



## Welcome...

By Robert Taber, Partner

In this issue of Super Sleuth we look at the ATO crackdown on SMSF's, we provide an outline of the May Budget and also some effects you need to consider when borrowing from a super fund. We also invite you to a free super seminar we are holding. This will be a great opportunity for you to raise your questions in an open forum and discuss the important topics and strategies amongst your peers.



### in this issue...

- 1 ATO crackdown's on SMSF's
- 2 May 2008 Budget Synopsis
- 3 This Super Life
- 4 Borrowing in super – here to stay?
- 6 Super promotion
- 7 30 June 2009 Deadline Approaches
- 8 Did You Know?

# ATO crackdown on SMSF's

*The Australian Taxation Office has been extremely vocal in their move from being in a position of educating Trustees to now ensuring adherence to the Rules and Regulations that Govern Self Managed Superannuation Fund's ("SMSF's").*



So what new measures have the ATO implemented to impress this?

They include the following:

- All newly established SMSF's need to report ANY/ALL breaches of the Superannuation Industry (Supervision) Act 1993 ("SISA") and Governing Rules of the Fund in their first year of operation – no matter how minor the breach.
- From 1 July 2007, expanded administrative penalties may be applied where SMSF's:
  - Fail to lodge their Annual Return on time
  - Provide false or misleading statements
  - Fail to keep and retain records
  - Fail to advise the ATO of a change of Trustee, or other changes in the Fund
- A new single Annual Return has been introduced which replaces the income tax and regulatory return and member contribution statement. The Annual Return has a far greater emphasis on the compliance with the regulatory provisions that govern SMSF's.
- From 1 July 2008, the reporting of contraventions will change. The changes include a provision outlining the issues an auditor must consider in determining whether a contravention must be reported. These issues include the type of contravention and the materiality level of the contravention.

So are the changes just scare tactics or is the ATO really cracking down?

The ATO are committing increased resources on an annual basis to complete reviews and audit's on SMSF's. At the end of the 2007 year, Cutcher & Neale had approximately 5% of our Fund's audited (the ATO were targeting related party transactions) of which all received a 100% clearance.

Furthermore, the ATO conducted an audit on one of our SMSF auditors – Sandy MacNeill – showing that they are not just targeting Trustees of SMSF's but are also looking at the professionals overseeing their completion. Sandy was given the ATO's tick of approval on completion of the audit.

As long as Trustees are aware of their role and responsibilities and adhere to them, the ATO's increased focus on compliance should not be a concern.



# May 2008 Budget Synopsis

*With the significant changes experienced within the superannuation environment over the past two to three years, superannuation specialists and auditors alike have had their hands full.*

*For those who watched this years Budget, it appeared that the Government has no plans to change the current superannuation landscape. Thank goodness for that!*

All eyes were focused on the Government and the anticipated changes (or even removal) of the Instalment Warrant legislation introduced last year. However, this did not eventuate and as a result the opportunities for SMSF investment in Instalment Warrant structures continues to be in place.

Whilst there were no major announcements in relation to superannuation in the Budget, there were some small changes centred around Government concessions and Social Security.

The government has proposed to expand the definition of income to include amounts such as salary sacrificed payments to super, net investment losses and reportable fringe benefits.

What impact does this have?

The inclusion of the above income will be used in determining an individual's eligibility for income support payments for people under age pension age, child support, **Government Co-contributions** and certain tax offsets.

Whereas in the past the implementation of a salary sacrifice strategy may have rendered an individual eligible for the Co-contribution (as salary sacrificed amounts were excluded under the income test), this may now not be the case.

The Commonwealth Seniors Health Card may also be affected. It is currently income tested to determine eligibility. The definition of income for this test will be expanded to include superannuation income streams and salary sacrificed amounts to superannuation.

Don't get caught out!

It is imperative that you discuss your situation with your financial advisor to ensure the right strategy is implemented for your situation. The strategies implemented in the past may now be void!

## New personal tax rates

Personal Tax Cuts – the proposed tax rates and thresholds for the next three years are as follows (bold numbers represent changes from prior year):

2008/09 Financial Year		2009/10 Financial Year		2010/11 Financial Year	
Taxable Income	Tax Rate	Taxable Income	Tax Rate	Taxable Income	Tax Rate
0 – 6000	0%	0 – 6000	0%	0 – 6000	0%
6,001 – <b>34,000</b>	15%	6,001 – <b>35,000</b>	15%	6,001 – <b>37,000</b>	15%
34,001 – <b>80,000</b>	30%	35,001 – 80,000	30%	37,001 – 80,000	30%
80,001 – <b>180,000</b>	40%	80,001 – 180,000	<b>38%</b>	80,001 – 180,000	<b>37%</b>
180,001 +	45%	180,001 +	45%	180,001 +	45%

# This super life



With the abolition of Reasonable Benefit Limits, more people are asking the question about having life insurance in superannuation.

## **What are the benefits?**

One of the main benefits is that the premiums for life insurance then become tax deductible for the fund whereas they would be non deductible to the individual member outside superannuation. The other benefit is being able to provide for your family and using the concessional tax superannuation environment to achieve this. Consider \$1m of life insurance paid to your spouse. The earnings derived on the \$1m will be taxed at the highest rate. With the new contributions limits restricting the amount of money put into superannuation, funding life insurance within super makes sense.

## **Can I transfer my current life insurance policy to my super fund?**

Generally no, as the Superannuation Industry (Supervision) Act 1993 "SIS Act" prohibits a super fund from acquiring assets from a member. While there are specific exceptions to this restriction, life insurance policies are not amongst them.

## **Can my SMSF hold trauma insurance?**

There is nothing stopping the fund holding trauma insurance however the issues are around access to the funds when the event occurs. The access rules in super still apply with respect to specific conditions of release to be met prior to payment of benefits. Of course the trust deed would also have to allow such insurance.

## **Would the premiums be tax deductible?**

The Income Tax Assessment Act 1997 provides that the Trustee of a complying SMSF can obtain a tax deduction in respect of the payment of premiums for insurance policies that covers events such as death, permanent disability and temporary disability for a period no longer than two years (or such longer period as the Commissioner allows). Trauma insurance is not included in these events and hence the premiums are non deductible to the Trustee.

## **What are some other benefits?**

Where the trustee of a fund pays out a temporary disability benefit they may be able to receive a deduction for that part of the benefit payment that relates to the member's future service period.

Insurance in a SMSF as a result of the changes brought about by the Simpler Super reforms provides many opportunities for members, however the rules are complex and should be accompanied with expert advice.



*The laws enacted in September 2007 around super funds being able to borrow seemed too good to be true. There were many who thought that Senator Nick Sherry would adjust or change the law to leave borrowing way outside super!*

# Borrowing in S

However, following the first Labor budget of May 2008 there is still no change to the borrowing provisions from last year.

That is not to say the Australian Taxation Office hasn't been thoroughly reviewing the arrangements in the market place and keeping a keen eye on developments around the borrowing in super market.

## **How does it work?**

Effectively the superannuation fund becomes the beneficial owner of the asset and the Security Trustee is the legal owner. In order to avoid stamp duty, capital gains tax and GST implications etc there is great importance on the documentation around the security trustee and the arrangements with the SMSF.

The SMSF will receive the income from the underlying asset and pays all necessary expenses. The loan is also shown in the accounts of the SMSF.

Considerations for this type of arrangement must include:

- Investment strategy of the fund (is the investment part of the overall strategy for the member's retirement benefits)
- Will the super fund have sufficient cash flow to finance the asset?
- Does the fund's trust deed allow such an arrangement?
- The loan must be a limited recourse loan (limited to the underlying asset)
- Set up or establishment costs may be high

## **So exactly what documentation is required and what costs are involved?**

The documentation required includes (a more detailed document list will be provided by the supplier):

- SMSF Deed Establishment/Upgrade
- Custodian Trust
- Loan Documentation (bank lending versus related party – the latter will require non-blank loan documentation)
- Mortgage Documents
- Lease Documents (where required)

# Super – here to stay?

The costs required to establish this structure includes:

- Stamp Duty (property) and conveyancing
- Lenders fees
- Advice fees from your Financial Planner including written Statement of Advice
- Legal advice, documentation (trusts) and lending documents
- Insurance – personal (life and salary continuance) and general (building, content etc)
- Accounting and taxation advice (where required)

## Does the role of the Trustee become more onerous when implementing an Instalment Warrant?

Yes. The Trustee must ensure that:

- The loan complies with the SIS Act
- The Fund has sufficient cash flow to repay the principal and interest
- The SMSF Trust Deed allows the Trustee to borrow to acquire the relevant asset

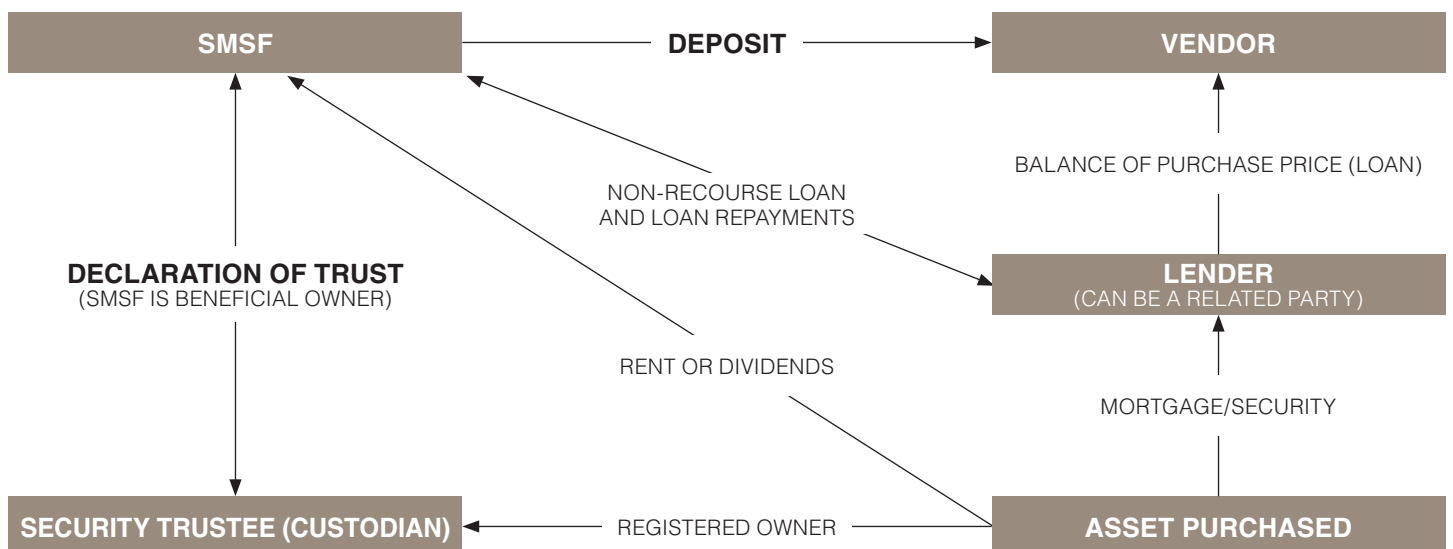
- The transaction is consistent with the SMSF investment and risk management strategy
- The structure of the transaction and the investment is signed off by the fund auditor as compliant with the SIS Act

The ATO has recently released a Taxpayer Alert on the subject (TA 2008/15) which amongst other items includes the following:

- Must be an arms length arrangement (ie. interest rate).
- Cannot capitalise interest.
- No personal guarantees.
- The purchase cannot be prohibited under another area of the law.
- Cannot be an existing asset of the fund.

The ATO focus in this area will continue as they scrutinise arrangements that have already taken place. Super funds undertaking this type or arrangement should seek expert advice and make sure all documentation is in place.

## The Typical Borrowing Structure





## Super promotion

Cutcher & Neale are pleased to announce the promotion of Shane Morgan to the position of Director

Shane joined the firm in January 2005 in the Business Services Division and has worked for most of his 18 years in the areas of taxation and superannuation. Sensing the need for a specialised division in the area of superannuation and specifically Self Managed Superannuation, the Cutcher & Neale Superannuation Technical Services Division was established in July 2005. In hindsight it was great timing given the wide ranging changes to superannuation as a result of the May 2006 Federal Budget.

Shane is a Newcastle boy, educated at Warners Bay High and the University of Newcastle. After completing an accountancy traineeship in Newcastle and attaining his degree and Chartered Accountancy qualifications, Shane spent eight years working in London and Sydney before making his way back home to Newcastle.

Shane is a Self Managed Superannuation Fund Professionals Association of Australia "SPAA" Specialist Advisor and is the Hunter Region Chairman of SPAA. Shane was also recently awarded the SPAA CEO Scholarship at the 2008 SPAA conference in Brisbane. This will allow Shane to complete post graduate studies in the specific area of Self Managed Superannuation.



*Shane Morgan receives his award from James Hird (ex AFL player) and Andrea Slattery (CEO of Self Managed Super Fund Professionals' Association of Australia).*

# 30 June 2009 deadline approaches



Self Managed Super Funds – SMSF’s – have until 30 June 2009 to take advantage of grandfathering provisions under the in-house asset rules.

The Superannuation Industry (Supervision) Act 1993 “SIS” was amended in late 1999 to broaden the definition of in house assets. Transitional arrangements that were put in place at this date cease to exist post 30 June 2009.

Where a super fund had an investment in a related entity (eg. a trust) at 11 August 1999, it could take advantage of one (not both) of the following exemptions:

- Make additional investments in that trust after that date, provided investments do not exceed the level of debt in the trust at that date and are made no later than 30 June 2009.

- Reinvest earnings from the related trust back into the trust after that date but not later than 30 June 2009 or if a fund had partly paid shares or units at 11 August 1999, it can make additional payments on those shares or units after that date (provided they are made no later than 30 June 2009).

It is also important that under these options the actual payment or reinvestment is made to the super fund before 30 June 2009.

The consequence of breaching these rules can be significant for an SMSF. Effectively any excess above the exemptions above becomes an in-house asset. If this breaches the in-house asset limit of 5% of the funds assets, the trustee must take steps to reduce this to under the 5% level or face non-compliance.



## Fact or Myth

*Following on from our March 2008 edition of Super Sleuth, we explore and clarify further ‘facts or myths’ that we have experienced over the last five months.*

**MYTH: A member turns age 65 in October 2008. If they wish to utilise the \$450,000 non-concessional contribution bring forward provision, they need to make this contribution before their 65th birthday.**

**FACT:** Where a fund member is aged 64 or younger on 1 July of a financial year (that is, at the start of the financial year), then they can access the bring forward non-concessional cap of \$450,000.

**MYTH: The taxing of earnings in a SMSF are the same irrespective of whether you draw a pension or superannuation lump sum (after meeting a condition of release).**

**FACT:** A SMSF needs to be in pension phase for the earnings to be exempt from tax. Taking a superannuation lump sum from an accumulation account will not render the earnings tax free.



# Did you know?



## Family law changes

The government has introduced *Family Law Amendment (de facto and financial matters and other measures) Bill 2008* into Parliament on 25 June 2008. This Bill amends the *Family Law Act 1975* to allow de facto couples (opposite and same sex) to use the federal family law legislation relating to property and maintenance issues. As de facto relationships are governed by state legislation, it is now necessary for the states to refer this power to the Commonwealth. The bill also includes changes to financial agreements for married couples, separation declarations and superannuation splitting.

## Making personal contributions

Members of super funds intending to claim a tax deduction for their personal contributions are reminded of the legislative requirements to ensure the deduction is valid. To be eligible for a tax deduction the superannuation contributions made in a financial year, all of the following must be satisfied:

- The contributions are made to a complying super fund;
- If you have employment income during the year, total assessable income attributable to employment does not exceed 10% of total assessable income;
- A valid notice is given of the member's intention to claim a deduction to the

trustee of the fund (this notice has changed this year);

- The trustee of the fund acknowledges receipt of this notice.

The notice must be lodged before the earlier of the day of lodgement of the member's income tax return or the end of the next income year.

Other areas to be mindful of when lodging these notices are the timing of pension commencement before a notice is given, if a contributions splitting application is in place and whether the member is at that particular time a member of the fund.

## SMSF statistics – up to March 2008

- SMSF's now account for 25.95% of the total superannuation pool.
- 40,642 SMSF's were established during the year to 30 March 2008

The table (right) shows the increase in superannuation assets for the following:

	Increase (\$B)	Total Assets (\$B)
Corporate	\$-5.4	\$64.0
Industry	\$14.2	\$197.5
Public Sector	\$4.4	\$170.2
Retail	\$-.04	\$343.8
SMSF	\$29.9	\$286.1

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