



SUPER RETIREMENT SOLUTIONS

Specialists in Self Managed Superannuation
A division of McConachie Stedman

Super Newsletter

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Carrying on a business in your self managed superannuation fund

There has been talk of late by some advisors and commentators that people are now able to run a business through their self managed superannuation funds (SMSFs). This followed an article released by the ATO in May this year.

In particular, the ATO stated:

The fact that activities undertaken by an SMSF trustee are considered business activities for income tax purposes does not necessarily mean that the trustee contravenes the regulatory provisions.

This has been interpreted by some in the industry that there has been a relaxing of the ATO's attitude to this issue. However, what the ATO has actually done is simply confirm its view that the superannuation legislation does not specifically prohibit a fund from carrying on a business.

The Sole Purpose Test

The main legislative provision in this respect is the sole purpose test. All superannuation funds, including SMSFs, must be maintained *solely* for the provision of retirement or death benefits, and may also be maintained for other permitted ancillary purposes (such as the provision of benefits in the event of total or permanent disablement).

According to the ATO, determining whether a SMSF is maintained in accordance with the sole purpose test involves an assessment of *all* the events and circumstances relating to the SMSF's maintenance.

What this effectively means in relation to the investments of a fund is that those investments must be purchased for their ability to provide retirement benefits (by either being income-producing or by the potential for capital growth or both), but not for other purposes. A simple illustration of an investment which would breach the sole purpose test is the purchase of a holiday home for the use of members at no charge. In this example, a fund's investment is not simply for retirement purposes but also to give members a place to stay on their holidays before they retire.

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or call 07 4632 1966 if you have any
questions relating to the purchase
of an investment by your SMSF.



Running a business

So what kind of activity would constitute running a business such that the ATO would consider it a breach of the sole purpose test?

The ATO has indicated that where a substantial portion of the funds assets are used to conduct a business with a self managed superannuation fund, the fund will almost inevitably contravene the sole purpose test. This is because generally the purpose for which the investment is made is not to generate retirement benefits but rather to enable the trustees to operate a business in a tax effective environment.

If, for example, a super fund owned farming land, but instead of just passively owning the farming land and deriving rental income, as many funds do, the fund trustees were to run the farming business in the super fund by buying seed and fertiliser, employing workers, selling crops and so on, it is likely that the ATO would consider it a breach of the sole purpose test. This is because the ATO would consider that the purpose of the arrangement was to enable the business to pay tax at 15%, rather than a higher rate, say 30%.

This is especially true if fund trustees were to do something in a superannuation fund which they normally do outside of the superannuation fund. For example, assume a fund owns a large vacant block on the outskirts of a town. The block was purchased for capital growth, and now the trustees, having examined options to sell the block, have decided to subdivide it into residential lots to maximise the return to the fund. Such a land development, whilst in the nature of a business, could conceivably be undertaken by the fund without breaching the sole purpose test.

However, if in the same example the fund had not owned the block for many years, but it had been recently acquired, and the trustees also conducted a land development business in their own names, then it is more likely that the ATO would consider such an investment a breach of the sole purpose test, because the imputation that the purpose of the investment was not only to provide a return to the fund, but also to enable a development to be done in a tax concessional environment.

There are a number of other investment rules to consider whenever a fund makes an investment purchase, such as:

- restrictions on acquiring assets from related parties;
- the requirement for all transactions to be on an arm's length basis (on commercial terms);
- restrictions on borrowing; restrictions on charging the assets of a fund; and
- restrictions on providing financial assistance to members or relatives of members.

As you may recall, the review into Australia's superannuation system, headed by Mr Jeremy Cooper, completed its final report on self managed superannuation funds (SMSFs) on 30 June 2010.

One of the recommendations by the review panel relevant to SMSFs was that the acquisition of collectables and personal use assets such as artworks, jewellery, antiques, wine collections, exotic cars and yachts be prohibited. SMSFs that already owned such assets would be given five years in which to dispose of them.

The Government has yet to formally respond to this recommendation. However, during the caretaker period before the last federal election, the Government indicated that it would allow SMSFs to continue to invest in collectables, provided that, from 1 July 2011, rules which would prevent the investments from giving rise to a personal benefit to members are met.

The Government has indicated that it will consult with industry and community groups on the detail of the proposed legislation. However, according to the Self Managed Super Funds Professional Association of Australia (SPAA), it is anticipated that the eventual rules will broadly reflect the best practice guidelines relevant to artworks that it has developed with the Australian Artists Association (AAA).

Some of the SPAA guidelines do not go beyond existing requirements of the superannuation legislation and include:

- the investment must be consistent with the fund's investment strategy and the sole purpose test;
- the investment must be permitted by the fund's governing rules (trust deed);
- the investment must not be acquired from a related party.

SPAA guidelines which are not contained in the current legislation include:

- SMSF trustees must seek professional independent advice from a licensed financial advisor to assist with the assessment of the appropriateness of the investment;

- the investment must be independently valued by an appropriately qualified valuer upon its purchase, every 12 months thereafter, and immediately before its disposal by the SMSF;
- the investment must be appropriately authenticated with its history, the name of the work and artist (if relevant), a correct description including distinguishing features, confirmed and documented;
- SMSF trustees must be able to demonstrate the commerciality of any lease and / or exhibition terms and conditions;
- the investment must be insured for its market value against damage or destruction for the entire period of ownership by the SMSF;
- the investment must be appropriately stored or exhibited so as not to cause deterioration to its condition;
- the investment must not be stored at any premises owned or occupied by a related party.

Some of these guidelines would likely already be able to be met by the prudent investor in artworks or collectables, for example those relating to provenance or insurance. However, some guidelines, for example the prohibition of storage at premises of a related party, are likely to significantly impact upon trustees.

Whilst the detail of any legislation is not known, given the anticipated introduction of rules from 1 July 2011, and the likelihood that any new rules will be more onerous than current requirements, trustees of SMSFs that own artworks or other collectables would do well to review their arrangements for the storage, insurance and valuation of these investments.

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Team member profile

In this and future newsletters we will be profiling our staff members to give clients some background as to who is looking after their fund and who they may communicate with from time to time.

In this edition we profile **Tim Bate**. Tim is an Accountant and joined the team in March 2010. After a five year stint as a solicitor with a local law firm, Tim saw the light and rejoined the accounting industry. Tim has experience as a superannuation accountant in Perth, having spent five years in a role similar to his current one. He also comes with a wealth of legislative experience, having worked for the Australian Prudential Regulation Authority (APRA), a government regulator of superannuation funds, for twelve years.

Tim is excited by the opportunity to contribute to the SRS team, and intends to add to his existing accounting and legal degrees by obtaining relevant financial planning qualifications in 2011 so he will be authorised to advise clients on setting up self managed superannuation funds and other significant events such as commencing pensions.

Quarterly Reporting services for your Self Managed Superannuation Fund

For some time now, Super Retirement Solutions has offered a Quarterly Reporting service.

This service provides trustees with an updated value of their investment portfolio, including accumulated gains or losses, income earned and performance compared to the share market overall.

Our Quarterly Reporting service can help you gain a better understanding of your self managed superannuation fund investments on a regular basis.



What do we provide?

Under our Quarterly Reporting service you will receive:

- Investment summary report
- Investment movement report
- Investment income summary report
- Realised capital gains tax report
- Graphical investment overview



What does it cost?

Our Quarterly Reporting fee is \$200 plus 0.02% of the value of share market portfolio assets.

Eg. for a \$1 million share market asset portfolio, the fee would be \$400.00.



Other information

To utilise this service, you will need to have registered to connect to our Banklink service (at no additional cost). Most funds using our services have already connected to Banklink.

At the end of each quarter, we will email or mail to you a short list of queries seeking details of any transactions occurring off-market.

If you are interested in Quarterly reporting, please contact Super Retirement Solutions at our office.



Christmas / New Year office closure

Our office will be closed on Friday 24th December for Christmas and will reopen on Wednesday 29th December from 8am.

The office will also close for the New Years Day holiday on Monday 3rd January, 2011 with normal business hours resuming on Tuesday 4th January.

On behalf of the Partners and staff we wish you and your families a safe and enjoyable festive season. We look forward to working with you in 2011.

Disclaimer*: The information in this document reflects Super Retirement Solution's understanding of existing legislation, proposed legislation, rulings etc as at the date of issue. In some cases the information has been provided to us by third parties. While it is believed the information is accurate and reliable, this is not a guarantee in any way. The information is not, nor is it intended to be, comprehensive or a substitute for professional advice on specific circumstances. The information in this document is of a general nature only and has not taken into account the investment objectives, financial situation or particular needs of any particular person. Before making an investment decision on the basis of the advice above, a prospective investor needs to consider, with or without the assistance of a professional adviser, whether the advice is appropriate in light of their particular needs, objectives and financial circumstances.

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