

SMSF Audit Tips and Traps

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Introduction

- Asset valuation issues
- Investment strategy issues
- NALI risks
- COVID impact and audit considerations

Asset Valuation Issues

- Reg 8.02B requires all assets to be reported at market value every year end
- Therefore, that means NO 3 year property valuations
- The auditor must be provided with sufficient appropriate audit evidence

Asset Valuation Issues

- ATO guidelines do appear contradictory – it notes the trustee doesn't need to source valuation information if there has been no significant event effecting the asset value
 - But without the valuation evidence, how would the auditor know if there has been a significant event or not?

ATO Guidelines

- The ATO believe trustees should source a variety of information to substantiate the market value
- One item of evidence is not sufficient for the ATO

ATO Guidelines

- ATO guidelines require property value evidence such as real estate agent appraisals to include comparable sales information

Asset Valuation Issues

- Unlisted investments are challenging, but without sufficient appropriate audit evidence on value expect a qualified part A, qualified part B and ATO reporting.

Asset Valuation Issues

- Extend to audit risks relating to
 - Member account balance manipulation
 - To allow more into pension
 - To allow more contributions
 - To manipulate member balances to disadvantage one member over another

Investment Strategies

- Ensure the strategy complies with the SIS requirements
 - Whole of the circumstances of the fund
 - Risk – of making, holding, realising assets
 - Likely return
 - Liquidity compared to cash flow requirements

Investment Strategies

- Ensure the strategy complies with the SIS requirements
 - Diversification and where necessary the risks from a lack of diversification
 - Insurance for one or more members
- Make sure the strategy is in writing
- Prefer the strategy to be dated, signed
- NO back dating!

Investment Strategies

- Annual review must be evidenced in a minute, or the adoption of a new strategy
- If your strategy has ranges, make them flexible, check they are complied with prior to year end so there are no audit issues at year end

Investment Strategies

- The trustee must give effect to the strategy
 - Investments are actually permitted
 - Assets held should be listed in the strategy, not just allocated to “other” - crypto is a good example
 - Investments are within the permitted ranges
 - If your strategy has ranges, make them flexible, check they are complied with prior to year end so there are no audit issues at year end

Investment Strategies

- The ATO have stated that the impact of the pandemic is not an excuse to be outside investment ranges noted in the strategy

Investment Strategies

- If the fund has a dominate or single asset, ensure the strategy considers the risks from a lack of diversification
- Return objective has been met
 - If the strategy has return objectives, make them achievable, allow for negative returns or omit the objective

NALI

- Any fund that has non-arm's length income or a non-arm's length expense has a tax consequence
 - Discretionary trust distributions
 - Non-arm's length trust distributions
 - Private company dividends
 - Other arrangements – rent exceeding market value

NALI

- Income is taxed at 45%, not concessionally, so there is a significant audit risk to manage

NALE

- Rules changed on 1 July, 2018 to capture fund income that may have a connection to non-arm's length expenses
- There is transitional relief for general nexus expenses, but there is no relief for specific nexus expenses

NALE

- Common issues
 - Fund invests in a private trust that has interest free debt
 - All trust distributions are NALI

NALE

- Common issues
 - Fund invests in a private trust that has no accounting fees incurred
 - All trust distributions are NALI

NALE

- Common issues
 - Fund owns property, trustee is also a real estate agent, and the fund property is managed by the business, but there are no management fees
 - Property rent (less property expenses) is NALI

Audit Impact Example

- Pension fund of a retired accountant, no accounting fees are charged for the preparation of the financials by the trustee's old firm
- Fund has assets of \$6.2m
- Fund has income for 2021 year of \$163k
- Tax refund was \$52k

Audit Impact Example

- Post transitional period if there are no accounting fee is charged at market rates, the tax refund would be \$3k – so a \$49k swing

Audit Impact Example

- Accumulation fund has undertaken a huge property development
- Taxable gain for the year is \$6.3m
- Property sales were managed via a related party legal firm

Audit Impact Example

- No legal fees were charged on the sales process for any property sold by the fund
- \$6.3m less discounting at 15% = \$630k tax expense
- \$6.3m less discounting at 45% = \$1.8m tax expense

COVID Audit Issues

- Rent relief for related party tenants
 - Establishing the relief was fair and reasonable
- Investment strategy requirements
 - Does any loss in value impact compliance with the ranges set by the trustee?
- Early release payments and the lack of paperwork permitting the release

Questions?



Super Sphere Pty. Ltd.

- Super Sphere provides audit, training and consulting services specifically in relation to SMSF audit issues.
- An SMSF Audit Toolkit is available for \$550 to assist professionals compile and complete an audit file.
- For more information visit

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