Managed investment schemes associated with Mark Letten

Guidance for investors in the Letten Schemes regarding the tax treatment of distributions from the Common Fund.

12 June 2013

Background

From 1998 to 2009, around 1,300 investors jointly invested in various ways in a range of undertakings of which Mark Letten was the controller (the Letten Schemes).

By the orders of the Federal Court on 25 February 2010 and 4 March 2010, receivers were appointed to these schemes (Receivers). On 11 November 2010, the court gave approval to pool the proceeds of sales of assets of the Letten Schemes into a 'Common Fund'. On 19 November 2012, the court gave approval on the method proposed by the Receivers to determine an investor's entitlement to receive a distribution from the Common Fund. In coming to the decision, the court made findings of fact as to the nature of the investors' interests in the schemes, the nature of any final distributions from the Receivers and any effect of the earlier actual and purported distributions by the scheme operators.

The way in which the tax law applies to these schemes is based on these findings of fact made by the Court. Even though the schemes were marketed as separate schemes, the money from the various schemes was mixed together, and because of the poor records of the schemes, the winding up of the schemes has been done collectively.

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Introduction

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This information applies to investors that receive an interim and final distribution as a result of the winding up of the Letten Schemes.

Further information

For more information about capital gains issues for personal investors, refer to **Personal investors guide to capital gains tax**.

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How does the law apply to investors?

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This law applies to assets held as investments rather than assets used in a business of trading or on revenue account. It would be expected that most, if not all investors are covered by the law set out in this fact sheet.

Tax outcomes for investors

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Tax outcomes for investors

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For investors who receive interim and final distributions, the tax consequences are outlined below.

Basic outcomes

Outcomes in detail

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Basic outcomes

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Generally, you will be able to offset a capital loss from your investment against capital gains in the year in which you receive your final distribution or later year returns. The capital loss is calculated by subtracting the amounts of interim and final payments received on winding up of the schemes from the money you invested.

Any amounts previously reported as income by the scheme operator but not paid to you should not have been declared on your tax returns. Where time limits permit, you will need to correct those past year tax returns.

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Outcomes in detail

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Your claim to the Common Fund, that arose when your invested money was mixed with monies invested in other schemes, is a CGT asset.

A CGT event occurs when you receive your interim distribution out of the Common Fund.

If your interim distribution is more than your cost base before the interim distribution is paid then a capital gain arises. Otherwise, your cost base is reduced by the amount of your interim distribution, but not below zero.

A CGT event occurs when you receive your final distribution out of the Common Fund, constituting the expiration of the CGT asset.

Your capital proceeds amount is the sum of any final amounts distributed to you out of the Common Fund.

Your cost base includes the sum of your total investment in the schemes, described as the member's total contributions ('A') in the court direction made on 19 November 2012, excluding the amount of your investment in YVG Direct and reduced by the amount of your interim distribution.

If your capital proceeds as a result of your final distribution out of the Common Fund are more than your cost base just before the final distribution is paid, there is a capital gain for that CGT asset for the year in which the CGT event occurs.

If your capital proceeds as a result of your final distribution out of the Common Fund are less than the cost base for your investment just before this time, a capital loss will result for that CGT asset for the year in which the CGT asset expired.

Where the scheme promoter advised you that you made a gain, but you never received that gain or the gain was purportedly reinvested, consistent with the Courts' findings, we do not accept that gain was made. Any such gain has no consequences for income tax purposes, either in the year it was reported, or in the year you receive your final distribution from the receiver. You may seek an amendment of your return to exclude that unpaid gain from your taxable income. You will need to substantiate that you did not receive that gain. Documents that may substantiate that you did not receive that gain include a notice from the Receivers of rejection of your claim against the Common Fund, or a letter from LGH Holdings Pty Ltd advising of the roll-over of a capital gain into a new project.

The following information explains how to correct mistakes in previous year tax returns.

Further information

For more information about correcting mistakes, refer to **Guide to correcting mistakes and disputing decisions**.

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Capital gains and losses

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The relevant taxation law applying to investors is capital gains tax (CGT).

Capital gains tax concerns gains or losses made as a result of CGT assets.

In the current situation, the relevant CGT asset is considered to be a claim on the Common Fund that arose when the monies you paid to invest in one scheme were mixed with investment monies from other schemes.

When you receive your interim distribution out of the Common Fund, a CGT event occurs, and there may be capital gains tax consequences.

When you receive your final distribution out of the Common Fund, your claim is considered to have expired and CGT event C2 occurs.

How to calculate capital gains and losses

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How to calculate capital gains and losses

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To work out capital gains and losses it is necessary to work out the 'cost base' and 'capital proceeds' for CGT purposes.

Cost base

Capital proceeds

CGT calculations

Previously declared but unpaid capital gains

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Cost base

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In working out capital gains or losses, the 'cost base' of a particular CGT asset is worked out by adding the total purchase price of the asset with other costs of buying, selling or owning it, such as brokerage or agent's fees, legal fees, stamp duty and investment advisers' fees (but not investment seminar costs).

In this case the purchase price is taken to be the member's total contributions ('A') as described in court's direction 1(d)(i) in the judgment made on 19 November 2012. This amount **excludes** capital gains and other entitlements that were reported but not paid. However, it **includes** other invested monies not relating to a specific project that were paid into the schemes, such as the 'Project Reserve Bonds', the 'War Chest', the 'LGH Development JVs' and 'LGH Joint Ventures'.

If your investment includes an investment in YVG Direct, and you claimed deductions relating to that investment, your cost base is reduced by the amount of those deductions, but not below zero.

Your cost base is reduced by the amount of your interim distribution, but not below zero.

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Capital proceeds

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Your capital proceeds are the final amount distributed to you on winding up the scheme by the Receivers.

The amount of capital proceeds is not impacted by any reported but unpaid amounts previously notified to you by a scheme operator as being assessable to you. There is no provision under the law which allows for such an unpaid amount to be taken into account.

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CGT calculations

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If your interim distribution is more than your cost base before the interim distribution is paid then a capital gain arises. Otherwise, your cost base is reduced by the amount of your interim distribution, but not below zero.

If the capital proceeds received in respect of your final distribution out of the Common Fund are more than the cost base just before this time, this will result in a capital gain being made from the CGT event. If the capital proceeds are less than the cost base, a capital loss arises.

For each income year, capital gains and losses are calculated to work out whether you have a net capital gain or net capital loss in that year. If you have a net capital gain, this is added to your taxable income for that year. A net capital loss is not counted as part of your taxable income but may be offset against net capital gains in future years.

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Previously declared but unpaid capital gains

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You have unlimited time to correct your earlier tax return to remove an incorrectly reported capital gain if:

- the capital gain was reported in an income year
- you did not receive the capital proceeds (ie the cash), or the promoter advised you that the proceeds were reinvested in another Letten scheme
- you are unlikely to receive some or all of those capital proceeds.

You will need to substantiate that you did not receive the proceeds.

> **Find out more**
>
> Introduction to capital gains tax

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Examples

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Example 1 – Capital loss

In the 2003–04 income year, Sue contributed $100,000 to participate in one of the Letten Schemes. In the 2007–08 income year, Sue paid an extra $50,000 as part of the 'Project Reserve Bonds'. She also incurred an expense of $1,000 in relation to legal fees concerning her investment in the Letten Schemes.

When the receiver determines Sue's entitlement to receive a distribution from the Common Fund, Sue's total contributions is determined to be $150,000, which is the total of amounts actually paid by Sue. Sue's entitlement to receive an interim distribution from the Common Fund is determined to be $15,000 and her entitlement to receive a final distribution from the Common Fund is determined to be $5,000.

On 15 April 2013, Sue receives $15,000 as an interim distribution out of the Common Fund.

Sue has a CGT event occurring on 15 April 2013 as a result of her claim to the Common Fund.

Prior to the payment of the interim distribution, the cost base of Sue's claim to the Common Fund will be the sum of her total contributions and other costs of investment, which will be:

$150,000 + $1,000 = $151,000.

The amount of the interim distribution ($15,000) is less than the cost base of Sue's claim to the Common Fund just before the interim distribution ($151,000). Consequently, Sue will not make a capital gain or loss in relation to her claim to the Common Fund in the 2012–13 income year.

On 15 February 2014, Sue receives $5,000 as the final distribution out of the Common Fund.

Sue has a CGT event occurring on 15 February 2014 as a result of her claim to the Common Fund.

Just before Sue receives the final distribution, the cost base of Sue's claim to the Common Fund will be the sum of her total contributions and other costs of investment less the amount received as an interim distribution, which will be:

$150,000 + $1,000 - $15,000 = $136,000.

The capital proceeds for the expiration of Sue's claim to the Common Fund will be the final distribution she receives from the receiver, which is $5,000.

Consequently, in the 2013-14 income year, in relation to her claim to the Common Fund, Sue has made a capital loss of $131,000 ($5,000 - $136,000 = -$131,000).

Sue can use this capital loss to offset against any capital gains arising in the 2013–14 year tax return or later year tax return.

Example 2 – unpaid capital gain

Following on from example 1, Sue was advised that she had made a capital gain of $5,000 from her investment in the Letten Scheme which she included in her tax return for the 2008–09 income year. Sue did not receive and is unlikely to receive any part of the $5,000 capital gain. Sue received her notice of assessment on 3 December 2009. Because Sue is unlikely to receive any part of the $5,000 capital gain, she has a unlimited period of review and can ask for her 2009 year tax return to be corrected so as to remove the incorrectly reported income.

Example 3 – prior deductions

In the 1997–98 income year, Sam contributed $150,000 to participate in the YVG project. As Sam's investment in the YVG project was between 1998 and 2000, he is described as a YVG Direct investor. Sam claimed tax losses in the 1997–98, 1998–99 and 1999–2000 income years, exceeding $150,000. In the 2008–09 income year, Sam paid an extra $35,000 as contribution to the 'War Chest'. He incurred an expense of $1,050 in relation to legal fees concerning his investment in the Letten Schemes.

When the receiver determines Sam's entitlement to receive a distribution from the Common Fund, Sam's total contribution is determined to be $185,000, which is the total of amounts actually paid by Sam. Sam's entitlement to receive an interim distribution from the Common Fund is determined to be $18,500 and his entitlement to receive a final distribution from the Common Fund is determined to be $2,500.

On 15 April 2013, Sam receives $18,500 as an interim distribution out of the Common Fund.

Sam has a CGT event occurring on 15 April 2013 as a result of his claim to the Common Fund.

Prior to the payment of the interim distribution, the cost base of Sam's claim to the Common Fund will be the sum of his total contributions and other costs of investment less his investment in YVG Direct, which will be:

$150,000 + $35,000 + $1,050 – $150,000 = $36,050

The amount of the interim distribution ($18,500) is less than the cost base of Sam's claim to the Common Fund just before the interim distribution ($36,050). Consequently, Sam will not make a capital gain or loss in relation to his claim to the Common Fund in the 2012–13 income year.

On 15 February 2014, Sam receives $2,500 as the final distribution out of the Common Fund.

Sam has a CGT event occurring on 15 February 2014 in respect of his claim to the Common Fund.

Just before Sam receives the final distribution, the cost base of Sam's claim to the Common Fund will be the sum of his total contributions and other costs of investment less his investment in YVG Direct and less the amount received as an interim distribution, which will be:

$150,000 + $35,000 + $1,050 – $150,000 - $18,500 = $17,550

The capital proceeds for the expiration of Sam's claim to the Common Fund will be the final distribution he receives from the Receiver, which is $2,500.

Consequently, in the 2013–14 income year, as a result of his claim to the Common Fund, Sam has made a capital loss of $15,050 ($2,500 - $17,550 = -$15,050).

Sam can use this capital loss to offset against any capital gains arising in the 2013–14 year tax return or later year tax return.

Example 4 – prior year deduction and capital proceeds greater than cost base

Continuing Example 3, if Sam had not paid the extra $35,000 contribution to the war chest, his cost base prior to the payment of the interim distribution would be:

$150,000 + $1,050 – $150,000 = $1,050

In the 2012–13 income year, as a result of his claim to the Common Fund, Sam has made a capital gain of $17,450 ($18,500 - $1,050 = $17,450).

In the 2013–2014 income year, as a result of his claim to the Common Fund, Sam has made a capital gain of $2,500 ($2,500 - $0 = $2,500).

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Help meeting your tax obligations

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If you are experiencing difficulty meeting your tax obligations, refer to **Financial difficulties**

for help understanding your tax responsibilities and the ways we can help.

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