DBA Lawyers

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Final SMSF Cooper Recommendations

Some key and somewhat controversial changes in the final Cooper SMSF report issued this Monday are summarised below. Note that our June News covered Cooper's preliminary findings on SMSFs.

Final Cooper Report

SMSFs not to be subject to the SCT

This is a back flip from the preliminary recommendation that certain SMSF death benefit disputes be subject to the Superannuation Complaints Tribunal. (All disputes involving SMSFs are currently excluded from the SCT.) The final report rejected extending the SCT's jurisdiction to SMSFs as this would have resulted in cross subsidisation by the majority of SMSFs paying an extra levy for the relatively small proportion that were expected to be involved in such a dispute. The review panel also considered that most SMSF disputes would probably end up in the courts in any event.

This leaves SMSFs in the court system, which can result in substantial time and costs to resolve a dispute. Hence, ongoing planning especially for death and other potential disputes such as divorce and separation is needed to minimise uncertainty.

No more in-house assets

Currently, SMSF trustees may have up to 5% of total fund assets invested in in-house assets (eg, a loan to or an investment in a related party of a fund). The final report confirms the prior recommendation of axing this exception so that no SMSF assets whatsoever may be invested in in-house assets.

Moreover — and what came somewhat as a surprise — SMSF trustees will only have five years to dispose of their in-house assets (rather than the 10 years as proposed in the preliminary review).

However, another option has been recommended to overcome the concern that some SMSFs may argue that 5 years is far too short — is for an SMSF to convert to a Small APRA Fund ('SAF'). Converting to an SAF may increase operating costs but would permit the fund to retain its 5% in-house asset limit.

Fortunately, the final report does not propose to unwind the previous 1999 grandfathering arrangements, eg, SMSFs with pre-1999 unit trusts will be able to retain their investments indefinitely.

No more collectables and personal use assets

The final report also confirms the ban on all new acquisitions of collectable and personal use assets by SMSFs and provides a five year period for SMSF trustees to dispose of any such assets they currently own.

SMSFs are also given the opportunity to convert to an SAF if they wish to retain their existing collectable or personal use assets.

Borrowing is here to stay (at least for two years)

The final report confirms that the SMSF borrowing provisions and the recently announced consumer protection provisions be reviewed in two years to ensure that borrowing does not become a 'significant focus' of SMSFs. This is good news as SMSF borrowings are here to stay for the immediate future.

SMSF advice to be licensed

Advisers to obtain an Australian Financial Services Licence to recommend the establishment of an SMSF. The current exemption for accountants in relation to SMSFs should be removed.

If implemented, this proposal will require many more accountants to be licensed to provide SMSF recommendations.

Other recommendations

There are a range of other recommendations in the final report that will increase compliance and reporting including:

- Independent valuations required for related party transactions as well as assets to be valued at net market value for financial statement purposes.
- The ATO to be given power to issue directions to trustees requiring rectification of any breach and requiring education for recalcitrant trustees.
- The ATO to be given power to issue binding rulings in relation to SMSFs.
- ASIC auditor independence standards to be prescribed which will result in full independence of annual SMSF auditors. Moreover, ASIC is to become the SMSF auditor registration body and the ATO to police auditors with exchange of information between ASIC and the ATO.

Recent changes impacting SMSF deeds

There have been numerous recent and ongoing developments that impact SMSF deeds. Here is a brief summary of some of these which you should keep an eye on.

Minimum pension payments

The extension to the 50% reduction of the minimum pension payments for 2010–11 that applies to account-based pensions, transition to retirement income streams and market linked pensions (aka term allocated pensions).

Note that this change was only recently announced and many SMSF deeds only cater for the 2008–09 and the 2009–10 financial years that the reduction initially applied to due to the global financial crisis and many illiquid investments.

While reviewing the pension provisions you should also be on the look out for the following powers:

- the ability to provide an account based pension
- the ability to provide a transition to retirement income stream and
- the ability to do internal roll-overs and to segregate pension assets or operate on an unsegregated basis.

Borrowing power

Expanded borrowing powers will soon be required in view of the proposed changes that will allow refinancing and, in the case of certain securities, replacement assets as proposed in ss 67A and 67B of the *Superannuation Industry (Supervision) Act 1993* (Cth).

Borrowings that occur after the date of the proposed borrowing changes will be subject to the new rules. Borrowings prior to that time will be subject to the current requirements in section 67(4A).

Given that banks are strict in requiring extensive powers to borrow, to enable a custodian to own and secure the assets being acquired and related powers, you should ensure that if the SMSF intends to borrow in the near future that the deed has appropriate provisions.

Estate and succession planning

Does the deed provide for binding death benefit nominations ('BDBNs') that last indefinitely or is the deed subject to a three year limit? Some deeds also now allow mechanisms to effectively lock in SMSF trustee succession and death benefit instructions, including express power for an enduring power of attorney to implement a BDBN on behalf of a member.

You should review your deed to make sure the succession and estate planning provisions are appropriate especially in view of the final Cooper Report recommendation above.

Sundry provisions

Numerous other changes include:

- an expanded general deeming provision that is consistent with that recommended in the Cooper report.
- There is power to release money for the payment of excess contributions tax (other than satisfying a condition of release).

DBA's 2010–11 SMSF deed

Naturally, the latest DBA Lawyers deed has all the above covered.

Keep SMSF trust deeds up to date

Note that ongoing changes are being made to tax and super rules and further changes are expected following the implementation of the Henry Review, the final Cooper Report, the 2010 Federal Budget and other reform measures currently in the pipeline. Moreover the new borrowing rules are currently before Parliament. The Annual Update Service is a cost effective solution to keep your SMSF deeds current and to drive efficiencies in your firm having one deed to refer to for all funds on the service for the entire financial year. For more information visit www.smsf.com.au.

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