The Ultimate SMSF Trustee’s Guide

Sick of paying fees to superannuation funds? Ever wondered about setting up your own Self-Managed Superannuation Fund (SMSF) but put off by the complexity? This guide will give you everything you need to know.

• Is an SMSF right for me?
• How hard is it to set up an SMSF?
• How do I manage my SMSF?
• What are the investment restrictions?
• What are my investment options?
• How do I set up a pension?
• How do I close down my SMSF?

You might find that it is easier than you first thought. This easy to understand guide will cut through all the jargon and give you the answers you need. That is not to say an SMSF is suited for everyone or that you can just set and forget your SMSF like you can a retail or industry fund. There are things you need to know and rules you need to follow. The guide will provide those to you.

With the ATO now having greater powers to take action against SMSF trustees, it is more important than ever that you keep your fund operating according to the laws and regulations that govern superannuation. A few dollars spent on this guide could save you hundreds in ATO administrative penalties.

Every SMSF trustee will find this guide an essential reference and reliable source of information to keep handy. Make the most of your fund by keeping on top of proven strategies while being mindful of your obligations, and taking advantage of the guide’s reliable insights that even the most experienced trustee will find useful.

The guide draws on Taxpayers Australia’s more than 20 years of experience in providing for the needs of the SMSF sector. The in-depth coverage of all things SMSF provided by Taxpayers Australia’s publication the DIY Superannuation Manual is perfectly complemented by The Ultimate SMSF Trustee’s Guide, which acts as an easy-to-understand assistant in the day-to-day running of your fund.

Other essential tools for the SMSF trustee’s arsenal include Taxpayers Australia’s Superannuation Quarterly, which analyses important compliance issues, and Superannuation Strategies, with its focus on the enhancement of super benefits and tax-effectiveness.

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1300 657 572

By Reece Agland
Ultimate SMSF
Trustee’s Guide

Everything you need to set up and run an SMSF

By Reece Agland
The Ultimate SMSF Trustee’s Guide

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ABOUT THE AUTHOR

Reece Agland is a graduate of the University of Melbourne with qualifications in law (LLB) and commerce (BComm) who has spent almost 20 years in the tax and superannuation industry. He started his career as a graduate at the Australian Taxation Office where he spent several years in different business units, including as a lay prosecutor. He then moved to National Institute of Accountants (now the Institute of Public Accountants) where he had a 13 year career in policy, ethics and financial services. In 2013 he made the move to Taxpayers Australia as the Head of Superannuation. Reece has played an active role in superannuation policy development including the Future of Financial Advice (FoFA) reforms and the Cooper review into superannuation.

Ensuring people make the most of their superannuation is important for Reece, who is convinced that Self-Managed Superannuation Funds (SMSFs) are an essential part of the super system. He has time and again successfully argued in favour of the SMSF sector in the face of criticism by both industry super funds and the retail fund sector.

While Reece does not believe that SMSFs are for all people, he is keen to demystify the sector and open it up to those who can benefit from it. The guide is a pathway for those interested in controlling their retirement.

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ABOUT TAXPAYERS AUSTRALIA LTD

Taxpayers Australia is a not-for-profit organisation providing tax and superannuation education.

Since 1919, we have been campaigning for a simpler and fairer system, providing clear and concise information with insight to tax and superannuation professionals, small businesses and individuals.

Superannuation Australia, a wholly owned subsidiary of Taxpayers Australia Ltd, provides SMSF trustees and service providers with valuable resources on how to set up and manage an SMSF. Membership to Superannuation Australia entitles you to the DIY Superannuation Manual, updates to the Manual, the Superannuation Quarterly, Superannuation Strategies (quarterly), helpline (3 calls) plus member discounts on seminars and publications. All this is available for just $28.50 per month.

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SUPERANNUATION AUSTRALIA MEMBER BENEFITS

DIY Superannuation Manual

Written in plain English with plenty of examples, tips and warnings, the DIY Superannuation Manual is an excellent resource for both the taxpayer running their own fund or the professional who may be operating funds for clients. Quarterly updates keep you abreast of changes to rules and regulations.

Superannuation Quarterly

The Superannuation Quarterly provides relevant superannuation updates, with analysis of important compliance issues for trustees and members of funds in easily digested and accessible format.

Superannuation Strategies

Focusing on strategies directed at the enhancement of superannuation benefits and the gaining of access to those benefits in a tax-effective manner, Superannuation Strategies is the essential companion to the Superannuation Quarterly.
CHAPTER 1: SHOULD YOU SET UP AN SMSF?

Even before you embark on the process of setting up a self-managed superannuation fund (SMSF) you need to consider the reasons for doing so, and whether or not you are the sort of person who is best suited to having an SMSF.

While the law generally does not set any limitations* on the sort of person who can set up an SMSF, there are pitfalls for the unwary and some people are just not suited to the complexity of running an SMSF. They may be better suited staying with a retail or industry fund and instead choose the investment options within such a fund rather than taking on the responsibilities and duties of a trustee of an SMSF.

*Under superannuation law, an individual, or if a company, a responsible officer (collectively referred to as a ‘person’) is a disqualified person and cannot act as a trustee of a superannuation fund, if that person:

- has been convicted of fraud or has been penalised for dishonest conduct (e.g. fraud or theft) in Australia or elsewhere, or

- has had a civil penalty order made in relation to them under the SIS legislation, or

- is an insolvent under administration (e.g. an undischarged bankrupt), or

- is a company, is in liquidation, or receivers have been appointed, or has begun to be wound up.

But others are well equipped to take on the role of running their SMSF and may be able to do so at a reduced cost. Whatever your situation you should make an informed decision before setting up an SMSF, and talk it through with your accountant or financial adviser before making this big decision.
1.1 THINGS TO CONSIDER BEFORE SETTING UP AN SMSF

Taking care of your own retirement savings is a big responsibility – how you live, and how comfortable your life can be when you’re no longer earning an income, will all depend on your own efforts.

Wanting greater control is often cited as one of the chief reasons that people want their own SMSF, followed closely by the desire to have greater flexibility over investment choice.

So given the fact that an SMSF is more hands-on, they are a super fund that needs a commitment to run, as managing your own super takes knowledge, time and skill. Members may be fine about investment control, but there are also regulatory responsibilities to shoulder and manage. So while an SMSF will be suited to a lot of people, they are not for everyone.

As the name implies, “self-managed superannuation fund” means that you are responsible, you are the trustee of your own fund, and you need to comply with the superannuation laws and regulations, and wear the consequences of all your investment decisions.

But it’s no free-for-all. There are strict rules in place about how you must run an SMSF and where you can invest your fund’s money. The Australian Taxation Office (ATO) is the regulator for SMSFs, and the Australian Securities and Investments Commission (ASIC) regulates the financial services firms that give professional advice to them as well as regulating SMSF auditors.

If you think managing your own super fund could be right for you, there are many factors to consider. Think about your options, get informed advice, and consider the following:

- make sure you have the time, skills – and sufficient assets – to run your own fund
- have a good understanding of all the laws and rules, and the risks
- your trust deed and investment strategy must suit every member of your SMSF
- make sure you can meet all record-keeping and reporting requirements
- don’t forget the compulsory annual audit, and what’s involved, and
- consider getting appropriate advice about running your fund (accountant or administrator) and investment advice (financial planner).

Remember however that if you decide to establish an SMSF, you will be either the trustee of the fund or a “director” of a corporate trustee for the fund. A professional can
provide advice and assistance, but you will be the one who wears ultimate responsibility for all decisions made. The ATO as the regulator of SMSFs now has enhanced powers to take action against trustees that, in its view, are not meeting their obligations.

The ATO can now issue the following:

- a rectification notice – this requires specific action be taken by the trustee within a specified timeframe to rectify a contravention

- an education notice – this requires a person to undertake a specified course within a certain time, and give the ATO evidence of completion. No fee may be charged for the course and any cost incurred in undertaking the course cannot be reimbursed or paid from the fund – trustees must pay the costs out of their own pockets, and

- an administrative penalty notice – for breaches of certain sections of the *Superannuation Industry (Supervision) Act* (SIS), a penalty notice may be issued to either individual trustees or a corporate trustee.

**Professional advice to assist running your fund**

There are many professionals who deal with SMSFs specifically, and can provide essential advice about all the requirements for, and costs of, setting up your SMSF – and keeping it going. It’s also helpful to have all your investment options and risks spelt out by someone who knows all the choices.

A licensed adviser can help with the set-up and establishment of an SMSF, and also advise on its structure, valuation and ongoing operation. They can also help with advice on which investments may suit your fund.

A licensed financial adviser can look at your situation and recommend products and investments. There is also recourse to a free and independent complaint scheme (the Financial Ombudsman Service) should anything go wrong.

Note however that at present there is no option for SMSFs to access any scheme for compensation for fraud, which is open to members of other superannuation funds.

Then there is the fact an SMSF must have proper accounts that will need to be drawn up, usually by an accountant. The tax return will also need to be filled and lodged. While the fund can do this itself, most use a licensed tax agent to do this for them.

**Cost of running your fund**

There are regular fees and costs to remember, especially as many SMSF owners will need professional help. This will come at a cost as well, so make sure you factor in these
Should you set up an SMSF?

annual costs into running your SMSF. If you require external experts, which will add to the cost of running the fund, this may mean it is more costly to run an SMSF than leaving your retirement savings in a retail or industry fund.

However, if you are capable and prepared to take on many of the tasks of running the fund yourself then the cost equation is significantly reduced. Therefore you should seriously consider the costs of administration before you set up your SMSF.

If the annual cost of running the fund is more than 2% of the fund assets then you should seriously consider whether an SMSF is right for you at the moment. It may be worth getting your superannuation balance up to a reasonable amount before setting up an SMSF.

**Sole purpose test**

One overriding obligation that every SMSF must meet is to pass the “sole purpose test”, which basically states that the fund is legally required to be maintained for the sole purpose of providing benefits to each member on retirement, or to their dependants upon the member’s death. A current day benefit must not be provided to the member or related parties of the member. Buying a holiday home or yacht is in breach of the sole purpose test where you use these assets for your own enjoyment or that of family members (even if only some of the time). Compliance with this requirement is fundamental, and straying from it can lead to severe penalties. If you want to use the investment for purposes other than providing for your own retirement then you need to consider an alternative investment vehicle. See Chapter 3 for more details of the sole purpose test.

**Investment strategy**

You will need to set up an investment strategy. This should not be done in a perfunctory way — the investment decisions you make need to be for the long term (remember you may be retired for more than 20 years). The investment strategy should spell out your SMSF’s investment objectives, and how you plan to achieve them. It should provide you and any other trustees/members with guidance on making investment decisions with an aim to increase member benefits.

An investment strategy needs to consider the personal circumstances of all members, such as age and risk tolerance. One strategy may not suit every member, especially where there are varying ages of members at different stages of life.

If the SMSF invests money in an investment and that investment fails to perform, it is possible that other members/trustees could seek redress for your failing to be diligent in your duties. However if these decisions are recorded in meeting minutes, and the
other trustees signed these minutes, there will be a record to show that all were in
c accordance with these decisions.

It is also a good idea to include in the minutes why a particular investment was chosen,
and that all trustees agreed with this decision.

**Annual audit**

Don’t forget the compulsory annual audit, and what’s involved. You will have a legal
obligation to have your SMSF independently audited every year. The auditor needs to
be at arm’s length from the person or firm that prepared the SMSF’s financial statements.

An essential role of an SMSF trustee is to keep proper and accurate tax and
superannuation records, and to make sure you meet all record-keeping and reporting
requirements. The annual audit will require certain records be made available, and
there are annual reporting requirements that the Tax Office will need. You may need to
provide other records of the fund to the Tax Office if asked, and all of these are required
to keep your SMSF compliant.

If your fund has breached any of the rules, the auditor will report this to the Tax Office
in the form of an “auditor contravention report”.

1.2 **PROS AND CONS OF SETTING UP AN SMSF**

Pros:

- easy to establish
- personal control of your retirement savings
- you can decide where and in what to invest (some restrictions apply)
- the ability to invest in real property (even your business premises)
- the tax concessions available in superannuation, low tax (15%) in accumulation
  phase, and zero tax when in full pension phase apply equally to an SMSF, and
- more options for estate planning and benefit payments.

If you know what you are doing, an SMSF is not necessarily that hard to set up. The
following chapter will go through the step-by-step approach that must be taken to set
up the SMSF. You will need a trust deed which can be provided by a lawyer, or you can
purchase one from a provider (the Taxpayers Australia website has a number of SMSF-
related documents, including an updated SMSF trust deed, that have been produced
by Cleardocs).
The number one reason given for setting up an SMSF is the degree of control that they provide in relation to the types of investments and how the fund is run. Many people who set up an SMSF do not trust the decisions and investments made by other funds where investment decisions may be seen to be made for the benefit of the fund manager rather than the individual members.

Having control of how, where and when to invest can mean that SMSF can be more nimble. Many SMSFs weathered the global financial crisis (GFC) of the late 2000s better than other funds because they were more able to quickly change investments from shares into income products and then back out again when the economy and markets recovered. Also most retail and industry fund investments are made to cater for the accumulation phase, which may mean investments are inappropriate for pension phase. With an SMSF you are better able to tailor your investment to your circumstances.

Another attraction of SMSFs is the ability to invest in real property. Many small business people with real property place these assets in their SMSF to protect the asset and ensure their long term wealth. SMSFs are also increasingly investing in residential property (particularly through “limited recourse borrowing arrangements”, or LRBAs) as a way into the property investment market. However, the investment must conform to the investment strategy of the fund and be bought with an expectation of both income and capital growth and not merely to follow a trend.

Like all superannuation funds, an SMSF has tax-preferred status, meaning that income earned is only taxed at 15% in accumulation phase and 0% in pension phase. This makes superannuation a very tax effective form of investment.

SMSFs also provide an effective means of estate planning and are a way to ensure that benefits are paid to parties as per the desire of the members.

Cons:

- some extra costs, such as compulsory annual audit fees
- audit costs can be relatively high (as a percentage of fund size)
- more responsibility on the trustee (you)
- regulatory and compliance demands to meet
- potential investment losses
- fines for breaching trustee conditions.

While it is relatively easy to set up an SMSF, there are costs involved such as advice about setting up the fund, legal advice in relation to the trust deed, and making sure you have in place suitable arrangements or software to record the activities of your
Should you set up an SMSF?

Fund. Then there are the ongoing costs. The only mandatory costs are the annual audit and annual ATO fee.

There may also be other additional costs depending on your level of involvement. For those who don’t want to be heavily involved in the administration of the fund, you can outsource this service to professional administrators or an accountant. If you want financial advice, you will need to add the cost of a financial planner. If you want insurance there will be an additional cost for that. So while the fees can be relatively low for those who do most things themselves, the more you outsource the more costly running your fund will be.

Funds with low balances will end up paying a higher percentage of their assets as fees compared to funds with higher balances. This may make the SMSF more costly in the beginning. Also if you have complex investments the audit fee will be higher than if there are simple investments.

The biggest negative though is the higher degree of responsibility as a trustee. As an SMSF trustee there are a number of obligations on you in relation to the running of the fund and the investment decisions you make. Breach these and the ATO now has the power to take appropriate action against you. You therefore have to be willing to take on these responsibilities — if not, then an SMSF is not right for you.

One of the advantages of a retail or industry fund is that all the complex regulatory work is done by others. In an SMSF they fall on your head. Even if you outsource these tasks you will be held legally responsible.

As with any investment, things can go wrong. And if you make a bad investment decision you only have yourself to blame. If something goes wrong you do not have access to statutory protection like retail and industry funds have. A recent example saw a number of retail funds and a number of SMSFs invest in a product that was fraudulent. Those in the retail funds were protected while the SMSF members had to bear the losses themselves.

Also not everyone is an investment guru. With an industry or retail fund you can rely on experts to invest for you. In an SMSF you can only fall back on your own decisions. Do you really know what you are doing? If not it may be better to leave it to the experts.

With the ATO’s increased powers it can now fine trustees for a number of breaches where previously it could not. These fines can be costly and it is no excuse that you did not know you were breaching a requirement. It is your duty to know. If there is more than one person in the fund but one is making all the decisions, the other members can be equally liable and subject to fines for mistakes made by the member in charge.

In the end you will need to weigh up the pros and cons of setting your own fund up. Just be honest with yourself as to your own abilities to run the fund yourself.
1.3 COST OF SETTING UP AND RUNNING AN SMSF

There will be a one-off cost to launch your SMSF, but this varies greatly. An essential element will be the establishment of the SMSF’s trust deed. There are providers in the marketplace, such as Cleardocs, that can supply a trust deed and can update the trust deed should the need arise. Other providers may charge for the deed only, and yet others may include a compliance establishment package, which includes forms for minutes, death benefit nominations and so on. Shopping around will be your best option.

A recent study from actuarial firm Rice Warner (Actuaries, 2013) found the following average range of costs in setting up an SMSF.

<table>
<thead>
<tr>
<th>Fee</th>
<th>Low</th>
<th>Medium</th>
<th>High</th>
</tr>
</thead>
<tbody>
<tr>
<td>SMSF setup</td>
<td>$345</td>
<td>$485</td>
<td>$990</td>
</tr>
<tr>
<td>ASIC fee</td>
<td>$433</td>
<td>$433</td>
<td>$433</td>
</tr>
<tr>
<td>Service provider fee</td>
<td>$138</td>
<td>$367</td>
<td>$612</td>
</tr>
<tr>
<td>Total</td>
<td>$916</td>
<td>$1,285</td>
<td>$2,035</td>
</tr>
</tbody>
</table>

**Audit fees**

The average audit fee for SMSFs, according to an ATO statistical report, varies between $350 and $1,500, depending on whether or not the auditor performs other SMSF services. While these may be the average, the auditor market is as full of choice and fee structures as any other. Auditing fees can also depend on variants such as fund size or number of investments.

Then again, some auditors start at a low fee but add extras as the audit progresses. There can be additional fees if a revision of financial statements results from the audit, or a “contravention report” needs to be prepared and lodged with the ATO.

**Administration services**

Making use of a professional SMSF administration firm can suit a lot of SMSF trustees, as these firms are in a good position to pick up on any compliance issues or changing requirements, can reduce the paperwork that trustees have to deal with, and add to the efficiency with which an SMSF is run.

But such a service comes at a cost. An average accepted “ballpark” admin cost is around $2,000 annually, which works out to 1% for a $200,000 SMSF. By way of
comparison, the biggest industry fund AustralianSuper charges an administration fee of $1.50 a week plus between 0.08% and 1.02% of balances (depending on investment option) to cover investment management.

So while the average may be said to be around $2,000 (and some administration firms charge a lot more – a flat fee of $3,960 for one provider for example), there are many ways to get to that average – and you can save your SMSF some costs, depending on individual circumstances.

A Rice Warner study for ASIC found that the average cost of an administration service ranged from a low of $2,225 to a high of $7,200 (Actuaries, 2013).

If an administration firm’s charges are based on a percentage of the SMSF balance, some may reduce the percentage if the balance is larger. The charge may be a certain percentage up to $200,000 in assets, for example, but less from there up to the next asset bracket as set out by the firm.

However many accounting firms may be more used to basing fees on the number of transactions or time involved in administering the SMSF, which is important to keep in mind if you are to take a hands-on approach to your SMSF investment decision making.

The reason is the administration software many accountants or SMSF administration firms use will probably be able to get data feeds of transactions from many of the service suppliers SMSF trustees use, such as brokers, bank accounts and so on. This means that most transactions may not have to be manually entered at all, but just extracted from a data download.

Similar to the above is charging based on the number of investments held. This can be a base cost for a certain number and then a surcharge for any above that number held for the year. Again you will have to judge if your SMSF portfolio is going to have a few tried-and-true investments only, or if you, as trustee, will be actively making different investments and making various transactions from the SMSF portfolio over the year.

Then there is a flat fee option, regardless of how many investments, transactions or the size of the fund. As with any cost structure, you will have to decide if this suits your particular SMSF.

Some recent data from Rice Warner provides data on the cost of running an SMSF. Though it includes costs such as accounting and tax, which while generally provided by an accountant, these could perhaps be done by fund members at no cost.

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1 Rice Warner Actuaries – ‘Cost of operating an SMSF’ – Table 3 p5 2013
Should you set up an SMSF?

<table>
<thead>
<tr>
<th>Fee</th>
<th>Low</th>
<th>Medium</th>
<th>High</th>
</tr>
</thead>
<tbody>
<tr>
<td>Annual ASIC fee (Special Purpose Company)</td>
<td>$43</td>
<td>$43</td>
<td>$43</td>
</tr>
<tr>
<td>ATO Supervisory Levy*</td>
<td>$200</td>
<td>$200</td>
<td>$200</td>
</tr>
<tr>
<td>Audit fee</td>
<td>$300</td>
<td>$440</td>
<td>$500</td>
</tr>
<tr>
<td>Financial statements and tax return</td>
<td>$620</td>
<td>$855</td>
<td>$1,624</td>
</tr>
<tr>
<td><strong>Total accumulation</strong></td>
<td><strong>$1,163</strong></td>
<td><strong>$1,538</strong></td>
<td><strong>$2,367</strong></td>
</tr>
<tr>
<td>Fee if in pension phase</td>
<td>$250</td>
<td>$264</td>
<td>$330</td>
</tr>
<tr>
<td>Actuarial certificate</td>
<td>$180</td>
<td>$210</td>
<td>$260</td>
</tr>
<tr>
<td><strong>Total pension no certificate</strong></td>
<td><strong>$1,413</strong></td>
<td><strong>$1,802</strong></td>
<td><strong>$2,697</strong></td>
</tr>
<tr>
<td><strong>Total pension certificate</strong></td>
<td><strong>$1,593</strong></td>
<td><strong>$2,012</strong></td>
<td><strong>$2,957</strong></td>
</tr>
</tbody>
</table>


Therefore it will cost on average between $1,000 and $2,000 to set up the fund and another $1,200 to $2,400 administer it per year. The cost of running your SMSF will be significantly higher though if you use an administration service (between $2,225 to $7,200) and more if you use a financial adviser (cost will vary according to type of advice and value of assets).

The Rice Warner report (Actuaries, 2013) made the following observations:

- SMSFs with less than $100,000 in assets were not cost competitive to Australian Prudential Regulation Authority (APRA) regulated funds
- SMSFs between $100,000 and $150,000 can be competitive against retail funds as long as they take on most of the administrative roles
- SMSFs with $200,000 or more can be competitive against industry funds as long as they take on administrative tasks
- SMSFs requiring full administrative services can only compete if they have $150,000 or more in assets and use a low cost provider, and
- SMSFs with greater than $500,000 in assets tend to be the cheapest to run even where they use admin services.