

Closely Held Investments

In this newsletter we commence an overview and discussion of the audit considerations of the investment by Self-Managed Superannuation Funds (SMSFs) in unlisted entities. We will initially focus on Pre99 and 13.22C Unit Trust audit evidencing considerations.

To commence this topic, we have included relevant definitions within SISA, that you will be familiar with as follows:

- ▶ Distinctions between closely held unlisted entities and widely held unlisted entities;
- ▶ Related party as defined by SISA; and
- ▶ Criteria that determines a related trust versus a non-related trust.

1. Closely held vs Widely held entities

When considering whether an unlisted entity investment can be acquired by a SMSF under superannuation law, this depends on:

- ▶ whether the unlisted investment is being acquired from a related party;
- ▶ the unlisted investment constitutes an investment in a related party of the SMSF; and
- ▶ whether the entity is widely held.

Our audit evidencing requirements for investment acquisitions reflects this consideration and is generally referenced as follows:

	Closely held (ITAA1936 – Schedule 2F - 272-105)	Widely held (S.71(1A) of SISA)
Unitholders	Less than 20	Equal or more than 20
Fixed entitlement	Less than 75% to income or capital	More than or equal to 75% to income or capital
S.66 of SISA Acquisition of certain assets from members of regulated superannuation funds prohibited	<ul style="list-style-type: none"> ▶ Unrelated: not exempt from S.66 ▶ Related entities: <ul style="list-style-type: none"> In-house Assets (IHA) <5% applies* R.13.22C Compliant Entity (allowable acquisition subject to advice)* <p>* the asset must be acquired at market value.</p>	Defined as Exempt per S.66

2. Related parties as defined by SISA

For SMSFs, related parties encompass individuals, entities or associates that share a close connection with the fund. Understanding how these are defined for SISA purposes is critical to determining relatedness. We have summarised this in [Related parties as defined by SISA](#).

An example trustee declaration confirming the investment is not a related party or part 8 associate of the fund [is available in our client library](#).

3. Summary of Criteria to determine related trust versus non-related trust

	Related trust	Non-related trust
<i>50% of units</i> S.70E (2)(a) of SISA	If a group (member or member' related parties) hold > 50% of total units/shares; OR	If a group (member or member' related parties) hold <=50% of total units/shares; AND
<i>Sufficient influence</i> S.70E (2)(b) of SISA Sufficient influence is defined in S.70E(1)	If a group (member or member' related parties) has sufficient influence; OR	If a group (member or member' related parties) does NOT have sufficient influence; AND
<i>The power to remove/appoint the trustee.</i> S.70E (2)(b) of SISA	If a group (member or member' related parties) has the power to remove/appoint the trustee	If a group (member or member' related parties) does NOT have the power to remove/appoint the trustee.

Please refer to the [related versus non-related trust criteria](#) within our document library for more details.

4. Audit requirements for closely held related investments

Pursuant to ATO guidelines a look through approach is considered in gathering audit evidence for related investments. The audit scope for the investment depends on the materiality of the asset to the fund. In most cases these are material assets of the fund.

POST 8/99 TRUSTS OR COMPANIES

A post 8/99 trust, also known as an ungeared related trust or Regulation 13.22C trust, as noted above is a trust controlled by related parties of the fund, either through unitholder voting control or trustee control, and established post 11 August 1999. This type of entity can hold real property and is governed by SIS Regulation 13.22C and 13.22D.

PRE 8/99 TRUSTS OR COMPANIES

Valuation of a pre 8/99 trust can require a more detailed consideration of the assets held and liabilities of the trust. It is noted, a Pre 8/99 trust has greater flexibility than a Regulation 13.22C trust, and may include borrowings.

Pre 8/99 trusts are not restricted to property and can hold other assets such as company shares, listed and unlisted unit trusts, loans, foreign investments, etc. Therefore, the trustees will need to consider the value of each asset and liability held by the trust. In this explanation of our audit requirements we consider loans as this and property are the usual investment assets of these trusts.

Summary of the audit requirements associated with related unit trust investments:

Assertion: Ownership - First Year audit only

Post 8/99 Related Unit Trust	Pre 8/99 Related Unit Trust
No declaration of SISA compliance required.	Declaration of compliance required If the fund made additional investments in the unlisted unit trust between 11/08/1999 and 30/06/2009 either by way of reinvestment of earnings or an additional investment a declaration that the additional investments comply with s71D and s71E. A declaration that no investments have been made by the fund in the unlisted unit trust post 30/06/2009. (View our example template)
<ul style="list-style-type: none"> ▶ Signed Copy of Trust Deed EITHER of the following: <ul style="list-style-type: none"> ▶ A signed copy of Unit certificates as available; ▶ A signed copy of Unit register; OR ▶ Signed Financial Statements clearly stating the name of the fund, and the units held at 01/07/20XX and 30/06/20XX; OR ▶ Signed declaration by unit trust trustees of units held at 01/07/20XX and 30/06/20XX. 	

Assertion: Ownership - Changes in ownership post first year audit

Post 8/99 Related Unit Trust	Pre 8/99 Related Unit Trust
Acquisition <ul style="list-style-type: none"> ▶ An updated signed copy of the unit register. ▶ Unit certificates as available. ▶ Supporting documents to evidence that the purchase was at market value. 	Acquisition If the fund acquires units from a related party or unrelated party <ul style="list-style-type: none"> ▶ Supporting documents for the purchase (transfer documents) and to evidence that the purchase was at market value. The investment acquired is an In-house Assets (IHA) by definition. The fund can acquire the investment from a related party pursuant to S.83 of SISA where: <ul style="list-style-type: none"> ▶ The IHA is less than or equal to 5% of the fund's total assets; and ▶ The acquisition of new IHA does not result in the total IHA >5% of the fund total assets or ▶ Where the total IHA is >5% of the fund total assets, a written plan is in place for rectification. This should be prepared by the fund trustee before the end of the next financial year as per S.82 and the fund trustee must ensure the steps in the plan to dispose of the excess have occurred by the end of that year.
Disposal <ul style="list-style-type: none"> ▶ Supporting documents for the sale (transfer documents) and to evidence that the disposal was at market value. 	Disposal <ul style="list-style-type: none"> ▶ Supporting documents for the sale (transfer documents) and to evidence that the disposal was at market value.

Assertion: Valuation - Existence, ownership and Valuation of Underlying Assets

Post 8/99 Related Unit Trust	Pre 8/99 Related Unit Trust
<ol style="list-style-type: none"> 1. Signed Financial Statements FY20XX and Income Tax Return; 2. Fund minute to document basis of valuation of unit trust investment (View our example template); 3. Calculation of Market value per unit at 30/06/20XX; and 4. Supporting documents of the MATERIAL asset balance sheet accounts and compliance considerations: <ul style="list-style-type: none"> <u>Bank:</u> <ul style="list-style-type: none"> ▶ A bank statement to confirm the balance as at 30/06/20XX. ▶ Where there are arrangements with related parties or Part 8 Associates, such as leasing or loan arrangements a copy of the bank statements for the FY20XX. The bank records for the year may be extracted from the trust accounting records where a bank feed is employed. <u>Property:</u> <ul style="list-style-type: none"> ▶ Property valuation along with supportable evidence (as per property valuation procedure where held directly by the fund, refer to our recent Newsletter issued September 2023); and ▶ Title search at year end or post year end (for NSW where we have a prior year title search this is only required where there is a change to the title). 	
<p>No other Assets permitted.</p>	<p><u>Property</u></p> <ul style="list-style-type: none"> ▶ Mortgage charge related to unit trust loan only. <p><u>Loan Assets (usual other asset)</u></p> <ul style="list-style-type: none"> ▶ Supporting documents to evidence the existence and valuation of the Loan as at 30/06/20XX (e.g. signed loan confirmation, borrower’s financial statements, interest or principal paid post year end); ▶ Signed Loan agreement with arm’s length terms and conditions (S.62 of SISA); and ▶ If we are unable to evidence the recoverability of the Loan or the Loan is unsecured or non-first mortgage, Part A Qualification may be raised in our audit report for the valuation of the fund investment in the unit trust, where this is material to the fund unit trust investment.

Assertion: Valuation - Completeness of liabilities & Compliance Considerations

Post 8/99 Related Unit Trust	Pre 8/99 Related Unit Trust
<p>1. Supporting documents of the MATERIAL liability balance sheet accounts and compliance considerations:</p> <ul style="list-style-type: none"> ▶ Reconciliation of the unitholder current account if not provided within financial statements. ▶ Distributions paid timely. Where unpaid distribution is outstanding >1 year this may be a loan. This may be a material breach of S.109 and the IHA provisions depending on the amount. 	
<p>Liabilities are associated with sundry creditors or unitholder current account</p>	<p><u>Borrowings</u></p> <ul style="list-style-type: none"> ▶ Signed Loan agreement with arm's length terms and conditions where related party (NALI consideration); ▶ Signed copy of loan confirmation or evidence to support loan was repaid post year end; ▶ Borrowing from financial institution: Loan statement as at 30/06/20XX; and ▶ The associated charge is over the unit trust property asset.

Assertion: Other Compliance Considerations

Post 8/99 Related Unit Trust	Pre 8/99 Related Unit Trust
<p>Distribution received by the fund agrees with the financial statement, Income Statement, and with the fund's holding percentage. S.62 or NALI issue may be raised if the income is not reasonable.</p> <p>Property Rental Income</p> <ul style="list-style-type: none"> ○ Lease agreement/Rental Statement from a real estate agent. A lease agreement is required where leased to related party or Part 8 Associate; ○ Rental appraisal is required if the property is leased to related party or Part 8 Associate; and ○ Where yield is abnormal, supporting documents and explanation may be required to support that the trust received rent at market rate. <p>Supporting documentation of Material Expenditure</p>	