# Understanding
# Self-Managed Super Funds



Self-Managed Superannuation Funds (SMSFs) are a highly personalised and flexible superannuation savings vehicle. Members of the fund are also the trustees, and are therefore able to determine the investment strategy and select specific investments of the fund. This provides an investor with a high degree of control over the investment portfolio, including member-directed investments.

**What is an SMSF?**

An SMSF, (sometimes referred to as a DIY fund) is a superannuation fund with fewer than six members, all of whom are usually family or business related.

All trustees must be members and vice versa up to a maximum of 6 with the exception of a single member fund. A single member fund must have a second trustee (all funds must have a minimum of 2 trustees), or a corporation may operate as the trustee.

Only resident funds will be complying funds for the purposes of the Income Tax Assessment Act (“ITAA”) and Superannuation industry (Supervision) (“SIS”) legislation. If a fund has elected to become regulated under SIS (a regulated fund) and the fund is a resident fund, then the fund will be classified as a complying fund, and be entitled to tax concessions.

**Trustee responsibilities**

Initially the fund must be established under a comprehensive and well - drafted trust deed. The fund must also have, and follow, a detailed investment strategy, which is discussed below.

In addition, trustees of SMSFs are required to:

- Keep accurate and accessible accounting records that explain the transactions and financial position of the fund for a minimum of 5 years;
- Prepare an annual operating statement and an annual statement of the fund's financial position and keep these records for a minimum of 5 years;
- Prepare minutes of trustee meetings (where matters affecting the fund were discussed), and prepare records of all changes of trustees and members written consent to be appointed as trustees. Each of these documents must be kept for a minimum of 10 years;
- Keep copies of all annual returns lodged for a minimum of 5 years;
- Have the fund audited annually by an independent auditor;

- Keep copies of all reports given to members for a minimum of 10 years.

Trustees cannot be paid with respect to their obligations or responsibilities in running the fund.

Poor and inadequate record keeping has been identified as a major problem for SMSFs. Trustees need to give this area detailed attention, as this can pose a compliance risk for funds. The Australian Taxation Office (ATO) is responsible for the regulation of SMSFs and has the power to remove the tax concessions afforded to superannuation funds, among other penalties, where a fund is found to breach the appropriate legislation and reporting requirements.

In cases where members no longer wish to undertake the trustee responsibilities, they can instead choose to appoint an approved trustee. This is an independent trustee, approved by the Australian Prudential Regulation Authority (APRA) under part 2 of SIS, who meets the relevant solvency, capital adequacy and operational capacity requirements. The fund will become a small APRA fund and be regulated by APRA instead of the ATO.

**Investment Strategy**

It is essential that the trustee establishes and documents a sound investment strategy that takes into account:

- The fund's liquidity requirements, and
- The goals and objectives of the members of the fund, and
- The members' risk tolerance and circumstances, and
- Members' ages and investment time frame, and
- Investment powers of the trustee (as detailed in the trust deed).

Trustees of SMSFs can be penalised if they fail to put an investment strategy in place. A member who suffers loss as a result of a breach of this requirement can sue the trustees to recover the loss. To ensure the trustee is protected from legal action by a member suffering any loss as a result of this breach, the underlying investments of the fund need to be considered in light of the investment strategy.

The investment/assets also need to be appropriate to meet the sole purpose test.

**Sole purpose test**

The sole purpose test requires that the fund be maintained for the sole purpose of providing its members with retirement benefits, or providing its members' beneficiaries or dependants with benefits in the event that the member dies before retirement. Certain other “ancillary” purposes are permitted within the sole purpose test, including payment of disability benefits for a member's retirement due to ill health or in other circumstances approved by APRA. It is absolutely imperative that SMSF monies are kept separate from monies for other purposes (such as living expenses). This will include keeping an entirely separate set of bank accounts, investments and accounts.

Contravention of the sole purpose test may arise where there is no retirement purpose behind the investment decision, or where funds are used for non-investment purposes. It is not the type of investment which is relevant for the sole purpose test but rather it is the intention for which the investment is made and maintained that determines its appropriateness.

An investment which is undertaken as part of a properly considered and formulated strategy, and which complies with the arm's length rule and other SIS investment restrictions, is unlikely to cause the fund to fail the sole purpose test unless exceptional circumstances exist. Failure to comply with the sole purpose test may also result in the fund becoming a non-complying superannuation fund for taxation and superannuation guarantee purposes. Employer contributions to a non-complying fund do not satisfy the employer's obligations under the superannuation guarantee scheme.

Given the significant penalties for trustees of SMSF for breaches of legislation, it is essential that the trustee has the structure and compliance of the SMSF reviewed on a regular basis by a qualified professional. Specialised SMSF administration services may also be of assistance.

**Other obligations**

Trustees must also:

- Conduct an investment review on a regular basis;
- Consider insurance for fund members as part of their strategy;
- Value the fund's assets at market value, and;
- Keep assets/money of the fund separate from personal assets/money.

Legislation is currently passing through parliament that requires acquisition and disposals of assets between related parties and SMSF must be conducted through an underlying market, if one exists. If it doesn't, the asset value must be supported by a qualified independent valuer.