SUPERMATTERS

SUPERANNUATION STRATEGIES FOR YOU AND YOUR BUSINESS

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SMSFs Breaking The Rules - Penalties & Punishments

One of the main differences between owning a Self Managed Super Fund ('SMSF') and owning other entities is that your SMSF must appoint an auditor (at least 45 days before your first annual return is due), and then have the SMSFs accounts audited each year by the auditor.

Not only does the auditor have to audit the accounts but they must also ensure that the fund has complied with all the rules. If the auditor determines that the fund has not complied with the rules they must report that contravention to the ATO.

Usually, when the auditor finds a contravention of the rules, they will discuss this with the trustees and work out how to rectify the contravention. When the auditor notifies the contravention to the ATO, they will also usually notify how it was fixed. This will usually lead to no action being taken by the ATO.

But sometimes the trustees are not so willing to fix their contravention, and in these instances, the ATO can impose substantial penalties on the trustees who have to pay those penalties personally rather than through the assets of the fund.

Although contraventions are not common and only occur in around 2% of funds each year, there are commonly occurring contraventions. These include things such as the fund lending money to a member or a relative of a member, or members taking money out of the fund before they are entitled to.

In any of these instances, it is essential that the money is paid back, with interest, as soon as it is realised that the money wasn't to be taken. If you don't do so, the penalties will usually end up costing more than the money that was taken.

Aside from financial penalties, the ATO can also impose other penalties. These can include education orders where they direct you to do some free study about being the trustee of an SMSF.

If you are not willing to show the ATO that you are interested in fixing any contraventions or your contraventions are too prevalent, they have the ability to disqualify you from having an SMSF.

The biggest penalty that the ATO can impose is classifying your fund as non-complying. This will result in the whole fund being taxed at around 47%, and you will immediately lose close to half of your overall superannuation total.

This is why it is of paramount importance that you work together with your auditor and ensure that you fix any contraventions as soon as possible, once you are made aware of them.

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Using Your Super For An Investment Property – Is It Worth It?

In 2007, the government changed the law to allow superannuation funds to borrow in order to buy assets. The most common asset that is generally bought with a loan is a property, and there are many super funds borrowing to buy properties. The question here is - is this a sensible move for you?

It depends on your circumstances. Borrowing to buy property is most certainly a suitable wealth creation strategy for many people, but it comes with risk, and that induces even more risk inside the superannuation environment.

On the positive side, you have access to gearing that should (over the long-term) provide you with a greater return on your investment. This is after all the reason that borrowing to buy assets occurs in the first place.

The downside however is that you have to be able to get a loan. At the moment, none of the four major banks will lend to a self-managed super fund to buy property. Other lenders will have severe restrictions on what they lend (such as only lending 70% of the value of the property).

Working out how to do it is a complicated process, so the advice of a licensed adviser should be sought. Their recommendation may be that you should only do it if you have a large super balance.

You will also need to be highly conscious of your cash flow requirements as well. In situations where you borrow money to buy a property, you will be required to contribute that money on an ongoing basis. As this is your superannuation that you may be looking to use, you need to be certain that you will be able to meet all of the cash flow requirements through super.

What if you need to fund a period of time with no tenants in your investment property? Will you be able to cover that.

With gearing, there is another risk to take into account before making a decision on whether or not to use your super when purchasing an investment property. Not only are your profits amplified, so are your losses. There have been instances where people have lost all their super because they have invested in the wrong asset. Upon the sale of that asset, they have had to use all of their super (and then some of their own money) to pay back the loan.

There is no doubt that borrowing to buy a property in your super fund is a great strategy but only for people with the right circumstances to do so. If you are looking for more information on this, come speak directly with us.

Case Study – How To Avoid Paying Additional Tax On Super

John is 84 years old and a widower with two adult children. John suffers a severe heart attack, is placed into intensive care and is given only days to live.

John has in his SMSF a property valued at $1 million. He and his former wife saved well throughout their lives, and had been told super was the best place to hold their assets.

As a result, it meant that they paid no tax throughout their retirement years. This was an ideal situation for the retirees.

After John passes, however, his super will have to go to either his estate or to one or both of his sons. Generally speaking, this would not create issues, but taxes will be incurred of at least $150,000 on the super.

What Can Be Done?

This is a frustrating issue to be dealing with at this precise moment for John and his loved ones, but it is an important one.

The property should be transferred out of the fund and into John's name personally, and immediately. This would mean that one (or both) of John's children have to have an enduring power of attorney over John.

This will involve taking urgent advice from John's accountant and solicitor, but handling the situation in a timely manner should save John's children $150,000 in tax.

New Rules In Place For SMSF Auditors

When an accountant does an audit there are rules that force the accountant to ensure that they are independent of the accounts they are auditing. Recently the rules were changed aroundindependence for SMSF Auditors.

Traditionally, where an auditor and an accountant were part of the same network or accounting firm, they could only audit a fund that was part of the same network/firm whereby the auditor could demonstrate that they were still acting independently of the accountant.

But from 1st July 2021, SMSF auditors are no longer able to audit a fund where the accounts have been prepared by either the same firm or network of firms.

This means that up to 300,000 SMSFs have had to appoint a new auditor this financial year.

This will also impact the trustees of those funds as they now have to formally engage a new auditor and then get used to the requirements of that new auditor.