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SMSF

SET-UP GUIDE

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Disclaimer: This guide contains general advice only and are prepared without taking into account particular objectives, financial circumstances and needs. The information provided is not a substitute for legal, tax and financial product advice. Before making any decision based on this information, you should assess its relevance to the individual circumstances of your client. While we believe that the information provided is accurate, no warranty is given as to its accuracy and persons who rely on this information do so at their own risk. The information provided in this guide is not considered financial product advice for the purposes of the *Corporations Act 2001* or specific legal advice.

Key Advice Issues

Steps to setting up an SMSF

This Guide outlines the steps required in order to set up and register an SMSF with the Australian Taxation Office (ATO).

The steps are required to be completed in a certain order before progressing. Furthermore, not having the right information or documents completed can result in a delay when establishing an SMSF.

ASIC Report 575 – SMSFs: Improving the quality of advice and member experiences

ASIC's Report 575 on improving the quality of advice and member experiences focused on whether advice providers are complying with the law when providing personal advice to retail clients to set up an SMSF. The findings from the review of SMSF advice found that the advice process, particularly around establishment of an SMSF could be improved.

This Guide also uses some of the findings and practical tips in the Report to ensure that advisers are not only providing the best advice possible, but are also meeting their regulatory requirements.

Is an SMSF the right fit?

An SMSF is not the right choice for everyone. It is important that you understand your obligations as SMSF trustees and the pros and cons of setting up an SMSF. ASIC released a list of 'red flags' indicators that may suggest an SMSF is not suitable for your client and these issues should be carefully considered.

Red Flags

The red flags include, but are not limited to, clients who:

- Have a low superannuation balance, and would have a limited ability to make future contributions.
- Would like a simple super solution.
- Delegate all of the running of the SMSF to a paid advice provider.
- Delegate all of the investment decision making to someone else.
- Do not have a lot of time to devote to managing their financial affairs.
- Have little experience in making investment decisions.
- Are an undischarged bankrupt or has been convicted of an offence involving dishonesty (as such, persons are prohibited from acting as a trustee).
- Have a low level of financial literacy.

Low Balances

While a low balance can be a red flag, we consider that this is not always a barrier to entry.

Assessing Efficiency and Competitiveness, SMSFs with smaller balances can be cost competitive with APRA-regulated superannuation funds depending on the level of fees and the amount of administration trustees are willing to undertake.

However, in many cases, a recommendation for a retail client to set up an SMSF with a starting balance of \$200,000 or below is unlikely to be in the client's best interests.

This conclusion is based on the report, "Cost of Operating SMSFs" for ASIC prepared in 2013, by actuarial consulting firm Rice Warner. This report has been an important source of information regarding SMSF costs and establishments since it was published and was the basis of ASIC guidance in 2015 that SMSFs should have a minimum balance of \$200,000.

Noting this, there will be cases where specialist SMSF advice may indicate that the establishment of an SMSF with a balance lower than \$200,000 is appropriate. For example, if the trajectory of anticipated contributions is such that the fund will grow to this point within a short period.

Time

The ASIC report found that 38% of respondents found running their SMSF to be more time consuming than expected.

Trustees underestimated the amount of time involved in setting up and managing an SMSF, including where tasks are outsourced to third parties. It is therefore important that trustees understand they are accountable for the decisions and actions of the fund and even outsourcing of administration activities will still require a time commitment from trustees.

Costs

The ASIC report found that 32% of respondents found the costs of setting up their SMSF was more than expected.

You should make sure they have a clear understanding of the fees they are being charged over the life of the fund and are aware of unavoidable costs including:

- The annual SMSF supervisory levy collected by the ATO.
- The cost of producing an annual financial statement, tax return and TBAR reporting.
- Annual independent audit fees.
- Costs associated to setting up the SMSF and advice, including
 - Trust deed.
 - Preparing ATO application forms.
 - Cash management application
 - Provision of binding death nomination forms.
 - Investment strategy.
 - General trust and legal advice.

Optional costs to discuss also include:

- The costs of establishing a corporate trustee, including
 - ASIC's fees to establish a corporate entity.
 - Annual corporate trustee fee.
 - Searches and reservation of company names.
- Ongoing SMSF administration costs.
- Professional investment advice fees.
- Accounting and bookkeeping fees.

- The cost of an actuarial certification (when required).
- Investment management fees.
- The cost of obtaining insurance cover; and
- Costs relating to winding up an SMSF, including compliance costs and transactions costs related to realising assets.

The Productivity Commission Report quantified SMSF establishment costs at ranging between \$916 and \$2,035. Costs can be more substantial where complex legal or financial advice is required to implement bespoke strategies for the SMSF members.

A significant difference in costs of SMSF compared to an APRA-regulated fund relate to the administration fees. SMSF members have the option to effectively manage the administration services of their SMSF such as managing compliance responsibilities, ATO correspondence and paperwork, or they can outsource these services to a professional SMSF administrator.

For example, some individuals choose to use a full or part administration service which may add \$1,000 to \$2,000 in fees (when compared to an APRA-regulated fund) but allows trustees to focus on other aspects of their SMSF or finances such as investment strategies and investments.

The below table highlights the most common costs that are not adequately disclosed to SMSF trustees on SMSF establishment.

Client files demonstrating inadequate disclosure of costs

Cost category	Proportion of files with inadequate disclosure
Types of costs associated with winding up an SMSF	54%
'Opportunity cost' associated with managing an SMSF	48%
Investment costs	16%
Insurance costs	14%
Ongoing costs associated with operating an SMSF	12%
Costs associated with setting up an SMSF	8%

Financial literacy skills

If you are struggling with your personal financial affairs, it will not be appropriate to recommend establishment of an SMSF.

SMSF trustees have a duty to exercise skill, care and diligence in managing an SMSF, and therefore need to possess a sufficient level of financial literacy to manage the fund and make investment decisions in line with the fund's investment strategy.

Switching from an APRA-regulated fund to an SMSF

When your advisor recommends switching from an APRA-regulated fund to an SMSF, they must explain in the Statement of Advice (SOA), in clear and simple terms, the following information (where it is known or could reasonably be found out):

- Information about the exit fees or any other charges applying to the withdrawal from the APRA-regulated fund.
- The loss of access to rights or benefits (e.g. insurance cover and compensation).
- The loss of other opportunities, including incidental opportunities associated with the existing product (e.g. rights or opportunities not presently available to the client, but which may become available in the future).
- The set-up costs and ongoing fees for the SMSF.
- Any other significant consequences for the client in changing their superannuation fund to an SMSF.

Record Keeping and SOAs

The ASIC report observed there were problems in record keeping, when setting up an SMSF. Record keeping is important part of the decision making process and while the relevant issues may have been discussed it is important they are also recorded.

When discussing setting up an SMSF, ASIC provides the following should be recorded:

- Why you are dissatisfied with your current superannuation arrangements.
- What you hope to achieve by setting up an SMSF.
- What outcomes you would like to achieve.
- Why any recommendations are suitable and consistent with your objectives and financial situation.

This should be clear and recorded in your own words your file and in the SOA.

The scope of advice should not exclude critical issues that are relevant to the subject matter of the advice sought. Where the subject matter of the advice is limited in scope at your request. This should be recorded carefully, including your reasons for the request. This should also be detailed in the SOA.

Complex financial products and strategies necessitate more extensive inquiries. The decision to move from an APRA-regulated fund to an SMSF is a significant decision.

Steps to setting up an SMSF

Step 1 – Choosing a structure

Approximately 81% of SMSFs are set up with corporate trustees. A corporate trustee structure, while adding costs to the setup can provide advantages to an SMSF in terms of succession and asset protection.

Each structure has its own set of requirements and fees.

Structure	Features
Comparison of member and trustee requirements for individual and corporate trustees	
Individual Trustees	<p>One to four members.</p> <p>Each member of the fund must be a trustee, and each trustee must be a member of the fund. (Exception for single member funds)</p> <p>Simple structure and SMSF is not subject to corporation law requirements</p>
Corporate Trustee	<p>One to four members.</p> <p>Each member of the fund must be a director of the corporate trustee, and each director of the corporate trustee must be a member of the fund. (Exception for single member funds)</p> <p>Company structure which acts as trustee under corporations law.</p>
Costs	
Individual Trustee	A trustee cannot be paid for their duties or services as a trustee.
Corporate Trustee	<p>ASIC fee to register a corporate trustee for the first time.</p> <p>Annual review fee, which is lower if the corporate trustee acts solely as a super fund trustee, but higher if the corporate trustee also performs another function, such as running a business.</p> <p>A corporate trustee cannot be paid for its services as a trustee, and directors of the corporate trustee cannot be paid for their duties or services as directors in relation to the fund.</p>
Ownership of fund assets	
Individual trustees	<p>If an individual trustee is removed or another added, the fund must change the titles of the SMSF's assets. This can be costly and time-consuming.</p> <p>State government authorities may charge a fee for title changes.</p> <p>Most financial institutions also charge a fee for title changes.</p>
Corporate trustees	<p>Recording and registering assets can be simpler, particularly for changes in membership.</p> <p>When a person starts or stops being a member of the SMSF (including death), they become, or cease to be, a director of the corporate trustee.</p> <p>ASIC and the ATO must be advised of any change in directors.</p> <p>The corporate trustee does not change, so the titles of the SMSF's assets are unchanged.</p> <p>Some banks require a corporate trustee arrangement when entering a LBRA to purchase property.</p>

Separation of assets	
Individual trustees	Fund assets must be in the fund's name. Fund assets must not be combined with personal assets.
Corporate Trustee	Fund assets must be in the fund's name. Fund assets must not be combined with director's personal assets. Although uncommon, may reduce personal liability by limiting the liability of the assets of the company where the trustee of a fund is subject to litigation – such as a personal liability action in relation to one of the fund's properties.
Succession	
Individual Trustee	Where changes in trustees occur, the fund is not likely to continue to operate as usual unless an appropriate succession plan has been prepared.
Corporate Trustee	A corporate trustee continues in the event of a member's death or incapacity. In the event of the death or incapacity of a member, control of an SMSF and its assets by a corporate trustee is more certain.

Step 2 – Drafting the Trust Deed

The trust deed is a legal document that covers how to establish and operate the SMSF. It details all the members and trustees, as well as the rules and regulations of the fund, and investment and contribution information, as well as wind-up procedures. It includes such things as the fund's objectives, who can be a member and whether benefits can be paid as a lump sum or income stream. The trust deed and super laws together form the fund's governing rules.

It is important to get the trust deed right and consider the rules of the fund across the lifetime of the fund. Amending the deed can be costly and time consuming. It is also important that certain contributions are allowable under the trust deed and you cannot go back and amend the trust deed after the fact. Therefore reviewing the trust deed when any law changes or changes in membership is also important.

We believe it is appropriate for trust deeds to not be too restrictive, as this will limit flexibility and strategies the SMSF may undertake.

For example, proposed and recent legislation changes may not be cohesive with current trust deeds. This may include matters such as increasing SMSF members to six, the proposed triennial audit, the transfer balance cap and contribution changes such as the new non-concessional limit and the downsizer contribution.

Modern trust deeds must ensure they are able to apply all aspects of superannuation legislation.

The trust deed must be:

- Prepared by someone competent to do so as it is a legal document which means a lawyer should have drafted the document.
- Signed and dated by all trustees.
- Properly executed according to state or territory laws.
- Regularly reviewed, and updated as necessary.

Step 3 - Establish the trust

To establish the trust, the fund must set aside a nominal asset for the benefit of members. This is typically a token amount until members are able to roll over their existing benefits from elsewhere or make contributions themselves.

This token amount is regarded as a contribution and must be allocated to a member.

If a member can't contribute to the fund (for example, they are over 65 or do not meet the work test), an administrative discretion is automatically applied to allow a nominal contribution for the member. The amount must be allocated to the member, solely for the purpose of registering the SMSF.

Step 4 – Sign an ATO trustee declaration

An ATO trustee declaration must also be signed by trustees and directors of a corporate trustee of an SMSF to declare they understand their obligations and responsibilities.

This declaration must be signed within 21 days of becoming a trustee or director. [Click here](#) to download the ATO's trustee declaration form.

Step 5 – Check on Australian Residency

An SMSF is an Australian super fund if it meets all three of these residency conditions:

- The fund was established in Australia, or at least one of its assets is located in Australia.
 - The fund was 'established in Australia' if the initial contribution to establish the fund was paid and accepted in Australia.
- The central management and control of the fund is ordinarily in Australia.
 - This means the SMSF's strategic decisions are regularly made, and high-level duties and activities are performed, in Australia. It includes formulating the investment strategy of the fund; reviewing the performance of the fund's investments; formulating a strategy for the prudential management of any reserves; and determining how assets are to be used for member benefits.
 - In general, a fund will still meet this requirement even if its central management and control is temporarily outside Australia for up to two years. If central management and control of the fund is permanently outside Australia for any period, it will not meet this requirement.
- The fund either has no active members or it has active members who are Australian residents and who hold at least 50% of
 - the total market value of the fund's assets attributable to super interests, or
 - the sum of the amounts that would be payable to active members if they decided to leave the fund.

Note: For the purposes of condition three, a member is an 'active member' if they are a contributor to the fund or contributions to the fund have been made on their behalf. See

<https://www.ato.gov.au/law/view/document?DocID=TXR/TR20089/NAT/ATO/00001>

Step 6 - Register with the ATO

The fund needs to be registered with the ATO within 60 days of being established and the trustee will need to elect for the fund to be regulated.

This is done by applying for an Australian Business Number (ABN) at the Australian Business Register. When completing the ABN application a tax file number (TFN) for the fund should also be obtained.

WARNING: before applying for an ABN the previous steps must have been completed.

When completing the ABN application ensure you:

- Apply for a TFN for the fund.
- Elect for the fund to be an ATO-regulated SMSF. This is important to ensure the fund is able to receive tax concessions and the members' employers can claim deductions for contributions.
- Register for GST (if necessary).

The ATO will review the ABN application before issuing the ABN to the fund. The following can cause delays or reviews:

Individual members and trustees	Administrators, agents and other professionals
Bankruptcy	Previous links to SMSF clients of concern
Debts owed to the ATO	Debts owed to the ATO
Poor lodgment or payment compliance history	Poor lodgment or payment compliance history
Ability to maintain an ongoing SMSF	
Previous links to other SMSFs of concern	

The SMSF may also need to be registered for PAYG withholding tax. This is the case where the fund is going to make payments (lump sum or pensions) to members aged less than 60 years old.

Registering for GST

Most SMSFs do not need to register for GST because SMSFs mainly make input-taxed sales which do not count towards GST turnover.

SMSFs with an annual GST turnover of more than \$75,000 must register for GST. Annual GST turnover does not include:

- Contributions
- Interest and dividends
- Residential rent or income generated outside Australia.

However, it does include gross income from the lease of equipment or commercial property.

Step 7 - Set up a bank account for your fund

A bank account should then be opened in the SMSF's name to accept cash contributions, receive income from investments, pay fund expenses and pay benefits to members. These details do not need to be provided to the ATO when the fund is registered however should be updated as soon as possible.

Incorrect or out of date banking details are a common reason for delay in payments and rollovers – so ensuring bank account details are correct is vital.

Note that this account should be completely separate from individual members' and related employer's bank accounts.

Provide member TFNs

Make sure that you provide each member's TFN.

If a TFN is not provided, the fund will be unable to accept personal contributions from members. The fund will also be liable for more tax on their employer contributions.

Step 8 - Get an electronic service address to receive employer contributions

If the fund receives employer contributions the fund will need an electronic service address (ESA) to enable it to receive SuperStream data. The employer will need to know the fund's ABN and bank account details, in addition to the fund's ESA.

The ATO has a public register of SMSF messaging services providers who can provide the SMSF with an electronic service address. [Click here](#) to view the Register of SMSF messaging providers.

A common error is providing the email address rather than the electronic service address, this will delay Super Stream payments until the correct details are provided.

Note: Employers and other super funds will not transfer benefits to the fund until the fund has a registered ABN and "registered" status on [Super Fund Lookup](#), this can take up to 2-7 days.

Super Fund Look Up (SFLU) status:

The status of the fund will change depending on their registration status:

<i>Election to be regulated is being processed</i>	Registration in progress - cannot receive contributions or rollovers from third parties at this time.
<i>Registered – status not determined</i>	Registration complete – can receive contributions or rollovers from third parties.
<i>Registration details withheld</i>	Registration on SFLU withheld due to risk - cannot receive contributions or rollovers from third parties

Proposed rollout to all SMSFs – Electronic Rollovers

On 28 September 2018, the Government tabled regulations which broadly extends the operation of SuperStream to cover SMSFs. From 30 November 2019 SMSFs will need to be compliant with SuperStream in order to receive and make rollovers as well as receive employer contributions. Member contributions will not require SMSFs to be compliant with SuperStream meaning that not all SMSFs will need to enter the SuperStream environment. This means that many SMSFs will not need to be SuperStream ready until they are about to receive or make a rollover.

To be SuperStream ready, SMSFs will broadly need to give the following information to the ATO:

- A unique superannuation identifier (e.g., ABN);
- Bank details that can receive electronic payments; and
- An internet protocol or other digital address (i.e., an electronic service address ('ESA')) that can facilitate SuperStream communication.

Other considerations

First year

The first SMSF annual return is due 31 October. Failure to lodge first return means the SMSF non-complying SFLU is updated to 'regulation details removed due to failure to lodge return'.

Notice of compliance

For an SMSF to qualify for concessional tax treatment for income tax purposes, it must be a complying superannuation fund under sections 42A and 45 of the *Superannuation Industry (Supervision) Act 1993* (SISA).

A newly established SMSF will normally be given a notice of compliance when its first SMSF annual return (which combines the income tax return and regulatory return, and member contributions information) is lodged, and the return indicates that it has complied with all relevant requirements under the SISA.

A notice is not required to be given to an SMSF for each and every year of income. A notice of compliance given in relation to a year of income will be effective for that year and all subsequent years until such time, if any, as a notice of non-compliance is given to the fund.

Prepare an investment strategy

One in three ASIC respondents were not aware an SMSF must have an investment strategy. In developing a strategy you should ensure the strategy meets and considers:

- The sole purpose test and investments are maintained on an arms-length basis
- The benefits of asset diversification
- It meets the needs of members across different phases
- Read and understand any statement of advice, including if the product meets your investment strategy and if the investment will generate a sufficient return to fund your member's retirement

The *Superannuation Industry (Supervision) Regulations 1994* (SISR). requires an investment strategy for the SMSF, and that it is regularly reviewed. The strategy must reflect the purpose and circumstances of the SMSF and consider:

- Investing in such a way as to maximise member returns, taking into account the risk associated with the investment.

- Appropriate diversification and the benefits of investing across a number of asset classes (for example shares, property, fixed interest) in a long term investment strategy.
- The ability of the SMSF to pay benefits as members retire and pay other costs incurred by the SMSF.
- The needs of members (for example, age, years to retirement and the type of benefit to be paid).
- Whether the trustees of the fund should hold insurance for one or more members of the fund.

Separate investment strategies can be formulated for each member of the SMSF. This can assist the trustee to deal with situations where different members of the SMSF have different risk profiles (e.g. someone who has just started working may have a higher growth asset allocation whilst someone near retirement age may be more conservative).

Property and SMSFs on establishment

If a client has a preference for a property investment, you should consider whether the property investment is appropriate.

If you are recommending a property investment, you should discuss with the client:

- (a) the needs and circumstances of the fund's members (e.g. their age and retirement needs);
- (b) if the recommendation involves an investment loan, how long it will take for the client to repay the loan;
- (c) the high upfront costs of purchasing the property (e.g. stamp duty, loan fees, estate agent fees);
- (d) the client's ability to repay the loan if an unexpected event occurs (e.g. the client becomes unemployed for a period of time);
- (e) how the client's retirement will be funded by the property investment (i.e. through sale of the property or through rental income);
- (f) how likely it is that the property can be sold quickly (i.e. whether it is in a high demand area); and
- (g) what the client will do if the property is not rented for a period of time.

Insurance via superannuation

While use of insurance in an SMSF is not common, it must be considered as part of the investment strategy.

Death, total and permanent disablement (TPD) and income protection policies can be purchased by an SMSF. The premiums for these policies are generally tax deductible (in full or part) to the SMSF as long as the fund is a complying superannuation fund.

Since 1 July 2014, it has not been possible to take out a new trauma policy or a new TPD policy for own occupation within any superannuation funds including SMSFs.

The potential loss of insurance benefits is an important issue to consider before setting up an SMSF.

When switching superannuation savings out on an APRA-regulated fund you may be uninsured unless you purchase a new insurance policy.

Trustees must consider insurance for fund members as part of the fund's investment strategy and should consider:

- The existing insurance cover.
- The level of insurance cover you will need in the future.
- The costs and options of maintaining, increasing or decreasing (as appropriate) their existing insurance cover through an SMSF.

- Any health issues which may affect your ability to get insurance cover.
- The advantages and disadvantages of retaining a portion of your APRA-regulated superannuation for insurance purposes.
- The impact of the insurance recommendation on your SMSF balance.

Prepare an exit strategy

It is also important upon setting up an SMSF that trustees consider preparing an SMSF exit strategy.

Having an exit strategy may reduce the impact of 'unexpected' events, particularly relationship breakdowns, incapacity and death. As part of an exit strategy, some of the things trustees should consider are:

- Ensure all trustees can access the SMSF's records and electronic transaction accounts.
- Include specific rules in your fund's trust deed that are triggered by events that could otherwise lead to the fund becoming unmanageable.
- Members to make binding death benefit nominations (and renew them every three years).
- Encourage members to appoint an enduring power of attorney.
- The likely costs involved in winding up an SMSF.

Contingency plans

An SMSF is a long-term plan. Much can happen during this time including illness, incapacity or death of a member.

Death – Given the introduction of the \$1.6 million transfer balance cap which means larger sums of money may need to leave the superannuation system sooner, planning has never been more important.

The rules of the SMSF, as set out in the trust deed and related documents, determine how the trustee structure is to be reconstructed on the death of a member as well as how death benefits are to be handled by the fund. Therefore, it is important to consider these issues when formatting the deed.

Legal tools to help direct superannuation can also include making a binding death benefit nomination or providing for a reversionary pension following death.

Diminished capacity – Consider the consequences if trustees are unable to carrying out their duties (e.g., due to mental incapacity).

Separating couple – Family law contains a number of options for superannuation to be split between a couple who separate or divorce. As superannuation is treated separately to other property, specialist advice may be needed.

Setting up an SMSF checklist

The establishment of an SMSF requires a lot of decisions to be made by your clients as SMSF trustees. Use the below checklist to ensure every step has been completed to comply with the regulatory requirements and considered if not a specific requirement.

- ☐ Work with your client to determine if an SMSF is 'right' for them and their specific circumstances.
- ☐ Prepare appropriate and clear documentation of the advice to establish an SMSF, including switching from an APRA-regulated fund.
- ☐ Choose an appropriate trustee structure for the fund.
- ☐ Appoint trustees or directors as required.
- ☐ Establish the trust with a nominal asset and associated trust deed
- ☐ Have the fund's trustees complete and sign the ATO trustee declaration
- ☐ Check that the fund has been established as an Australian super fund.
- ☐ Consider whether the fund needs to be registered with the ATO for:
 - ABN
 - TFN
 - GST
 - PAYG withholding.
- ☐ Set up a bank account in the name of the SMSF.
- ☐ Get an Electronic Service Address (ESA)
- ☐ Prepare an investment strategy
- ☐ Consider insurance and whether it is appropriate to take out policies within the fund for its members
- ☐ Ensure any property and gearing is appropriate
- ☐ Prepare an exit strategy and what will occur in the case of unexpected events (e.g. incapacity of a member) ensuring that all members agree