PS LA 2006/17 - Self-managed superannuation funds - disqualification of individuals to prohibit them from acting as a trustee of a self-managed superannuation fund

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Practice Statement Law Administration

PS LA 2006/17

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FOI status: may be released

This practice statement is issued under the authority of the Commissioner and must be read in conjunction with Law Administration Practice Statement PS LA 1998/1. It must be followed by tax officers unless doing so creates unintended consequences or is considered incorrect. Where this occurs tax officers must follow their business line's escalation process.

SUBJECT:	**Self-managed superannuation funds – disqualification of individuals to prohibit them from acting as a trustee of a self-managed superannuation fund**
PURPOSE:	**To outline the circumstances in which the Commissioner will consider disqualifying an individual under section 126A of the *Superannuation Industry (Supervision) Act 1993* and thereby prohibit them from acting as a trustee of a self managed superannuation fund**

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BACKGROUND

1. A trustee of a self-managed superannuation fund (SMSF) may either be one of two or more individuals to a maximum of four, or a body corporate. Where the trustee is a body corporate, the director of the body corporate is referred to as a 'responsible officer'.[1] Unless it is indicated otherwise, where the word trustee appears in this practice statement, it is referring to each of the individual trustees or an individual as a responsible officer of a corporate trustee.

2. A person must not act as a trustee of an SMSF or a responsible officer of a corporate trustee when they know they are a disqualified person. A disqualified person who acts as a trustee or responsible officer while they are disqualified commits an offence (section 126K of the *Superannuation Industry (Supervision) Act 1993* (SISA)).

3. An individual may be a disqualified person either by operation of law (section 120 of the SISA) or by decision of the Commissioner (section 126A of the SISA).

4. Under section 120 of the SISA an individual is a disqualified person by operation of law where they have been/are:

   - convicted of an offence involving dishonesty (subparagraph 120(1)(a)(i))
   - subject to a civil penalty order (subparagraph 120(1)(a)(ii))
   - an undischarged bankrupt (paragraph 120(1)(b)), or
   - disqualified by the Commissioner under section 126A of the SISA (paragraph 120(1)(c)(i)).

5. The Commissioner may disqualify an individual under section 126A of the SISA where the:

   - person has contravened the SISA or the *Financial Sector (Collection of Data) Act 2001* (FS Act) (subsection 126A(1) of the SISA)
   - corporate trustee has contravened the SISA or the FS Act and the individual was a responsible officer at the time of the contravention (subsection 126A(2) of the SISA), or
   - individual is otherwise not a 'fit and proper' person (subsection 126A(3) of the SISA).

6. In making the decision to disqualify an individual under subsection 126A(1) or (2) of the SISA the Commissioner must take into account the nature or seriousness of the contraventions and the number of contraventions.

7. When the nature, seriousness or number of contraventions are not considered sufficient to disqualify under either subsection 126A(1) or (2) of the SISA the Commissioner will determine whether the individual is a fit and proper person under subsection 126A(3) of the SISA.

8. When the Commissioner disqualifies an individual the Commissioner must give the individual written notice of the disqualification and publish details of the disqualification in the *Gazette* (subsections 126A(6) and 126A(7) of the SISA).

9. The decision by the Commissioner to disqualify an individual is for an indefinite period, subject to an application by the individual to have the decision reviewed.

[1] Section 10 of the *Superannuation Industry (Supervision) Act 1993* also includes a secretary and executive officer within the definition of a 'responsible officer'.

10. However, disqualifying an individual is not the only option available to the Commissioner in developing a compliance strategy in relation to a particular SMSF. Other options include:

- accepting an undertaking from the trustee to rectify the contravention(s)[2]
- issuing the fund with a notice of non-compliance,[3] or
- as part of an investigation, freezing the assets of the fund where there is a risk of the members' benefits being eroded or further eroded.[4]

STATEMENT

11. This practice statement deals only with SMSFs and outlines the factors the Commissioner will take into account in determining whether an individual should be disqualified under section 126A of the SISA.

12. Disqualification is not a punishment, penalty or sanction to the individual.[5] It is used where the Commissioner is concerned about the compliance attitude of an individual and/or their suitability to act as a trustee.

13. Only an officer from the Senior Executive Service (SES) is authorised to make the decision to disqualify an individual. Where a case officer requires a decision in relation to disqualification, the officer must make a recommendation to the SES officer providing them with sufficient information to make the decision.

14. In assessing the nature or seriousness or number of contraventions of either the SISA or the FS Act for the purposes of subsections 126A(1) or (2) of the SISA, and making the decision to disqualify an individual, the Commissioner will:

- look at the acts of the individual
- consider all the facts of the case
- act in accordance with the Australian Tax Office (ATO) compliance model and the taxpayers' charter
- apply the good decision-making model, and
- consider whether there is a future compliance risk.

15. In making the decision to disqualify an individual for not being a 'fit and proper' person (subsection 126A(3) of the SISA) the Commissioner will take into account:

- any contraventions of the SISA
- where the individual has contravened the SISA, the circumstances surrounding the contravention
- considerations other than the individual's compliance with the SISA which go to establishing the character and repute of the person

  Examples include:

[2] The policy on undertakings is contained in Law Administration Practice Statement PS LA 2006/18.
[3] The policy on issuing notices of non-compliance is in Law Administration Practice Statement PS LA 2006/19.
[4] Section 264 of the SISA.
[5] *AAT Case* [2002] AATA 1233.

- non-compliance with other taxation laws, and
- whether the individual has been subject to sanctions under any other relevant laws. Relevant laws would generally include those laws dealing with financial responsibilities, honesty and business transactions

- the association the individual has with other trustees of the SMSF and the impact this relationship has on their ability to perform their duties as a trustee, and
- all the circumstances of the case including the honesty, competence, diligence, knowledge and ability, soundness of judgment, reputation and character of the individual.

Individual in a position as a trustee

16. Where an individual is in the position of a trustee, it is possible to disqualify them under either subsection 126A(1) or (3) of the SISA. Where an individual is the responsible officer of a corporate trustee, it is possible to disqualify them under either subsection 126A(2) or (3) of the SISA.

17. As a general rule, prior to disqualifying an individual the Commissioner should allow the individual to preserve their benefits. For example, the Commissioner may provide the individual with the opportunity to roll over the funds to an independently managed superannuation fund. The Commissioner will clearly state the time limits within which this action must take place.

18. Where the Commissioner is of the view that an individual is not suitable to continue to act as a trustee of an SMSF, the Commissioner may disqualify them. This may be done in isolation or in conjunction with other compliance option/s. Further, where a disqualified person continues to act there will be a contravention of the SISA.

19. A person who continues to act when they know they are disqualified commits an offence.[6] Where the individual does not remove themselves, the Commissioner may remove them.

Individual not in a position as a trustee

20. A person may be disqualified as a preventative measure. That is, by determining a person is not fit and proper before they become a trustee the Commissioner can look to the future and disqualify them. In these circumstances an individual can only be disqualified for not being a 'fit and proper' person under subsection 126A(3) of the SISA.

21. Where an individual is not presently acting as a trustee of an SMSF or has never acted as a trustee and the Commissioner has reason to believe the individual presents a future compliance risk, the individual may be disqualified.

EXPLANATION

22. Section 126A of the SISA broadly provides two circumstances where the Commissioner may disqualify a trustee.

    Firstly, where there is a contravention of either the SISA or the FS Act by:

[6] Section 126K of the SISA.

- an individual (subsection 126A(1) of the SISA), or
- a corporate trustee at the time the individual is a responsible officer of the body corporate (subsection 126A(2) of the SISA),

and after the Commissioner has taken into account the nature or seriousness or number of contraventions.

Secondly, where the Commissioner is not satisfied an individual trustee is a 'fit and proper' person (subsection 126A(3) of the SISA).

23. As the laws that enable the Commissioner to disqualify refer to individuals, any decision to disqualify an individual must be based on the action or inaction of a particular individual. Where the individual is a responsible officer of a corporate trustee, it is necessary to look at the contraventions of the corporate trustee at the time the individual was a responsible officer.

24. The decision to disqualify an individual requires consideration of all the circumstances of the case and is a question of fact and degree. All the facts of the case must be considered with no one particular factor being determinative.

25. Where a decision is made to disqualify one particular individual this does not lead to the conclusion that all other individuals who are/were trustees of the same fund should be disqualified. The circumstances surrounding each individual's actions must be considered.

26. An individual trustee may only be disqualified under subsection 126A(1) of the SISA where there is a contravention of either the SISA or the FS Act. A trustee, who does not contravene a provision of the SISA or the FS Act personally, but performs their duty in a manner which allows other trustees to contravene the SISA or the FS Act, may be found not to be a 'fit and proper' person under subsection 126A(3) of the SISA.

27. A responsible officer of a corporate trustee may be disqualified under subsection 126A(2) of the SISA where they are a responsible officer at the time the corporate trustee contravened either the SISA or the FS Act. A responsible officer may be disqualified under this provision regardless of whether they were personally involved in the contravention. Additionally, the lack of involvement in the decision making of the corporate trustee may indicate the particular responsible officer is not a 'fit and proper' person under subsection 126A(3) of the SISA.

28. To ensure that a fair and reasonable outcome is achieved, the decision making process will take into account:

- the statements and principles set out in the taxpayers' charter
- the approach for managing taxpayer compliance outlined in the compliance model, and
- the good decision-making model.[7]

29. A key factor in making the decision to disqualify an individual is whether, by not taking such action, there will be a future compliance risk. Case law supports the view that disqualification is designed to protect the investing

[7] Under the good decision-making model, decisions must be legal, ethical, equitable, overt, sensible, timely and in accordance with the principles of natural justice.

public against the risk that people with a history of non-compliance will re-offend. Disqualification is not a punishment for their past acts.[8]

30. If the Commissioner is prepared to enter into an enforceable undertaking with a trustee to rectify a contravention, this demonstrates that the Commissioner is confident the trustee will be compliant in the future. As a general rule, in these cases the trustee should not be disqualified while they are demonstrating a commitment to fulfil the terms of the undertaking.[9]

31. An individual will be considered a future compliance risk where it is reasonable to draw the conclusion from their compliance history that there is a high probability that they will contravene a provision of the SISA in the future.

32. The compliance history of an individual includes more than how they have complied with their obligations in their capacity as a trustee of the SMSF. It extends to their compliance history in relation to both their personal tax affairs and those of any other entity in which they have been in a position of responsibility. Generally, this will be information gathered about an individual in relation to their compliance with taxation obligations from information supplied by the individual, other parties and ATO records.

33. There are four areas relevant to complying with the tax system:

- *Registration* – registration compliance looks at whether the trustee is registered for all relevant roles.
- *Lodgment* – lodgment compliance looks at whether the individual has lodged all returns in the correct format on time without prompting from the Commissioner.
- *Reporting* – reporting compliance looks at whether the individual has demonstrated a willingness to report correctly.
- *Payment of debt* – payment of debt looks at whether the individual paid debts voluntarily by their due dates. Further, if the individual has an outstanding debt, whether they have entered into a payment arrangement and fulfilled their payment obligations under the arrangement.

34. When assessing the compliance history of an individual, it is important to recognise that people make mistakes and they will not always have a perfect compliance history. What is important is the individual demonstrates a willingness to comply with their obligations.

35. The compliance history should take into account the time both before and after the contravention. It is not sufficient to look solely at the acts of the individual leading up to the contravention as the actions of the individual after the contravention may provide strong evidence of their attitude to future compliance.

Disqualification for contraventions of the SISA or the FS Act

36. Where there is a contravention of either the SISA or the FS Act by:

- an individual (subsection 126A(1) of the SISA), or
- a corporate trustee at the time the individual is a responsible officer of the body corporate (subsection 126A(2) of the SISA),

[8] *AAT Case* [2002] AATA 1233.
[9] The policy on undertakings is contained in Law Administration Practice Statement PS LA 2006/18.

the Commissioner must look at the nature or seriousness or number of contraventions.

37. The number or seriousness of contraventions is a question of fact and degree and as such it is not possible to put in place prescriptive rules as to when a trustee should be disqualified.

38. The seriousness of an offence should be determined on a case by case basis having regard to the ability of the fund to meet the obligations it has to its members. For example:

- The behaviour of the trustees in relation to the contravention.
- The extent to which the fund's assets were affected by the contravention.[10] The greater the proportion of the fund's assets affected by the contravention, the more likely it is that the contravention is serious.
- The extent to which the fund's assets were exposed to financial risk and whether there was any loss to the value of the fund.
- The number and extent of contraventions over a period of time. A single contravention on its own may not be considered serious, but a number of contraventions taken together may make the situation serious.[11]
- The nature of the contravention in the overall scheme of the legislation. For example, a contravention involving an artificial arrangement intended to undermine the regulatory provisions or the tax concessions offered to SMSFs is likely to be serious.

39. It is not possible to state that after a specified number of contraventions have occurred a trustee will automatically be disqualified. It is important the decision to disqualify is based on the conclusion that allowing the trustee to continue in the role will present a real risk to the fund being able to meet its obligations in the future.

40. Where an individual agrees to remove themselves from the position of a trustee, it may no longer be necessary to disqualify them. This is because the act of removal may demonstrate a change in attitude of the individual and that the individual does not present a future compliance risk. The act of removal must be taken into account when deciding whether the trustee is fit and proper.

41. Where the Commissioner accepts an enforceable undertaking from the trustee the Commissioner will not disqualify the trustee provided they gave the undertaking in good faith and are making all reasonable efforts to comply with its terms.

Disqualification for not being a 'fit and proper' person

42. The decision to disqualify an individual as not being fit and proper requires an assessment of two separate issues. Firstly, the fitness of the person and secondly whether the individual is a proper person to be a trustee.

[10] For example, see *Case 47/94* 94 ATC 417; *AAT Case 9689* 29 ATR 1086.
[11] For example, see *Re Pruess and Australian Prudential Regulation Authority* [2005] AATA 748.

43. The following explanation of 'fit and proper' was provided in the case of *Australian Broadcasting Tribunal v. Bond*:[12]

> The expression 'fit and proper person', standing alone, carries no precise meaning. It takes its meaning from its context, from the activities in which the person is or will be engaged and the ends to be served by those activities. The concept of "fit and proper" cannot be entirely divorced from the conduct of the person who is or will be engaging in those activities. However, depending on the nature of the activities, the question may be whether improper conduct has occurred, **whether it is likely to occur**, whether it can be assumed that it will not occur, or whether the general community will have confidence that it will not occur. The list is not exhaustive but it does indicate that, in certain contexts**, character** (because it provides indication of likely future conduct**) or reputation** (because it provides indication of public perception as to likely future conduct**) may be sufficient to ground a finding that a person is not fit and proper to undertake the activities in question**…(Emphasis added)

44. The decision that a person is not fit and proper is based on an overall evaluation of the facts. It is a question of fact and degree and requires a number of factors to be considered with no one particular factor being determinative in any given case.

45. The fitness of an individual relates to all matters which affect the capacities of a person to perform their role as trustee[13] and includes their qualifications and competence. The fitness of an individual is determined with reference to the particular skills required for them to satisfy their obligations as a trustee.

46. The propriety of an individual refers to their general behaviour and conduct. This can be assessed by reference to such things as an individual's conduct in the discharge of their duties (past and present) and the reputation and character of the individual. This is, we are looking to the ethical attributes of the individual.

47. The factors must be assessed in light of how they will impact on the risks associated with allowing the individual to act as a trustee. These risks include the trustee:

- misappropriating the funds
- dealing with the assets in an illegal way
- failing to keep proper records, and
- providing dishonest information to the ATO.

Technical skills[14]

48. The individual's competence and experience should be commensurate with the scale and scope of the SMSF's operations. Factors to consider include whether the person:

- possesses the relevant skills, knowledge, expertise, experience, diligence and soundness of judgment to undertake and fulfil particular duties and responsibilities of being a trustee of an SMSF

[12] *Australian Broadcasting Tribunal v. Bond* (1990) 170 CLR 321 per Toohey and Gauldron at 380.
[13] *Monty Financial Services Ltd v. Delmo* [1996] 1 VR 65.
[14] Refer to APRA release SGN 110.1 which deals with attributes that apply to APRA regulated fund trustees. These attributes are similar to those that apply to trustees of SMSFs.

- has demonstrated the appropriate competence in fulfilling occupational, managerial or professional responsibilities in relation to any prior business activities, and
- is able to answer questions by the ATO in a satisfactory manner.

Ethical attributes

49. Ethical attributes are the person's honesty, integrity and reputation in the conduct of business activities, including a consideration of whether the person has:
    - demonstrated a willingness to comply with regulatory or professional requirements and has assisted and been truthful in dealings with regulatory bodies
    - carried out their role and functions with the degree of independence required
    - not been reprimanded, or disqualified by a professional or regulatory body
    - good fame, integrity and character
    - managed their personal debts satisfactorily, or
    - been substantially involved in the management of an entity which has been wound up or its business has failed, where that event has been occasioned in part by deficiencies in that management.
50. Where an individual has not acted properly in the past, however has demonstrated a change in behaviour, it may not be appropriate to disqualify the individual for not being fit and proper.

Notice of decision

51. The Commissioner must give written notice of disqualification; review of disqualification; or a refusal to revoke a disqualification (subsection 126A(6) of the SISA). The issue of revocation is not considered in this law administration practice statement.

Review rights

52. A person affected by the Commissioner's decision to issue a notice disqualifying them may, if dissatisfied with the decision, request the Commissioner to reconsider. A request to reconsider must be made in writing, setting out the reasons for making the request, and must be made within 21 days after the person receives notice of the decision, or within such further time the Regulator allows.[15]

[15] Sections 10 (definition of 'reviewable decision') and 344 of the SISA.

Amendment history

Date of amendment	Part	Comment
20 May 2010	Paragraph 1	Minor clarification explaining SMSF membership can be either one of two or more individuals to a maximum of four.
	Contact officer	Updated.
2 September 2009	Contact officer	Updated.
6 April 2009	Paragraph 1	Amended so it only refers to a director of a body corporate.
	Paragraph 2	Deleted word intentionally.
	Paragraphs 16 to 20	Amended to remove references to appointing an acting trustee in making the decision to disqualify an individual.
	Paragraph 20	Replaced by new paragraph 20.
27 June 2008	Generally	Section 120A is now 126A and section 121 is now 126K.
	Paragraph 10.	Updated to clarify that assets are only frozen where it is part of an investigation.
	Paragraph 19	Corrected to advise acting trustee is appointed only where all trustees are removed.
	Legislative references	Updated.
	Contact phone number	Updated.

Subject references	disqualification of trustee fit and proper person self managed superannuation fund trustee
Legislative references	SISA 10 SISA 120 SISA 126A SISA 126A(1) SISA 126A(2) SISA 126A(3) SISA 126A(6) SISA 126A(7) SISA 126K SISA 344 Financial Services (Collection of Data) Act 2001
Related public rulings	
Related practice statements	PS LA 2006/18 PS LA 2006/19
Case references	AAT Case [2002] AATA 1233 Case 47/94 94 ATC 417 AAT Case 9689 29 ATR 1086 Re Pruess and Australian Prudential Regulation Authority [2005] AATA 748 Australian Broadcasting Tribunal v. Bond (1990) 170 CLR 321 Monty Financial Services Ltd v. Delmo [1996] 1 VR 65
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