



JULY 2014

The July Investor Update

Welcome to the AIA July Investor Update. This month *Investor Update* contains four articles about Self Managed Super Funds, which is appropriate at the start of a new financial year. We also have an article on international investing, the topic of a recent AIA seminar.

A reminder also about our **2014 Annual Conference** which is just 2 weeks away. Visit the website or phone the office 1300 555 061 to register.

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Offer from the Switzer Report

We are pleased to offer a free copy of a new eBook by Peter Switzer and Paul Rickard on their *5 Big Investment Ideas for the New Financial Year*. The eBook covers the main themes that Switzer thinks are going to come into play over the next 12 months and beyond, and which listed companies could be set to benefit from these themes.

The eBook offer includes a free 3-week trial to the *Switzer Super Report*. If members aren't interested in the trial and only wanted the eBook, simply unsubscribe. To download the e-book, click [here](#).

Upcoming Events

2014 AIA Annual Investors Conference
**Outcome Oriented
Investment Strategies**
for the individual investor

Sunday 3rd to Wednesday 6th August
At the Marriott Resort, Gold Coast



This year's conference will be focused on investment **outcomes** for the individual investor.

Full details on AIA website

If SMSF means “Screwing My Super Fund” to you, pack now**Marcus Padley.****Saturday 7 June. Copyright © 2014. The Sydney Morning Herald**

Every year I attend the Australian Investor Association's Gold Coast conference. For a busy bloke who has sworn never to be "taken for a mug" after once being presented with a coffee cup in return for giving a presentation on a weekend, it may come as some surprise - it surprises me - that I take the time to spend four days in the company of strangers.

But they're not so strange any more and after a few years I am beginning to see the same faces.

The beauty of the conference, apart from the 43 presentations on equities, fixed income, property, superannuation, estate planning, aged-care issues, investment structures, investment strategies, hybrids and capital protection, is that over four days, three lunches, three morning teas, three afternoon teas, four happy hours and one conference dinner, you have the opportunity to chat with the 300-odd delegates and presenters.

While I take it for granted while attending events that people in my space know what they are doing, aren't stupid, can spot the predators and know who's on the right side of the moral fence, the truth is that the people who know what they are doing are a minority.

Given the political imperative for an underfunded government to pass the responsibility for retirement onto the individual (let them take the blame) and given the prolific marketing of the need to "take control", the explosive growth in self-managed super funds and the access to "everything you need" to invest online, a lot of people who are not prepared for the responsibility of money are fumbling around in the early stages like shell-shocked troops in no man's land with targets painted on their back and the words "I don't know what I'm doing, come and get me" sputtering out every time they click on some investment product's banner ad.

This conference is for them, the beginners, as well as the regulars. It is the opportunity to rub shoulders with people who do know what they're doing and have in many cases been humbly doing it for years.

People who have been where you are. People who have experienced it all, survived their mistakes and know who is to be trusted and who is not. People who are only too willing to talk to you at lunchtimes, tea stops and during

happy hours. It is the chance to gain objectivity from some of the most accomplished investors and retirees in the country, and that's before you attend the presentations.

If anyone will keep you honest it's other people, and let me tell you they're busting to tell you if you only just ask. The motto of the AIA sums it up as "Investors helping Investors", and it's true.

Of course, you occasionally get caught at lunch next to someone who just loves talking about themselves and is very slow to pick up on your signals of disinterest, but I have a tip for that taught to me by an experienced delegate.

"When you are being pounded with someone's tedious life story," he said, "just mention a stock code." The effect you will find, in this company at least, is astonishing. "It's like the Miracle of Surfers Paradise," he said, "suddenly the deaf can hear" because, as it turns out, the only thing that really interests an experienced investor is what stock you bought, when you bought it and what happened next, they are interested in "the battles" and to talk about safe subjects or listen to life stories is to waste the opportunity. "I like to throw in the odd stock code that doesn't exist," he said. "It keeps them busy for hours. They love that!"



Of course, the AIA doesn't have the marketing budgets or the profile it deserves because it is not for profit and as a result the success of its events and growth in membership is not bought by slick TV ads and glossy press ads, but is hard won by individuals whose primary motive isn't money but their generous interest in spreading the word.

The conference is from August 3 to 6 on the Gold Coast. What better spot for a break and, you never know, it may even be tax deductible. See you there.

Marcus Padley is the author of the sharemarket newsletter *Marcus Today*.

Think Global - Why, Where and How to Invest Overseas (A Sydney one-day seminar 4th July 2014)

Did you know that the average SMSF has less than 1% of its assets invested overseas? By comparison, large professionally managed super funds allocate 25-30% offshore. Why the disparity? The NSW Committee of the AIA sought to explore this question through a 1-day seminar on international investing on 4th July 2014, which attracted nearly 70 members.

Why? Kathryn Young from Morningstar started the day by discussing “Why invest overseas?” She demonstrated how diversifying a portfolio with international shares reduces the overall volatility of portfolios and allows investors to gain exposure to industries that are poorly represented on the ASX, especially important given the high degree of sector concentration in the Australian stock market. International investments also benefit from a falling Australian dollar.

How? Richard Cowan, AIA NSW Committee, described the range of methods for investing overseas - managed funds, ETFs, LICs, structured products and direct purchase of securities via a broker. Richard also prepared a handout listing a range of managed funds as well as ETFs and LICs listed on the ASX.



Where? Nick Griffin, K2 Asset Management, discussed the structural changes, themes, regions and industry sectors he expects to perform well in the future, and demonstrated the value of a understanding how a professional investor goes about identifying opportunities and structuring a portfolio.

ETFs can be used to easily access overseas markets. Tim Bradbury of ETF Consulting described the structure of exchange-traded funds (ETFs), how they work and the types of products currently listed on the ASX. ETFs represent a rapidly growing market, leading to lower fees and an ever-expanding choice of products on the ASX.

Managed Funds and LICs. Frank Casarotti of Magellan Asset Management highlighted the differences between traditional unlisted managed funds and Listed Investment Companies (LICs), their structure, tax treatment and costs. Frank gave examples of well-known global brands that Magellan believes have competitive advantages over their rivals. He showed how difficult it is to get exposure to firms selling to the vast number of emerging market consumers if we limit ourselves to Australian investments.

Direct investment in overseas shares. Matthew Jones, Capital 19 Global Investments, described some platforms and brokers an individual investor can use to directly access overseas markets. Brokerage costs for overseas stocks can vary widely across different providers.

Did the seminar make a difference? The short answer is: Yes! At the start of the seminar, attendees were polled on their current exposure to international investments. One-half of attendees had international exposure under 5%, and only one-tenth had international exposure greater than 20%. In contrast, professional managers average 25% to 30% international.

Following the seminar, attendees were asked whether the meeting had changed their view on investing overseas. Over half said “yes”, and a further 20 percent said “seriously considering”. Less than 5 percent said no. Typical comments from attendees were:

- “Today has changed my investment philosophy to include overseas investment”.
- “I really value this opportunity and am now in a much better position to consider ETFs, LICs, and even direct international”.
- “AIA seminars are always good but this was the best yet!”

Good reasons to support your local AIA activities. Let your committee know of topics you’d like to hear about in future seminars, information evenings or discussion groups.

Presentations and handouts from the Seminar are available to AIA members on the AIA website <http://www.investors.asn.au/resources/papers-presented/seminars/>

Richard Cowan, Toya Adams and Brian Spies, NSW Committee

Superannuation Rates and Thresholds for 2014/2015

The Australian Taxation Office has released the key superannuation rates and thresholds for the 2014/2015 year.

- Superannuation Guarantee Charge Rate – the rate has increased to 9.5% for the 2014/2015 financial year.
- Concessional Contributions cap – the cap has increased to \$30,000 for the 2014/2015 year. Higher caps of \$35,000 apply to older Australians aged 59 years or over on 30 June 2013 or aged 49 years or over on 30 June 2014.
- Non-Concessional Contributions cap – the cap for 2014/2015 will be \$180,000. Under the bring forward rules, the cap over three years from the 2014/2015 year is \$540,000 (\$180,000 x 3).
- CGT cap amount – the CGT cap amount for 2014/2015 is \$1,355,000.
- Superannuation Guarantee – the maximum superannuation contribution base for 2014/2015 is \$49,430 per quarter.
- Superannuation Co-Contribution – the maximum entitlement for the 2014/2015 year remains at \$500. The lower income threshold increases to \$34,488 and the higher income threshold increases to \$49,488 for the 2014/2015.
- Tax-Free Part of Genuine Redundancy Payments and Early Retirement Scheme Payments – for genuine redundancy and early retirement scheme payments for 2014/2015, the base limit is \$9,514 and for each complete year of service \$4,758.

Speeding ticket legislation for SMSFs: A snapshot

A new penalty regime will apply to SMSFs from 1 July. Richard Livingston and Liam Shorte explain the new rules.

Key Points

- Current penalty regime for SMSFs has only harsh penalties for breaches
- New regime allows ATO to impose monetary penalties or issue orders to trustees
- Structure of financial penalties benefits corporate trustees

The current penalty regime for superannuation funds, including SMSFs, is brutal and complicated. The Tax Office can make a fund non-complying (resulting in a massive tax bill), apply to the court for financial penalties to be imposed on a trustee, disqualify a trustee or accept an enforceable undertaking from them.

For many breaches, these penalties (and the processes to be followed) are out of proportion with the crime committed. So either the trustee gets whacked with an excessive penalty, or doesn't get penalised at all.

Come 1 July 2014, this situation will change. New rules, colloquially known as the 'speeding ticket legislation', will commence and give the Tax Office other options when it comes to penalising SMSF trustees. The speeding ticket rules give the Tax Office three additional penalty options: rectification directions, education directions and administrative penalties.

Rectification directions

A rectification direction is issued to a trustee (or director of a corporate trustee) and requires them to take action to fix up a contravention of the superannuation rules (the **SIS Act** or related regulations). For example, if a fund has borrowed money, the Tax Office might issue a rectification direction requiring it to be repaid.



Before issuing a rectification direction, the Tax Office is required to consider the scale of any financial detriment that might be suffered and the seriousness of the breach (including past compliance history). The idea here is to make the punishment fit the crime.

Education directions

An education direction requires a trustee (or director) to undertake an approved course, provided by the Tax Office or other educational bodies. The courses are to be provided free of tuition fees.

Once completed, the person must provide the Tax Office with a signed declaration that they understand their duties as trustee of a SMSF.

Administrative penalties

In addition to the rectification and education directions, the Tax Office will have the power to impose an administrative penalty on trustees (or directors) who breach one of seventeen listed SIS Act rules (see Table 1).

Ref. SIS Act?	Rule breached	Penalty (\$)*
s34	Contravene a prescribed standard. Eg. the requirement to formulate, review regularly and give effect to an investment strategy (including consideration of insurance)	3,400
s35B	Failure to prepare financial statements	1,700
s65	Lending or financial assistance to members or their relatives	10,200
s67	Super fund borrowings outside the exemptions (eg limited recourse)	10,200
s84	Trustees not taking steps to comply with in-house asset restrictions	10,200
s103* *	Failing to keep trustee elections and minutes for at least 10 years	1,700
s104	Failing to keep records of change of trustees for at least 10 years	1,700
s104A	Failing to sign trustee declaration within 21 days of appointment and keeping for at least 10 years	1,700
s105	Failing to keep member reports for at least 10 years	1,700
s106	Failing to notify ATO of an event that has significant adverse effect on the fund's financial position.	10,200
s106A	Failing to notify ATO of change of status of SMSF (eg super fund ceasing to be a SMSF)	3,400
s124	Failing to appoint investment managers in writing	850
s160	Failing to comply with Tax Office education directive	850
s254	Failing to provide the Regulator with information on the approved form within the prescribed time upon establishment of the fund	850
s347A	Failing to complete a form with requested information provided by the Regulator as part of the Regulator's Statistical Program	850

Ref. SIS Act?	Rule breached	Penalty (\$)*
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Notes:

*Penalties are defined as a fixed number of units, with each unit being worth \$170. So the penalty which applies to, for instance, 'failure to prepare financial statements' is 10 units.

** Technically, this is three separate breaches grouped together.

Table 1: Administrative penalties under new SMSF penalty regime

Where the breach is of an obligation that applies to trustees generally (for instance, the requirement to prepare accounts) each trustee will be subject to the penalty. So, if a fund has four individual trustees, they'll be required to pay a combined total of \$6,800 for failure to prepare accounts. A corporate trustee only counts as a single trustee no matter how many directors or fund members.

Directors (at the time) are jointly and severally liable for penalties imposed on a corporate trustee. So if you become a director of a trustee company you can become liable for prior breaches.

Who bears the cost?

Trustees, or directors, can't be reimbursed by the SMSF for any education costs or administrative penalties they incur. However, there is no prohibition on the SMSF bearing the costs of a rectification direction.

However, if the trustees have breached their duties or failed to exercise reasonable care, they may not be permitted under trust law or the fund's trust deed to seek reimbursement.

Rights of review

Trustees have the right to request that the Tax Office vary a rectification or education direction. The request must be made before the specified date for completion of the direction and the Tax Office has 28 days to consider the request.

If a trustee or director seeks cancellation of the direction, they need to take the matter to the Administrative Appeals Tribunal (AAT).

Other considerations

One point to keep in mind is the difference in the potential penalties applying to corporate and individual trustees (if there are more than one). In the example

above, a total penalty of \$6,800 could apply where a fund had four individual trustees. However, a corporate trustee with four directors would only be liable to a penalty of \$1,700.

This is another point to add to the list of reasons why you're better off with a corporate trustee (see [Why your SMSF needs a corporate trustee](#)).

Remember also that the new 'speeding ticket regime' adds to the penalty options available to the Tax Office. It doesn't replace the old, harsh penalties – the Tax Office remains free to impose them on wayward trustees – and it probably means the Tax Office is less likely to overlook contraventions.

Finally, whilst it will hopefully never affect you, harsher penalties (including up to five years imprisonment) have also been introduced for those promoting schemes providing early access to super accounts.

Final words

The new light touch penalty regime isn't an excuse to start making mistakes, but may help to match the punishment with the crime. Whilst it means you're less likely to suffer a brutal penalty for a minor mistake, it also makes it less likely breaches will go unpunished, making it as important as ever that your SMSF's house is in order.



Switching your SMSF to pension mode: Starting a transition to retirement pension

If you've turned 55 you can start a super pension. We explain how.

By **Richard Livingston**

Key Points

- Most people will start by taking a transition to retirement pension
- Start with your trust deed
- 'Pension kits' are available from a range of online providers

You've spent years, possibly decades, building up your super and you've finally hit the ripe old age of 55 (the current [preservation age](#)). It's time to think about switching your SMSF to 'pension mode'.

First cab off the rank, when it comes to super pensions, is the transition to retirement pension (TTR). Unlike the 'regular' [account-based pension](#), a TTR can be taken while you're still working. Like an account-based pension, you're required to make [minimum withdrawals](#), but a TTR has the added restriction of you not being allowed to take more than 10% (based on opening account balance) each year.

Should I take a TRP?

The benefit of taking a TTR is that it puts your super account in pension mode, making it tax-free. If you're under 60, you'll be taxed on the TTR at your [marginal tax rate](#), but with a 15% tax offset (credit). If you're 60 and over, the pension is tax-free.

A TTR strategy makes most sense when drawing a pension allows you to make a larger salary sacrifice (or deductible) contribution to super ([see ASIC's MoneySmart example](#)). This way you're effectively reducing your personal tax by 15% (due to the tax offset) plus paying no tax on your super account. But a TTR pension can also be used to wind down your working hours, whilst maintaining your income ([see example](#)).

Taking a TTR makes sense for most people, although not everyone. If you're a high income earner and your super doesn't have a large tax-free component, the cost of the tax you pay on your super pension can exceed the benefit of making your super account tax-free.

Liam often finds people earning more than \$200,000 are better off not taking a TTR, although it depends in your personal circumstances. If you've got a large tax-free component (for instance, from making [non-concessional contributions](#)), or a high level of income in your fund (for instance, you've realised a [capital gain](#)), the story might be different.

Once you've decided to take a TTR, the next question is how you do you go about it?

Consult your trust deed

First step is to read your SMSF's trust deed and see what it says about pensions, since the trustees must comply with it. Ideally it will say very little, giving you maximum flexibility to pay pensions as the trustees see fit. But it should give a fund with individual trustees the power to pay a lump sum benefit – assuming you might want to

pay a lump sum one day – otherwise the [SIS Act](#) won't allow it.

If you've got one that's problematic, has 'whacky wording', or you're just not sure, consider updating it, especially as it will make the other steps easier. Buying a trust deed from an online provider (see Table 1) and using their pension kit (more below) saves you worrying about whether they work in concert.

Provider	Website
Cleardocs	www.cleardocs.com.au
DBA Butler	www.dbalawyers.com.au
Heffron	www.heffron.com.au
Reckon Docs	www.reckon-docs.com.au
Super Central	www.supercentral.com.au
Super Dynamics	www.superdynamics.com.au
Topdocs	www.topdocs.com.au

Notes: Liam uses each of the above providers from time to time. Not all focus on 'direct to retail' (some mainly work with advisors) although we understand they will all serve retail customers.

Table 1: Online document providers

Application form

Next step is to apply for the pension. For SMSFs, this involves you (as member) handing yourself a letter (as trustee) that says you've reached your [preservation age](#) and you'd like to commence a pension. You also indicate the date the pension is to start, what percentage you require and the frequency (for example, monthly).

If you wish, you can start a pension on 1 July and not take a payment until as late as the following June (which helps in the year you turn 60, as pension payments become tax free from your birthday onwards).

If you're nominating a reversionary beneficiary (See [Why you should take a reversionary pension](#)) you should include them in the application.

Trustee documentation

At this point, the trustee(s) takes over. Once the pension has been requested, the following steps need to take place:

1. *Product Disclosure Statement (PDS).* The trustee needs to provide the member with a PDS. The PDS essentially describes how super pensions work (in tune with your Trust Deed).

2. *Pension Agreement.* The trustee should also provide the member with a draft pension agreement, which, again, largely sets out the mechanics of how a pension works under the legislation.

3. *Trustee Resolution.* The trustee(s) then passes (signs) a written resolution setting out the pension terms and resolving to enter into the pension agreement, set up and pay the new pension account, register for PAYG withholding (if necessary) and obtain actuarial certificates (if one is needed).

Typically, Liam recommends to his clients that they do this on 1 July where possible. Since accounts are prepared (and assets valued at market value) at 30 June, it's easy to establish the member's account value and there's no need to worry about what's happened in the interim.

But this isn't a requirement. If you're establishing a pension mid-year, the Tax Office will generally accept working from the prior 30 June accounts up to six months after year-end (with appropriate adjustments) or you'll need to do interim accounts.

Assuming you take the 1 July approach, you won't have the accounts when you pass the trustee resolution and do the documents. The trustee can deal with this by stating (in the pension terms) that the exact pension account value and tax-free component will be determined once the accounts are available. Once the accounts are final, the trustees then pass another resolution to settle the numbers.

How do you get the documents? The best way is by purchasing a 'pension kit', available through your SMSF administrator or the online document providers mentioned in Table 1 (Liam's favourites are the Topdocs and Super Central versions). As an example, you can order the email version of the kit from Topdocs for \$165.

Paying the pension

You can start paying your pension immediately based on an estimate of the account value, but you'll need to make sure you 'square up' once the accounts are finalised and the exact account value known. The minimum pension that needs to be taken each year is based on the final account value, not your estimate.

You can make the timing of your pension payments whatever suits (for instance, weekly, monthly, quarterly or more). But to satisfy the minimums, you'll need to take at least one payment annually and Liam generally recommends his clients make at least two payments a

year so there's no doubt it's a super income *stream* (quirky technical issues come up from time to time on this point).

Pension payments will come from the existing SMSF bank account, if you're not [segregating](#) the fund's assets. If the fund is to be segregated we recommend having two separate bank accounts, with one designated as the 'pension account'. In this case, pension payments will come from here. We'll cover the question of whether to segregate in a future article.

Investment Strategy

The shift to pension mode means you'll also need to reassess your [investment strategy](#). You'll need to consider whether to focus on more income-oriented investments and also address the fund's [liquidity](#) needs, given the need to make pension payments. Liam typically sets out, in the investment strategy document, the next five years' cash requirements and confirms that the adopted strategy meets the requirements. Essentially, as a trustee, you're aiming to show that you understand your pension payment obligations and are investing to meet them.

Final comments

It's easy to get blasé about the paperwork, but don't. Liam has experience picking up the pieces when accountants have left it until after the financial accounts are completed to 'fill in the paperwork'. Interim events – for instance, the death or incapacity of a member – can leave you with a mess (including not having a valid pension).

Given the cost involved in buying a kit (especially relative to the damage mistakes can inflict), we don't recommend trying to do this completely on your own. If you're reviewing the appropriateness of your current trust deed, be sure you know what you're doing. If in doubt, we strongly recommend seeking personal advice.

SMSF Alert: June 2014

Liam Shorte and Richard Livingston highlight the past month's key SMSF developments.

By [Liam Shorte, Richard Livingston](#)

Key Developments

- Rules on insurance in super changed 1 July
- Court decision emphasises importance of estate planning
- Tribunal reminds us mistakes won't be tolerated
- After the excitement of May's budget, the past month has been relatively low key. July is fast approaching and we've recently covered some important changes, such as [Superstream](#) and the new '[speeding ticket](#)' penalty regime. In this month's SMSF Alert, we'll outline the new rules on insurance.

In future, we'll produce the SMSF Alert earlier each month. So, unless there's some major developments in the next fortnight that can't wait, our next SMSF Alert will be published in the week commencing 11 August.

Insurance rule changes

From 1 July, the rules will change for new insurance policies taken out inside super. These will limit the types of policies that can be taken through your SMSF.

Currently, SMSF trustees may choose to take out life insurance, trauma, total and permanent disablement or income protection policies inside the fund. However, under the [SIS Act](#), the insurance proceeds may only be paid to a member who has already satisfied a standard 'condition of release' or who meets specific conditions of release relating to insurance – death, permanent incapacity, temporary incapacity or terminal medical condition.

The practical effect is that there are differences between when an insurance claim can be made and when the funds can be paid to the member. For instance, a claim under a trauma policy generally won't match up with a condition of release. The funds remain 'stuck' in the super fund (but can be paid out when a condition of release is subsequently met).

New policies taken out from 1 July will be required to only have claims which are consistent with a condition of release. This will make it difficult to take out a trauma policy inside super and will cause problems for many ancillary benefits and claim definitions. For instance, 'own occupation' income protection cover (see [Navigating the insurance minefield](#)) won't be possible inside super.

Policies already in place will be ‘grandfathered’. The rules will only apply to new policies taken out from 1 July 2014.

Importance of estate planning

A recent court decision (*McIntosh v McIntosh* [2014] QSC 99) highlights the importance of having a will and [binding death benefit nominations](#) in place.

In this case, a mother was appointed as the administrator of her deceased son’s estate (he died without a will), which required her to collect her son’s assets and divide them equally between herself and his father (divorced from the mother).

The mother, who lived with the son, was also the named beneficiary of the son’s super (via a non-binding death benefit nomination). The bulk of his assets were in his super accounts.

Whilst the mother applied for, and was paid, the super death benefits (by the trustees of three large external super funds), the court ordered that this money be paid across to the estate and shared equally with the father. The court held that her fiduciary duty, as administrator of the estate, required her to maximise its value, contrary to her personal interests.

There are indications that the decision might have been different if the son had made a will, or a binding death benefit nomination had been in place.

Mistakes and poor advice not special circumstances

While the recent changes to excess contributions alleviate some of the sting, a recent Administrative Appeals Tribunal decision (*Thomson and Federal Commissioner of Taxation* [2014] AATA 339) serves as a reminder that there is little tolerance when it comes to mistakes on contributions.

In this case, the taxpayer had withdrawn money from her super, paid it into a personal account, and later made contributions to super. The total contribution in the 2010 financial year was \$205,000, of which she claimed a deduction for \$23,905. The remainder (\$181,095) was held to be a [non-concessional contribution](#), in breach of the cap.

The taxpayer argued that she had received incorrect advice, which amounted to a ‘special circumstance’ in which the Tax Office could disregard the breach. But the tribunal disagreed, finding there was nothing special about wrong advice.

Other recent developments

Members may also be interested in the following:

1. **Tax Office guidance on tax avoidance schemes** – The Tax Office has [updated its website with a list of tax avoidance schemes](#) targeting SMSF trustees.
2. **Tax Office educational videos** – The Tax Office has released two more videos in its series explaining SMSF obligations. The videos are available in the [most recent SMSF News](#).
3. **White paper on Australians approaching retirement** – REST have produced [a white paper](#) which provides an insight into the attitudes of Australians aged 50 plus, approaching retirement.

Note: Liam Shorte is an SMSF Specialist Advisor™ with [Verante Financial Planning](#) and author of [The SMSF Coach](#).

Disclaimer: This article is general in nature and does not take your personal situation into consideration. You should seek financial or legal advice specific to your situation before making any financial decision. This disclaimer is in addition to our standard Terms and Conditions. Liam is an Authorised Representative of Genesys Wealth Advisers Limited, AFSL No 232686, ABN 20 060 778 2156.

SUPERCHARGING YOUR SMSF PART 2

No the bottom hasn't fallen off the related party loans to SMSF's

SMSF LAWS CHANGE AS TIME ADVANCES. SO SHOULD YOUR SMSF DOCUMENTS!

As I have always said, “You can only ever comply with the current law at the time advice is being given to a client, and if the law changes, which the law is subject to doing from time to time, then at the time of the change if there is a need to vary the documentation or the approach on the facts, adjustments can be made.”

It is vital that you ensure that you and your advisors keep up to date with the SMSF laws and that you adjust your SMSF documents and investment strategy to maintain compliance. Never, ever rely on the media to correctly state the law. Please rely on your legal advisory team to do that!

BEING UP TO DATE PROTECTS YOU

Your SMSF Deed and documents must deal with the matters that you wish to undertake in your SMSF, and they must be up to date. The fee for being up to date pales into insignificance compared to the risks of non-compliance.

A SMSF Deed or other documents that do not comply with the laws can mean losing your tax concessions, possible fines, & even striped pyjamas. With the ATO upping its policing policies for SMSFs these fines are VERY substantial. Each trustee can be fined \$10,200.00 for a breach of the laws!

HERE'S A QUICK SUMMARY OF THE CURRENT SMSF RELATED PARTY BORROWING LAWS

You have the ability to apply to the ATO for a Private Binding Ruling (PBR) in relation to your tax affairs. A PBR is a tax ruling NOT a SMSF ruling! The Disclaimer at the start of a PBR says>>> “You cannot rely on the rulings in the Register of private binding rulings in your tax affairs.

You can only rely on a private ruling that we have given to you or to someone acting on your behalf. The Register of private binding rulings is a public record of private rulings issued by the ATO. The register is an historical record of rulings, and we do not update it to reflect changes in the law or our policies.

The rulings in the register have been edited and may not contain all the factual details relevant to each decision. Do not use the register to predict ATO policy or decisions.”

The ATO is the legislative regulator in charge when it comes to what a SMSF can and cannot do. When asked whether a SMSF borrowing from a related party on terms favourable to the SMSF was a breach of the laws, the ATO said:

“Decision: No. The terms cannot be more favourable to the related party than would have been the case had the parties been dealing at arm's length, but there is no contravention of section 109 of the SISA if the terms are more favourable to the SMSF.” [My emphasis]

The ATO expects the related party loans to be fully documented and conducted in a businesslike manner in the same way as dealing in an arm's length transaction,

but there is no contravention of section 109 of the SISA if the terms of the loan are more favourable to the SMSF.

The ATO also has its own form of Disclaimer on ATO IDs which says>>>

CAUTION: This is an edited and summarised record of a Tax Office decision. This record is not published as a form of advice. It is being made available for your inspection to meet FOI requirements, because it may be used by an officer in making another decision. This ATOID provides you with the following level of protection:

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ASSETS HELD BY BARE/HOLDING TRUSTS ARE NOT IN HOUSE ASSETS?

The Self Managed Superannuation Funds (Limited Recourse Borrowing Arrangements – In-house Asset Exclusion) Determination 2014 deals with the issue of the SMSF in house assets rules and bare/holding trusts. The ATO said>>>

“This instrument addresses concerns raised by industry

about the application of the in-house asset exemption provided by subsection 71(8) of the SIS Act to an investment in a related trust held by an SMSF as a required part of [an] LRBA,” the ATO stated.

“This instrument ensures that an investment in a related trust held by a SMSF as a required part of a LRBA is excluded from being an in-house asset of the SMSF in the circumstances described in the instrument.” In plain English>>> assets held by a bare/holding trust for the SMSF in the circumstances described in the instrument are not in house assets of the SMSF.

SO HOW DO YOU PROCEED WITH YOUR MIND AT EASE WITH RPLs?

“By closely following the ATO’s guidance on the issue”, is the correct answer to that question. It is the trustees of your SMSF that ultimately decide the issues and are responsible for what the SMSF does. Summing it up from what we have seen in the material in this article it seems the ATO is happy that related party loans can be more favourable to the SMSF, and there are PBRs confirming they can be on a “0” interest basis if the parties choose to do so. The quality of the documents is critical.

The documents used in RPLs must strictly comply with the SMSF borrowing law’s requirements and are of the same nature as dealing with a non-related party as lender such as a bank. Such issues as loan to value ratios, security such as guarantees for the loan from the members of the SMSF, duration of the loan, and the need for any repayments along the way all need to be considered. That list is not exhaustive of course.

Beyond that I think it is unlikely that the ATO could tell taxpayers across the board what is a “commercial arm’s length” relationship, because this is a subjective determination on the facts of each case and not an objective one. It will likely depend on the strength of the commercial market place at any given time, and the financial quality of any guarantor of a loan.

Where security and the financial strength of a guarantor are high loans can, and are made, for 100% LVR and in some circumstances beyond 100% in the commercial market place. The best approach would be to fully research the current market and the strength of the guarantors (members) providing the guarantee for the

RPL.

If there is sound commercial security from the guarantee why wouldn’t the loan be considered to be then on an arm’s length commercial basis if it has a 100% LVR??? Of course this is for the trustees to decide.

SMSF INVESTMENT STRATEGY

An SMSF must have its investment strategy reviewed regularly. Whilst this is an objective test, which depends on the type of fund assets and the type of investor each member within the fund is, we would recommend that this should be done regularly and at least bi-annually.

*Shane Ellis is the Managing Director of Equityprotect & SMSF Law. He is a Senior Consulting Lawyer specialising in **SMSF ESTATES & LAW, FAMILY ESTATE PLANNING, Asset Protection Structuring & Business Structures**. He is one of few lawyers in Australia to hold **SPAA ACCREDITED SMSF SPECIALIST ADVISOR** status & ASIC RG 146 **SPECIALIST SELF MANAGED SUPERANNUATION FUND ACCREDIT***

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Australian Investors Association Ltd
PO Box 7439
Gold Coast MC QLD 9726
Tel 1300 555 061
Fax 07 5538 8376
Email aia@investors.asn.au