

FLOODS BRING SMALL BLESSINGS FOR DIY FUNDS

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They say an ill wind blows no good, but the Queensland floods did an unlikely favour for DIY super funds.

They prompted the Australian Taxation Office to clarify just what qualifies as legitimate repairs to properties, which isn't much but it is an advance on the previous policy of no alterations, and they depressed prices in southeast Queensland, the most popular location for DIY super fund property investment.

DIY super funds have been allowed to borrow since 2007, though on a non-recourse basis, so the lender has a call over the property only, not the other assets.

"It's a quicker way of building up super," says Kathy Evans, superannuation principal at accountants WHK.

But she warns it involves "a complicated structure" and the fund needs to be able to commit to repayments. Total and permanent disability life insurance is critical.

The key tax break is no capital gains tax after 60 when the fund is in pension-paying mode. It is also a way of avoiding land tax for investors with more than one investment property.

The other benefit is that salary sacrificing and employer contributions can be harnessed to pay off the loan.

The biggest disadvantages are that the property can't be developed or subdivided and that when the fund is in pension stage there is a minimum draw-down, which could result in cash-flow problems.

Inquiries for super fund mortgages have jumped 25 per cent in the past month, says Craig Morgan, director of brokers SMSF Loans, with the most popular investment location by loan volume being south-east Queensland, where prices have fallen in the past year.

Lenders are more amenable to lending to DIY super funds and “their processes have become more streamlined”, he says.

But they charge about 0.2 per cent more than the advertised standard variable rate, which can put the interest rate up to 1 per cent above a normal loan.

The higher rate and fees aren’t worth it, says Kevin Lee, director of Smart Property Adviser.

One of the biggest lenders to DIY super funds is St George, but as well as paying 1 per cent higher interest than it would have cost outside super, there’s a \$12 monthly fee, and the upfront cost is \$2115 compared with \$100 to \$600 on an ordinary loan, Lee says.

Then there are extra costs for the fund itself. A bare trust has to be set up for the loan, separate from the fund’s trustee. “It’s a win-win for the banks, accountants and the legal profession,” Lee says.

Ancillary costs for the fund are likely to be in the order of \$1500 for setting up a corporate trustee (usually preferred by the lender) and Morgan estimates the “lender legal review fee” which covers checking the fund’s deed can range from \$1500 to \$2500.

These are on top of the normal annual fees for DIY super funds.

The paperwork for a DIY super fund loan takes twice as long as a normal loan, says Morgan.

There are more booby traps. Get the sequence wrong in producing and stamping documents and the fund could face double stamp duty, warns Michael Hallinan, special counsel for Townsends Business & Corporate Lawyers.