PS LA 2006/18 - Self-managed superannuation funds - enforceable undertakings

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Practice Statement Law Administration

PS LA 2006/18

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FOI status: may be released

This practice statement is issued under the authority of the Commissioner of Taxation 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 where it is considered incorrect. Where this occurs, tax officers must follow their business line's escalation process.

SUBJECT:	**Self-managed superannuation funds – enforceable undertakings**
PURPOSE:	**To outline the factors the Commissioner will consider in deciding whether to accept a written undertaking proposed by trustees to address contraventions of the *Superannuation Industry (Supervision) Act 1993***

TABLE OF CONTENTS **Paragraph**

BACKGROUND	**1**
STATEMENT	**5**
EXPLANATION	**17**
When it is appropriate to accept an undertaking	18
Formulating an undertaking with a client	21
The essential terms for an undertaking	24
The circumstances in which it would be appropriate to permit a trustee to withdraw or vary the undertaking	26
The consequences of not fulfilling an undertaking	30
Informal arrangements	32
Review rights	37

BACKGROUND

1. Section 262A of the *Superannuation Industry (Supervision) Act 1993* (SISA) allows the Commissioner to accept a written undertaking given by the trustee[1] of a self-managed superannuation fund (SMSF)[2] in relation to a contravention of the SISA.

2. Section 262A of the SISA was introduced to provide a flexible and cost efficient tool for managing contraventions of the SISA.

3. When a written undertaking is accepted by the Commissioner it becomes enforceable. If the Commissioner considers that a trustee has breached a term of the undertaking, the Commissioner can apply to a court for an order in relation to the breach.

4. This practice statement only applies to undertakings under section 262A of the SISA.

STATEMENT

5. Where the Commissioner identifies a contravention of the SISA, the Commissioner may if it is appropriate, give the trustee the opportunity to provide a written undertaking to remedy the contravention where this is possible. This will normally be done by accepting an undertaking from the trustee.

6. However, an enforceable undertaking is not the only option available to the Commissioner in developing a compliance strategy in relation to a particular SMSF. Other options available under the SISA include:

   - issuing a fund with a notice of non-compliance[3] (subsection 40(1))
   - seeking a court order under subsection 262A(4)
   - disqualifying a particular individual and prohibiting them from acting as a trustee of a superannuation fund[4] (section 126A)
   - suspending or removing a particular trustee (subsection 133(1))
   - freezing the assets of a fund if there is a risk of the members' benefits being eroded (section 264), or
   - seeking civil and/or criminal penalties through the courts (Part 21)

7. Whether an undertaking is an appropriate means of addressing a contravention will depend on the individual circumstances of the case. The factors to be considered in deciding whether an undertaking is appropriate are listed in paragraph 19 of this practice statement.

8. To ensure that a fair and reasonable outcome is achieved in each case, the statements and principles set out in the taxpayers' charter, the compliance model and the good decision-making model[5] must be followed.

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[1] The term 'trustee', as used in this practice statement, refers to either the individual trustees or the corporate trustee of the fund, as the case may be.

[2] The term 'SMSF', as used in this practice statement, refers to either an SMSF or a former SMSF. A former SMSF is a fund that has ceased being an SMSF and has not appointed a registrable superannuation entity licensee as trustee.

[3] The policy on issuing a notice of non-compliance is in Law Administration Practice Statement PS LA 2006/19

[4] The policy on disqualifying an individual is in Law Administration Practice Statement PS LA 2006/17

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

9. In developing a compliance strategy, a notice of non-compliance will not be given to an SMSF if the Commissioner has accepted an undertaking by the trustee to rectify a contravention, provided the trustee is genuinely attempting to satisfy the terms of the undertaking.

10. An undertaking must contain, as a minimum, the essential terms described in paragraph 24 of this practice statement. A template to assist in the construction of an undertaking is provided in Attachment A.

11. In limited circumstances the Commissioner may be prepared to enter into an informal arrangement with a trustee to rectify a contravention. An informal arrangement is not entered into under section 262A of the SISA and would only be used in low risk cases.

12. In all cases it is the trustee who should propose the undertaking, not the Commissioner. However, the Commissioner may discuss with the trustee the various alternatives available, including the option of proposing an undertaking to rectify the contravention and what can be included in the undertaking.

13. The Commissioner will not accept an undertaking where the information available to the Commissioner indicates that the trustee will not or cannot comply with the undertaking.

14. Where the Commissioner decides not to accept an undertaking a notification will be sent to the trustee informing them of the decision and the reasons.

15. A trustee may withdraw or vary an undertaking at any time, but only with the consent of the Commissioner.

16. If the Commissioner considers the trustee has breached a term of the undertaking, the Commissioner can apply for a court order. However, the Commissioner will consider all compliance alternatives available (listed in paragraph 6) prior to making any decision.

EXPLANATION

17. Where it is fair and reasonable and the proposed undertaking is the appropriate way of addressing a contravention the Commissioner will enter into an enforceable undertaking.

When it is appropriate to accept an undertaking

18. It is recognised that contraventions may occur as a result of lack of knowledge or skills by the trustee, or other difficulties that a trustee may face in fulfilling their obligations. Therefore, where we find that a trustee is genuinely making an effort to meet their obligations, we will work with them to rectify the contravention wherever possible.

19. Factors to consider in deciding if an undertaking is appropriate:

- Can the contravention be rectified? For example, a contravention of the in-house assets rules can be rectified by the fund disposing of relevant assets. If a contravention cannot be rectified, then an undertaking is not appropriate.
- Does the contravention give rise to criminal consequences? Where there are criminal consequences it is not appropriate to accept an undertaking. This reflects the principle that a person may not contract out of criminal liability.

- Past behaviour of the trustee. It would be appropriate to accept an undertaking where the behaviour indicates that the trustee is likely to comply with it. However, it may not be appropriate to accept an undertaking if the trustee has contravened the provisions which they had previously completed an undertaking to rectify.
- The nature and seriousness of the contravention indicates that it is inappropriate to accept an undertaking. For example, 100 per cent of superannuation contributions, when received, are immediately lent to members.

20. It would also be inappropriate for the Commissioner to accept an undertaking in circumstances where there is evidence that the trustee/members have been knowingly involved in an arrangement where the anti-avoidance provisions in the tax laws may apply.

Formulating an undertaking with a client

21. When entering into discussions with a trustee, tax officers should identify the contraventions and explain what steps the trustee needs to take to comply with the law. For example, explaining that the trustee needs to reduce the fund's in-house asset level to 5% or less to comply with the in-house asset rules.

22. These discussions should help the trustee to formulate an acceptable undertaking for the rectification of the contravention. This does not preclude the trustee from providing their own alternatives.

23. For an undertaking to be enforceable it must be in writing and be accepted by the Commissioner.

The essential terms for an undertaking

24. The following are considered essential terms for an undertaking:

- What actions will be taken to rectify the contravention?.

  The undertaking should specify the manner in which the contravention will be rectified and should set out what actions the trustee will take to achieve this. For example, a loan to a relative of a member will be fully repaid to the fund with appropriate commercial interest.

- The time in which the contravention is to be rectified.

  Rectification should be completed by the trustee within a reasonable period of time. What is a reasonable period will depend on the circumstances of the case. For example, it would be reasonable to give a longer period of time to dispose of an asset such as residential property, than shares in a publicly listed company.

- How and when the trustee will report to the Commissioner on the progress made towards completion of the undertaking.

  The trustee needs to report their progress in fulfilling their commitment under the undertaking. The undertaking should specify how and when the trustee will report their progress to the Commissioner.

- A commitment to cease the behaviour which resulted in the contravention.

- If appropriate, the strategies required to be implemented by the trustee to prevent the contravention from occurring again.

  The trustee should provide details to the Commissioner of strategies that will be implemented to prevent the contravention from occurring again. These could involve changes in accounting and management practices.

25. Attachment A provides a format that may be adopted by a trustee in drafting an undertaking.

The circumstances in which it would be appropriate to permit a trustee to withdraw or vary the undertaking

26. A trustee gives an undertaking proposal to the Commissioner based on an assessment of their capacity to fulfil the proposal using the best information available to them at the time. However, following the making of the proposal, unforseen events may occur which make it necessary for the trustee to seek to change the terms of the undertaking.

27. The Commissioner will generally consent to the trustee withdrawing or varying the terms of the undertaking where the trustee proposes an alternative and appropriate course of action that will result in the timely rectification of the contravention and the protection of the retirement benefits of members. For example, the trustee may have undertaken to sell a residential property within three months; a contract has been signed however settlement will not occur until the fourth month and the trustee has submitted a request for an extension of time to comply with the undertaking.

28. The Commissioner will not consent to the trustee withdrawing or varying the terms of an undertaking where the trustee cannot show reasonable cause for requesting the withdrawal or variation.

29. The withdrawal or variation of the terms of an undertaking will not be allowed by the Commissioner if it compromises the rectification of the contravention or results in an adverse impact on the retirement benefits of members that did not exist with the original undertaking.

The consequences of not fulfilling an undertaking

30. Where a trustee fails to fulfil the terms of an undertaking, the Commissioner will consider if this has resulted in the rectification of the contravention being substantially incomplete.

31. If the Commissioner considers that there has been a substantial failure to rectify the contravention and this requires further compliance action, then the Commissioner will consider all the options listed below prior to making any decision:

    - issuing a fund with a notice of non-compliance
    - seeking a court order under subsection 262A(4)
    - disqualifying a particular individual and prohibiting them from acting as a trustee of a superannuation fund
    - suspending or removing a particular trustee
    - freezing the assets of a fund if there is a risk of the members' benefits being eroded, or
    - seeking civil and/or criminal penalties through the courts

Informal arrangements

32. In some cases the contravention and the behaviour of the trustee will be such that the Commissioner will be satisfied with the trustee making an informal arrangement to rectify the contravention.

33. An informal arrangement can be accepted where the risk of the contravention not being rectified is considered to be low and the rectification action will be completed within a short period of time. An example of this is where the trustee has already commenced the action required to correct the contravention.

34. It is expected that an informal arrangement will identify the actions to be taken by the trustee to rectify the contravention and the timeframe for doing so.

35. Informal arrangements should only be accepted from a trustee with a reasonable compliance history. In making this decision the Commissioner will consider a trustee's compliance with all their obligations under different taxation laws.[6]

36. The informal arrangement may be made orally, or it may be a written statement that does not contain all the essential elements for a written undertaking. If accepted the Commissioner will make a record of what has been proposed in discussions with the trustee for the purposes of reviewing the case for compliance with the informal arrangement.

Review rights

37. The decision regarding the acceptance of an undertaking is not a reviewable decision as defined in section 10 of the SISA. However, in line with the Commissioner's commitment under the taxpayers' charter, the Commissioner will conduct an informal internal review if a request is received from a trustee who is dissatisfied with the decision. The request should be in writing, setting out the reasons for the request, and must be made within a reasonable period of time after the trustee receives the notice of decision. As a general rule, a reasonable period of time will be 28 days after the notice of the decision.

38. The decision by the Commissioner not to accept an undertaking is reviewable under the *Administrative Decisions (Judicial Review) Act 1977*.

[6] Taxation law includes an Act of which the Commissioner has the general administration (including a part of an Act to the extent to which the Commissioner has the general administration of the Act) or legislative instruments made under such an Act (including such a part of an Act) – subsection 995-1(1) of the *Income Tax Assessment Act 1997*.

Amendment history

Date of amendment	Part	Comment
6 September 2012	Contact details	Updated
30 March 2012	Contact details	Updated.
21 October 2011	Contact details	Updated.
16 August 2011	Paragraph 35	Revised to clarify a trustee's obligations are under certain tax laws. Footnote 6 inserted to define those tax laws.
19 March 2009	Footnote 2	Inserted.
	Paragraph 31 and Attachment A	Significant revisions.
	Paragraphs 5, 16, 19, 21, 24, 27, 32, 33 and 36	Minor revisions.
9 January 2009	Paragraph 6	Legislative reference 120A of the *Superannuation Industry (Supervision) Act 1993* updated to section 126A of that Act.
	Contact details	Updated.
16 April 2008	Contact details	Updated.
11 February 2008	Contact details	Updated.
20 December 2007	Title (purpose) and paragraph 32	Replaced 'an enforceable' with 'a written'.

Subject references	enforceable undertaking informal arrangement self managed superannuation fund
Legislative references	ITAA 1997 995-1(1) SISA 10 SISA 40(1) SISA 126A SISA Pt 21 SISA 262A SISA 262A(4) SISA 264 AD(JR) Act 1977
Related practice statements	PS LA 2006/17 PS LA 2006/19
File references	06/17267
Date issued	30 November 2006
Date of effect	30 November 2006
Other Business Lines consulted	ARL, OCTC, SME, GST, OPS

Attachment A

ENFORCEABLE UNDERTAKING

AUSTRALIAN TAXATION OFFICE

SUPERANNUATION INDUSTRY (SUPERVISION) ACT 1993

Section 262A

The commitments in this undertaking are offered to the Commissioner of Taxation by:

The Trustee

<insert name> Superannuation Fund (ABN: <insert fund's ABN)

<insert address>

1.0 **Background**

1.1 <*This needs to clearly describe how you as a trustee of the fund contravened. Only those aspects relevant to the fund and the contravention should be mentioned.*>

1.2

1.3

2.0 **Undertakings**

Pursuant to section 262A of the *Superannuation Industry (Supervision) Act 1993* (SISA), the trustee(s) of the <insert fund's name> give(s) the following undertakings to the Commissioner of Taxation:

2.1 <*Insert the rectification/undertaking requirements here*. *These undertakings must describe the actions you as a trustee of the superannuation fund will do*.

2.2 *These undertakings need to include:*

- *what actions will be taken by you as the trustee of the fund to rectify the contravention*
- *the time in which you as the trustee of the fund intend to complete each of these actions*
- *how and when you as the trustee of the fund will report to us on your progress towards completion of the undertaking*
- *the records you as the trustee of the fund will maintain to prove that you have rectified the contravention*
- *your commitment as the trustee of the fund to cease the behaviour which resulted in the contravention*
- *the strategies required to be implemented by you as the trustee of the fund to prevent the contravention from occurring again (if appropriate).*>

3.0 **Acknowledgments** <*The undertaking will not be accepted if the acknowledgments are changed.*>

The trustee(s) of the <insert fund's name> acknowledge(s) that:

3.1 The undertaking may be withdrawn or varied only with the consent of the Commissioner of Taxation.

3.2 If any of the terms of the undertaking are contravened or not met the Commissioner will consider all the options listed below in determining the appropriate compliance treatment:

- issuing a fund with a notice of non-compliance
- seeking a court order under subsection 262A(4)
- disqualifying a particular individual and prohibiting them from acting as a trustee of a superannuation fund
- suspending or removing a particular trustee
- freezing the assets of a fund if there is a risk of the members' benefits being eroded, or
- seeking civil and/or criminal penalties through the courts

3.3 This undertaking does not inhibit or restrict the Commissioner or any other person impacted by the conduct of the trustee in fulfilling the undertaking from pursuing the rights and remedies available under the law.

3.4 The Commissioner's acceptance of this undertaking does not affect the Commissioner's powers to investigate a contravention arising from future conduct.

3.5 The undertaking has no effect until accepted by the Commissioner.

EXECUTED BY

The Trustee

<insert name> Superannuation Fund (ABN: <insert ABN of fund>)

_____	_____	_____
Director/Trustee	Print name	Date
_____	_____	
Director/Trustee	Print name	Date
_____	_____	
Director/Trustee	Print name	Date
_____	_____	
Director/Trustee	Print name	Date