

In touch with the law

No. 1, 2004

The law is constantly changing and this newsletter describes developments which may be relevant to you. If you are in any doubt about these or any other aspects of the law, please make an appointment to see your solicitor.

DIRECTORS

Increasing responsibility and liability

Australian courts may be placing significantly higher levels of responsibility on company directors, and the trend is not limited to additional duties of care and diligence.

The concept of the limited liability company evolved to provide investors who wanted to engage in risky enterprises with limited liability protection, so that their risk was limited to the amount they invested in the company. Limited liability also protected the directors. Directors had duties and responsibilities they had to observe, but as long as they acted within the scope of those duties, they were largely free from risk.

In one recent case, the Australian Securities and Investments Commission (ASIC) brought proceedings against four of a company's six directors. The non-executive chairman applied to have the proceedings against him dismissed, apparently thinking he

should have been treated in the same manner as the two other non-executive directors – against whom no action was brought.

ASIC argued that the chairman was better qualified and more experienced than the other directors to supervise the compa-

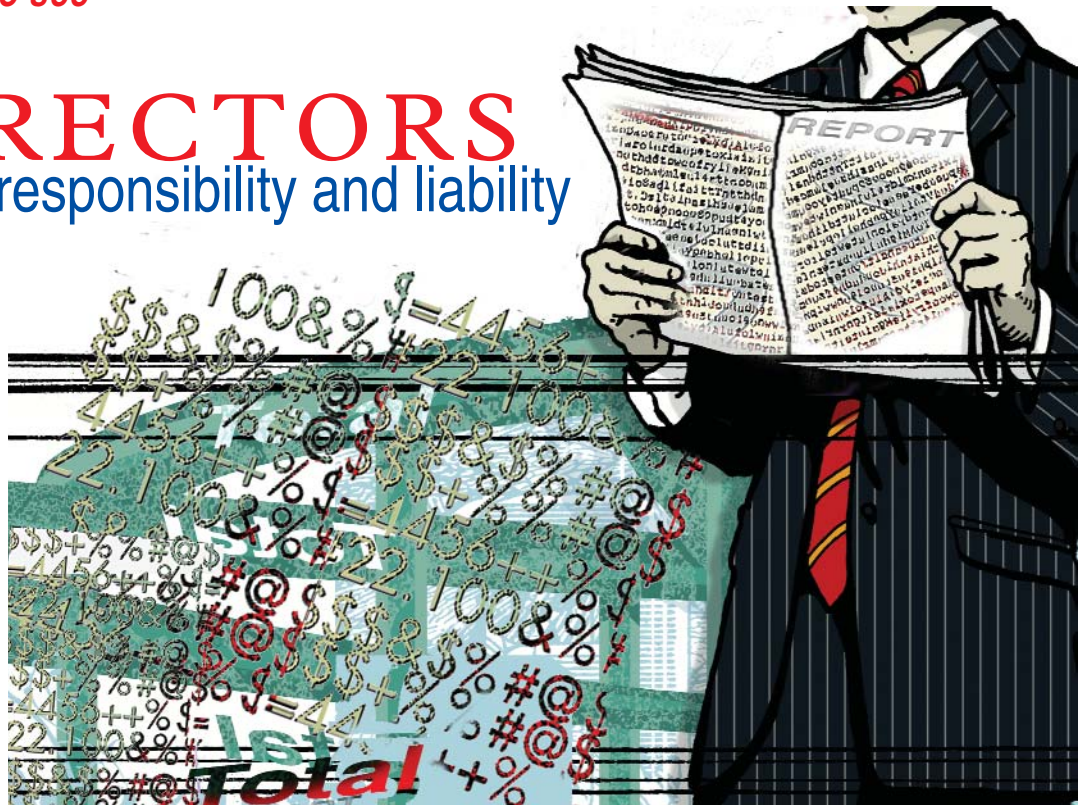
ny's financial management. The court agreed, finding the responsibilities of a director include arrangements flowing from any special role they may have undertaken due to the skills and experience they held when appointed.

In another case, the court

found the directors of a company had permitted it to trade while insolvent, and that increasing onus was being placed on non-executive directors in such situations.

The court accepted ASIC's contention that directors should regularly obtain from management a list of debtors and creditors by age and amount, regular profit and loss and cash flow statements, and reports on negotiations with creditors whose debts were outside trading terms, to ensure they were in a position to be aware of any reasonable grounds for suspecting insolvency.

Directors of the company had failed to exercise their responsibilities and were found liable to compensate creditors for an amount of over \$1.4 million. □



BREASTFEEDING

New legislation makes discriminating unlawful

The Sex Discrimination Act has been amended to make it explicit that discrimination against a woman because she is breastfeeding is unlawful.

The new legislation also makes it clear that it is unlawful to

ask women for information about a pregnancy or potential pregnancy where it is unlawful to discriminate against them on these grounds. For example, because it is unlawful to refuse to employ a woman because she is or may become pregnant, it is unlawful to

ask her about this in a job interview. Requests for such information may only be made for legitimate reasons, such as occupational health and safety. This also covers areas such as purchasing goods or services, applying for a loan or renting accommodation. □

POWERS OF ATTORNEY

New safeguards against financial abuse

We all hope those close to us will do the right thing if we become dependent on them as we age – particularly if they become responsible for making financial decisions on our behalf through a power of attorney. New laws have now increased the safeguards that govern such arrangements.

A power of attorney is a legal document, by which you authorise someone (known as your attorney) to make financial decisions and sign papers on your behalf.

If you are travelling overseas for a lengthy period you may want to give someone a power of attorney to manage things while you are away. You may also wish to grant one if your health has deteriorated.

If you want to arrange for someone to look after your affairs in the event that you lose capacity through unsoundness of mind (as may occur with senile dementia or Alzheimer's disease), the power of attorney must be in a specific form that complies with the law, and must be witnessed by someone – such as your solicitor – who has explained the effect of it to you. Such a document is called an 'enduring power of attorney'.

Can I just fill in a form?

There is a special printed form for a power of attorney available from some newsagents, but in February 2004 a new form was issued, and only the new form should now be used. Enduring powers of attorney made on the old forms after February 2004 may not be legally valid.

Simple powers of attorney may be drafted without qualified legal advice, but where your future care and financial security is involved, your solicitor is best placed to ensure that the detail of the document is properly tailored to meet your particular requirements and wishes, and that it takes ac-

count of the possibility of changing circumstances. Your solicitor can also make certain that all the safeguards are in place, and that you fully understand the implications of signing the power of attorney.

Whom should I appoint as my attorney?

This is a very important decision which you should consider carefully. Usually a close friend or a relative is appointed: it must be someone you can trust. Sometimes your solicitor or accountant may be willing to act. Trustee companies are also willing to carry out such duties. You may appoint more than one attorney.

Do I have to register the power of attorney?

A power of attorney must be registered if it will be used for dealing with the sale or leasing of land in New South Wales. Registration attracts a lodgment fee with the government agency involved.

Your solicitor can look after the registration of an enduring power of attorney to guarantee that it can take care of any dealings over your home or other property that may need to be made on your behalf.

New safeguards

New laws on powers of attorney that came into effect in February 2004 make clearer the extent of the attorney's freedom to use a person's funds, while at the same time recognising that there needs to be limits on what an attorney can do. The new laws increase the protections against financial abuse.

A person must now expressly authorise an attorney to use their funds to give benefits to other people (such as dependents) for their reasonable living and medical expenses.

The person giving the power of attorney must also expressly authorise an attorney to use their funds to give gifts, such as seasonal or occasional gifts to close

friends or relatives. Donations are covered by the same requirement, and they must be limited to ones similar to those the person made when they were capable, or ones they could reasonably be expected to make.

If the power of attorney is silent about giving gifts, donations and benefits, then none can be given. The new reforms in this area give an individual the opportunity to consider what they really want to do, and then to empower the attorney accordingly.

Unlike a will, a new power of attorney doesn't cancel out an earlier one, so you should formally revoke any previous power of attorney in writing be-

fore proceeding to draw up a new one.

When does the power of attorney start?

The new power of attorney form gives an options list for you to choose when the power comes into effect.

The power can operate immediately, when the attorney accepts the appointment, at a specified time, "when my attorney considers that I need assistance managing my affairs", or at another time. Again, your solicitor is best placed to help you make the decision about when your attorney should take on their responsibilities. □



NEW BUSINESSES

It pays to choose the right structure

Choosing the right structure for your new business can produce long-term benefits that outweigh any short-term disadvantage.

The form of organisation of a business determines many things, including how tax is paid and how profits are disbursed, and it should be geared to help you achieve maximum benefits.

Consider the case of two businessmen who started a business in 1997 and have since decided to sell. The price is \$5 million for goodwill, plus stock and plant at book value. When it was set up, it was decided to operate the business as a company because of limited liability and the lower tax rate than applies to individuals.

You may think that as the goodwill has no cost base, the company will only pay 30 per cent capital gains tax on the capital gain of the goodwill at sale.

But that is only part of the story. Not only will the company pay 30 per cent tax on the goodwill, but the two partners will also pay a further 18.5 per cent when the company is liquidated. That means that in total the team will pay 48.5 per cent of their \$5 million capital gain in tax – a cool \$2,425,000.

Had they run the business as a partnership or discretionary trust, so that the capital gain could have been distributed to individuals, they would have been entitled to a general discount of

50 per cent. That is, instead of paying tax on the full capital gain, they would have paid it on half. This would have given them a

tax bill on sale of \$1,212,500.

Your solicitor can advise you of the most tax-effective structure for your business. □



PROPERTY

Implications in joint ownership

There are two types of joint ownership of property.

One type is joint tenancy which is how most couples buy property. In a joint tenancy all parties jointly own the whole property. That means that on the death of one party the survivor automatically become entitled to the property.

By purchasing the property in this way, buyers effectively make wills leaving the other their share in the property. This has the advantage that if a joint tenant dies without a will, he or she is not intestate as regards that share in the property.

The other type is tenancy in common. Each of the tenants in

common owns a separate fraction of the property and may sell without the other's consent and can leave his or her share in the property by will to anyone.

Ownership can be in equal shares or in any other proportions the parties decide. Tenancy in common does not have the characteristic of sur-

vivorship. If a share is inherited by someone under 18 the property cannot be disposed of without a Court order until that child turns 18. That is one risk involved in a purchase as tenants in common. It is often appropriate for people not closely related to purchase as tenants in common. □

WIDENING TAX BASE

New costs for small business with property interests

New legislation significantly widens the land-rich duty base in what has been seen by some as a revenue-raising exercise by the NSW Government.

The new provisions will operate in a broad range of commercial transactions, resulting in an increasing need for taxpayers, especially small businesses, to obtain valuations of their assets more frequently, and to investigate closely the assets of entities in which they have interests, even minority ones.

Broadly, land-rich duty is a type of stamp duty that applies to the acquisition of interests in land-rich private companies and private unit trust schemes.

Two changes have been made to the test for determining whether a landholder is "land-rich". In a win for taxpayers, the unencumbered value of NSW



landholdings has been increased from its current \$1 million to \$2 million.

However, in a win for the State revenue, the threshold beyond which one becomes liable

has been reduced from 80 to 60 per cent (that is, the total land holdings as a proportion of the total value of the assets).

The reduction to 60 per cent is likely to mean that many small businesses are now caught by the provisions. Particularly if they are underperforming, many small businesses are likely to have as their most valuable asset the land or buildings on which their business is carried on.

In another significant win for the State revenue, the Act has replaced the former liability trigger for land-rich duty from acquisition of a *majority interest* in a landholder (that is, greater than 50 per cent), to a *significant interest* (which in the case of a private company is 50 per cent or more).

Contact your solicitor for further information on these and other changes brought about by the new legislation. □

FRANCHISES

Franchisor's failed attempt to avoid obligations

Franchisees have a wide range of rights and are protected by a mandatory code which business promoters cannot avoid simply by attempting to exclude it from a contract.

Under the Franchising Code, a franchisor must disclose specific information to potential franchisees, including the basis for income projections, whether franchise territories are exclusive, other existing franchisees, and the background business experience of the franchisor.

There is also a requirement for a cooling-off period during which franchisees can withdraw from an agreement.

In a recent case that came before the courts a company had

advertised throughout Australia to sign up consultants, and entered licence agreements to promote and sell its small-business program. More than 30 licence deeds were sold, mainly for between \$11,000 and \$24,000.

The company included a clause in the deed that attempted to exclude it from obligations under the Franchising Code, and did not provide a cooling-off period.

The Australian Competition and Consumer Commission argued that the arrangement was in fact a franchising scheme, and that the company was trying to deprive franchisees of their rights.

The directors of the company were ordered to inform the franchisees that their arrangement

was in fact covered by the Franchising Code. They were also ordered to provide franchisees with a cooling-off period

of seven days, and to refund the franchising fee if the franchisee elected to terminate the agreement within the period. □

WILLS

Can I make a will myself?

There is no requirement that a solicitor draft a will, and printed will forms are available from many stationers. However, it is not in your best interests to draft your will yourself.

There have been many cases where homemade wills were either unclear, not properly drawn up or caused an unwanted tax liability.

In general, solicitors do not charge a large fee for making a will, and since it is one of the most important legal documents you will ever make, it can be false economy to try to do it without skilled professional advice.

In addition, your will needs to be kept in a safe place. Solicitors hold wills on behalf of people, often at no charge. You should keep a copy of your will and note on it where the original is kept. □