Australian SMSF Audits

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JUNE 2015 SMSF NEWSLETTER

The following topics highlight a number of issues I have encountered in recent times. The Trustees do need to be aware of these to ensure the fund they control is complying with the SIS Act and Regulations.

Valuation of Assets at 30 June

Regulation 8.02B of the SIS Act requires all assets held by the SMSF to be reported in the financial accounts at market value as at 30 June each year. While values of shares and managed funds are easy to ascertain, it is much more complex for other investments like real property or unlisted investments. While the SIS Act does not mention how a valuation should be ascertained, it does define what market value is.

Section 10 of the SIS Act defines Market Value as *the amount that a willing buyer of the asset could reasonably be expected to pay to acquire the asset from a willing seller if the following assumptions were made:*

a) that the buyer and the seller dealt with each other at arm's length in relation to the sale;
b) that the sale occurred after proper marketing of the asset; and
c) that the buyer and the seller acted knowledgeably and prudentially in relation to the sale.

Where a SMSF does hold such an asset, trustees need to provide details to the auditor of how they ascertained the market value of each asset. Failure to do so may place each trustee in breach of Reg. 8.02B, which is a reportable contravention.

Failure to do so may cause each trustees to incur a penalty of 10 Penalty Units.

Individual v Corporate Trustee

Questions are often asked whether it is better to have individual trustees or a corporate trustee administering a SMSF. Both have benefits, some of which are outlined below:-

Individual:-

- Easier to establish;
- Lower cost to establish and maintain

Corporate:-

- If a trustee dies, there is no need to find a replacement trustee;
- Because there is no change of trustee, the ownership of assets does not change;
- Should the SMSF incur a penalty under the current regime, each trustee can incur a separate penalty. As there is only one trustee (the company, only one penalty can be incurred.

PAYMENT OF PENSIONS

There are a number of issues that can arise where a SMSF is in pension mode. The following are a few of those issues:

What is a pension?

When a member elects to commence a pension, the SMSF is required to pay to the member a series of recurring payments that when combined meet the minimum requirement percentage based on the member's age. Trustees must be aware that a series of payments means more than one payment, even though they can make only one payment in a year. This means the pension cannot cease after only one payment. If that occurs, the single payment is deemed to be a lump-sum payment and the SMSF will be deemed to be in accumulation mode for the full year, so will not be exempt from income tax.

Short payment of a pension

When a member's fund is in pension mode and the SMSF fails to make the minimum pension payment, the SMSF is generally deemed to be in accumulation mode for the full year. The Commissioner of Taxation does have the discretion to allow the account to remain in pension mode and in limited circumstances the trustee can make an election, however the 3 following conditions do apply for that to occur:-

- The shortfall must be less than $1/12^{th}$ of the annual minimum pension;
- The trustees have not previously self-assessed; and
- The trustees must make a catch-up payment immediately the shortfall has been identified.

In all other situation, the trustees must apply to the ATO for discretion. Trustees should be aware that in 80% of recent requests, that request was refused because the ATO did not believe the discretion was outside the control of the Trustees. Examples where the ATO declined to exercise discretion include:-

- Only one trustee was effected by the circumstances. AS an example, if one trustee was in hospital, another should be able to attend to the trustee duties;
- Assets were incorrectly valued and the minimum pension was not paid at the true value;
- Professional advice given was not correct;
- The trustees made a banking error.

Irregular payments from a SMSF

In some instances, I have noted trustees paying personal expenses from their SMSF. Even though the fund may be in pension mode, this practice is not recommended.

- Random payments may be deemed to be lump sum withdrawals and so minimum pension payments are not met
- The SIS Act requires SMSF money to be kept separate from other, personal funds. The payment of personal expenses from a SMSF bank account may indicate that is not happening, making the SMSF in breach of SIS Act Reg. 4.09A. They may also be deemed to be a loan to the member, a breach of s. 65.

It is therefore recommended the SMSF make regular pension payments to the member, who then pays the expenses. The SMSF should document pension requests for each year. Any additional funds required should be requested in writing as a lump sum withdrawal.