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SMSF valuation requirements

For trustees

Peter Townsend

The Australian Taxation Office (ATO) has recently published 'Regulation 8.02B and evidence to support real property valuations' which outlines its evidence approach and requirements for real property valuations. The approach elaborates but generally accords with the ATO's previously published valuation principles. This paper explains the ATO valuation requirements for real property and other asset classes and situations.

1. When does the trustee need to provide valuations?

With superannuation reform and the duties imposed on trustees under superannuation law, market valuation is an integral part of self-managed superannuation fund (SMSF) investment transactions, assets valuation and income activities.

- Regulation 8.02B of the *Superannuation Industry (Supervision) Regulations 1994* requires the assets of superannuation funds to be valued at market value when preparing the assets and financial statements of the fund.
- Market valuation is integral to determining the arm's length basis of SMSF transactions, especially when dealing with related parties (where permitted), for the purpose of *Superannuation Industry*

(Supervision) Act 1993 (SIS Act) section 109 investments and to avoid non-arm's length income (NALI) (section 295.550 of the *Income Tax Assessment Act 1997*).

- Market valuation is required to determine the account balances for pension commencement, determination of the transfer balance cap and total superannuation balance amounts and compliance with the 5% ceiling for in-house assets. These will affect the member's exempt current pension income (ECPI), eligibility for non-concessional contributions (NCCs), carried-forward NCCs and other measures (in the ensuing year) as well as the SMSF's use of segregated asset method to calculate ECPI.

2. Role of the trustee

It is the trustee's role to provide objective and supportable evidence of their SMSF assets valuation to their auditors, in accordance with market valuation requirements.

It is not the auditor's role to determine the market value of an asset.

The ATO guidelines state that the valuation has to be arrived at using a "fair and reasonable" process and the trustee must meet all of the following conditions:

- They take into account all relevant factors and considerations.
- They have undertaken the valuation in good faith.
- They use a rational and reasonable process.
- They are capable of explaining the valuation to third parties.

The auditor's role, on the other hand, is to obtain sufficient appropriate evidence in accordance with the federal government Auditing and Assurance Standards Board's Auditing Standard ASA500 *Audit Evidence* to form an opinion whether the SMSF has complied with market valuation requirements, and document that evidence and any judgments made.

An approved auditor can seek an independent valuation of the fund's investments, as part of their audit and assurance engagement.

3. ATO review

The ATO may review a valuation as part of its compliance processes. The ATO review considers:

"As part of this review you may be asked to provide evidence of the valuation method that has been used to allow us decide whether to accept the valuation or not. This evidence would include documentation of the valuation method used."

4. Valuation methodologies

4.1 First method: valuation by an external qualified independent valuer (QIV)

Apart from certain related-party transactions in relation to collectables and personal-use assets, generally a QIV valuation is not mandatory. However, there are advantages in using the QIV valuation, as covered in the following discussion.

The advantage of using a QIV apart from precision is that an external valuation is not required each year. A new valuation will only be required if the existing external valuation has become materially inaccurate or a significant event occurred that may change the value of the asset since last valuation. Significant events may include:

- natural disaster
- macroeconomic events (e.g. effects of COVID-19)
- market volatility
- changes to the character of an asset.

The ATO recommends using a QIV if an asset represents a significant proportion of the fund's value, or the nature of the asset indicates that the valuation is likely to be complex.

A valuer is qualified either through holding formal valuation qualifications or being considered to have specific knowledge, experience and judgment by their particular professional community. A valuer is independent if they are independent of the interest of the fund. The valuer should not be a member of the fund or a related party.

4.2 Second method: trustee to provide objective and supportable evidence

The SMSF trustee can provide objective and supportable evidence to their auditor in accordance with ATO guidelines. The valuation can be undertaken by anyone, as long as it is backed by objective and supportable evidence. There are specific requirements for different asset classes and situations.

5. Asset classes specific requirements

5.1 Real properties

In relation to real property, the trustee may use a QIV (especially where the real property represents a significant proportion of the fund's value) or provide objective and supportable evidence to their auditors.

Where the valuation is to provide market value (MV) for the financial reports, the evidence should support MV as close to 30 June as possible.

Real estate agent appraisals stating what the property is likely to sell for based on sales in the area without listing those sales would not on its own be sufficient.

A variety of sources of evidence will be required, unless the property has recently been sold, including:

- independent appraisals from a real estate agent (kerb-side)
- a contract of sale if the purchase is recent and no events materially impacting property value have happened since purchase
- recent comparable sales results
- rates notice (if consistent with other evidence on valuation)
- net income yield of commercial properties (only appropriate where tenants are unrelated).

5.2 Listed shares and managed investments

The market value is the closing price on each listed security's approved stock exchange or licensed market (30 June for accounts and financial statements).

5.3 Unlisted securities and unit trusts

An example is shares in private companies. The factors to consider are:

- consideration paid on acquisition
- independent valuation of underlying properties if substantial
- price of recent sales between unrelated parties.

5.4 Collectables and personal use assets

Valuation by a QIV is mandatory for the following transactions.

- The asset was acquired on or after 1 July 2011 and transferred or sold to a related party after that date.
- The asset was acquired before 1 July 2011 and transferred or sold to a related party on or after 1 July 2016.

In relation to investment in gold bullion, it should be noted that gold bullions/bars that can be purchased for the current spot price of gold is not a collectable. Numismatic bullion coins that have a value which exceeds their face value above spot price of the metal content are collectables.

5.5 Investments without a ready market

The ATO considers that trustees should be aware of the value of an asset at the time of acquisition, its potential for growth and its capacity for income. Otherwise, it would not be considered a prudent investment to support retirement goals.



The quote

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There may be instances where an investment fails and there is neither a current value nor a ready market. This may mean the asset is held and recorded in the financial reports and statements at a nil or nominal amount.

6. Events—valuation requirements

Table 1 summarises the valuation requirements in relation to particular events/activities.

Table 1. Events and valuation requirements

Event	Valuation requirement
Preparation of accounts and statements (valuation at financial year end)	MV based on objective and supportable data
Testing MV of in-house assets for the 5% ceiling	MV based on objective and supportable data
Acquisition of permitted asset from related party	Price at MV based on objective and supportable data
Disposal of an asset to related party	MV to reflect a true market rate of return (arm's length requirement)
Determine value of assets that support superannuation pension and ECPI	MV based on objective and supportable data
Determine value of assets for total superannuation balance (30 June) and transfer balance cap (event based)	MV based on objective and supportable data

Source: SuperCentral based on ATO data

7. COVID-19 impact

During the 2019/20 and 2020/21 financial years, if the trustee has difficulty obtaining valuation evidence due to the impact of COVID-19, SMSF auditors should provide reasons on the auditor/actuary contravention report (if required) as to the reason why the trustee was unable to obtain appropriate evidence. If the ATO is satisfied this was due to the impact of COVID-19, the trustee will receive a letter advising them to ensure they comply with valuation guidelines and have supporting valuation evidence by the time of the next audit. No penalty will be issued.

Conclusion

Understanding the ATO valuation requirements will enable SMSF trustees to put in place procedures and documentations that support the required evidence and methodologies. **FS**