SMSFD 2008/1 - Self Managed Superannuation Funds: how does the happening of an event in subregulation 13.22D(1) of the Superannuation Industry (Supervision) Regulations 1994 affect whether a self managed superannuation fund's investments in related companies or unit trusts are in-house assets of the fund?

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Self Managed Superannuation Funds Determination

Self Managed Superannuation Funds: how does the happening of an event in subregulation 13.22D(1) of the Superannuation Industry (Supervision) Regulations 1994 affect whether a self managed superannuation fund's investments in related companies or unit trusts are in-house assets of the fund?

Preamble

Self Managed Superannuation Funds Determinations (whether draft or final) are not legally binding on the Commissioner. However, if the Commissioner later takes the view that the law applies less favourably to you than the final version of this ruling indicates, the fact that you acted in accordance with the final version of this ruling would be a relevant factor in your favour in the Commissioner's exercise of any discretion as to what action to take in response to a breach of that law. The Commissioner may, having regard to all the circumstances, decide that it is appropriate to take no action in response to the breach.

Ruling

1. The happening of an event in subregulation 13.22D(1) of the Superannuation Industry (Supervision) Regulations 1994 (SISR)[1] may mean that a self managed superannuation fund's (SMSF's) investments in related companies or unit trusts are no longer excluded as in-house assets of the SMSF under subparagraph 71(1)(j)(ii) of the *Superannuation Industry (Supervision) Act 1993* (SISA).

[1] All legislative references in this Determination are to the Superannuation Industry (Supervision) Regulations 1994 unless otherwise indicated.

2. If the event in paragraph 13.22D(1)(a) happens,[2] it happens in relation to the SMSF. From the time when the event happens, *all* investments held by an SMSF in related companies or unit trusts are not excluded as in-house assets of the SMSF under subparagraph 71(1)(j)(ii) of the SISA. Therefore, from that time those investments are in-house assets of the SMSF.[3] Further, the existing investments and any future investments in those related companies or unit trusts can never again be excluded as in-house assets under subparagraph 71(1)(j)(ii) of the SISA even if the number of members of the SMSF is again less than five. However, if the members of the SMSF are again less than five (that is, paragraph 13.22C (2)(a) is satisfied) and the other requirements of regulation 13.22C are satisfied, regulation 13.22C can apply to later investments in *other* companies or unit trusts, which means those investments are excluded from being in-house assets under subparagraph 71(1)(j)(ii) of the SISA. The happening of the event in paragraph 13.22D(1)(a) is illustrated in Example 1 at paragraph 6 of this Determination.

3. If one of the events in paragraphs 13.22D(1)(b) to (n) happens, it happens in relation to a particular company or unit trust. From the time when the event happens, investments held by the SMSF in that *particular* related company or unit trust are not excluded from being in-house assets of the SMSF under subparagraph 71(1)(j)(ii) of the SISA. Therefore, from that time those investments are in-house assets of the SMSF.[4] Further, the existing investments and any future investments in that particular related company or unit trust can never again be excluded from being in-house assets under subparagraph 71(1)(j)(ii) of the SISA even if the circumstance that caused the event to happen no longer exists. However, regulation 13.22B or 13.22C, as appropriate, can continue to apply to investments in other related companies or unit trusts held at the time when the event in paragraphs 13.22D(1)(b) to (n) happened, which means those investments are excluded from being in-house assets under subparagraph 71(1)(j)(ii) of the SISA. Regulation 13.22C can also apply to later investments in a related company or unit trust that is not a company or unit trust in relation to which an event in paragraphs 13.22D(1)(b) to (n) happened. The happening of the event in subparagraph 13.22D(1)(c)(i) is illustrated in Example 2 at paragraph 10 of this Determination.

Funds to which this Determination applies

4. This Determination applies to Self Managed Superannuation Funds[5] (SMSFs) and former SMSFs.[6] References in the Determination to SMSFs include former SMSFs unless otherwise indicated.

[2] This event happens if the number of members of the fund increases to five or more. Upon the happening of this event, the fund is no longer an SMSF under section 17A of the SISA, which requires an SMSF to have fewer than five members – see paragraph 17A(1)(a) of the SISA. Instead, it is a 'former SMSF'; that is, a fund to which subsection 10(4) of the SISA applies.
[3] This assumes that no other provision of the SISA applies to exclude the investment as an in-house asset.
[4] This assumes that no other provision of the SISA applies to exclude the investment as an in-house asset.
[5] As defined in section 17A of the SISA.
[6] A former SMSF is a fund that has ceased being a SMSF and has not appointed a registrable superannuation entity (RSE) licensee as trustee – see subsection 10(4) of the SISA.

Date of effect

5. This Determination applies both before and after its date of issue. However, the Determination does not apply to taxpayers to the extent that it conflicts with the terms of settlement of a dispute agreed to before the date of issue of the Determination.

Commissioner of Taxation
20 February 2008

Appendix 1 – Examples

This Appendix is provided as information to help you understand how the Commissioner's view has been reached.

Example 1 – the event in paragraph 13.22D(1)(a) happens as the number of members of the SMSF increases from four to five

6. On 1 June 2000 an SMSF invests in related unit trusts (Trust A and Trust B). At this time the number of members of the SMSF is four. The SMSF's investments in Trust A and Trust B are excluded from being in-house assets under subparagraph 71(1)(j)(ii) of the SISA.[7]

7. On 1 February 2007 the number of members of the SMSF increases to five. As the event in paragraph 13.22D(1)(a) has happened it affects the SMSF's investments in Trust A and Trust B. From 1 February 2007 the SMSF's investments in Trust A and Trust B are not excluded from being in-house assets of the SMSF under subparagraph 71(1)(j)(ii) of the SISA.

8. On 31 July 2007 the number of members of the SMSF reduces to four. Notwithstanding this, the existing investments in Trust A and Trust B and any future investments in Trust A and Trust B still cannot be excluded from being in-house assets of the SMSF under subparagraph 71(1)(j)(ii) of the SISA. Assuming that no other exception in section 71 of the SISA applies, the SMSF's existing investments in Trust A and Trust B are in-house assets of the SMSF under subsection 71(1) of the SISA. Any future investments made by the SMSF in Trust A or Trust B would also be in-house assets of the SMSF.

9. On 15 August 2007 the SMSF invests in another related unit trust (Trust C). As the SMSF did not hold an investment in Trust C at the time when the event in paragraph 13.22D(1)(a) happened the investment in Trust C can be excluded from being an in-house asset under subparagraph 71(1)(j)(ii) of the SISA. The investment in Trust C must meet all the requirements of regulation 13.22C if it is to be excluded under subparagraph 71(1)(1)(j)(ii) of the SISA from being an in-house asset. Regulation 13.22C is relevant as the investment in Trust C was acquired by the SMSF on or after 28 June 2000.

Example 2 – the event in subparagraph 13.22D(1)(c)(i) happens as a related unit trust in which the SMSF has invested borrows money

10. On 1 June 2000 an SMSF invests in a related unit trust (Trust D). On 1 January 2007 the SMSF invests in another related unit trust (Trust E). Both investments are excluded from being in-house assets under subparagraph 71(1)(j)(ii) of the SISA.[8]

[7] That is, the investments in Trust A and Trust B meet all the requirements of regulation 13.22B. Regulation 13.22B is relevant as the investments in Trust A and Trust B were acquired by the SMSF before 28 June 2000.

[8] That is, the investment in Trust D (which was acquired before 28 June 2000) meets all the requirements of regulation 13.22B and the investment in Trust E (which was acquired on or after 28 June 2000) meets all the requirements of regulation 13.22C.

11. On 15 May 2007 the trustees of Trust D borrow money, which is the event mentioned in subparagraph 13.22D(1)(c)(i). As this event has happened to Trust D it affects the SMSF's investments in Trust D. From 15 May 2007 the SMSF's investment in Trust D is not excluded from being an in-house asset under subparagraph 71(1)(j)(ii) of the SISA. Assuming that no other exception in section 71 of the SISA applies, the SMSF's existing investment in Trust D is an in-house asset of the SMSF under subsection 71(1) of the SISA. Any future investments made by the SMSF in Trust D would also be in-house assets of the SMSF.

12. However, the SMSF's investment in Trust E is not affected by the borrowing undertaken by the trustees of Trust D. Therefore, the SMSF's investment in Trust E continues to be excluded from being an in-house asset of the SMSF under subparagraph 71(1)(j)(ii) of the SISA.

13. Any future investments in a related company or unit trust other than Trust D can also be excluded from being in-house assets of the SMSF under subparagraph 71(1)(j)(ii) of the SISA provided that the requirements in regulation 13.22C are met in relation to those investments.

Appendix 2 – Explanation

This Appendix is provided as information to help you understand how the Commissioner's view has been reached.

Background

14. Subsection 71(1) of the SISA sets out the meaning of 'in-house asset'. An investment in a related company or a related unit trust is included as an in-house asset. However, subparagraph 71(1)(j)(ii) of the SISA excludes certain investments specified in the regulations (namely regulations 13.22B and 13.22C in Division 13.3A) from the meaning of 'in-house asset' in subsection 71(1) of the SISA. Thus the investment in a related company or related unit trust must meet the requirements of either regulation 13.22B or 13.22C to be excluded from being an in-house asset under subparagraph 71(1)(j)(ii).

15. Regulation 13.22B is relevant if an investment was acquired before 28 June 2000. Regulation 13.22C is relevant if an investment is acquired on or after 28 June 2000.

Explanation

16. If regulation 13.22B or regulation 13.22C applies to an investment in a related company or related unit trust, that investment is excluded from being an in-house asset under subparagraph 71(1)(j)(ii) of the SISA.

17. However, if an event in regulation 13.22D(1) happens it can affect whether an investment continues to be excluded from being an in-house asset under subparagraph 71(1)(j)(ii) of the SISA. Depending upon the event that happens, it may mean that all investments held in related companies and unit trusts at the time when the event happens become in-house assets of the SMSF, or it may mean that only investments in a particular related company or unit trust become in-house assets of the SMSF.

The event in paragraph 13.22D(1)(a) happens

18. The event in paragraph 13.22D(1)(a) happens if the number of members of the SMSF increases to five or more. In contrast to the events at paragraph 13.22D(1)(b) to (n) this event happens in relation to the SMSF and not in relation to a particular related company or unit trust.

19. If an SMSF has investments in related companies or unit trusts to which either regulation 13.22B or 13.22C applies and the event in paragraph 13.22D(1)(a) happens, regulation 13.22B or 13.22C (as applicable) ceases to apply to *all* those investments. From the time when the event happens the SMSF's investments in those related companies or unit trusts are no longer excluded from the in-house assets of the SMSF under subparagraph 71(1)(j)(ii) of the SISA.

20. Subregulation 13.22D(3) provides that if regulation 13.22B or 13.22C ceases to apply to an investment in a related company or unit trust, neither regulation can apply to any investment made at any time by the SMSF in that related company or unit trust.

21. This means that even if the number of members of the SMSF is again less than five, neither regulation 13.22B nor 13.22C can apply to any existing or future investments in those companies or unit trusts in which the SMSF held investments at the time when the event in paragraph 13.22D(1)(a) happened. Therefore, investments in those related companies and unit trusts can never again be excluded from being in-house assets of the SMSF under subparagraph 71(1)(j)(ii) of the SISA.

22. However, regulation 13.22C can apply to an investment made by the SMSF in a related company or unit trust in which the SMSF did not have any investments at the time when the event in paragraph 13.22D(1)(a) happened, if the members of the SMSF are again less than five (that is, paragraph 13.22C(2)(a) is satisfied) and the other requirements of regulation 13.22C are met. If regulation 13.22C applies the investment is excluded from the in-house assets of the SMSF under subparagraph 71(1)(j)(ii) of the SISA.

23. The effect of the event in paragraph 13.22D(1)(a) happening is illustrated by Example 1 at paragraph 6 of this Determination.

An event in paragraph 13.22D(1)(b) to (n) happens

24. An event mentioned in paragraph 13.22D(1)(b) to (n) happens in relation to a *particular* company or unit trust. As the event happens to a particular company or unit trust it only affects the investments held by the SMSF in that particular company or unit trust.

25. If an SMSF has investments in a related company or unit trust to which either regulation 13.22B or 13.22C applies and an event in paragraph 13.22D(1)(b) to (n) happens in relation to that company or unit trust, regulation 13.22B or 13.22C (as applicable) ceases to apply to the SMSF's investments in that particular company or unit trust. From the time when the event happens the SMSF's investments in that particular related company or unit trust are no longer excluded from the in-house assets of the SMSF under subparagraph 71(1)(j)(ii) of the SISA.

26. Subregulation 13.22D(3) applies in the same way as explained in paragraph 20 of this Determination. This means that even if the circumstance that gave rise to the event happening no longer exists, neither regulation 13.22B nor 13.22C can apply to any existing or future investments in that particular company or unit trust. Therefore, investments in that particular related company or unit trust can never again be excluded from being in-house assets of the SMSF under subparagraph 71(1)(j)(ii) of the SISA.

27. However, regulations 13.22B and 13.22C continue to apply to investments held by the SMSF in other related companies or unit trusts in respect of which the event in paragraph 13.22D(1)(b) to (n) did not happen. Regulation 13.22C can also apply to future investments in the other related companies or unit trusts. If regulation 13.22B or 13.22C applies the investment is excluded from the in-house assets of the SMSF under subparagraph 71(1)(j)(ii) of the SISA.

28. The effect of the event in subparagraph 13.22D(1)(c)(i) happening is illustrated by Example 2 at paragraph 10 of this Determination.

References

Previous draft:

SMSFD 2007/D2

Subject references:

- in-house assets
- self managed superannuation funds
- superannuation

Legislative references:

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- SISA 1993 10(4)
- SISA 1993 17A
- SISA 1993 17A(1)(a)
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- SISR 1994 Div13.3A
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- SISR 1994 13.22D(1)(e)
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- SISR 1994 13.22D(1)(k)
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- SISR 1994 13.22D(1)(m)
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- SISR 1994 13.22D(3)

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