged in paid employment involving his travelling to a number of other countries.

148. Wilcox J's view as to the meaning of 'temporary' in *Hafza* is consistent with the views of the Administrative Appeals Tribunal in *Re Houchar and Director-General of Social Security*<sup>75</sup> (*Re Houchar*) in relation to whether an absence was temporary for the purposes of the same provision of the *Social Services Act 1947*. In this case, the taxpayer and her children departed Australia in March 1977 to the village in Lebanon in which the taxpayer was originally born. The taxpayer was joined by her husband in October 1977. It was intended that they would be returning to Australia after about 12 months from the date of the husband leaving Australia. The taxpayer and her family returned to Australia in March 1982.

149. In determining whether the taxpayer's absence from Australia was temporary, the Tribunal stated:<sup>76</sup>

...The question whether a person's absence from Australia is temporary must be resolved by the application of objective criteria. Most important among them must be his intentions from time to time, as ascertained objectively from all the evidence available to the decision-maker...For a person's absence from Australia to be 'temporary only' for the purposes of sections 103 and 104 it must be intended not to last indefinitely. The intention may change during the period of absence...

Probably, if a person intends that the period of his absence should be related to a certain event (for example the completion of a certain task or the exhaustion of his funds), he should be taken to intend not to be absent indefinitely. There is, however, also another element in the concept of temporariness: that is transience. For an absence to be temporary, not only must it be intended not to last indefinitely but the time for which it is intended to last must not be of great length. That involves considerations of questions of degree which must be decided by reference to all the circumstances of the particular case. Once a person's absence has come to an end by his return to Australia, it obviously has not lasted indefinitely. It may not have lasted as long as another person's absence which has been accepted as temporary. However, the question whether it was 'temporary only' has to be decided not by viewing it in retrospect but by reference to the person's intention during his absence, or rather to his intention at different stages of the absence.

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<sup>75</sup> (1984) 5 ALN No 308.

<sup>76</sup> (1984) 5 ALN No 308 at N452.

150. On the basis of the facts of the case, the Tribunal held that the taxpayer was not eligible for child endowment for any part of the period she was absent from Australia as she ceased to have her usual place of residence in Australia and her absence from Australia was not ‘temporary only’.

151. Taking into account the context in which the term ‘temporarily’ appears in subsection 295-95(2) of the ITAA 1997 and the purpose underlying subsection 295-95(4) of the ITAA 1997 as discussed at paragraph 136 of this draft Ruling, the views expressed in *Hafza* and *Re Houchar* as to whether an absence is temporary are applicable in determining whether a fund’s CM&C is ‘temporarily’ outside Australia. This is because, as noted, it is the trustee of the fund which normally exercises the CM&C of the fund.

152. Accordingly, the CM&C of a fund will be ‘temporarily’ outside Australia if the person or persons who exercise the CM&C of the fund are outside Australia for a relatively short period of time. The duration of the absence must either be defined in advance or related (both in intention and in fact) to the fulfilment of a specific, passing purpose. Whether a period of absence is considered to be relatively short involves considerations of questions of degree which must be decided by reference to the circumstances of each particular case. The intention to return to Australia at the expiration of a particular time will normally be a feature of a temporary absence.

153. Whether an absence is temporary must be established on a ‘real time’ basis. It cannot be established in retrospect.

154. Ultimately, whether a fund’s CM&C is temporarily outside Australia in a particular situation is a question of fact to be determined in light of all the circumstances of each case.

155. Notwithstanding this, the following factors have been considered relevant by the Courts and the Administrative Appeals Tribunal when determining whether an absence is temporary for the purposes of social security legislation. For the reasons stated above, these factors are also relevant in considering whether the CM&C of a fund is temporarily outside Australia:

- (a) the intended and actual length of stay in the overseas country of the person or persons who exercise the CM&C of the fund;
- (b) any intention of the person or persons exercising the CM&C of the fund to return to Australia at some definite point in time or to travel to another country;
- (c) whether the person or persons exercising the CM&C of the fund have established a home (in the sense of a dwelling place; a house or other shelter that is a fixed residence) outside Australia;
- (d) whether any residence or place of abode exists in Australia or has been abandoned because of the overseas absence; and

- (e) the durability of association that the person or persons exercising CM&C have with a particular place in Australia, for example maintaining bank accounts in Australia, place of education of children and so on.

156. While the weight to be given to each factor will vary with the individual circumstances of each case, it is clear from *Hafza* and *Re Houchar* that the intention of the person or persons exercising the CM&C of the fund, as ascertained objectively from the facts of the case, will be of considerable importance and will often be decisive in determining whether the CM&C of the fund is temporarily outside Australia. The fact that the person or persons exercising the CM&C of the fund know that they will be returning to Australia at a definite point in time does not, of itself, mean that the CM&C is temporarily outside Australia.

157. These factors are equally relevant in determining whether the CM&C of the fund is 'ordinarily' in Australia for the purposes of paragraph 295-95(2)(b) of the ITAA 1997. As mentioned in paragraph 140 of this draft Ruling, if the CM&C of a fund is outside of Australia, but not on a temporary basis, then the conditions of paragraph 295-95(2)(b) will not be satisfied.

***Can the CM&C of a fund be 'ordinarily' in Australia and another country at the same time?***

158. In the context of superannuation funds, particularly SMSFs with 2 or 4 trustees, there may be situations where there is an equal number of trustees both in Australia and overseas who equally participate in the CM&C of the fund.<sup>77</sup> The question thus arises as to whether the CM&C of the fund is 'ordinarily' in Australia in these situations. There is no case law which has dealt with such a question.

159. In the context of companies, the courts have acknowledged the possibility that the company's CM&C could be divided between two or more places.<sup>78</sup> This is where control of the company's general affairs (that is, 'the superior or directing authority by means of which the affairs of the company are controlled') is located in several places, and the control of the company's general affairs is divided between the places in such a way that on the facts it is not 'centred' in one place in particular.

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<sup>77</sup> When the definition of an SMSF was inserted into the SISA, it was stated that the purpose or object of requiring all members of SMSFs to be trustees was to ensure that each member is fully involved and has the opportunity to participate equally in the decision making processes of the fund – see the Explanatory Memorandum to the Bill which became the *Superannuation Legislation Amendment Act (No.3) 1999*. Therefore, it is possible that situations will occur where there are an equal number of trustees both in and outside Australia who equally participate in the CM&C of a superannuation fund. However, see comments in paragraph 162.

<sup>78</sup> *The Swedish Central Railway Company Ltd v. Thompson* (1925) 9 TC 342; *Egyptian Delta Land and Investments Company Ltd v. Todd* [1929] AC 1; *Koitaki Parra Rubber Estates Ltd v. FCT* (1940) 64 CLR 15 at 19; (1940) 6 ATD 42 at 45, per Dixon J; (1941) 64 CLR 241 (Full High Court).

160. The courts have also expressed the view that a person can be 'ordinarily resident' in more than one place or country at the same time. For example, in *Re Taylor*, Lockhart J made the following observations:<sup>79</sup>

At first blush it may seem strange to say that a person can be ordinarily resident in more than one country at the same time; but on closer analysis it is not. Plainly you cannot be physically present in more than one place at the same time. But the lifestyles of people vary greatly. Some people in the ordinary pursuit of their lives regularly or customarily live in more than one place, each of which has an element of permanence about it and is not merely a place of casual or intermittent resort.

...It may, depending on the circumstances, be permissible to say that at a particular time they are ordinarily resident in each of the places...

161. In light of the case law authority for both the proposition that the CM&C of a company can be divided between two or more places and the proposition that a person can be ordinarily resident in more than one place at the same time, we consider that, by analogy, the CM&C of a superannuation fund can 'ordinarily' be in more than one place at the same time. Whether this is the case is a question of fact and degree and will depend on the circumstances of each particular case.

162. Accordingly, in those situations where there are an equal number of trustees both in Australia and overseas who *equally* participate in the CM&C of the fund, the CM&C of the fund will 'ordinarily' be in Australia within the meaning of paragraph 295-95(2)(b) of the ITAA 1997, even though the CM&C of the fund is also ordinarily being exercised overseas.

163. However, it is considered that situations where there is in fact an *equal* split of the CM&C function would be rare. The mere fact that an equal number of trustees are located both in Australia and overseas will not of itself lead to a conclusion that there is equal division of the CM&C function between these two locations. Regard must be had to the types of activities undertaken by each of the trustees to determine if those activities in fact did form part of the high level and strategic decision making functions of the fund.

### ***Relevance of residency status of trustee in their personal capacity***

164. As stated in paragraph 124 of this draft Ruling the residency status of the trustee or trustees of a superannuation fund is not of itself determinative of where the CM&C of the fund is located. In the context of an SMSF with individual trustees, it is noted that there may be a tension between the desire of the trustee to be a non-resident for their own individual tax purpose but to maintain Australian residency status for their SMSF.

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<sup>79</sup> (1992) 37 FCR 194 at 198.

**The ‘active member’ test**

165. The third test that a fund is required to satisfy to be an Australian superannuation fund is the ‘active member’ test in paragraph 295-95(2)(c) of the ITAA 1997. The ‘active member’ test is satisfied if, at the relevant time, either the fund has no member covered by subsection 295-95(3) of the ITAA 1997 (an **active member**) or at least 50% of:

- (i) the total market value of the fund’s assets attributable to superannuation interests held by active members; or
- (ii) the sum of the amounts that would be payable to or in respect of active members if they voluntarily ceased to be members;

is attributable to superannuation interests held by active members who are Australian residents.

166. The terms of paragraph 295-95(2)(c) of the ITAA 1997 therefore contemplate two situations:

- the first situation is that the fund has no active members at a particular time. In this case, paragraph 295-95(2)(c) is satisfied at that time.
- the second situation is where the superannuation fund does have an active member (as defined in subsection 295-95(3) of the ITAA 1997 and further discussed in paragraphs 171 to 179 of this draft Ruling). In such a situation, the conditions in subparagraphs 295-95(2)(c)(i) and (ii) of the ITAA 1997 must be considered to determine whether the fund satisfies the active member test.

167. A fund with an active member can apply either method in subparagraphs 295-95(2)(c)(i) and (ii) of the ITAA 1997 to determine whether it satisfies the active member test.

**Superannuation interests**

168. ‘Superannuation interest’ is defined, relevantly, as ‘an interest in a superannuation fund’.<sup>80</sup> It is beyond the scope of this Ruling to discuss the meaning of ‘superannuation interests’. The Commissioner’s view as to what constitutes a ‘superannuation interest’ in relation to the different kinds of superannuation fund is set out in a fact sheet titled ‘How many superannuation interests does a member of a superannuation fund have in their fund?’<sup>81</sup>

<sup>80</sup> See the definition of ‘superannuation interest’ in subsection 995-1(1) of the ITAA 1997.

<sup>81</sup> This fact sheet is available at [www.ato.gov.au/super](http://www.ato.gov.au/super).

***Australian resident***

169. 'Australian resident' in paragraph 295-95(2)(c) of the ITAA 1997 means a person who is a resident of Australia for the purposes of the ITAA 1936.<sup>82</sup> The term 'resident of Australia' is defined in subsection 6(1) of the ITAA 1936 in relation to both individuals and companies. It is outside the scope of this ruling to discuss the meaning of resident of Australia so far as an individual is concerned. A number of other rulings issued by the Tax Office discuss the issue of residency in relation to individuals.<sup>83</sup> For present purposes, it is sufficient to note that the definition, in effect, provides four tests to ascertain whether an individual is a resident of Australia, satisfaction of any one being sufficient to render an individual an Australian resident:

- residence according to ordinary concepts;
- the domicile and permanent place of abode test;
- the 183 day test; or
- the Commonwealth superannuation fund test.

170. A 'foreign resident' is a person who is not a resident of Australia for the purposes of the ITAA 1936.<sup>84</sup>

**Definition of 'active member'**

171. Subsection 295-95(3) of the ITAA 1997 sets out the definition of 'active member' for the purposes of the 'active member' test in paragraph 295-95(2)(c) of the ITAA 1997. Subsection 295-95(3) states:

A member is covered by this subsection at a time if the member is:

- (a) a contributor to the fund at that time; or
- (b) an individual on whose behalf contributions have been made, other than an individual:
  - (i) who is a foreign resident; and
  - (ii) who is not a contributor at that time; and
  - (iii) for whom contributions made to the fund on the individual's behalf after the individual became a foreign resident are only payments in respect of a time when the individual was an Australian resident.

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<sup>82</sup> Subsection 995-1(1) of the ITAA 1997.

<sup>83</sup> Taxation Rulings IT 2615 Income tax: Medicare Levy – test for Australian residency – payable by Australians living overseas and by visitors to Australia; IT 2650 Income tax: Residency – permanent place of abode outside Australia; IT 2681 Income tax: residency status of business migrants and Taxation Ruling TR 98/17 Income tax: residency status of individuals entering Australia.

<sup>84</sup> Subsection 995-1(1) of the ITAA 1997.

***Contributor to the fund at that time***

172. The term ‘contributor’ in subsection 295-95(3) of the ITAA 1997 is not defined. Therefore, it is to be given its ordinary meaning subject to the context in which it appears.

173. In the case of a superannuation fund, a ‘contributor’ is an individual who makes a contribution for the purpose of providing for future retirement or superannuation benefits (see paragraphs 180 to 184 of this draft Ruling for a discussion on the meaning of ‘contribution’). It appears from the context of the provisions that the focus of the test is on the *status* of the member as a contributor at a particular point in time, and not actually on the specific act of contributing.

174. Whether a member of a superannuation fund is a contributor to the fund at a particular time is to be objectively determined with reference to the individual circumstances of each member, including their intentions. For example, the member may intend to and actually make personal contributions on a regular or periodic basis.<sup>85</sup> In such a situation, the member would be a contributor for the purposes of subsection 295-95(3) of the ITAA 1997, not only at the actual point in time the contribution is made to the fund but also for the period of time between the making of the contributions.

175. On the other hand, if it is established on the facts of the case that a member, that had been making contributions to the fund over a period of time no longer has the intention to make any further contributions to the fund and in fact ceases to make any further contributions, then they would cease to be a ‘contributor’ from the time they formed the intention to cease contributing. If that member later intends to and actually makes any further contributions, then their status as a ‘contributor’ is reinstated.

176. If the member is a contributor to the fund at a particular time, they will be an active member within the meaning of subsection 295-95(3) of the ITAA 1997, irrespective of whether the member is an Australian resident or foreign resident.

***An individual on whose behalf contributions have been made***

177. Subject to the exception relating to foreign residents (which is discussed in paragraph 178 of this draft Ruling), an individual on whose behalf contributions have been made will be an active member within the meaning of subsection 295-95(3) of the ITAA 1997.

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<sup>85</sup> In some superannuation funds, mostly public sector superannuation schemes, the members of those schemes are under an obligation to make personal contributions on a periodic basis, for example, fortnightly. In other types of funds, such as an SMSF, the members may make contributions over an extended period of time although not on a regular or periodic basis such as that described in respect of public sector superannuation schemes.

178. If the member is a foreign resident and a contribution is made on their behalf after they became a foreign resident, they will only be an active member at the relevant time if the contribution is made in respect of the time when the individual was a foreign resident. If the contribution to the fund relates to a period of time when the individual was an Australian resident, they will not be an active member at the relevant time.

179. A member of a fund will also be an active member at a particular time if the member's employer is on a 'contributions holiday'. In broad terms, a 'contributions holiday' exists where a defined benefit superannuation scheme is in surplus (that is, broadly, that the assets of the scheme exceeds its liabilities) and the employer is not required to make contributions until that surplus is reduced.

### ***Meaning of 'contribution'***

180. The term 'contributions' in subsection 295-95(3) of the ITAA 1997 is not defined. Therefore, it is to be given its ordinary meaning subject to the context in which it appears.

181. The term 'contribution' is defined by *The Australian Oxford Dictionary* as: '1. the act of contributing; 2. something contributed, especially money.'

182. For the purposes of subsection 295-95(3) of the ITAA 1997, the context in which the meaning of the word 'contribution' is relevant is Part 3-30 of the ITAA 1997.

183. Part 3-30, which was inserted into the ITAA 1997 by the *Tax Laws Amendment (Simplified Superannuation) Act 2007*, provides the legislative scheme for the taxation of superannuation in all phases of the superannuation cycle, that is the contributions phase, investments phase and the benefits phase. There are a number of provisions within Part 3-30 which contain a reference to contribution. Relevantly, they include:

- section 290-5 of the ITAA 1997 – which states that the rules in Division 290 of the ITAA 1997 for deductions and tax offsets for superannuation contributions do not apply to the contributions mentioned in section 290-5;
- sections 292-25 and 292-90 of the ITAA 1997 – which sets out an individual's 'concessional' and 'non-concessional' contributions for a financial year;
- section 292-465 of the ITAA 1997 – which provides for the Commissioner's discretion to disregard or allocate to another financial year, an individual's concessional and non-concessional contributions;
- section 295-155 of the ITAA 1997 – which explains the types of contributions that are assessable to a superannuation entity; and

- section 295-610 of the ITAA 1997 – which explains the amounts that are ‘no-TFN contributions income’.

184. When these provisions are analysed, it is clear that the term ‘contribution’ has a very broad meaning. Accordingly, when interpreted in the context of the aforementioned provisions in Part 3-30 of the ITAA 1997, ‘contributions’ in subsection 295-95(3) of the ITAA 1997 would include such amounts as:

- direct cash payments made by an employer or an individual to the fund;
- a transfer of property (or other asset) to the fund ‘in-specie’ by an employer or individual;<sup>86</sup>
- spouse contributions;
- Government co-contributions;
- superannuation guarantee shortfall amounts – these amounts form part of the superannuation guarantee charge collected by the Commissioner and paid to a superannuation fund under the *Superannuation Guarantee (Administration) Act 1992* when an employer fails to make sufficient superannuation contributions to a complying superannuation fund or Retirement Savings Account;
- transfers from the Superannuation Holdings Account Special Account – this occurs when an individual’s account balance in the SHASA is transferred to a superannuation fund;<sup>87</sup>
- a roll-over superannuation benefit – in relation to superannuation funds, this is a superannuation lump benefit paid from one complying fund to another complying fund at the direction of the member;<sup>88</sup>
- a directed termination payment – these are transitional ‘employment termination payments’ that an employee directs the employer to pay to a superannuation fund on behalf of the employee;<sup>89</sup> and
- a superannuation lump sum that is paid from a foreign superannuation fund or an amount transferred to the superannuation fund from a foreign superannuation scheme.

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<sup>86</sup> Section 285-5 of the ITAA 1997 states that a contribution can be or include a transfer of property.

<sup>87</sup> Under section 61 or 61A of the *Small Superannuation Accounts Act 1995*.

<sup>88</sup> The definition of ‘roll-over superannuation benefit’ is contained in section 306-10 of the ITAA 1997.

<sup>89</sup> Section 82-10F of the *Income Tax (Transitional Provisions) Act 1997*. Since transitional termination payments cannot be received on or after 1 July 2012, such payments cannot be directed to a superannuation fund from that date.

**What are the consequences of a fund ceasing to be a complying fund because it fails to satisfy the residency test?**

185. A fund that ceases to be a complying superannuation fund in a particular year of income because it fails to satisfy the definition of Australian superannuation fund faces a number of taxation consequences. In the income year that it becomes non-complying, it must include in its assessable income an amount equal to the total of the market values of the fund's assets (as calculated just before the start of the income year), less any crystallised undeducted contributions made between 30 June 1983 and 30 June 2007 and any non-concessional contributions made from 1 July 2007.<sup>90</sup> This amount is taxed at the highest marginal tax rate.

186. Furthermore, the fund is not eligible for the tax concessions available to a complying superannuation fund. For example, for every year that the fund remains non-complying, its income is taxed at the highest marginal tax rate.

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<sup>90</sup> Item 2 of the table in section 295-320 of the ITAA 1997 and section 295-325 of the ITAA 1997.

## Appendix 2 – Your comments

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187. We invite you to comment on this draft Taxation Ruling. Please forward your comments to the contact officer by the due date. (Note: the Tax Office prepares a compendium of comments for the consideration of the relevant Rulings Panel or relevant Tax officers. The Tax Office may use a version (names and identifying information removed) of the compendium in providing responses to persons providing comments. Please advise if you do not want your comments included in the latter version of the compendium.)

<b>Due date:</b>	<b>18 July 2008</b>
<b>Contact officer:</b>	<b>Peter Bou-Samra</b>
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## **Appendix 3 – Detailed contents list**

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Not previously issued as a draft

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TR 98/17

### *Subject references:*

- complying superannuation funds
- self managed superannuation funds
- superannuation fund residency

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NO:	2007/19018
ISSN:	1039-0731
ATOlaw topic:	Income Tax ~~ Assessable income ~~ superannuation entities Superannuation Entities ~~ Complying superannuation funds