

Thinking about a self managed super fund?

Jarrold Rogers CPA June 2011

Taking control of your retirement savings

Self managed super funds (SMSF) hold more of Australia's super assets than any other type of fund.

According to government statistics from December 2010, 32% of all superannuation assets were held in a Self Managed Super Fund.

The total number of SMSFs is 439,397 and growing. There were 6,000 new funds in the most recent quarter.

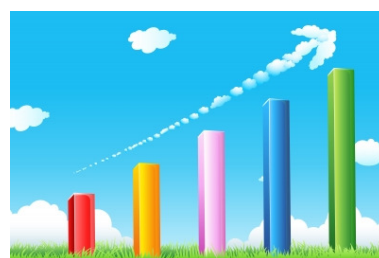
The stats are clear: managing your own super is no longer the choice of a small number of wealthy Australians.

Instead, it is becoming more and more common for Australians to take control of their own retirement savings.

So is a Self Managed Super Fund (SMSF) for you?

What does it cost?

Are you eligible to start your own fund?



What benefits does it provide that your existing super fund can't?

This leaflet is designed to answer these questions and help you decide if a SMSF is the best place for your super.

What is a Self Managed Super Fund?

To explain what a SMSF is we first need to understand what a super fund is.

A super fund is a special tax structure that is designed to help people save for retirement.

Once money has been contributed to super it cannot be accessed until a member meets a "condition of release", usually retirement, death or upon reaching age 65.

The trade off for this restriction is a concessional rate of tax on the investment earnings of the fund (normally 15%, but 0% if the fund is paying pensions).

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What is a Self Managed Super Fund?

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“The main feature that distinguishes a self managed fund from other funds is that **the fund trustees are also its members.**”

All super funds have two key players:

the **trustee**, who is in charge of running the fund; and

the **members**, who benefit from the money invested in the fund.

A SMSF is subject to most of the same rules as any other super fund, like a retail or industry fund.

The main feature that distinguishes a self managed fund from other funds is that the fund trustees are also members.

The fund members control the investment of their own super.

All trustees of a SMSF must be a member, and all members must be a trustee.

A SMSF is limited to

only four members, and the trustee can't receive any remuneration for their services.

So put simply, a self managed super fund is a fund where the members **control** their own **investments, contributions and benefit payments.**

It is this control which is the main appeal and advantage of a SMSF.

SMSF setup checklist

Before you can begin to consider the option of having your own super fund you need to check that you are eligible to do so. Certain people are discouraged from having a SMSF, and others are prohibited all together.

Do I have enough super for a SMSF?

Government watchdog ASIC considers that a SMSF with less than \$200,000 will not be cost competitive with other superannuation options. This limit refers to the size of the whole fund.

Note: The \$200,000 limit is a recommendation, not a rule.

- I / we have more than \$200,000 in super.
- Our combined super is less than \$200,000

Am I disqualified from being a SMSF trustee?

Superannuation law prevents a person from being a trustee if they: have been convicted of an offence involving dishonest conduct; have a civil penalty against them by the super regulator; are insolvent under administration; or if the ATO has disqualified them for other reasons.

- No member of the fund is a disqualified person
- Any member of the fund is a disqualified person

Can I roll over my existing super?

Some government and corporate super schemes are a defined benefit scheme. Defined benefit means that your final lump sum or pension is based on a measure such as years of service or average final salary.

These types of super entitlements cannot be rolled into a SMSF.

- I am allowed to rollover my existing super.
- My existing super cannot be rolled over.

Can I satisfy the residency requirements?

To comply with the law a SMSF must be an Australian resident fund. This means that “central management and control” must be ordinarily in Australia. While a trustee can be temporarily absent from Australia (two years is usually a rule of thumb), that person cannot be permanently absent.

- I / we are based permanently in Australia.
- I / we are based permanently outside Australia.

Advantages of a Self Managed Super Fund

Choice of investments

One of the biggest reasons for setting up a SMSF is choice of investment.

A SMSF can choose its own share portfolio, with local or overseas shares.

You can even sell your existing portfolio of listed shares to your super fund.

It can also invest in

residential and commercial property.

This includes *business real property* used in your own business, such as a factory, shop or a farm.

Other investments could range from an online savings account to gold and silver bullion to collectables like artwork.

Low tax on investments

The earnings of a superannuation fund are taxed at 15%. If the super fund is paying a pension the tax is 0%.

Compare this to the tax rates of 30% for a company and anything from 16.5% to 46.5% for individuals.

So superannuation is clearly the best tax environment in which to hold investments.

With a self managed super fund, your existing assets can be transferred in to utilise this tax benefit.

A member under 65 can contribute up to \$450,000 at one time.

A self managed super fund combines the tax advantages of super with the control of an investment portfolio.

Use super to build your business

A self managed super fund cannot have financial dealings with its members.

However an exception applies to *business real property*, which includes a factory, shop or even a farm.

A SMSF can own the property that one of its members uses to operate their business.

The SMSF and the business must deal at arms length (e.g. a market level rent must be paid to the fund).

Having a SMSF can benefit your business in two key ways.

If you don't own the property in which you run your business, your SMSF allows you to use your super to provide the capital to

purchase the property.

If you are an existing business owner you can transfer your property into a SMSF.

This frees up additional capital outside super, reduces the tax payable by the business, and puts the property in a structure with low tax and good asset protection.

The key to a self managed super fund is control: control of investments, tax strategy and estate planning.

Combined investment power

Having a self managed super fund allows up to four people to combine their superannuation assets into a single fund.

Combining accounts can provide greater investment power than if the accounts were kept separately.

For example, a couple with only \$150,000 each in super could have \$300,000 in a SMSF together.

This could enable them to get a loan to buy a property worth \$1,000,000. This would not be possible for either member on their own.

Lower fees on high balances

Most super funds base at least part of their fee on the amount of money in your account. This is typically somewhere between 0.5% and 2%.

With a SMSF the costs do not increase with the size of the fund.

If the fund compliance cost is \$2,500 p.a. this

is only 0.33% of a \$750,000 account.

This offers a much cheaper alternative to managed funds.

Conversely, the same \$2,500 fee is 2.5% of a \$100,000 account. This is why ASIC is concerned about the economy of low balance SMSFs.

Thinking about a self managed super fund?

Trustee obligations & restrictions

The trustee of a super fund is responsible for ensuring that the fund complies with the super law.

Strict penalties apply for failing to meet these requirements. If a breach of the law is serious enough the fund could be deemed "non complying" and be penalised 45% of all its assets.

General trustee obligations

Each trustee of the fund must:

- Act honestly in all matters concerning the fund;
- Act in the interest of (all) the beneficiaries; and
- Exercise the same skill and care that an ordinary prudent person would in dealing with the assets of another person.

The prudent person test requires that the trustee(s) must either have the necessary skills to run the fund, or that they obtain professional help to do so.

Sole purpose test

The fund must be run with the purpose of providing retirement benefits to its members, or death benefits to the dependants of a member.

When making an investment decision for your SMSF, there must not be any immediate monetary or non monetary benefit to members.

Separation of fund assets

Fund assets must be kept strictly separate from members' personal assets and all assets properly documented as being owned by the fund.

Dealing at arms' length

The fund must make and maintain all investments on an arms' length basis.

Dealings with members

The fund cannot loan money or provide any financial assistance to members or their relatives.

The rule book for your super fund

What your super fund can and cannot do is determined by three things: legislation, the trust deed and the investment strategy. Any trustee decision must be permitted by *all* of these documents in order for the decision to be valid .

Legislation (the law)

Like any super fund your SMSF must comply with a range of laws, including:

- Superannuation law;
- Taxation law;
- Trustee law (state);

Some examples are

- super contribution limits,
- fund tax rates,
- conditions for withdrawing money from super

Trust Deed

The trust deed of a super fund is a legal document that sets out the rules of the fund.

The trust deed cannot make rules that override the law.

The deed sets rules like: which investments are allowed or forbidden; procedures for receiving contributions and paying benefits; and other fund administration issues.

Investment Strategy

The investment strategy documents how the trustees plan to invest the assets of the super fund.

The investment strategy cannot override the law or the trustee—it must operate within them.

The strategy must consider the whole of the circumstances of the fund, including risk, liquidity, cash flow and the allocation of funds between asset classes.

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Please visit our website for more information on SMSFs:
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Links and resources

FREE ATO Guide: [Thinking about Self Managed Super](#)

(Go to www.ato.gov.au and enter "72579" in the search box)

FREE SMSF trustee education : www.smsftrustee.com

The SMSF Trustee program is a designed to educate trustees of SMSFs throughout Australia about their roles and obligations.

The program is created by the professional accounting bodies.