

Article Information

Author: Rod Jones

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ATO self-managed super funds trustee updates

ATO Consultation on SMSF LRBAs and In-House Asset Rules

The ATO is consulting on a [draft legislative instrument](#) upon intermediary limited recourse borrowing arrangements (LRBAs).

Section 67 of the SIS Act prohibits a trustee of a regulated superannuation fund from borrowing money or maintaining an existing borrowing of money, subject to certain exceptions including where money is borrowed under an LRBA that meets the conditions set out in the SIS Act.

Different conditions had applied for LRBAs entered into between 24 September 2007 and 6 July 2010 and those arrangements entered into on or after 7 July 2010 when changes were made to rules concerning a single acquirable asset and related borrowing expenses. These conditions were previously set out in subsection 67(4A) (now repealed) and now section 67A of the SIS Act. Until July 2010 certain practices had developed that had led to prudential concerns with the borrowing arrangements by trustees of SMSFs whereby the subject of the borrowing was being replaced at the discretion of the trustee of the SMSF or the lender (see SMSFR 2012/1).

Now, under an LRBA, an SMSF's trustee may borrow money from a lender through an intermediary holding trust to acquire an asset, provided that the SMSF maintains the borrowing and the lender only has recourse, in the event of default, to the asset acquired using the borrowed money. While the borrowing remains outstanding, the asset is to be held on trust so that the trustee of the SMSF acquires a beneficial interest in that asset.

The draft determination, intends to ensure that an investment by an SMSF in a related trust that comprises an intermediary LRBA (particularly those affected between 2007 and 2010) which complies with s67A(1) of the SIS Act is excluded from being an in-house asset of the fund in the circumstances described in the instrument.

Once finalised, the determination would apply from 24 September 2007. The last day for comments is Friday, 13 March 2020.

ATO guidance updated - SMSF investment strategy requirements

The ATO has updated its website to provide [further guidance](#) to SMSF trustees upon their investment strategy, an operating standard under regulation 4.09 of the SIS Regulations.

In August 2019 the ATO had contacted some 17,700 SMSFs who the ATO had identified by their annual return data that the fund may be holding 90% or more of invested funds in one asset or a single asset class. Very frequently this will be because the fund is holding a lumpy asset like commercial real property. Many of the SMSFs the ATO contacted had also used a LRBA to acquire a single asset or asset class such as commercial or business real property. Because of this, the ATO had expressed concern that those SMSFs may not have given due consideration to the diversification and liquidity investment strategy considerations under regulation 4.09. .

Further ATO guidance on what trustees need to consider when drafting their SMSF's investment strategy, includes:

- what needs to be included in the strategy;
- any investment restrictions under the superannuation laws; and
- what happens if the ATO receives an auditor's contravention report.

What needs to be included

The SMSF investment strategy should be in writing. It should also be tailored and specific to the relevant circumstances of the members rather than a document which just repeats the words in the legislation.

Relevant circumstances may include members' ages, employment status, retirement needs and risk appetite. Best practice would dictate that the strategy should explain how the investments meet each member's retirement objectives. For example, a member parent approaching retirement will have different needs to a member child.

Restrictions on SMSF investments

The ATO notes that trustees are free to choose what type of assets to invest in, providing those investments:

- are permitted by the SMSF's trust deed;
- are not prohibited by the superannuation laws; and
- meet the sole purpose test.

For instance, trustees need to be aware of the in-house asset rules and acquisitions from related party rules. Trustees also need to be aware of the non-arm's length income rules for income tax purposes. The ATO was not shy to state that if investments breach the super laws that it can take compliance action against trustees by applying penalties and disqualify trustees. Data kept by the SMFS Segment of the ATO demonstrates increasing enforcement, education directions and a significant increase in the imposition of penalties. The ATO is asking itself, not when to apply penalties, but why not impose penalties?

What happens if the SMSF strategy is not compliant?

If the SMSF auditor identifies that the trustee of an SMSF has breached the investment strategy requirements then the trustee should fix the breach. If the strategy failed to adequately address some of the factors mentioned above, such as the risk of diversification, this can be fixed by attaching a signed and dated addendum to the strategy or a trustee minute which adequately addresses the requirements. The trustee should then give this to the auditor prior to finalisation of the audit.

The SMSF auditor will need to lodge an ACR notifying the ATO of the breach if it meets the ACR reporting criteria. For most SMSF's, this reporting criteria will be met if either:

- the auditor has identified the same breach in a previous income year and it has been repeated in the current income year; or
- it is a breach from a previous year that remains unrectified at the time of audit.

A penalty of \$4,200 (indexed each 1 July) can be applied on each individual trustee or the corporate trustee for a breach of the investment strategy requirements. The directors of a corporate trustee are jointly and severally liable to pay the penalty.