



Explanatory Statement

Self Managed Superannuation Funds (COVID-19 Rental income deferrals – In-house Asset Exclusion) Determination 2020

General Outline of Instrument

1. This instrument is made under paragraph 71(1)(f) of the *Superannuation Industry (Supervision) Act 1993* (SISA).
2. This instrument provides that an asset of a self-managed superannuation fund (SMSF) is not taken to be an in-house asset for the 2019-20, 2020-21 and future income years where the SMSF, during one or both of the 2019-20 and 2020-21 income years:
 - a) allows a related party to defer the payment of rent owing under a lease agreement (on arm's length terms) to ease the financial impact of the coronavirus known as COVID-19 which creates the asset held by the fund, or
 - b) holds the asset that is an interest in a company or unit trust which would not otherwise be an in-house asset under regulation 13.22B or regulation 13.22C of the SISA and that company or unit trust allows a tenant to defer the payment of rent under a lease (on arm's length terms) to ease the financial impact of COVID-19.
3. The instrument is a legislative instrument for the purposes of the *Legislation Act 2003*.
4. Under subsection 33(3) of the *Acts Interpretation Act 1901*, where an Act confers a power to make, grant or issue any instrument of a legislative or administrative character (including rules, regulations or by-laws) the power shall be construed as including a power exercisable in the like manner and subject to the like conditions (if any) to repeal, rescind, revoke, amend, or vary any such instrument.

Date of effect

5. This instrument commences the day after it is registered on the Federal Register of Legislation.
6. Under subsection 12(2) of the *Legislation Act 2003* this instrument does not adversely affect the rights or liabilities of any person other than the Commonwealth.

What is the effect of this instrument

7. The effect of this instrument is that assets covered by this Legislative Instrument are taken not to be in-house assets of the SMSF in the income year/s in which there was an agreement on arm's length terms that the payment of rent owed could be deferred or any future income years.

Compliance cost assessment

8. Minor – there will be minimum impact for both implementation and ongoing compliance costs. The legislative instrument is minor and machinery in nature.

Background

9. This instrument provides that deferral of the payment of rent owed under a lease (on arm's length terms as described in paragraph 15 below) during one or both of the 2019-20 and 2020-21 income years, does not result in an in-house asset or cause the SMSF to lose its in-house asset exemption in relation to an interest in a company or unit trust under regulation 13.22B or regulation 13.22C of the SISR. In the absence of this Instrument, the deferral of rent would be taken to be a loan as defined in the SISA triggering the application of the in-house asset rules.

10. The definition of 'loan' in subsection 10(1) of the SISA includes the provision of credit or any other form of financial accommodation, whether or not enforceable or intended to be enforceable by legal proceedings. This definition therefore covers financial accommodation arrangements where a creditor grants a deferral of payment of rent owed by a tenant: see paragraph 11 of SMSFR 2009/4 *Self Managed Superannuation Funds: the meaning of 'asset', 'loan', 'investment in', 'lease' and 'lease arrangement' in the definition of an 'in-house asset' in the Superannuation Industry (Supervision) Act 1993*.

11. Where a trustee of an SMSF agrees to allow a deferral of the payment of rent owed under a lease (on arm's length terms) from a related party, the deferral results in the trustee acquiring or holding an in-house asset that is not covered by any of the exemptions in subsection 71(1). When the value of an SMSF's in-house asset investments exceeds 5% of the total value of its assets, the trustee of the SMSF is required to prepare and implement a written plan to dispose of assets equivalent in value to the excess by the end of the following year of income: section 82. It also means that the SMSF trustee cannot acquire any other assets that would be taken to be in-house assets: section 83. There are penalties for not complying with the in-house asset rules.

12. The restrictions that apply to in-house assets do not apply to an investment by an SMSF in a unit trust or company if it specified in the regulations 13.22B or 13.22C not to be an in-house asset under paragraph 71(1)(j). These entities are often referred to as a non-gear company or unit trust. However, regulations 13.22B or 13.22C will cease to apply if any of the events in regulation 13.22D occur, including the company or unit trust providing a loan to another entity: subparagraph 13.22D(1)(b)(ii).

13. Where a company or unit trust covered by regulations 13.22B or 13.22C allows a tenant to defer payment of rent under a lease (on arm's length terms) due to the income impacts of COVID19, the company or unit trust will have made a loan as defined. Accordingly, the SMSF investment in the company or unit trust will become an in-house asset for the current and all future income years. This will mean that the SMSF will need to dispose of the investment where the value exceeds the 5% threshold.

14. Given the context of the COVID-19 pandemic and the long term effects of triggering an event under regulation 13.22D, the Commissioner believes it is appropriate to exercise his power as Regulator under paragraph 71(1)(f) to exclude the SMSF's investment from being an in-house asset where the deferral of rent is provided on arm's length terms and where none of the other events in regulation 13.22D are triggered during one or both of the 2019-20 and 2020-21 income years. This also means that SMSF auditors will not be required to report a contravention to the ATO or to advise trustees of the contraventions which would otherwise result, in relation to the 2019-20, 2020-21 or future income years.

Arm's Length Terms

15. The determination will only apply where the landlord has acted in good faith and has agreed that the tenant can defer payment of rent on arm's length terms during one or both of the 2019-20 and 2020-21 income years in order to ease the financial hardship caused by COVID-19. In

assessing whether the rental deferral has been negotiated in good faith and on arm's length terms, the National Cabinet Mandatory Code of Conduct or any relevant State based Codes or legislation may assist. There must be contemporaneous documentation reflecting the terms of the deferral agreement including the terms for payment of the deferred amount agreed to by the landlord and the tenant to ensure the parties agreement is on arm's length terms and the lease remains enforceable. For the rental deferral arrangement to remain on arm's length terms, any deferred amounts should also be repaid by the tenant as soon as is practicable.

16. The exclusion only applies to the deferral of rental income under a lease (on arm's length terms and where no other events in regulation 13.22D are triggered) made in one or both of the 2019-20 and 2020-21 income years, being the income years during which tenants are likely to be adversely financially impacted by COVID-19.

Exemption from disallowance and sunseting regime

17. Part 4 of the *Legislation Act 2003* (LA) provides for the sunseting of legislative instruments. However, paragraph 54(2)(b) of the LA provides that Part 4 of the LA does not apply if the legislative instrument is prescribed by regulation. Section 11 of the *Legislation (Exemptions and Other Matters) Regulation 2015* (EOMR) provides a list of instruments that are not subject to sunseting. Item 6 of the table in section 11 of the EOMR lists instruments (other than regulations) relating to superannuation. As a result, Part 4 of the LA does not apply to this instrument. Therefore this instrument will not sunset.

18. Section 42 of the LA provides for the disallowance of legislative instruments. However, paragraph 44(2)(b) of the LA provides that section 42 does not apply to legislative instruments prescribed by regulation. Section 9 of the EOMR provides a list of instruments that are not subject to disallowance. Item 4 of the table in section 9 of the EOMR lists instruments (other than regulations) relating to superannuation. As a result, this instrument is not a disallowable legislative instrument under section 42 of the LA.

Consultation

19. For this instrument, broad public consultation was undertaken for a period of 4 weeks from 3 August to 31 August 2020. The ATO received 8 submissions.

20. The draft instrument and draft explanatory statement were published to the ATO legal database. Publication was advertised via that 'What's new' page on that website, and via the 'Open Consultation' page on ato.gov.au. Major tax and superannuation publishers and associations monitor these pages and include the details in the daily and weekly alerts and newsletters to their subscribers and members. This ensures advice of the draft is disseminated widely across the tax professional community, and that they are in an informed position to provide comments and feedback.

21. Of note, one submission requested the legislative instrument refer to a fund that holds an in-house asset, in addition to a fund that acquires an in-house asset. The ATO responded to this feedback by amending the legislative instrument and explanatory statement to specify it applies where the fund acquires or holds an in-house asset.

22. Several submissions sought clarification of how the exclusion is intended to apply beyond the 2020-21 income year in relation to relevant events that occur during one or both of the 2019-20 and 2020-21 income years. The ATO responded to this feedback by amending the legislative instrument and explanatory statement to specify it applies for the 2019-20, 2020-21 income years and any future income years.

23. Other submissions sought clarification of the definition of 'arm's length' and the repayment of deferred rent, as well as confirmation the exclusion does not apply where other events in regulation

13.22D of the SISR are triggered during one or both of the 2019-20 and 2020-21 income years. The ATO responded to this feedback by providing greater detail in the explanatory statement.

24. Some submissions sought clarification on the scope of exclusions covered by the Legislative Instrument. This has been covered by providing greater detail in the explanatory statement.

Statement of compatibility with Human Rights

25. As section 42 of the LA does not apply to this instrument, a Statement of compatibility with Human Rights in respect of this instrument is not required under section 9 of the Human Rights (Parliamentary Scrutiny) Act 2011.

Legislative references

Acts Interpretation Act 1901

Legislation Act 2003

Superannuation Industry (Supervision) Act 1993

Superannuation Industry (Supervision) Regulations 1994