Super Concepts

FACT SHEET

You need to be present:
SMSFs and residency

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To be a complying superannuation fund and enjoy concessional tax treatment, a self-managed superannuation fund (SMSF) needs to satisfy the 'residency test' at all times.

The residency test will be an issue for those who depart Australia permanently and have an SMSF, and may also cause issues for members who intend to depart Australia for an extended period of time to travel or work overseas.

Understanding the residency test is important as there are significant adverse tax implications for SMSFs who fail it. They lose concessional tax treatment and pay tax on income at the highest marginal rate, currently 45%. Further, in the year the fund first fails the residency test, its income will include the market value of the assets less any non-concessional contributions at the start of the year. That is, potentially you could lose up to 45% of the value of your SMSF in tax!

Demonstrating residency

For an SMSF to meet the residency test, it must be considered an "Australian Superannuation Fund" and satisfy the following three requirements at all times during the year.

Requirement 1

"The fund was established in Australia, or any asset is situated in Australia"

This test will be met if the initial contribution made to establish the fund was paid to and accepted by the trustee(s) in Australia. The test is also met if any asset of the fund is situated in Australia. For example, if the fund has a bank account that was set up in Australia.

Requirement 2

"The fund has no active members, or where there are active members, at least 50% of the market value of fund's assets attributable to active members, are held by active members who are Australian residents for income tax purposes"

Active members are those in receipt of contributions or rollovers to the fund. The "active members test" requires that a fund either has no active members or, where the fund does have at least one active member, that 50% of:

i The total market value of fund assets that are attributable to active members; or

ii The sum of withdrawal benefits payable to active members is attributable to active members who are Australian residents for income tax purposes (tax resident).

This generally means that the SMSF should not accept contributions from members whilst overseas and who are not considered a tax resident, unless the fund has tax-resident active members who hold a majority member balance.

Some members may choose to direct their contributions to a public offer fund whilst overseas and not a tax resident. They may then consider a rollover from the public offer fund to their SMSF, once they return to Australia and become a tax resident.

Requirement 3

"The central management and control of the fund is ordinarily in Australia"

The ATO's view on the central management and control is covered in Taxation Ruling TR 2008/9 "The meaning of Australian Superannuation Fund". The central management and control is generally performed by the trustee(s) and relates to the strategic and high-level decision-making processes and activities of the fund, including:

- Formulating the investment strategy for the fund;
- Reviewing and updating or varying the fund's investment strategy as well as monitoring and reviewing the performance of the fund's investments;
- Determining how the assets of the fund are to be used to fund member benefits.

Other day-to-day activities do not generally constitute the central management and control as they are of a more formalistic or administrative nature. Examples of such activities include:

- The actual investment of the fund's assets;
- The fulfilment of administrative duties;
- The acceptance of contributions that are made on a regular basis; and
- The payment of benefits.

How to meet the 'central management and control' requirement

Establish the absence is temporary

The central management and control of a fund can still be ordinarily in Australia even where it is temporarily outside Australia, provided the person or persons who exercise the central management and control are absent from Australia for a relatively short period of time.

Temporary absence is determined by the intention of the members, supported by the facts of the situation, such as employment contracts, the location of assets and family. Temporary absence must also be determined objectively and on a real-time basis, that is, it cannot be established in retrospect. For example, where a member departs overseas to fulfil a specific passing purpose, such as the completion of a two-year employment contract, this would support the absence is temporary.

Taxation Ruling TR 2008/9 includes examples (specifically example 6, 7 and 8) that assist with determining when the central management and control is "ordinarily in Australia". It would be recommended that trustees document the circumstances of their departure to establish the temporary nature of their absence.

Small APRA Fund

The SMSF could organise for a resident commercial organisation to act as the approved trustee of the fund. In this case, the SMSF would become a 'Small APRA Fund' and be regulated by APRA. This solution will overcome the issue in relation to the central management and control of the fund, as the fund would have a resident trustee.

Equal number of residents vs non-residents

Where there are an equal number of trustees or trustee directors located in Australia and overseas, who each substantially and actively participate in central management and control of the fund from these locations, the ATO considers that the central management and control of the fund is ordinarily in Australia.

To establish equal representation, an option could be to add additional trustees or directors to the fund. It is important that the resident party doesn't simply follow instructions from the non-resident party and that all individuals substantially and actively participate in the central management and control of the fund.

Enduring powers of attorney (EPOA)

Another option is to delegate the central management and control to another person. An enduring power of attorney can give the person nominated the power to replace the delegator as trustee (or director of the corporate trustee) and make decisions on behalf of the fund. It is important to note that having a power of attorney alone doesn't provide the nominated person with the power to act as trustee, they must also be formally appointed as trustee of the fund (or director in the case of a corporate trustee). The power of attorney can be restricted to decision making powers for the fund only.

When the central management and control is delegated to another person, it is important that the functions are performed by this person in their own right, rather than under instruction or influence from the delegator. In cases where the person in one location passively accepts the decisions made by a person in another location, it cannot be said that they are participating in the central management and control of the fund.

Once appointed as a trustee or trustee director, the EPOA assumes the duties, responsibilities and obligations in their own capacity and not as an agent for the member.

If an EPOA is used, the delegator would have to resign as a trustee or trustee director (except when the EPOA is acting as an alternate director), with the EPOA becoming a trustee or trustee director of the SMSF with all the appropriate changes to title and signatory rights that come with it.

Combination of EPOA and equal number of trustees

A common option for a fund with two trustees both going overseas is for only one of the existing trustees to resign as trustee but remain as a member and appoint a family member or friend who holds the EPOA to be the fund trustee in place of the delegator. This means one of the trustees remains and only one party is appointed as trustee.

Deal with residency before you leave Australia

It is important that residency issues are dealt with prior to trustees leaving Australia, as it may be too late to put in place the appropriate solution after the trustees have left or after their subsequent return. The residency test is one that must be met "at all times" and once failed, cannot be rectified retrospectively, which may result in significant adverse tax consequences. If you're planning to be outside of Australia, consider whether it may affect your SMSF's ability to meet the residency test. If in doubt, get professional advice before you leave.

Further information

CALL
1300 023 170

EMAIL
enquiries@superconcepts.com.au

VISIT
superconcepts.com.au