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NEWS

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30 June 2009: what happens next for pre-1999 unit trusts?

SMSF trustees with pre-1999 investments in related unit trusts should now be mindful that any further reinvestment after the deadline of 30 June 2009 will generally constitute an in-house asset.

Our readers will recall our April 2009 news which discussed the deadline in detail. More recently, the ATO was asked whether it would show any leniency towards SMSF trustees who reinvest their entitlement for the 2008–09 financial year after 30 June 2009 (given that accounts are typically prepared after year end). The ATO confirmed that it did not consider there was any scope to adopt this relaxed approach under the transitional rules (refer to ss 71D and 71E of SISA).

Opportunities may still exist post 30 June 2009!

Despite the strict deadline, some SMSFs may have opportunities to undertake further investment.

Many unit trusts that were formerly geared have now repaid their borrowings and might have become 'non-geared' unit trusts. In this case, the exception for non-geared trusts could apply, meaning that further reinvestment by an SMSF even after 30 June 2009 could be exempt from being an in-house asset. (Those unit trusts that still have outstanding liabilities could eventually become non-geared and the same would apply at that time.)

SMSF trustees and advisers should note that the SIS Regulations contain numerous strict requirements in order for a trust to meet that exception. The term 'non-geared unit trust' can be misleading because the requirement that there are no borrowings is just one of many requirements. SMSF trustees should seek advice before reinvesting after 30 June 2009 to get the tick of approval that the trust is within the safe harbour.

It is also important to be aware that once a unit trust becomes a non-geared trust, it must generally stay a non-geared trust. Broadly speaking, if a unit trust ceases to meet all of the requirements, it cannot simply rectify the breach to come back within the exception — SMSF trustees will generally be required to offload their post-30 June 2009 investments in the trust and can never again rely on the non-geared exemption to undertake any further investment in that trust. (See SMSFD 2008/1.)

However, with careful planning it will be possible for some SMSF trustees to undertake investment and advisers should not overlook this possibility for their SMSF clients.

Unpaid entitlements: ATO concedes some ground but SMSFs must remain vigilant

The ATO has finalised its contentious draft ruling on unpaid present entitlements ('UPEs') owing from related unit trusts to SMSFs. See SMSFR 2009/3.

Essentially, the ATO is concerned that in some circumstances where a UPE is owing to an SMSF and it is not called on, the UPE could constitute a 'loan' from the SMSF to the related trust. This is because the term 'loan' in the SISA is defined broadly and includes the provision of any form of financial accommodation (see s 10 of SISA).

The ruling is of major significance for SMSF trustees and advisers because the consequences of a UPE being treated as a 'loan' are potentially serious:

- A loan to a related party (eg, a related unit trust) is typically an in-house asset. In practice, many SMSFs in this position would breach the 5% cap on in-house assets, particularly if there are many years of UPEs owing to an SMSF trustee.
- UPEs that are not called upon may also call into question compliance with other laws such as the sole purpose test and the requirement to only invest with related parties on arm's length terms.
- If an SMSF trustee has been relying on the 'non-geared' unit trust exemption in order for its units in a related trust to be exempted from being in-house assets, the trust could cease to be 'non-geared' as it could now be considered to have a borrowing. This could mean that the SMSF has two kinds of in-house assets — both units in the trust and the 'loan' amount to the trust (ie, UPE).

Fortunately, the ATO has revised its earlier implied position that a UPE which is not called on within 30 days of the end of a financial year could be a 'loan'. The ATO now agrees that the amount of a UPE is unlikely to be known in many cases for some months (ie, not until the accounts for the financial year have been prepared). However, it states that this amount must be known by the time the entities lodge their tax returns and thus it appears that the ATO could take a tough stance on any UPEs that remain uncalled for after that time.

Trustees and advisers should be alert to this issue and address any outstanding UPEs owing from a related trust to an SMSF.

Annual Update Service

Keeping SMSF governing rules up-to-date

DBA Lawyers offers an 'Annual Update Service' to ensure SMSF governing rules are kept up-to-date.

Every 1 July the service provides cutting edge governing rules to every SMSF that subscribes. Naturally, the most recent update occurred on 1 July 2009. Once subscribing SMSFs have paid for their 2009–10 subscription, they can access their update at www.smsf.com.au.

Advantages

- *Compliance* — governing rules are kept up-to-date and comply with all the latest laws and requirements. With the ATO boosting SMSF audits, this is more important than ever!
- *Administrative ease for advisers* — all SMSF clients using the Annual Update Service have the same governing rules.
- *Rules available online 24/7* — no more trying to hunt down copies of governing rules from clients and other advisers. Simply log on to our secure website and access the governing rules.
- *Maximum convenience* — no more 'ad hoc' updates.

How the Annual Update Service works

- Upon subscribing, an SMSF is given a secure homepage (log in at www.smsf.com.au).
- Every 1 July:
  - New rules are added to the SMSF's homepage. This by itself has no legal effect.
  - Trustee resolutions adopting the new rules are added to the SMSF's homepage.
  - The resolutions are printed and executed. Upon execution, the new rules are adopted by the SMSF.

Find out more

To find out more, visit www.smsf.com.au or call or email Olivera Ivcovici (tel: 03 9682 0903 or email: oivcovici@dbalawyers.com.au).

Subscribe

To join the Annual Update Service, an SMSF's governing rules (deed) must first be updated (see www.dbalawyers.com.au/index.php?p=smsfdeeds).

When completing the order form to update the deed, also tick the box indicating that you wish to subscribe to the Annual Update Service.

Anti-Detriment Memo

This is a must read for all SMSF advisers, especially those with an interest in SMSF estate planning. It contains the information to become an expert in anti-detriment deductions and is the most detailed explanation ever written on the topic. It includes detailed commentary on the law, practical guidance when actually claiming such a deduction, 15+ detailed examples and explanations, the latest from the regulators, template minutes to implement and invaluable tips that come from our years of hands-on experience.

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I want to order the Anti-Detriment Memo ($550 incl GST). I acknowledge that I may only distribute this Memo to staff of my office. If I want to distribute this Memo to anyone else (including staff at other offices within my organisation) I acknowledge that further copies of the Memo must be purchased. Volume discounts available.

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