SWIM BETWEEN THE FLAGS

SMSF TRUSTEE PROGRAM

MODULE 1 OF 7

INTRODUCTION TO SMSFS

an initiative of spring FINANCIAL GROUP

WEALTHADVISER

No Advice Warning

Letter from Wealth Adviser

Dear *Reader*

The goal of Wealth Adviser is to ensure that concise, informative financial education is available to everyone at no cost. Our educational material seeks to inform people of not only the benefits but also the potential risks and pitfalls of various strategies and investments.

Close to 600,000 self-managed super funds (SMSFs) are in operation according to the ATO and thousands of funds are being established each quarter. SMSFs are touted as the most flexible way for accumulating a retirement nest egg, offering significant investment choice and control. With this comes additional responsibilities for trustees, who are in control.

This free SMSF Trustee Program aims to equip trustees and financial services professionals with an awareness and knowledge of the relevant super rules and regulations. The program comprises seven modules, to be completed in sequential order via our Online Learning Centre. There is a short assessment at the end of each module to test your understanding. You must successfully complete each assessment in order to proceed to the next module.

The SMSF Trustee Program comprises the following modules:

1. Introduction to SMSFs
2. SMSF Trustee Responsibilities
3. Contributing to Superannuation
4. Withdrawing money from superannuation
5. SMSF Investment Rules
6. Taxation of SMSFs
7. Winding up an SMSF

By successfully completing the seven modules and online assessments you will receive a Certificate of Completion for the SMSF Trustee Program.

New SMSF trustees are required to sign a declaration that they understand the duties and responsibilities required of them according to the superannuation rules and regulations. A thorough working knowledge of the requirements is essential for trustees. An SMSF is not right for everyone and being informed is essential to maximising the opportunities from this type of super fund and minimising the risks of an SMSF.

This course is also suitable for SMSF trustees who have received an education direction and are required to complete an approved Australian Taxation Office (ATO) education course. To meet your education direction obligations, you are required to sign the Trustee Declaration (or re-sign this declaration if you have previously signed it) within 21 days of completing this course and forward the certificate of completion to the ATO by the date specified on your education direction.

We hope that this education course is beneficial and of service to you. From there, once you have a general understanding of options available to you, we believe that it is important for you to seek personal advice that is appropriate to your situation. If you are an SMSF trustee, you should find a trusted adviser and work with them.

Best regards

Wealth Adviser

Contents

Learning outcomes

After completing this module, you should be able to:

- Outline the basic features, structures and operations of a self-managed super fund
- Evaluate the advantages and key risks of self-managed super funds
- Compare individual versus corporate trustee structures
- Outline the requirements to become a trustee and their general duties
- List the legal responsibilities and liabilities of trustees
- Identify the sources of legislative requirements of self-managed super funds

What is superannuation?

Superannuation is a dedicated vehicle to save for retirement. Contributions made by employers and individuals can be made, are invested and accumulated until the member's retirement or other specified event, such as disablement.

Types of super funds available in Australia include:

Type of fund	Description
Industry super fund	Industry super funds are run solely for the benefit of members. They typically target a group of related industries and may be operated by employer associations and/or unions. Some industry funds are open for anyone to join.
Corporate/ Employer fund	Employer funds (standalone) are established only for employees of a particular employer.
Retail super fund	These funds are run by financial institutions such as banks and typically open to anyone. A variety of investment options, minimum balances and insurances is available across the market.
Public sector fund	These funds are only open to employees of federal and state governments.
Self-managed super fund (SMSF)	Commonly referred to as Do-It-Yourself funds, these funds are owned and managed by the members and limited to four individuals. The members are required to be trustees of the fund.
Small APRA fund (SAF)	A small APRA fund is similar to an SMSF in that it has no more than four members. However, a professional licensed trustee (regulated by the Australian Prudential Regulatory Authority (APRA)), is responsible for the legislative, administrative and compliance obligations of the fund.

For the purposes of this course we will refer to all super funds that aren't SMSFs as public offer super funds.

What is a self-managed super fund?

A Self-Managed Super Fund (SMSF) is a super fund with no more than four members where each member is a trustee (or director, if a corporate trustee).

As the name suggests the members are responsible for operating the fund and hence take on full legal responsibility. This includes fund administration and investment decisions. Complying super funds, including SMSFs are eligible to receive concessional tax treatment.

Unlike other super funds, SMSFs are regulated by the Australian Taxation Office (ATO).

SMSFs may have an individual or corporate trustee.

Multi member fund

To comply with the law an SMSF must meet the following criteria:

- Have four or less members
- Each member of the fund must be either an individual trustee, or a director of the corporate trustee
- If the trustee of the fund is a company, also known as a 'corporate trustee', then each director of the company must be a member
- No member of the fund can be employed by another member of the fund unless those two people are related
- The trustees of an SMSF are responsible for running the fund and cannot receive any remuneration for performing this role.

Single member funds

It is possible to set up an SMSF with only one member.

If this fund has a corporate trustee, then the member must either be:

- The sole director of the corporate trustee
- Or one of only two directors of the corporate trustee, where the member is not an employee of the other director, unless the two are related.

Alternatively, you can have a single-member SMSF with two individual trustees - the member and one other individual, provided the member is not an employee of the other trustee, unless they are related.

IMPORTANT POINT

In certain situations, other people may be permitted to act as a fund trustee on a member’s behalf without causing the fund to fail the SMSF definition. These situations might include where a member has a legal disability, for instance.

Advantages and risks of self-managed super funds

Before establishing an SMSF you should closely compare their possible advantages and disadvantages.

Advantages of SMSFs

SMSFs have a number of possible advantages. These include:

- Pooled family assets - SMSFs can be used to pool your super assets with a partner or extended family. With an SMSF, you can have up to four members. This means you are able to consolidate multiple super accounts to create a larger pooled balance.
- Control and flexibility - the fact that the members of an SMSF are also required to act as trustees makes SMSFs more flexible than other fund types as trustees have the ability to tailor their fund's rules and to make decisions based on the members' needs and circumstances. This flexibility can relate to a number of issues such as in-specie contributions, payment of retirement benefits for instance.
- Investment control and choice - SMSFs offer a wider range of investment options than typical retail or industry super funds. With an SMSF, you can invest in direct shares, high yielding cash accounts, corporate debt, direct property, unlisted assets, artwork and much more. In addition, SMSF's can acquire business real property from members.
- In addition, more sophisticated investment strategies can be implemented, such as derivatives and hedging. Other examples include small business owners leasing their business real property (that is used by their business) from their SMSF, borrowing to invest via instalment warrants and direct property investments.
- Borrowing – SMSFs may borrow via a limited recourse borrowing arrangement to acquire assets such as a property
- Estate Planning – keeping in mind that your will does not automatically control your super benefits, an SMSF will allow you to exercise a higher level of control over the provision of any death benefits than public offer super funds. Further to this, SMSFs can make binding nominations that do not lapse, unlike public offer super funds which have to be continually updated.
- Cost - while SMSFs are not necessarily cheaper to run than public offer super funds, the real benefit trustees enjoy is greater control of their costs. With an SMSF, you will incur certain fixed costs. You'll be required to pay for an annual tax return and audit, as well as ATO fees such as the annual supervisory levy. With respect to fixed costs, the larger your SMSF balance grows the more cost effective it becomes. The total cost of running your SMSF will depend on the investments you make within the fund and whether you decide to pay for any professional SMSF services or specialist advice.
- Tax control - even though SMSFs are not subject to different tax rules compared to other types of super funds, a major benefit of SMSFs is the control and flexibility that trustees have over the tax position of the fund. Through either strategic investment planning (such as maximising franking credits from Australian shares) or internal structuring, tax can often be legitimately minimised.
- Asset protection - assets held in super funds, including an SMSF, are generally protected from creditors. However, it is important to note that this exception does not apply where a member makes contributions to their super fund for the specific purpose of defeating claims from their creditors.

Risks and disadvantages of SMSFs

There are several benefits in using an SMSF to save for your retirement. However, there are certain features of SMSFs which mean they may not be suitable for everyone. These include:

- Increased time commitment - the very nature of an SMSF requires all trustees to take an active interest in the management of the fund. It is therefore not a 'set and forget' investment and will require a certain time commitment from you. It should be noted, however, that this commitment can be reduced by making use of specialist SMSF service providers and professional advisers.
- Costs - cost savings can be one of the greatest benefits of making use of an SMSF. However, the opposite can also be true. Investors with very minimal funds to invest and those who are not familiar with the costs and investment options involved may find managing an SMSF prohibitively expensive.
- Risk of non-compliance - where a trustee fails to maintain their fund in accordance with the legal requirements, the ATO can impose a number of penalties. Where a penalty is applied, the trustee will generally be personally liable and cannot be reimbursed from the fund for the penalty incurred. A non-complying fund may be taxed up to 47%.
- Trustee/ member moves overseas - to qualify for concessional tax treatment, an SMSF must meet specific requirements in relation to residency. Where trustees permanently move overseas or where contributions are made for a member while they are living overseas this could result in the fund failing the Australian Superannuation Fund requirement and become non-complying.
- Lack of investment knowledge and financial literacy - SMSF members should have a thorough understanding of the basics of investing and adequate financial literacy and investment expertise to properly manage the fund's assets and undertake trustee duties.
- Fraud and theft - if an SMSF trustee loses their money as a result of fraud or theft, they are not entitled to receive government compensation, as may be available to public offer funds.
- Complaints and disputes - when resolving disputes, SMSF members don't have access to the Superannuation Complaints Tribunal (SCT), as is available to APRA regulated funds. Instead, the parties in dispute may need to commence legal proceedings to have the issue resolved by a court, which can be extremely expensive and time consuming.
- Trustee duties and responsibilities - trustees should have an understanding of super and tax laws, as they are legally responsible to ensure that the SMSF complies with those laws.
- For more information on a trustee's duties and responsibilities, please see the module: SMSF Trustee Responsibilities.
- Possible poor and costly outcomes - if trustee responsibilities are neglected, poor investment decisions made, or too much risk taken on, poor outcomes may result – and at a considerable cost too. Unexpected events such as relationship/ marriage breakdown or a member becoming a non-resident could have serious repercussions, such as the fund becoming non-complying.

Individual versus corporate trustee structure

To qualify as an SMSF, you must appoint either a group of individuals or a company to act as the trustee of the fund. The trustee structure you choose will influence how your fund is administered and the cost of setting up and running your fund.

Feature	Individual Trustee	Corporate Trustee
Change in membership	Member leaving or joining fund must be removed or appointed as trustee. This requires: • amendment of trust deed • change of legal ownership of fund assets. You are not permitted to act alone as the single trustee of your fund.	Member leaving or joining fund must be removed or appointed as director of corporate trustee. Requires: • resolution to appoint/remove director • ASIC notification of change of director.
Change of members & ownership of assets	As the assets of the fund are registered in the name of the individual trustees of the fund, the fund will be required to re-register all assets held in the SMSF each time a member is added or removed.	The assets of the fund are registered in the name of the company (corporate trustee). If there is a change of fund members, it's not necessary to change the name on the ownership documents for each fund asset as the trustee of the fund remains the same. Reduces risk of fund assets being mixed with personal assets or being inadvertently sold or offered as security for a personal loan.
Borrowing to purchase property	Many banks will not lend to an SMSF with an individual trustee structure.	Many banks require a corporate trustee structure when lending to an SMSF
Personal Liability	Members are jointly and severally liable for their actions. This means that you may be personally held responsible for losses incurred due to the dishonest, reckless or intentional misconduct of another trustee. Trustee personal assets not protected where sued for damages.	Director's personal assets generally protected where a trustee is sued for damages. Liability is often restricted to assets held within the SMSF.
Cost to establish and maintain	No additional costs are incurred to set up an SMSF with individual trustees.	Cost of setting up company to act as a trustee can increase fund establishment costs.

Feature	Individual Trustee	Corporate Trustee
ATO administration penalties	ATO administrative penalties applied against each individual trustee.	ATO administrative penalty only applied against corporate trustee as directors of the corporate trustee are jointly and severally liable to pay the penalty.

TIP: In the case of a corporate trustee it is considered best practice to use a dedicated trustee company to minimise the possibility of mingling any of the fund's assets with other assets belonging to the company or another related entity.

Trustee requirements

Who is eligible to become an SMSF trustee?

To be eligible to become an SMSF trustee, a person must be age 18 years or older and generally not:

- be under a legal disability
- have been convicted of an offence involving dishonesty
- have been subject to a civil penalty order under the SIS Act
- be insolvent under administration e.g. an undischarged bankrupt
- or have been disqualified by a regulator previously to act as a trustee.

Where the trustee of the SMSF is a company, the company must not:

- know or suspect that a responsible officer of the company is a disqualified person
- have had a receiver, official manager, administrator or provisional liquidator appointed
- or have had action taken to wind up the company.

WARNING

Persons who knowingly act as a trustee of a super fund while disqualified can be subject to severe penalties, such as imprisonment.

Other trustee requirements

Other requirements of trustees include:

- Each trustee of an SMSF must be a member of the fund and vice versa (there are separate rules for single member funds)
- No member of the fund can be an employee of another member of the fund unless they are related
- No trustee of the fund can receive any remuneration for their services as trustee
- Trustees must have a thorough understanding of the super laws, the trust deed, general rules such as those imposed under tax or trust law and administrative requirements
- Trustees must consent to their appointment as trustee in writing
- New trustees must sign a declaration acknowledging their roles and responsibilities.

Other persons who may act as trustee

There are specific circumstances where other persons will be permitted to act as a trustee (or director of a corporate trustee) on behalf of a member without causing the fund to fail the SMSF definition.

Death of a member

When a member dies their legal personal representative (LPR) may act as a trustee or a director of the trustee company from the member's death until payment of death benefits commence. The LPR could be the executor of the will or administrator of the estate.

If at the end of this transitional period the LPR continues to act as trustee in place of the deceased member, a 'period of grace' of up to six months may apply during which time a fund will remain an SMSF even though it no longer satisfies the specific definition of an SMSF.

However, it is important to note that the ability of a deceased member's LPR to step in and act as a trustee on behalf of the member will be subject to the rules in the fund's trust deed.

Member under a legal disability

If an SMSF member is under a "legal disability" (e.g. due to mental capacity), the member's legal personal representative must be a trustee of the fund (or a director of the corporate trustee).

Member has granted an enduring power of attorney

A member's enduring power of attorney is permitted to act as a trustee (or as a director of the corporate trustee) in place of a member.

An Enduring Power of Attorney allows one person to give another person the authority to make decisions on their behalf if they find themselves unable or incapable of conducting their affairs at any time in the future.

The member's enduring power of attorney must actually become a trustee of the fund (or a director of the corporate trustee).

Member is a minor

If the member of an SMSF is under age 18 their legal personal representative must be a trustee of the fund (or a director of the corporate trustee) in place of the member.

If the member does not have a legal personal representative, then their parent or guardian must be a trustee of the fund (or a director of the corporate trustee) in place of the member.

Trustee suspended or removed by regulator

The ATO may disqualify an individual from acting as a trustee or director of a corporate trustee if they have contravened super laws. In this case the ATO will appoint an acting trustee.

Trustee legal responsibilities

As a trustee of a super fund, the trustee of an SMSF must maintain the fund in accordance with the relevant super laws and regulations. SMSF trustees also have a range of duties and obligations under general law.

General Law duties of trustees

The factors influencing trustee' behaviour come from the interpretation by the courts, general fiduciary law and the trust deed itself. These include the duty to:

- ensure he/she has been properly appointed and familiarises themselves with the property of the trust and trust deed
- adhere to the terms of the trust and not go against the trust
- invest the trust fund properly, which encompasses:
  - act impartially toward beneficiaries and different classes of beneficiaries
  - not engage in speculative / hazardous investments
  - act in the best interests of beneficiaries
  - take reasonable advice
  - adhere to the requirements of the trust as an override to any of the duties listed above
- act personally
- keep proper accounts and provide information when required
- complete and lodge any required returns for the trust
- pay correct beneficiaries by transferring trust property to the persons entitled to it
- act gratuitously (not profit from the role as trustee)

Super legislation covenants

The application super laws and legislation contains covenants (rules) that are automatically deemed to be included in the trust deed of every regulated super fund in Australia. These covenants reflect the duties imposed on all trustees under general trust law, and require trustees to:

- act honestly
- act in the best interests of the beneficiaries
- keep the assets of the fund separate from other assets
- exercise the same degree of care, skill and diligence as an ordinary prudent person in managing the fund
- not enter into contracts or behave in a way that hinders trustees from properly performing their duties or powers
- formulate, regularly review and give effect to an investment strategy for the fund
- manage reserves responsibly where these are in existence
- allow beneficiaries access to information and documents.

WARNING

While trustees can engage other people to do certain acts or things on their behalf, such as an accountant or financial planner, the ultimate responsibility and accountability for running the fund lies with the trustees.

Trustees cannot contract out their liability of operating the SMSF in a prudent manner in line with the super laws.

WARNING

A trustee who has breached their duty would be liable for any loss arising from that breach. Where a trustee has failed to comply with the terms of the trust a court can act to compel the trustee to comply.

Comply with sole purpose test

An SMSF must be established for one or more of the core purposes; or one or more of the core purposes and one or more of the ancillary purposes, which include:

Sole Purpose Test – Core Purposes

- provision of retirement benefits
- provision of benefits after reaching an age specified in the regulations (such as preservation age)
- provision of death benefits

Sole Purpose Test – Ancillary Purposes

These include:

- provision of benefits after termination of employment
- provision of benefits after leaving work due to ill-health
- other benefits approved by the regulator, such as terminal illness, severe financial hardship or compassionate grounds.

WARNING

The ATO may consider the following an indication of a breach of the sole purpose test:

- the trustees specifically sought out the benefit
- the decision making of the trustees was influenced by the benefits
- the provision of the benefit imposes a cost on the fund

For more information on the sole purpose test and how it interacts with the super investment rules, please see the module: SMSF Investment Rules.

Regulation of self-managed super funds

While the ATO is the principal regulator of SMSFs, other government bodies such as the Australian Securities & Investments Commission (ASIC) and the Australian Prudential Regulatory Authority (APRA) also have regulatory roles in relation to SMSFs to the extent that the legislation they administer contains provisions relevant to SMSFs and the provision of SMSF advice.

Australian super fund

The SMSF must meet the definition of an 'Australian super fund' at all times in the income year to remain complying and so receive the taxation concessions afforded to super funds. The three tests to determine if a fund meets the definition of an Australian super fund are:

1. The fund was established in Australia or any asset of the fund is situated in Australia.
2. The central management and control of the fund is ordinarily in Australia.

   Central management and control involves the strategic and high level decision-making processes and activities of the fund, for example:

   - formulating, monitoring, reviewing, updating or varying the investment strategy
   - formulating a strategy for the prudential management of any reserves
   - determining how assets are used to fund member benefits.
3. The fund meets the 'active member' test. An active member is one who contributes to the fund or an individual on whose behalf contributions have been made.

   A fund either has no active members or if the fund has active members, at least 50% of one of the following amounts must be held by active members who are Australian residents:

   - the total market value of the fund's assets attributable to those super interests held by active members
   - the total amount that would be payable to or in respect of active members if they voluntarily left the fund and so ceased to be members.

WARNING

The above tests impact members who temporarily or permanently leave Australia and cease to be Australian residents. However, it is possible for a member who plans to live overseas for a period of time to pass the 'central management and control' test, provided they leave Australia with the intent to return.

Australian Taxation Office (ATO)

The ATO is the principal regulator of SMSFs, aiming to:

- ensure SMSFs comply with the relevant provisions of the super rules, legislation and regulations
- provide information and forms to assist with set up and ongoing management of SMSFs
- take enforcement action where required for breaches of the super laws/ rules
- SMSF auditors are undertaking their checks on funds to the required standard.

However, the ATO does not focus on the prudential regulation of SMSFs as the members, being trustees, are responsible for protecting their own interest in their fund.

Australian Securities & Investments Commission

The Australian Securities & Investments Commission (ASIC) is responsible for regulating the relationship between consumers (such as SMSF trustees) and providers of financial products and services, such as financial advice and financial product providers; to ensure compliance with the Corporations Act 2001, such as disclosure.

In relation to SMSFs, ASIC is responsible for the registration of SMSF auditors and maintaining a register of these.

Australian Prudential Regulation Authority

The Australian Prudential Regulation Authority (APRA) is the regulator of all super funds other than SMSFs. Therefore, APRA does not technically have a significant role in relation to SMSFs other than in relation to data collection.

The ATO and APRA have entered into a Memorandum of Understanding to ensure the consistent application of super law by both agencies. This includes confirming that both agencies will consult each other on any proposed policy statements, technical documents, legislative modifications, publications, circulars or press releases which will have an impact on either agency.

Therefore, any relevant prudential standards, circulars and guidance notes that are published by APRA will also apply to SMSFs as both regulators have agreed to apply a consistent approach.

Relevant legislation

SMSFs are subject to numerous legislation, including the:

- Superannuation Industry (Supervision) Act 1993 (‘SISA’)
- Superannuation Industry (Supervision) Regulations 1994 (‘SISR’)
- Income Tax Assessment Act 1997
- Income Tax Assessment Act 1936
- Taxation Administration Act 1953.

Trustees also have an obligation to maintain their fund in accordance with the clauses of their fund’s trust deed. However, where a fund’s trust deed conflicts with the super laws, the super laws will take precedence and override the fund’s trust deed.

TIP

In this course we collectively refer to the numerous legislation and regulations as ‘super laws’

Learning check

Below is a repeat of the learning outcomes. This lists the key areas developed in this module and is designed to help address gaps in your knowledge which you may choose to seek further guidance on.

After completing this module, you should be able to:

- Outline the basic features, structures and operations of a self-managed super fund
- Evaluate the advantages and key risks of self-managed super funds
- Compare individual versus corporate trustee structures
- Outline the requirements to become a trustee and their general duties
- List the legal responsibilities and liabilities of trustees
- Identify the sources of legislative requirements of self-managed super funds

Readers Notes

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Spring Financial Group is not owned by a bank or large institution. Spring offers services and solutions that best suit your circumstances, goals and objectives.

Our advisers are educated and experienced in Financial Planning, specialising in advanced investment strategies for wealth accumulators. We also provide deep expertise in sourcing and investing in direct residential investment property.

We provide a balanced approach to investing between property and shares; plus considerable expertise in Self-Managed Superannuation Funds and wealth creation.

We are a fully integrated firm; consisting of:

- Spring FG Wealth - Financial Planning
- Spring FG Accounting - Accounting and tax
- Spring FG Finance - Mortgage broking and structuring advice
- Spring FG Realty - Investment Property advice
- Spring Equities - Shares and trading advice
- Wealth Adviser - free financial educational eBooks.

We operate a primarily fee-for-service based advice model.

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