

Sole purpose companies

The advantages of a corporate SMSF trustee over individual trustees are well known, eg, greater asset protection, greater certainty in succession planning and less paperwork on death. However, SMSF clients should also consider the benefits of a sole purpose company, as opposed to a company which acts in multiple capacities (eg, trustee of a family or unit trust or trading company). These include:

- A reduced annual ASIC fee of \$40 (rather than \$212).
- Fewer administrative errors: often, the wrong TFN or ABN of a company acting in multiple capacities can be entered by, eg, a bank clerk. These errors can take some time to be noticed and might be difficult to reverse or rectify.
- Greater certainty as to asset ownership: when title to an asset such as real estate only lists the name of a company which acts in multiple capacities, it can be confusing whether the asset is held on trust for the SMSF or, eg, the family trust.

This can in turn lead to difficulties if the company in its non-SMSF role becomes insolvent or suffers financial problems and creditors incorrectly identify SMSF assets as being available to satisfy debts.

- Less scope to deal with related parties: in most States, an entity cannot contract with itself and any such contract is unenforceable. It makes no difference whether the entity is claiming to enter into the contract in different capacities (eg, in their capacity as a trading company and also in their capacity as SMSF trustee).

This means that otherwise legitimate SMSF strategies such as leasing BRP to a related entity or borrowing from a related entity to acquire an asset might therefore be invalid if the two parties are the same company. Authorities might view such arrangements as shams because they are not legally enforceable.

The costs of incorporating a new sole purpose company are generally outweighed by the above benefits in the longer term. Advisers should encourage SMSF clients to consider these before making a quick decision to re-use a company to save a small upfront cost.

SMSFs & artwork revisited

The recently released draft SMSF Ruling 2008/D5 examines 'in-house assets', including the question of

whether an artwork held in an SMSF and displayed in a member's home is an 'in-house asset'.

It is easy to become confused when reading the ATO's various pronouncements on this issue in recent years, particularly with the withdrawal of several ATO IDs. A key point to remember is that the sole purpose test and the in-house assets test are separate tests: you can pass one but fail the other. DBA distills the position below:

- An SMSF can **buy** artwork provided this is consistent with the fund's investment strategy and the sole purpose test: ID 2004/248 (withdrawn, superseded by SMSFR 2008/2).

The sole purpose test becomes an issue if the artwork provides related parties (eg, members) with benefits which are more than merely incidental to maintaining the fund for retirement purposes. Trustees should ideally seek expert advice on this aspect before purchasing artwork.

A breach of the sole purpose test can also be inferred if the SMSF breaches its own investment strategy in order to acquire the artwork (eg, if the fund liquidates all its shares to buy an artwork when its strategy requires a certain portion of fund assets to be held in shares). Maintaining and revising a sound investment strategy that is consistent with the SMSF's investments is therefore crucial.

- Displaying SMSF-owned artwork in a member's residence **for no fee** or a less than commercial fee will generally indicate a breach of the sole purpose test: ID 2004/249 (withdrawn, superseded by SMSFR 2008/2).
- Displaying SMSF-owned artwork in a member's residence **for no fee** or a less than commercial fee also breaches the requirement to deal with related parties at arm's length: ID 2004/251.
- Displaying artwork in a member's residence **is always an in-house asset** (other than certain pre-1999 leases): ID 2004/250 (withdrawn, superseded by SMSFR 2008/2 and confirmed in SMSFR 2008/D5). This is the case regardless of whether a commercial fee is charged or a formal lease arrangement is in place.

However, recall that in-house assets up to the 5% limit are permitted. It is therefore possible to lease artwork to related parties for a fee, within limits.

In other words, a SMSF's investment in artwork is permitted if (1) the initial purchase of the artwork is consistent with the fund's investment strategy and

sole purpose test, (2) if the leasing fee charged by the SMSF trustee to the member is commercial and (3) provided the lease (and any other in-house asset of the fund) does not exceed the 5% limit of the fund's total assets.

Trustees should seek advice before implementing an artwork strategy to ensure they do not breach any of the rules outlined above. DBA can assist with advice and artwork leasing and related documentation.

Guaranteed pensions in a downward market?

Members with Defined Benefit Pensions (DBPs) should consider whether their guaranteed income stream can be met in light of current market conditions. Many funds may now be facing a deficit in this respect. Unless the minimum pension is paid each period, the SIS regulations might be breached, resulting in potential penalties. The DBP's assets test exempt status might also be jeopardised unless carefully managed.

Expert advice should be obtained, particularly for those who wish to keep their DBPs on foot. Depending on the member's particular circumstances, this may be an opportune time to restructure these pensions and consider the possibility of a Market Linked Pension or Account-Based Pension.

DBA can assist with advice and documentation, including documents to convert a DBP to an MLP.

New Guidance Statement for SMSF auditors

The Auditing and Assurance Standards Board (AUASB) has recently developed Guidance Statement GS 009 to assist with auditing of SMSFs. This includes a checklist for auditing an SMSF deed, setting out numerous provisions auditors should address in their review.

DBA has reviewed its own SMSF deed rigorously to ensure it meets with the guidelines and confirms that it meets each of the suggested requirements. Those using other deeds should undertake their own audit and DBA can assist to review and provide feedback.

Advisers looking to establish a new SMSF or upgrade the deed of an existing SMSF should not be guided by price alone. In making a recommendation to their clients as to an appropriate SMSF deed, the adviser's recommendation should also take into account:

- The quality of the deed and the level of technical service and support offered.
- The process behind the preparation of the new deed or deed upgrade, eg, whether a qualified lawyer signs off on every fund's deed.
- The professional indemnity insurance (if any) held by the deed supplier. Many suppliers do not hold PI, or void their PI by, eg, undertaking legal work they are not qualified to perform.

NEW Geared Unit Trust Kit

The Geared Unit Trust Kit provides valuable guidance and practical tools for SMSFs who invested in a pre-August 1999 geared unit trust. SMSF trustees and advisers must ensure they understand this area and act promptly to ensure the SMSF's investment potential is maximised in the lead up to the 30 June 2009 deadline.

The Kit outlines options for dealing with the 30 June 2009 deadline and describes how further investments can be made before this date. The Kit includes a detailed explanatory Memo, sample SMSF and unit trust resolutions and useful forms to assist advisers. The Kit is \$550 incl. GST. To order simply return the form below.

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Send or fax to DBA Butler Pty Ltd. Please do not send any money as you will be invoiced upon receipt of documentation.

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