

## PROPERTY PROBLEMS – PETER FREEMAN SAYS SMSF LOANS CAN BE MINEFIELDS

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Peter Freeman



It is now four years since Self-Managed Super Funds were granted the right to gear into property, be it residential, commercial, retail or industrial. This concession was an important shift given that, up to that time, SMSFs were banned from borrowing to invest in property and had only very restricted avenues for taking a geared exposure to the share market.

And, in one sense, all direct borrowing by an SMSF is still banned. The change that took place on September 24, 2007 didn't totally reverse that ban but instead set out a series of rules, some of which were subsequently modified, to allow SMSFs to invest using "limited recourse" debt.

In other words, when an SMSF borrows to invest it has to be done in such a way that, should the investment turn sour, the lender has no claim against the other assets of the fund. This is the case, for example, when you invest in shares using instalment warrants or a geared share fund.

Satisfying this "limited recourse" requirement isn't so easy when it comes to direct property investment, mainly because it involves setting up a separate trust to hold the property, a process which triggers additional complications.

This is no doubt one of the main reasons SMSFs generally have approached this sort of property gearing with caution.

Craig Morgan, the director of mortgage broker SMSF Loans, says industry estimates indicate that around 5000 SMSF mortgages were taken out in 2010-11. Morgan, speaking at a conference organised by SMSF administrator Multiport, noted that the complexity of the borrowing process means it takes about 50% longer to settle an SMSF loan than it does a standard mortgage.

Just how complex the loan structure can be, and the problems it can cause, were highlighted by another speaker, Michael Hallinan, special counsel with Townsends Business & Corporate Lawyers.

"We have noticed a number of mistakes or poorly developed approaches commonly being made by trustees and their accountants and advisers," he said.

According to Hallinan, careful planning is required to settle the loan correctly, so as not only to ensure compliance with the legislation but also to ensure that only nominal stamp duty has to be paid when the property eventually is transferred from the holding trust to the SMSF.

One mistake that can result in a lot of wasted time is failing to make the effort at the beginning of the borrowing process to understand fully a lender's mortgage requirements. These can include a demand that the trustees provide personal guarantees for the loan, a requirement that the trustee be a company and an insistence that the fund's accountant, adviser or lawyers sign off on the loan arrangement.

### **Risk Reduction**

An account-based pension being paid to the sole remaining member of an SMSF can result in non-dependent beneficiaries being hit by a hefty tax bill when the member dies. While it has long been known that this can happen if a pension account consists of a lot of concessional super contributions, tax office draft ruling TR 2011/D3 has raised the prospect of another tax slug.

If confirmed, it would mean that all the gains accumulated in a pension account of a sole surviving member could incur capital gains tax when the member dies. One way to reduce this risk would be to keep liquidating capital assets, with the aim of ensuring only cash was left in the account.