Collins Financial Planning Pty Ltd

AFSL 227250

Self Managed Superannuation Fund

A Quick Guide ©

We appreciated the assistance of ANZ Self managed Super in the preparation of this booklet.

Are you ready to take full control over your super?

Self managed super funds have become a popular way for Australians to build their retirement savings.

In fact they're now the fastest growing part of the superannuation market, with more than one million of us being members of an SMSF.

Thousands of SMSF are being established every year and, with more than half a billion now invested, they represent about one-third of Australian's total superannuation savings.

According to Paul Kelly of Collins & Co. Accountants the popularity of SMSFs can largely be attributed to the fact that more people are deciding they want to have greater control over their investments.

"People want the flexibility to make their own decisions about what to invest in and the ability to change direction quickly, if needed," says Kelly.

Technology is another factor that has contributed to the growth in self managed super funds. For example, Collins Financial Planning can consolidate portfolios and give fund members instant access to the performance of their investments anywhere and at anytime.

Technology has also simplified the management of ongoing and changing SMSF compliance tasks.

"Members of SMSFs have annual reporting obligations and other rules they need to stay on top of, and these rules don't apply to the average retail super fund member," Kelly said.

If you think a self managed super fund could be right for you, or if you're simply interested in understanding a bit more about them, then we hope this booklet will be of help.

For further assistance please contact us so that we can talk to you about your personal financial situation and your future goals and will help you decide whether an SMSF is suitable for you. This will involve a discussion about the benefits and challenges of running your own super fund, including set-up and operating costs and ways to make it easier than you might think.

Are you ready to manage your own superannuation? Find out yourself by booking an appointment with Mark Ducret on 03 9680 1000, or you can send an email to financialplanning@collinsco.com.au.

Self-Managed Super Funds—Introduction

Today, SMSFs represent about a third of all the money invested in all Australian superannuation funds. And there are more than half a million SMSFs in Australia, representing more than one million individuals members.*

Why are they so popular?

The popularity of SMSFs can be generally be put down to the greater control and flexibility they offer. Here are some key advantages:

- Investment control: the members/trustees can choose their own fund investments, including shares, property, cash and many others (within legislative limits).
- Flexibility: trustees can make their own decisions as a result of changing market movements and options for retirement income streams.
- Family first: a SMSF is a true inter-generational wealth accumulation and wealth transfer vehicle. There is no legal time limit on how long a SMSF can last—it can keep going for generations.
- Fee savings: the SMSF fee structure may deliver substantial savings when compared to other retail funds.
- Creditor protection: a member's fund assets are normally protected from creditors in the event of bankruptcy.
- Tax effective: generally super lump sums are tax-free to members who are over 60, which is a huge benefit during their retirement, especially compared to other non-super investment structures.

Will an SMSF suit you?

Running an SMSF is not for everyone. There are trustees responsibility and time commitment factors you should consider.

As trustee, you'll need to design, implement and actively monitor an investment strategy that:

- Protects members' retirement benefits;
- Minimizes the risk of irresponsible/incompetent investments; and
- Meets your stated SMSF investment objective.

Your financial adviser can help you with this part, but you'll need to be ready and able to take on board the following things by yourself:

- Time commitment: Running an SMSF can be time-consuming for trustees, this can be aided if you choose to use a specialist, daily-managed administration service.
- Risk of penalties: Non-compliance with legislation and rules can mean significant tax penalties on the fund and potential prosecution, for extreme breaches.
- Balancing act: Ongoing costs to operate an SMSF e.g. mandatory annual audit costs, can be uneconomic for members with balances less than $200,000.
- More responsibility: The ultimate legal responsibility rests with you and any other trustees in your fund, even if assistance has been sought from other professionals e.g. auditors or registered tax agents.
- No 'captain's call': All members need to agree on investment decision, if you take action outside of that agreed by all parties, you risk being sued by your fellow trustees.
- For love, not money: As a trustee you can't be paid for running your SMSF, nor can you be an employee of another trustee (unless they're family).

What does it cost to run?

It is important you to take the time to understand the cost incurred to operating your SMSF in order to ensure it is economically viable to run.

These are generally two types of costs-set up costs and ongoing operating expenses (including your personal time).

1. Set-up costs

These can vary quite a bit, depending upon how you go about it. You'll pay a bit more to set-up an SMSF if you also seek financial advice and/or a financial plan, but this is a smart move, especially if you're a relatively inexperienced investor.
A self-managed super fund (SMSF) allows up to four people to pool their super and take full control and responsibility for managing it as trustees. The sole purpose of the SMSF is to provide benefits to its members on their retirement.

2. Operating expenses

According to the ATO, around two-thirds of SMSFs have an estimated operating expense ratio of 1% of fund assets or less.*
So on a $500,000 account balance, an expense ratio of 1% equates to $5,000 in annual fees. Many operating expenses are fixed— and mandatory—for example, annual audits, preparation of accounts and the ATO supervisory levy. Of course, as a fund balance grows, these fixed expenses become a lesser percentage with less impact.

3. Personal time commitment

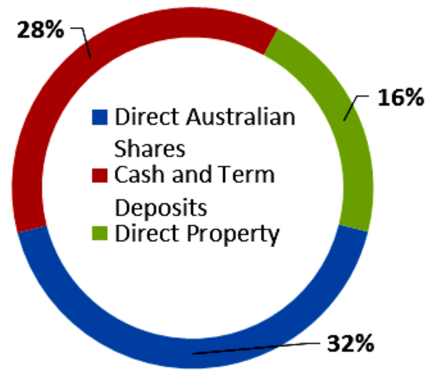
Of course, you'll also need to factor in the cost of your personal time in managing the fund. This can vary, depending upon how much of the management you outsource to professionals and how much investment research and active investment management you want to do.

Time commitment can vary from a few hours per month, up to a number of days per month, depending on how involved you want to be with investment and other decisions that need to be made for your fund.

What can an SMSF invest in?

The three most popular investment classes for SMSF trustees are direct shares, cash and direst property.

As of December 2014, these three asset categories represented 76% of all SMSF assets.*



The Rules

SMSF investments must be for the 'sole purpose' of providing retirement benefits for the members of the fund.
Members, relatives or associates of the trustees must not gain any immediate benefit from the fund's assets or activities.
For example, any property owned by the fund cannot be used by the members or their families, even if rented out at market rental, unless the property is less than 5% of the total fund assets.

Other rules include:

- SMSFs can only borrow money in limited circumstances;
- SMSFs must limit investments in, or loans to, 'related parties' to 5% of the market value of the fund; and
- Generally, SMSFs cannot buy assets from a member, or relative or associate of a member, except in limited circumstances such as with business real property, listed securities and manages funds.

However, SMSFs have the added benefit of being able to invest in all major asset classes offered by regular super funds— with the addition of direct real property and personal collectibles.

How can a financial adviser help?

Setting up your SMSF properly is critical. If you get this wrong, it can create a lot of issues down the track that can be expensive to fix.
An SMSF-accredited financial adviser can help you chart the most appropriate course of action with your SMSF, from how to best structure your SMSF to the most appropriate investment and wealth protection strategies for you and your fellow SMSF members.

**self managed super funds: A statistical overview 2012-13, Australian Taxation Office.*

Insurance and your SMSF

You can purchase insurance within your SMSF and more importantly, the super laws require trustees to consider the insurance needs of members when drafting and reviewing the fund's investment strategy.

Considering the insurance needs of SMSF members doesn't mean you must purchase insurance within your SMSF.

Also it's important to note that life insurances policies held outside of a super fund cannot be transferred into an SMSF. Although, some providers will allow you to cancel your existing policy and then re-establish it again in your SMSF without impacting you level of cover.

Recent insurance rules changes

On 1 July 2014, regulations were introduced requiring all new insurance policies issued to SMSFs be consistent with the Superannuation Industry (Supervision) regulations conditions of release:

The upshot of this is that you can hold insurance policies within your SMSF for:

- Life insurance;
- TPD insurance with an Any Occupation definition; and
- Standard Income Protection insurance policies.

It also means your SMSF can't purchase or hold the following insurance policies (unless you are increasing cover that was already held prior to 1 July 2014):

- Own Occupation TPD;
- Trauma cover; and
- Comprehensive Income Protection

Although Life, Any Occupation TPD and Standard Income Protection policies can be purchased by SMSFs, the cover will have some restrictions compared to the same cover purchased outside super.

SMSF Life Insurance

Life insurance policies can be purchased by an SMSF for the members of the fund and the premiums will be deductible expenses to the fund.

Key things to consider:

- The SMSF version of the life insurance policy will only cover the core benefits of death and terminal illness.
- The insurance company will pay the proceeds of the policy directly to the fund and the trustees then have the discretion to decide on the distribution of the funds in accordance with the trust deed.
- Payouts from SMSFs may be subject to tax under certain circumstances, unlike policies outside super where payouts are generally tax-free.

SMSF TPD insurance (Any Occupation)

Any Occupation TPD policies can be purchased by an SMSF for the members of the fund and the premiums will usually be deductible expenses to the fund.

More information

There are lots of advantages to managing your super and retirement savings via a self-managed super fund, but there can be complicated areas and considerations that are best addressed with SMSF-specialist advice. So please talk to your SMSF financial adviser for specific information related to your needs.

SMSF What they can and can't invest in?

SMSFs have become very popular, with more than one million members now representing the fastest growing segment of Australia's superannuation market.

The main reason for the popularity of SMSFs is the unrivalled investment flexibility and control they offer members.

However, there are various compliance requirements to running an SMSF and some common pitfalls to avoid, especially when it comes to what you can and can't invest in. As with all superannuation members, SMSF trustees should regularly review their asset allocations to ensure their portfolio remains appropriately diversified in line with the fund's investing strategy.

Trustees should also consider how much is held in cash (or other liquid assets) so the fund can meet its liquidity obligations, e.g. fees and pension payments.

The investment basics

SMSF investments must be for the 'sole purpose' of providing retirement benefits for the members of the fund. This means that members, relatives or associates of the trustees must not gain any immediate benefit from the fund's assets or activities.

For example, any property owned by the fund cannot be used by the members or their families, even if rented out at market rates, unless the property is less than 5% of the total fund assets.

Other rules dictate that SMSFs:

- Can only borrow money where the loan is on a limited recourse basis;
- Must limit investments in, or loans, to 'related parties' to 5% of the market value of the fund; and
- Generally cannot buy assets from a member, or a relative or associates of a member, except for business real property, listed securities and managed funds.

What can SMSFs invest in?

In Australia, the three most popular investment classes for SMSF are direct shares, cash and direct property.

As at December 214, these three asset categories represented about 76% of all SMSF assets.*
At this point in time, SMSFs held around 32% of fund assets in direct Australian shares, 28% in cash and term deposits, and 16% in direct property.*

Here's a quick overview of some of the assets SMSF can invest in:

- Cash management accounts
- Term deposits
- Managed funds (Australian and international)
- Listed Australian shares
- Listed unit trust
- Listed investment companies
- Overseas listed shares
- Residential property
- Commercial property
- Industrial property
- Property purchased with borrowed funds (limited recourse borrowing)
- Property partnership with non-related parties
- Shares in unrelated private companies
- Artwork and collectables

SMSFs—investing in property

As at December 2014, property represents around 16% of all SMSF assets.*

This short guide focuses on some insights into property investing and SMSFs.

Property investing

SMSFs can invest in the following types of real property:

- Commercial property, this may include a factory, warehouse, business leased premises, a doctor's surgery; and
- Residential property, such as units, semis and houses.

The rules

You can only buy property through your SMSF if you comply with certain rules, including:

- Not acquiring the property from a related party of a member;
- Not being lived in by a fund member or any fund members' related parties; and
- Not being rented by a fund member or any fund members' related parties.

However, an SMSF can purchase business premises (also known as business real property) from its own members (or related parties of the members), allowing them to pay rent directly to their SMSF at the market rate.

SMSFs are forbidden from investing in the family home or a holiday home for personal use, but they are able to invest in investment properties—as long as the property is only used for investment purposes. This means fund members can't stay in the property or rent it out to family members.

The property should generally be managed by a real estate agent to satisfy the sole purpose test regulations, unless you can show evidence that you are managing it professionally yourself.

Borrowing for property

Borrowing or gearing you super into property must be done under very strict conditions called a 'limited recourse borrowing arrangement'.

If gearing is involved in the purchase of a property, a 'holding trust' (or custodial trust) must be set up to hold the new asset until it's no longer required as security. This arrangement requires a holding trust to be set up for each asset purchased, for example a residential or commercial property.

Before committing to a geared property investment you should assess whether the investments is consistent with the investment strategy and risk profile of the fund.

Additional risks for consideration with a geared property investment in your SMSF includes:

- **Higher cost—**SMSF property loans tend to be more costly than other property loans.
- **Cash flow—**loan repayments must be made from your SMSF which means your fund must have sufficient liquidity or cash flow to meet them.
- **Hard to cancel—**if your property loan documentation and contract is not set up correctly, you may not be allowed to 'unwind' the arrangement without needing to sell the property, potentially with substantial losses.
- **Possible tax losses–** any tax losses made by the SMSF from the property cannot be offset against your taxable income outside the fund.
- **Cannot borrow to improve the property—**borrowed funds can be used to maintain a property but not for improving it e.g. renovating the kitchen or bathroom beyond the need for normal repairs to enhance the value of property is prohibited.

SMSFs—Trustee types

SMSF have become very popular, with more than one million members now representing the fastest growing segment of Australia's superannuation market.

Under the superannuation Industry (Supervision) regulations, an SMSF must either have a company act as trustee of the fund or the trustee can be a group of individuals.

Trustee requirements

SMSFs with individual trustee adhere to the following requirements:

- Only allowed up to four member
- Each member is a trustee (provided they are over the age of 18) and no member is an employee of another
- No trustee is paid for performing their duties or services as a trustee.

SMSFs with a corporate trustee will adhere to the following requirements:

- Also only allowed up to four members
- Each member of the fund is a director of the corporate trustee (provided they are over the age of 18)
- No member is an employee of another member (unless they are relatives)
- The corporate trustee is not paid for its services as a trustee
- No director of the corporate trustee is paid for performing their duties or services as a director in relation to the fund.

Single member funds

You can set up your SMSF with only one member, although some of the requirements are more restrictive. If your single member fund has individual trustees:

- There must be two trustees;
- One trustee must be fund member; and
- If the fund member is an employee of the other trustee, two must be relatives.

If your single member fund has a corporate trustee:

- The trustee company can only have one or two directors;
- The fund member must be either the sole director or one of the two directors; and
- If there are two directors and the fund member is an employee of the other director, the two must be relatives
- None of the trustees or directors can be paid for their services as a trustee (or as director of the corporate trustee) in relation to the fund.

**Self-managed super funds: A statistical overview 2012-13, Australian taxation Office.*

Trustee trends

Recent data from the Australian Taxation Office shows almost 75% of the SMSFs have individual trustees. The up-front and added complication of establishing the corporate trustee are the main reasons for this trends.

Which trustee structure is the best?

As with all decisions around SMSFs, there are pluses and minuses when it comes to deciding whether to have a corporate trustee or individual trustee(s).

Set-up costs—ongoing administrative requirements and establishment costs can be less for individuals trustees than those associated with a corporate trustees. Upfront and annual establishment fees are payable to ASIC in the case of a corporate trustee.

Changing trustees—with individuals trustees, if you remove or add another trustee to your SMSF, you must change the titles of the fund's assets as these are held in the trustee's name. This can be costly and time-consuming.

However, with a corporate trustees structure, member and director changes can be made without the need to change titles of the fund's assets, as these are in the name of the corporate trustee.

Separation of assets—the use of a corporate trustee with a separate identity, reduces the risks of personal assets becoming intermingled with fund assets, as can be the case with individual trustees. Also, as companies are subject to limited liability, a corporate trustee will provide greater protection if a party sues the trustee for damages.

Penalties—if there has been a breach of the super law, administrative penalties will be levied on each trustee within SMSF, whereas the same penalty only applies to one person in the case of a corporate trustee.

Successional planning—a fund with individual trustee is not likely to continue to operate as usual when changes in trustees occur, unless an appropriate succession plan has been prepared. With a corporate trustee however, control of an SMSF and its assets is more certain in the event of the death or incapacity of a member.

Contact Us
for more information about our services.

Collins Financial Planning Pty Ltd
AFSL 227250
127 Paisley Street,
Footscray VIC 3011

T: (03) 9680 1000
F: (03) 9689 6605
E: financialplanning@collinsco.com.au

Visit us on the web at
www.collinsco.com.au/wealth-creation

@CollinsCoCPA
/CollinsCoCPA
/company/collins-&-co