



Mr Justin Smart
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Dear Justin,

Purchase of units in Trilogy Group Holdings Unit Trust

Thank you for your recent enquiry regarding the purchase of units in the above unit trust by a self-managed superannuation fund (SMSF).

Background

You are currently the holder of units in the Trilogy Group Holdings Unit Trust (Trilogy). You have an opportunity to purchase additional units in Trilogy and are considering taking up this further investment within a self-managed superannuation fund (SMSF). This additional investment involves the issue of new units in Trilogy, rather the purchase of existing units from another unitholder.

Your currently unitholding is 1,000,000 units out of a total of 10,000,000 on issue or 10% of the total units. The new issue of units will double the total units on issue and you propose for your SMSF to purchase 1,000,000 units such that between you and your SMSF, you will still only hold 10% of the total units on issue.

Before proceeding with setting up an SMSF, you are keen to ensure that the investment in Trilogy by the SMSF would comply with relevant superannuation and taxation laws.

Trilogy is a closely held unit trust with a limited number of unitholders. You have confirmed that the other unitholders in Trilogy are not related to you. Rather, they are all unrelated executives working at Trilogy Capital Services Pty Limited or SMSF's belonging to those individuals.

You have confirmed that the opportunity to make a further investment is not part of any employee arrangement. That is, it is not linked to your employment with Trilogy Capital Services Pty Limited or any other related entities of Trilogy. The only relationship between Trilogy and your employer is that they both own units in Trilogy Services Trust.

You do not currently have an SMSF and would be looking to set one up to undertake this investment.

Should any of the above information be incorrect, please advise us immediately as this may change the advice below.

The information contained in this document does not constitute "financial product advice" within the meaning of the Corporations Act 2001 (Cth) (Corporations Act). The PricewaterhouseCoopers

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Advice

There are generally very few restrictions on the types of assets in which an SMSF can invest. However, there are a number of restrictions when it comes to investments with or in a related party of an SMSF. Further, any transactions involving an SMSF must be undertaken on an arm's-length basis.

Investing in unit trusts

SMSF investments in unlisted unit trusts are a permissible investment under superannuation law. Where the unit trust is a widely held trust or an unrelated trust, there are no restrictions on the quantum of the investment, subject to the investment strategy of the fund.

Where a trust is a related party of the fund, the fund will be restricted on the quantum of the investment it can make. Investments in entities that are found to be related parties are called in-house assets (IHA). While an SMSF is able to invest in an IHA, the investment must be no more than 5% of the market value of the fund's total assets. This is assessed at the time of purchase and at 30 June each financial year.

There are some exceptions to the IHA rules including where the related unit trust only invests in business real property and adheres to a range of other restrictions. In these cases, the trust can be excluded from the definition of an IHA and the SMSF will not be restricted in the level of investment in that trust. We note that in addition to only holding business real property, the related trust inter alia cannot borrow, lend, invest in another entity or operate a business.

What is a related party?

A related party of a super fund is defined under Section 10 of the Superannuation Industry (Supervision) Act 1993 (SIS Act) as a member of the fund, a standard employer-sponsor of the fund and a Part 8 associate of either of these two.

A Part 8 associate of an individual member is defined under Section 70B of the SIS Act and includes:

- a relative of the member
- the other members and trustees (or trustee directors) of the fund
- business partners in a partnership (and their spouses and children) and the partnership itself
- a trust controlled by a member of the fund
- a company sufficiently influenced, or for which majority voting interest is held by a member; or another entity or entities to which these provisions would also apply.

A relative of a member of an SMSF is defined in Section 10 of the SIS Act and includes a spouse, parent, grandparent, brother, sister, uncle, aunt, nephew, niece, lineal descendant or adopted child of the individual or their spouse. It also includes the spouse of any of the above.



Under Section 70E of the SIS Act, sufficient influence of a company or control of a trust is taken to exist where a majority of its directors or unitholders are accustomed or under an obligation (formally or informally) or might reasonably be expected to act in accordance with the directions, instructions or wishes of an entity or individual, and such influence resulted in a majority voting interest in the company or trust.

Is Trilogy a related party of an SMSF for which the member/trustee is Justin Smart?

Based on the facts provided, at this time and following the issue of additional units to your SMSF, it is unlikely that Trilogy would be considered to be a related party of you or the fund.

As per the background facts, now and following the issue of additional units, you and the SMSF will own 10% of the total units on issue. Prima facie, the combined unitholding of you, your SMSF and any of your related parties would need to be in excess of 50% for Trilogy to be deemed a related party.

However, ownership is not the only test in ascertaining if an entity is a related party. The determination of a related party can extend to the level of influence an individual has over other unitholders in the decisions of the trustee and trust. Therefore, to the extent that you have such influence over the trustee and other unitholders, Trilogy could still be deemed to be a related party, notwithstanding the level of ownership. You will need to consider if it could be determined that you currently have such influence within Trilogy or its trustee. At this time, it seems unlikely that this is the case.

Despite the current status, you should be aware that subsequent investments by you, the SMSF or any other person or entity that is a related party of you (as defined above) may risk Trilogy becoming a related party of the SMSF. Should the total investment exceed 50% of total units, Trilogy will likely become an IHA of the fund and the fund will be restricted to an investment in Trilogy that is no more than 5% of the market value of the SMSF's total assets.

Acquisition of assets from a related party

Section 66 of the SIS Act places a general prohibition on the acquisition of assets from a related party. There are a number of exceptions to this rule which include business real property and listed securities but not unlisted shares or units.

On the basis that the acquisition of units by the SMSF will be a new issue of units as outlined in the background information above, the acquisition of the units is prima facie, an allowable acquisition. Should any arrangements be amended such that the SMSF was not acquiring new units, it is necessary to ensure that the purchase is at market value from an unrelated party. As defined above, you will be a related party of your SMSF. Therefore, your SMSF is unable to acquire units from you.



Arm's Length Transactions

We note that an SMSF has an obligation under Section 109 of the SIS Act to at all times, undertake, transact and maintain investments on an arm's-length basis. Therefore, any proposed transactions must be conducted on commercial terms and at market valuations. This includes future distributions from Trilogy.

You will need to ensure that the issue of the additional units is being undertaken at market value. If these new units have the same rights as the existing units, then the purchase price will need to be in line with the market value of the old units rather than a separate issue price. Should there be a difference in price, the SMSF may be seen as not complying with its obligations under the arm's-length provisions of the SIS Act. Should this be the case, please let us know so that we can advise you on the ramifications accordingly.

Further, the returns of investment from Trilogy must be determined and distributed on an arm's-length basis. These returns cannot be determined by reference to transactions or dealings outside of these two entities. For example, a reduced/increased distribution in exchange for an increased/reduced deal price with another entity.

Can your SMSF purchase units in Trilogy?

We do not believe that circumstances give rise to Trilogy being deemed to be a related party of an SMSF of which you are the member and trustee. As such, this transaction would not give rise to the fund being subject to IHA rules that would restrict the investment to no more than 5% of the market value of the fund's total assets.

Should the fund or any other related party of the members of the fund or any of its related parties wish to make future investments in Trilogy, the above advice should be revisited to ensure the fund's ongoing compliance.

Further, to the extent that the purchase of units is pursuant to an additional issue of units, the acquisition is permissible under superannuation law. However, we note that the issue of the units must be at the true market value of those units.

From a SIS Act compliance perspective, we see no reason that the fund should not be able to proceed with the purchase of units in Trilogy, subject to the relevant provisions as described above.

Other matters for consideration

Setting up an SMSF

While you have not sought specific advice on the setup of an SMSF, there are a range of factors to consider before undertaking this action. We have attached a copy of the trustee declaration form from the Australian Taxation Office (ATO). This document outlines some of the roles and responsibilities of SMSF trustees and will be required to be signed by you upon becoming a new SMSF trustee (or director of a trustee company). If you have any questions regarding this document or your role as a trustee, please let us know and we can assist accordingly.



Should you proceed in your decision to setup an SMSF, we can further assist in the setup procedure which includes obtaining a trust deed and other paperwork as well as registration with the ATO. Where you choose to use a corporate trustee, we can assist in setting this up also.

Financing the Acquisition by your SMSF

Once you have setup your SMSF, you are able to rollover other existing superannuation holdings that you have into this fund. We strongly advise you to seek independent financial advice in this regard on the implications of doing so including any potential loss of insurance in your existing superannuation accounts.

Rollovers however can take a considerable amount of time. If you need to finance the investment in a more timely way, you may need to make a direct contribution to the SMSF. Contribution caps apply to limit the amount an individual can contribute to their superannuation fund on an annual basis, as follows:

Concessional contributions	Non-concessional contributions
Generally, contributions on which you or your employer claim a tax deduction	Contributions from after tax dollars (no deduction has been claimed)
\$25,000 per annum	\$100,000 per annum or \$300,000 for a three year period (that is, bring forward two years contributions to make a larger contribution in the first year)

You should ensure that any contribution you make, together with contributions made to any of your other superannuation funds do not, in total, exceed these caps.

Please let us know if you would like to discuss this aspect further.

Should you wish to discuss any aspect of this advice, please do not hesitate to contact Liz Westover on 03 8603 2011.

Yours sincerely

Naree Brooks
Partner