Setting Up An SMSF In 7 Steps

Managing an SMSF requires time and financial education, therefore before setting up an SMSF, it is important to first understand:

The costs and benefits of an SMSF versus the current fund

What is involved in managing an SMSF and the obligations of a trustee.

Once the decision has been made to commence an SMSF, a number of superannuation, corporate, trust and tax laws must be followed to properly set up an SMSF, for it to be a complying superannuation fund eligible for tax concessions.

Most of these are administrative processes, while others usually require the assistance of a financial adviser.

Step 1 – Decide on fund structure The first thing to decide on is whether the fund should have individual trustees or a corporate trustee structure.

The corporate trustee structure generally trumps the individual trustee structure from a strategic perspective but is more expensive. For example, the corporate trustee structure is generally chosen for trustee succession and asset protection reasons despite the extra costs involved.

The trustees need to choose the best way to structure the SMSF so it complies with the law and suits the circumstances of the members.

The requirements are different depending on whether the fund has a corporate trustee, individual trustees or is a single member fund.

All members of the fund must be individual trustees or directors of the corporate trustee.

Ensure the people who become trustees or directors of the SMSF:

Are eligible to be a trustee or director

Understand what it means to be a trustee or director

Consent in writing to their appointment

Sign the trustee declaration stating that they understand their duties and responsibilities (this must be done within 21 days of becoming a trustee or director).

All trustees and directors are bound by the trust deed and are equally responsible if its rules are not followed.

Individual trustees

In general, if the fund has individual trustees, it legally qualifies as an SMSF if:

It has four or less members

Each member is a trustee

No member is an employee of another member, unless they are related no trustee is paid for their duties or services as a trustee.

Corporate trustees

In general, if the fund has a corporate trustee, it legally qualifies as an SMSF if:

It has four or less members

Each member of the fund is a director of the company

Each director of the corporate trustee is a member of the fund

No member is an employee of another member, unless they are related the corporate trustee is not paid for services as a trustee

No director of the corporate trustee is paid for their duties or services as director in relation to the fund.

Single member fund

For single member funds with corporate trustees, the member needs to be either a sole director of the company or one of only two directors, that is either related to or not an employee of, the other director. A fund can also have two individual trustees provided one trustee is a member and the other is either a person related to the member, or another person who does not employ them.

Table 1 contains general information about some of the things to consider when choosing the type of SMSF trustee.

Table 1: SMSF structures

Feature	Individual trustees	Corporate trustee
Administrative costs	No additional costs at establishment. There are no ASIC fees, so establishment costs and ongoing administrative requirements are less. However, changes in trustees due to members exiting or entering the fund can result in potentially significant paperwork and administrative costs.	There are higher costs in establishing a corporate trustee. Currently, the initial ASIC registration fee is $495 plus $267 p.a. (standard) or $54 p.a. (sole purpose). Having a corporate trustee can make it easier to administer ownership of fund assets and keep assets separate from any personal or business assets.
Ownership of assets*	Ownership of all assets is in the name of all individual trustees. Changing trustees can be time-consuming and costly if the fund owns many assets.	The easiest way to comply with the ownership rules is for your fund to have a company set up solely for the purpose of being trustee of the fund. Recording and registering assets can be simpler, particularly for changes in membership.
Limited recourse borrowings	Some lenders are refusing to grant limited recourse loans to individual trustees or they otherwise offer lower loan to value ratios (LVRs).	The corporate trustee would satisfy any lender's trustee requirement.
Asset protection	Individual trustees may be exposed to liability actions in relation to the fund (e.g. property claims) making personal assets exposed. They also share joint liability at trustee level regardless of who commits the offence.	Companies have limited liability, which offers greater protection if the trustee is sued for damages. For special purpose trustees, any action is limited to the assets of the company, not the directors themselves. The directors may also be indemnified from any illegal conduct undertaken by the other directors without their knowledge.
Succession planning	There is often a lack of continuity in the event of death and increased administration. A fund with individual trustees is not likely to continue to operate as usual when changes in trustees occur, unless an appropriate succession plan is in place.	A company continues in the event of a member's death. Control of an SMSF and its assets is more certain in the event of the death or incapacity of a member. The company continues indefinitely and can provide transition control post-death (e.g. by bequeathing shares to the next trustee that is also executor).

Source: Adapted from ATO 2011 Corporate trustee

If a corporate trustee is selected:

Decide on a name for the corporate trustee (not similar to other entities of the members). It is generally best to make it personal — even link it to a goal, aspiration or favourite place.

Check the ASIC website to ensure the chosen name is available on the company register.

Ensure the member trustee laws are satisfied by making sure that all members are trustee directors and all trustee directors are members (limited exceptions apply).

Use a new SMSF special purpose corporate trustee, not a company with a history or a standard company, to create greater separation.

In terms of the offices held, the following appointments apply:

Director

A director of a company is a person who is responsible for managing the company's business activities. Each member must be a director.

Shareholder

While not compulsory, it is generally recommended for the directors to be equal shareholders. In terms of the number of shares to be held, consider the family dynamic when allocating the shares.

Public officer

A public officer is the representative for a company, and therefore that person will serve as the face of the company for tax purposes. All actions carried out in their capacity as a public officer are deemed to have been done by the company. For practical purposes, this normally goes to the more financially astute member or the one with the longer life expectancy.

Secretary

The role of the secretary is to support the chair in ensuring the smooth functioning of the management committee. In summary, the secretary is responsible for ensuring meetings are effectively organised and minuted and maintaining effective records and administration. Again, for practical purposes, this normally goes to the more financially astute member or the one with the longer life expectancy.

Shareholdings and control of an SMSF

For a family of five, the trustee of a two-member SMSF might allocate 60 shares in the trustee company each to the two shareholders, since the shareholdings are divisible by five, four, three and two. In the event of death, these shares form part of the deceased estate and would be dealt with in accordance with their Will. The holding of these shares would be instrumental in determining who controls the SMSF post-death.

It is essential for the corporate trustee to be executed before the SMSF trust deed for the SMSF set-up to be legally effective.

Step 2 – Trust deed and governing rules

To create a superannuation fund, you need to have:

Trustees (e.g. individual or corporate)

Governing rules (such as a trust deed)

Property (assets or cash, such as an initial nominal consideration to give legal effect to the trust, can be used, for example, $10 attached to the trust deed)

Identifiable beneficiaries (e.g. fund members).

Having a trust deed evidences the existence of a trust, which together with the superannuation laws, form the fund's 'governing rules', that detail the powers, duties and responsibilities of the fund's trustees, as well as the rights of fund members.

The trust deed covers areas such as:

The fund's objectives

Appointment of trustees

Admittance of fund members

Acceptance of contributions and rollovers

Calculation basis for member accounts administrative procedures

Apportioning taxes and other expenses

Benefit payment conditions

Existence of reserves

Asset valuation procedures

Investment powers

Fund wind-up provisions

All trustees need to sign and date the trust deed and ensure it is properly executed according to state or territory laws.

Ideally, the trust deed should be easy to understand and broadly worded in order to facilitate a wide range of strategic options.

It is important to ensure the trust deed:

Does not contain any provisions which might limit its strategic ability

Can satisfy any special needs of the members

Ensures that minimal amendments are required following superannuation law changes.

The ATO has provided guidance stating that in order for an SMSF to be established, it must have assets set aside for members. ATO systems generally will not allow an annual return to be lodged with nil assets (unless it is a wind-up return).

If a rollover, transfer or contribution is expected in the near future, a nominal amount (for example, $10) can be held with the trust deed. This amount is regarded as a contribution and must be allocated to a member.

Getting complying fund status

An SMSF can elect to be a regulated fund under one of two powers:

Corporations power (i.e. company established under corporation’s law).

Pension’s power (i.e. primary purpose of fund is to provide old age pensions).

Once the ATO has processed the election notice, it will issue a notice to the fund confirming the election within 60 days.

Remember, the entity must be an Australian superannuation fund to be a compliant SMSF (i.e. broadly established in Australia, central management and control is in Australia, and Australian resident active members have at least 50% of the total assets of active members).

Sign the trustee declaration

New trustees (or directors of a corporate trustee) need to sign a declaration within 21 days of becoming a trustee or director stating they understand their obligations and responsibilities as a trustee or director of the corporate trustee.

Trustees must keep the completed declaration for the life of the SMSF and for at least 10 years after the SMSF winds up.

Applications for membership and consents to act as trustee

New members are required to complete an application for membership form to join the SMSF. On acceptance, the trustee would usually provide a letter of confirmation. The trust deed will outline the rules of eligibility regarding fund membership.

The trustees or directors would also be required to make the following declarations in consenting to act as trustee or director:

1. I have not been convicted of an offence in respect of dishonest conduct.

2. I have not had a civil penalty order made against me under the Superannuation Industry (Superannuation) Act 1993.

3. I am not an insolvent under administration.

4. I have not been disqualified to act as trustee under section 120A of the Superannuation Industry (Superannuation) Act 1993.

The trustee of the SMSF is also required to provide new members (even if the same person) with notices or documents outlining the main benefits of the fund, the purpose of the fund, and the rules of fund membership.

Get an electronic service address

If your SMSF is to receive contributions from employers (other than related-party employers), it needs to be able to receive the contributions and associated SuperStream data electronically.

SuperStream is a data and payment standard that applies to superannuation contributions made by employers to any superannuation fund, including SMSFs. To receive SuperStream data you need an electronic service address, which is a special internet address and different to an email address (ATO 2020).

For SuperStream message solution providers:
https://www.ato.gov.au/Super/SuperStream/Selfmanaged-super-funds/Electronic-service-address/Register-of-SMSF-messaging-providers/

The employer will need their ABN, bank account details (BSB and account number) and an electronic service address.

Step 3 – Dealing with the ATO Once the fund is established and all trustees have been appointed (including signing the trustee declaration), trustees have 60 days to register the SMSF with the ATO by applying for an Australian Business Number (ABN).

For the fund to be 'live' and ready to receive rollovers, it would need to be evidenced by being 'registered' on the 'Superannuation Fund Lookup' tool located on the ATO website. Also, funds that are not regulated are not entitled to tax concessions and the employer (and eligible members) cannot claim a tax deduction for contributions made to the fund.

When completing the application process:

Ask for a tax file number (TFN) for the fund

Elect for your fund to be an ATO-regulated SMSF (if not, the fund will not receive tax concessions and there will be no tax deductions for contributions)

Register for GST (if necessary).

ATO election methods

To summarise, there are two options to lodging your election with the ATO.

These are:

Online via the ATO website "Register your fund and get an ABN"

Alternatively, a tax agent can apply for registration and obtain necessary ABNs/TFNs online. Tax professionals can use the Australian Business Register's 'tax professional's services' to register SMSFs and apply for an ABN on behalf of clients.

If a member has not quoted their TFN:

The fund cannot accept member contributions made on their behalf, including personal and eligible spouse contributions

The fund needs to pay extra tax on contributions, such as employer and salary sacrifice contributions

The member may not be able to receive the superannuation co-contribution.

Registering for GST

SMSFs with annual GST turnover of more than $75,000 must register for GST (otherwise its optional). Annual GST turnover does not include: ▯ contributions ▯ interest and dividends ▯ residential rent or income generated outside Australia.

If a fund does not register, there will be no refund of any GST payable in relation to fund expenses and it will not charge GST on any of its commercial/lease income.

Step 4 – Get the banking and ownership right Once an SMSF is established and registered, the trustee will need to set up a bank account. This can generally be done online or by visiting a branch.

A bank account is required to manage the fund's operations and accept contributions, rollovers of superannuation and income from investments, as well as pay the fund's expenses, pensions and other liabilities.

It is a serious compliance breach if your personal and business assets become mixed up with your SMSF assets.

It is generally best to have your SMSF bank accounts quarantined from your other personal and business accounts to lessen the likelihood of mistaken payments that may cause big problems for your SMSF.

If the trustee has not yet received their ABN or TFN from the ATO, this should not prevent trustees from establishing the SMSF bank account. The bank will withhold tax on any interest earned until the bank receives the ABN or TFN, which can be later refunded.

Protecting SMSF assets

Consider implementing a few safeguards to help protect your SMSF assets. Here are a few ideas to consider:

Have joint bank account signatories to safeguard the assets from misuse and to minimise the risk of compliance breaches.

Ensure your internet banking provides for co-authorities.

Ensure the fund's bank account is kept separate from other personal or business accounts.

Where possible, have your chosen SMSF bank different to that of your other accounts to further minimise the risks of costly mistakes (i.e. keep it quarantined from other accounts).

Similarly, on SMSF set-up, try to keep the names of the SMSF entity distinct and different to your other entities.

Ensure chosen bank account has the full legal ownership correct.

Step 5 – Investment strategy Once an SMSF has been established and registered with the ATO and the banking is sorted, it is important to then consider the appropriate time to move moneys into your newly established SMSF, whether that be in the form of a 'rollover' from another Superannuation fund or by way of 'contributions'.

It is recommended that you do not rollover any moneys until you are very clear on your initial investment strategy. The timing often depends on the investment strategy to be employed.

For example, if your investment strategy involves acquiring a property, it is generally wise to hold off 'cashing up' the SMSF in readiness for the purchase until you have an unconditional contract otherwise you might be left with large amounts in cash out of the market, if the contract falls over.

The investment strategy sets out the fund's investment objectives and specifies the types of investments your fund can make.

Your investment strategy should be in writing and must:

Be reviewed regularly to ensure it continues to reflect the purpose and circumstances of your fund and its members (your review and any decisions made should be documented)

Consider whether to hold insurance cover (such as life insurance) for each member of your SMSF (ATO 2015).

When preparing and reviewing your investment strategy, consider the personal circumstances of all fund members, including age and risk tolerances.

Superannuation law requires all trustees to formulate and implement an investment strategy, which addresses issues such as:

Diversification

The risk and likely return from investments

The liquidity of fund's assets

The fund's ability to pay benefits

The members' retirement needs.

Step 6 – Appoint your service providers

You must appoint an approved SMSF auditor to audit your fund each year, not later than 45 days before you need to lodge your SMSF annual return.

Step 7 – Prepare an exit strategy. Even when you are setting up your SMSF you need to consider what might happen when your SMSF ends, or finally winds up.

Sometimes SMSFs become difficult to manage because of an unexpected event such as:

A relationship breakdown between the trustees

An illness or accident that leaves a trustee incapacitated (and unable to perform their role as a trustee)

A trustee is overseas

A trustee dies.

Having an exit strategy or plan may help reduce the impact of such unexpected events.

As part of your exit strategy, consider the following precautions:

Ensure all trustees can access the SMSF's records and electronic transaction accounts.

Include specific rules in your fund’s trust deed that are triggered by events that could otherwise lead to the fund becoming unmanageable.

Ensure all members make binding death benefit nominations (and renew them every three years or as required under the trust deed).

Encourage members to appoint an enduring power of attorney to enable the fund to function in the event of incapacity.

Be aware of any taxes that might be payable in the event of death when non-dependent beneficiaries are favoured.

Be aware of the likely costs involved in winding up an SMSF.

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