Client Newsletter

No. 3, 2008

In touch with the law

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.

FORFEITED DEPOSITS

Will you pay GST if the sale falls through?

Following a recent court decision, GST-registered vendors who sell property as part of their business are now liable to pay GST on forfeited deposits. The Tax Office also considers that GST applies, regardless of whether the underlying supply would have been GST-free had the contract been completed.

GST only applies to a forfeited deposit if the vendor is GST-registered (or ought to be) and entered the contract as part of its business – a developer, for instance. It doesn't apply to deposits forfeited under a contract to purchase a private home. Also, as most residential property investors are not GST-registered, GST wouldn't generally apply to forfeited deposits paid under a contract in respect of a residential investment property. However, there are exceptions. For example, GST may apply if the vendor is a GST-registered, self-managed super fund selling a residential property.

Vendors who ceased paying GST on forfeited deposits following an earlier court ruling, may now have to pay, subject to the time limits that apply to the recovery of unpaid GST.

In most instances, where GST applies there is little a vendor can do. The best option is to ensure that the contract includes a GST clause that allows the seller to recover an additional amount on account of GST if it makes a taxable supply to the purchaser. However, recovering it in practice may be difficult. Another difficulty is that a contract may not allow for recovery if the purchase price is expressed as GST-inclusive.

Another option may be to increase the deposit to 11 per cent. However, this is risky because deposits that exceed 10 per cent may be viewed as either a penalty or an instalment payment, with potentially adverse consequences. ❑

TRUSTS

The tax sting in death benefits

Many people now have self-managed superannuation funds constituted as trusts and are concerned to ensure funds are passed on without any loss of value.

In one case, a couple nominated their children or each other to receive death benefits so they could access the benefits of a testamentary trust, under which the trustee would have a discretionary power to distribute between the various beneficiaries. A testamentary trust was attractive because it can have great tax benefits, as well as providing good asset protection.

However, if the estate is nominated to receive the death benefit, it is assessed at 15 per cent tax on the taxable component of the death benefit.

No tax would be payable at the death of the first partner if the couple chose to nominate each other to receive the death benefit. At the second death, assuming that by then the children are no longer dependants, it would be logical for the death benefit to go to the estate and into a testamentary trust.

Contact your solicitor for advice on self-managed superannuation, trusts and the terms of your will. ❑

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REPUTATION

Can a company sue for defamation?

The laws on defamation have changed but small companies and charities still have some recourse if they consider matter published about them is defamatory.

New laws introduced across Australia in early 2006 limit action by corporations on the publication of defamatory matter unless they are excluded corporations at the time of publication. Excluded corporations are non-public bodies which either employ less than ten people and are unrelated to another corporation, or were not formed to obtain financial gain for their members or corporations.

The primary means by which defamation law protects and vindicates reputation is by the award of compensatory damages commensurate to the harm suffered. A corporate plaintiff cannot claim for injury to feelings or standing in the community and should, if possible, tender evidence to prove actual financial loss. However, while the reality is that harm to a corporation's reputation will ordinarily cause harm to business, the causal link may be difficult to prove.

The courts can declare a matter is defamatory but there will be little incentive to seek this as an alternative to damages as there is no power to require publication of the order.

And while the primary objective of a corporation may be to prevent or limit publication of the material causing concern, this will only be granted in very clear cases because of its interference with the right to freedom of speech.

The new laws do not apply to situations prior to 2006. ❑

PREDATORY WORKPLACES

Damage control when key staff leave

How can you retain key staff or delay competitors from poaching them?

A properly crafted contract of employment is the first ingredient of any effective employment relationship, and it should include a clear understanding of what each party is owed if the relationship sours.

In drafting any restraint-of-trade clause, it is crucial that employers be reasonable in the restraints they seek.

In a recent case, a company tried to restrain a key employee who had begun looking for alternative employment and had signed a letter of intent to be a non-equity partner in a competing consulting company.

His employer sought to stop him from performing information management services for any of its own clients for 12 months from the date of termination.

The general rule is that such restraints are against public policy and void. To be enforced, the company would have had to demonstrate that the restraints were no more than were necessary for the protection of its legitimate interests. A judge described them as "extraordinarily broad" and found them to be unreasonable.

The company went on to make the employee go on 'garden leave', that is, to stay away from work for the notice period while continuing to be paid. The thinking behind garden leave seems to be that it may be better to pay an employee's full salary than see them work for a competitor.

However, in this case the employee said he intended to begin work for the other company the following month.

The court found that even on garden leave, the employee would be 'working', in the sense of doing as directed by his employer. His remuneration was not affected as his performance bonuses were not commission based. And he was not considered to be in the sort of position where his future employment would be undermined by an enforced break from the marketplace.

The employer was not found to be required to provide him with work, and putting him on garden leave would not repudiate the contract. However, the court did not restrain the employee from working for the firm's competitors during the notice period so the directive may have had little effect. ❑

NEIGHBOURS

What can I do about nuisance trees?

Cutting back the branches and roots of your neighbour's tree that protrude on to your property would usually require the consent of your local council.

Councils' preservation orders generally cover trees above a certain size and may include large bushes, but regulations vary widely between different councils. You should check with your council about their specific regulations before proceeding with any cutting back.

If a neighbour's tree causes damage on your property, for instance by its roots lifting a driveway or a dead branch falling and knocking tiles off your roof, you may be able to sue for compensation. A court can make an order to remedy, restrain or prevent damage caused by a tree. ❑

CAPACITY

Assessing decision-making ability

Correctly identifying whether someone is capable of making their own decisions is fundamental to the protection of their human rights.

Anyone who needs to assess decision-making capacity, such as friends, family or social workers, must consider the particular elements of the legal test specific to the decision.

For instance, in assessing whether someone has the capacity to make their own financial decisions, you will need to consider two questions.

First, is the person capable of managing their own property and affairs? They don't have to be able to manage them in the best possible way, they just have to be able to manage them. Issues to consider include whether the person is able to deal in a fairly capable way with the ordinary regular dealings in life so as to provide for their own welfare and anyone dependent on them, whether they understand their assets and outgoing expenses, and whether they can manage their money to provide food, clothing, medicine and other necessities.

Second, if they can't manage their affairs, is there a risk that they may be disadvantaged or harmed, or their money or property wasted or lost?

In addressing capacity it is important to avoid discrimination. Don't assume a person lacks capacity based on age, appearance, disability, behaviour or any other condition or characteristic.

Before concluding lack of capacity, ensure that everything possible has been done to support the person to make a decision.

If all assisted decision-making efforts fail, then a determination that the person lacks capacity with respect to the decision is appropriate, and information can be sought from a substitute decision-maker. This is a last resort.

Substitute decision-making need not always be formal. It can be on an informal basis where the person has family, friends or carers who can make decisions for them when the decisions are not significant. More formal legal arrangements exist in the form of an advance care directive, an enduring guardianship, or a power of attorney, or by order of the Guardianship Tribunal, Mental Health Review Tribunal or Supreme Court. ❑

WILLS AND SUPER

Can you say who'll benefit after you're gone?

Large sums are often payable from a super fund when someone dies, particularly with recent super reforms, and with many funds containing life insurance policies. However, death benefits are not automatically distributed according to a will, nor even necessarily in accordance with any nomination a person has made to the trustee of a fund.

A death benefit from a super fund must either be paid out as a lump sum or as a pension – it cannot merely be left in the fund. But a lump-sum death benefit from a super fund does not by law form part of a deceased's estate. When someone has validly nominated a preferred beneficiary before their death, the trustee will consider the nomination, but is not bound by it, unless it was a binding nomination.

Often on joining a fund, members are given a form to nominate preferred beneficiaries. If the fund's trust deed allows binding nominations, these generally need to be updated every three years to stay valid. It is also important to update non-binding nominations regularly.

Recent changes to the law mean that those in same-sex and other interdependency relationships can be eligible to receive super death benefits, and forms should be updated for this situation too.

While binding nominations provide certainty, they can produce results the deceased might not have desired – if, for example, they had not been kept up to date, and the deceased had separated, married or had a child. For this reason they have not been as popular as anticipated.

Trustees usually distribute the benefit directly to the dependants rather than the estate. This avoids any loss of funds if an estate is insolvent or subject to litigation – payments directly from a super fund will not generally be available to creditors of an estate.

Only if the fund trustee, after reasonable enquiries, has not found either a legal personal representative or a dependant of the deceased, can payment be made to another person. In practice this will rarely happen.

As the amount of money in super increases, so too does the risk of litigation in respect of death benefits. It is vitally important to minimise confusion and angst, and maximise benefits. Remember to include super in any estate-planning discussions with your solicitor. ❑

FORGERY

Invalidating the security on a loan

A recent appeal case is a timely reminder to everyone with financial interests that not only should steps be taken to ensure that fraud is not perpetrated which may render a security interest unenforceable, but that care should be taken to properly describe any security interests in loan and security documents.

Mrs X was the registered proprietor jointly with her husband of property over which a mortgage was registered in their names.

The wife's signature was forged by her husband on both the mortgage and a housing loan contract that the mortgage was intended to secure.

There was no dispute that the registration of the mortgage gave the lenders rights over the property that had been mortgaged. There was also no dispute that the husband was liable for the indebtedness under the housing loan contract and that that indebtedness was secured by the mortgage over his interest in the property.

When the matter first went to court the judge decided that the bank had rights over all of the property – both the husband's and the wife's share. However, Mrs X's solicitors prepared an appeal that argued to protect her interests. They put to the judge that the bank's rights created by its registered mortgage were limited to her husband's interest in the property and did not extend to her own.

The appeal judge agreed that as there was no joint borrowing by virtue of the forged loan agreement, then the mortgage could not have been secured over the wife's interest in the property. ❑

TENDERS

Are disclaimers effective?

Businesses inviting tenders for construction projects often have to decide how much information to provide about latent conditions and how much site access to allow.

Frequently, reference documents, technical drawings, plans and geotechnical and environmental surveys are provided to assist in tender preparation. This information is normally supplied with a disclaimer by the principal of the business that tenderers must satisfy themselves of the accuracy of the information.

In a recent case, a contractor who won a contract for the excavation of materials at a quarry found that the natural surface level at the site differed from the excavation plan included in the tender documents, and the company faxed a latent condition notification, claiming almost $7 million in additional costs because of the materially different physical conditions of the work.

The contract provided that latent conditions are those not associated with physical conditions or characteristics of the site which have been identified or could have reasonably been expected to exist from site investigation.

The principal was not able to point to any particular fact or matter in the information they supplied "which would cause a non-expert in the position of a contractor to seek the assistance of a geotechnical engineer".

The courts confirmed that the test to determine whether a contractor should be entitled to claim for a latent condition is what "a reasonably competent contractor" should expect to encounter. It decided the contractor could not have been expected to investigate further, and that the disclaimers made by the principal did not succeed in avoiding liability for the latent condition. ❑

DISPUTE RESOLUTION

Should I go to court or mediate?

Mediation is a confidential conference, where all the participants attend to cooperate to resolve the dispute between them.

Mediation can be more 'user-friendly' than going to court and it has a proven success rate. It is informal and, if successful, provides a cheaper and quicker means of settling a dispute.

Statistics show that more than 90 per cent of cases are settled before they reach court. Mediation can enable settlement to occur even earlier. Early settlement reduces the stress inevitably involved in court proceedings, particularly where a party may have to give evidence. Early settlement also reduces legal and other costs such as those involved if parties have to take time off work or from business.

Mediation can help the relationship between parties to survive their dispute because it allows them to formulate their own mutually acceptable solutions.

Even if parties do not settle their dispute, they can clarify and narrow the issues at the mediation, thereby reducing the time and expense of a court hearing. At the very least, parties who have been through a mediation will have had an opportunity to discuss and clarify the disputed issues.

Mediation is suitable for all civil cases where the parties are committed to reaching settlement, including personal injury matters, multi-party commercial cases, contract cases, family law matters, disputes over wills, and debt recovery matters. Cases in which the parties want an early and amicable solution are particularly appropriate.

Your solicitor can advise you whether your case is suitable for mediation. ❑