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Welcome to the first edition of TP SuperNews. In this edition we touch on recent developments involving superannuation and in particular the self managed super fund (SMSF) sector.

Trustee education

In a recent speech, the minister for Superannuation and Corporate Law, Senator Nick Sherry outlined the government's intentions regarding superannuation reform, in particular relating to the SMSF sector. The biggest issue at the moment appears to be trustee education. A recent survey conducted by the Australian Tax Office (ATO) found that 30% of new trustees could not explain the sole purpose test and 15% did not have an investment strategy. Given the generous tax concessions associated with SMSFs and the fact it is now the fastest growing sector of the superannuation industry, this

has sparked significant interest in government ranks. It appears that the Senator is looking to introduce a form of mandatory trustee education for SMSF trustees to make them better equipped to run their own SMSF. Whether this applies to new trustees only or existing trustees as well, remains to be seen.

Consequence of non-compliance

Whilst most trustees are aware of their responsibilities, there are still those that cannot or will not follow the rules associated with running a SMSF. According to the ATO the top 3 contraventions relating to SMSFs include loans made to a relative or a member; breach of the in-house asset rules; and assets not being in the name of the fund.

In the past, the ATO have taken more of an educational approach to breaches,

rather than the big stick approach, however this is now changing. So far this year the ATO have made 60 funds non-complying as a result of the breaches outlined above, compared with only 24 last year. In addition to making a fund non-complying, the ATO is also looking at more frequently disqualifying or prosecuting trustees directly.

We would like to remind clients that being made non-complying results in a 'penalty tax' of 46.5% being applied to the fund's assets as well as income. If you feel you have done something wrong, or need further help understanding your responsibilities as trustees, please contact Damian or Winsome so we can help. Our experience in dealing with the ATO in the past has shown that the earlier problems are picked up and rectified the more favourable the ATO will look upon the trustees of the fund.

"30% of new trustees could not explain the sole purpose test"

SMSF investing in pre-1999 unit trusts

On 11 August 1999 the rules relating to SMSFs investing in related unit trusts changed significantly. Transitional rules were introduced to allow a SMSF to continue to invest in a pre-1999 unit trust for 10 years, without the investment being deemed an in-house asset. **These transitional rules cease to apply after 30 June 2009.**

In order to take full advantage of the transitional rules the trustees may wish to maximise the investment in the trust prior to 30 June 2009 via:

1. If there are partly paid units, they may be paid up fully.

What happens to the Pre-1999 Unit Trusts after 30 June 2009?

There is a common misconception that these trusts need to be wound up. This is not the case. Pre-1999 trusts do not have to be wound up and may maintain existing borrowings, and even new borrowings after 30 June 2009. There is no restriction on the level of borrowing undertaken in the trust itself. However as from 1 July 2009 the trustee of the unit trust will be required to distribute all income to the SMSF unit holder by making a cash payment. As such this may limit the trust's ability to repay existing loans and it may wish to convert existing loans to interest only or ensure that capital repayments are less than non-cash deductions in order for the trust to be able to pay the

Same sex & de facto couples

The Commonwealth Government recently passed the *Same-Sex Relationships (Equal Treatment in Commonwealth Laws—General Law Reform) Act 2008* to recognise same-sex couples. **From 1 July 2009**, taxation laws will be reformed to allow same-sex couples to access the same tax benefits and concessions that are available to married and opposite-sex de facto couples. From a superannuation perspective a same-sex de facto partner could only receive a death benefit from a superannuation fund if he or she qualified as a financial dependant or interdependent. The reforms expand the definition of 'spouse' to include

“the unit trust will be required to distribute all income to the SMSF unit holder by making a cash payment”

2. If the fund has re-invested distributions in the past, the trustees may wish to make an interim distribution for the 2009 year and reinvest the profits prior to midnight 30 June 2009. (The ATO does not allow for the re-investment of the 2009 profits after the 30 June 2009 within the transitional rules.)
3. If an election was made prior to 23 December 1999 to allow the fund to invest up to the level of debt in the Trust at 11 August 1999, then the fund should try to invest up to that amount before 30 June 2009.

The first two options can be used in conjunction with each other, however the election in item 3 excludes the use of the other two options.

distributions each year. Another option is to admit additional unit holders into the trust and use their cash contribution to help reduce the debt, as the SMSF will no longer be able to do so.

If the trust cannot make a cash distribution to the SMSF beneficiary, and the beneficiary loan extends for a period of 12 months or more, it will be deemed an in-house asset. Similarly any additional investment by the Fund in the related trust after 30 June 2009 will be deemed an in-house asset and is restricted to 5% of the Funds assets.

Should you wish to explore these options further, please contact Damian or Winsome of this office.

same-sex de facto partners, and the definition of 'child' to include most children in same-sex families. Same-sex de facto partners will now also be eligible for the superannuation tax offset if they make an after-tax superannuation contribution on behalf of their low-income earning partner.

Instalment warrants

Gearing within a SMSF has changed the SMSF landscape dramatically. One thing SMSFs cannot be called is boring. They are a dynamic vehicle with numerous and constantly changing opportunities. Since we raised the gearing issue in our last newsletter, we have fielded numerous queries with regards the types of assets that can be geared and how to go about it. This newsletter will

touch on gearing the two most common assets in SMSFs – Real estate and shares. No matter which is your preferred investment class, consideration must be given to important factors such as your fund's investment strategy, whether your fund is in accumulation mode or pension mode, the age and expected retirement date of the members.

Real Estate

SMSFs can purchase residential and commercial property with loans of up to 70% of the value of the property without affecting your ability to borrow outside superannuation. Due to the tax benefits associated with superannuation funds, this strategy could make your net position after 20 years, up to 35% better off than if you continue growing a property portfolio outside super.

Besides being the best asset protection vehicle, super is now also the best tax effective vehicle for holding property for the long term. For example, trustees can take advantage of existing negative gearing strategies in super, **release equity in commercial property already owned outside super** and increase the amount accumulated in super significantly which when coupled with the tax free status upon retiring after 60, makes such a transaction quite attractive.

We stress however that you shouldn't undertake this strategy on your own without expert help. Not only does it involve the establishment of a bare trust, and ensuring your trust deed permits such a strategy, the SMSF loans are linked to superannuation legislation which normal loans are not subject to. The ATO closely monitor such transactions and given our comments regarding non-compliance earlier, it is important to get it right from the outset.

“this strategy could make your net position after 20 years, up to 35% better off”

Superannuation and tax legislation dictates certain characteristics that these loans must have and therefore the documentation for them is very different to normal loans.

Given the complex nature of such transactions, we are now in a position to offer our clients access to one of the industry's very few experts on SMSF finance. Jenny New has joined forces with our firm to provide you with a total solution for your property growth strategies. Jenny can source the best loans available on the market at the moment suited to SMSF gearing and having worked with and educated financial planners and accountants in this space since the change in legislation in September 2007, she is well placed to guide you through the borrowing process.

If you have over \$200,000 in super you may qualify to undertake such a gearing strategy. Call our office to speak to Jenny and discuss how she can help you grow your wealth faster in your SMSF.

Shares

If shares rather than property are your preferred asset class in your SMSF then there are various products on the market that allow you to acquire shares using a gearing facility also. Macquarie Equity Lever is one such product. An Equity Lever product allows a fund to acquire, as an example, \$20,000 worth of CBA shares under an instalment receipt arrangement. The fund can choose to use \$10,000 of its own cash and have \$10,000 loaned by Macquarie. The loan of \$10,000 is a non recourse loan which means that in the event of default, the issuer (in this case Macquarie) can only

claim back the underlying securities as repayment of the loan, regardless of value, not any other assets of the fund. The fund also receives full dividend entitlements and any capital gains (or losses) based on the instalment receipt.

Interest can be either fixed or variable depending on your preference and the loan term is typically 10 years with a minimal initial investment of \$20,000. If you are interested in gearing your SMSF to acquire listed shares, please contact Andrew Crews of this office who will be able to model various options for you.

Investment market commentary

We have spoken to many clients over the recent months and there is obviously significant concern regarding the state of the investment markets (and the wider economy) at the moment. Whilst the ASX has begun some sort of a rally in recent weeks, it remains to be seen if it has any driving force behind it, or it is simply a false run.

Opinions as to whether Australia is in a recession (technically or not) have been offered to the point of exhaustion by various media commentators, politicians and the like. We thought it prudent to remind our clients of one of the most important fundamental rules of investing; and that is the old saying - 'Time in the market; not timing the market'. The years have shown that the share market goes through rapid periods of growth and then periods of decline. Investors generally know these times as bull and bear markets. Since November 2007, the ASX All Ordinaries Index has

fallen by 53.2% (Source: Iress). Fuelled by speculation and warnings of doomsday scenarios, investors are questioning if their resilience to the bear market will be rewarded.

Yet despite of all of this, a bear market can be an opportune time to take advantage of deflated prices in order to further diversify a portfolio.

Whilst past performance doesn't indicate future performance, the history of bear markets shows that over the longer term the share market has always rebounded. By remaining focused on the long term and diversifying a portfolio to help cushion the impact of a sharp market downturn, investors have been successful in riding out market volatility.

Share bear markets in Australian shares	Months to low	% fall	Months after low to make new high	% gain in first 12 months after low
Sep 1960 - Nov 1960	2	-23.2	33	+12
Feb 1964 - June 1965	16	-20.4	25	+9
Jan 1970 - Nov 1971	22	-39.0	94	+52
Jan 1973 - Sep 1974	20	-59.3	59	+51
Nov 1980 - Jul 1982	32	-40.6	17	+39
Sep 1987 - Nov 1987	2	-50.1	75	+35
Aug 1989 - Jan 1991	15	-32.4	30	+39
Feb 1994 - Feb 1995	12	-21.7	20	+25
Mar 2002 - Mar 2003	12	-22.3	15	+27
Nov 2007 - ?	16*	-53.2*	?	?
Average	15	-34	41	+32

* Current position

No one can pick when a market rises and when it falls but it is always important to note that as an investor it is not about **'timing the market, but spending time in the market'**.

Next Edition

We will look at the 2009 Federal budget proposals, the superannuation thresholds for the 2009 and 2010 financial years and impact of pensions on the Commonwealth Senior's Health Card.

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