

Key SMSF investment rules

Superannuation law places a number of investment restrictions on superannuation funds which aim to protect members by ensuring fund assets are not exposed to undue risks, such as the failure of a related business.

Failure to comply with the investment rules can result in significant penalties for both the trustees and the fund. Following is a brief summary of some of the investment rules applying to self-managed superannuation funds (SMSFs).

Sole purpose test

The sole purpose test requires your SMSF to be maintained for the sole purpose of providing retirement benefits to members, or to dependents if a member dies before retirement.

If an investment decision is made that provides a member with a financial benefit prior to meeting a condition of release this rule may be breached and the fund could be classified as non-complying. This would result in all earnings (plus the taxable component of the fund) being taxed at the top marginal tax rate plus levies.

Investment strategy

As trustee of your fund, you are required to prepare and implement an investment strategy. An investment strategy helps the fund focus on its goal of providing retirement benefits and reduces the risks associated with unplanned investment decisions.

Some of the key considerations for a fund's investment strategy include:

- The investment objectives for the fund
- Diversification and the benefits of investing across a number of asset classes (such as fixed interest, property and shares)
- The fund's liquidity, including its ability to pay member benefits and other fund expenses
- Whether to hold insurance cover for members
- The circumstances of each member, including their age, income needs and retirement goals.

The investment strategy should set out the fund's investment objectives and the methods that will be used to achieve those objectives. All investment decisions for the fund must be made in accordance with the investment strategy.

The investment strategy must be reviewed at least annually and whenever there is a change to the fund, such as if a new member joins or if an existing member commences a pension.

Ownership of assets

Important: Any advice in this communication has been prepared without taking into account your objectives, financial situation or needs. Because of this you should, before acting on any advice in this communication, consider whether it is appropriate to your personal circumstances.

Assets belonging to the SMSF must be kept separate to your personal assets. Having a separate bank account for your SMSF will help your fund meet this requirement. All fund expenses can then be paid from that bank account only.

The Australian Tax Office (ATO) prefers assets to be owned in the name of the trustee. If the fund has individual trustees, assets should be owned by all trustees in that capacity. If the fund has a corporate trustee, assets should be owned in the name of the company as trustee for the fund.

Value all assets at market value

All fund assets should be valued at market value. The market value should be used when preparing your fund's accounts, statements and the SMSF annual return.

Arm's length transactions

All SMSF investments must be made and maintained on a strict commercial basis. This means that the purchase and sale price of assets and any income received from those assets should always reflect the true market value for the asset.

Loans and financial assistance

An SMSF cannot lend money or provide financial assistance to a member or their relative. Financial assistance is defined to include non-arm's length dealings with a related party, loans, provision of a guarantee and forgiveness of a debt.

Related party acquisitions

An SMSF cannot acquire assets from a related party of the fund, except in limited circumstances. These limited circumstances include the acquisition of:

- listed securities
- business real property (generally relates to land and buildings used wholly and exclusively in any business)
- in-house assets providing the total of in-house assets is not more than 5% of total fund assets
- units in widely-held unit trusts.

In-house assets

The value of in-house assets cannot exceed 5% of the total value of the SMSF. These assets are defined to include:

- a loan to, or an investment in a related party of the fund
- an investment in a related trust of the fund
- an asset that is leased to a related party (unless it is business real property).

Borrowings

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An SMSF is only able to borrow money in very limited circumstances, including:

- For a maximum of 90 days to meet benefit payments due to members or to meet an outstanding surcharge liability. The borrowings in this circumstance cannot exceed 10% of the fund's total assets.
- For a maximum of 7 days to cover the settlement of security transactions if, at the time the transaction was entered into, it was likely that the borrowing would not be needed. The borrowing in this circumstance cannot exceed 10% of the fund's total assets.
- If using instalment warrants or limited recourse borrowing arrangements that meet certain conditions.

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