

SMSF owning property jointly with another entity

Thinking of your SMSF co-owning residential real property with a non-related entity? There are important super compliance and contract considerations arise that must be considered. Carter Holdings Pty Ltd is the corporate trustee of the J. C. Superannuation Fund. Ms Carter, the sole member of the Fund and the sole company secretary/director of the corporate trustee, is looking to buy a two-bedroom apartment as part of her superannuation investment strategy.

Investment strategy

The two-bedroom apartment will be jointly owned by Ms Carter's life-time friend, Mr Lee. Under their proposed co-ownership agreement, both Ms Carter and Mr Lee will each own a 50% share in the property as tenants in common. Does this transaction violate the provisions of the Superannuation Industry (Supervision) Act 1993 (Cth) (SIS Act)? The Australian Taxation Office has greatly emphasised the need for SMSFs to formulate and incorporate a clear and transparent 'investment strategy' when acquiring real property. Generally, this involves the Trustee proving that they have developed a methodology for the purpose of accumulating the Fund's superannuation benefits. The issue here is whether Carter Holdings Pty Ltd and Mr Lee have entered into a valid transaction.

Where Carter Holdings Pty Ltd is concerned, co-ownership of real property is not prohibited provided that both entities deal 'at arm's length'. Essentially, the term 'at arm's length' primarily refers to:

1. the relationship between the two parties (section 70B to 70E of the SIS Act); and
2. any requirement under the SIS Act relating to limited recourse borrowing arrangements and the giving of security over the property.

Here Ms Carter (as a member of the Fund) and Mr Lee are not related parties for the purposes of section 70B to 70E. Whilst the term 'related-party' is a relatively broad term, it is generally understood as:

- relatives of each member of the fund (spouse, children, siblings etc.)
- business partners of each member of the fund
- any spouse or children of those business partners
- any company controlled by the member or any of the above associates, or
- any trust controlled by the member or any of the above associates.

Co-ownership agreement

The proposed co-ownership agreement will also have a substantial influence on the transaction and may affect the Fund's investment strategy in the future. Generally, a co-ownership agreement will state the rights and obligations of each co-owner with regards to the administration of the property. Important provisions may refer to, but are not limited to, the right to sell or force a sale of the property and the right to refuse proposals of sale. As Ms Carter's fund trustee is purchasing the property as part of that fund's investment strategy, the right to sell (and refusal to sell) are important prerogatives which ought to be formalised in a co-ownership agreement. Should the Fund need to sell the property in order to make payments to its member, the right to sell and/or the right to refuse sale will be of paramount importance. In the absence of a co-ownership agreement, the matter is likely to end up in Court, causing excessive financial and emotional distress, not to mention the huge amount of time usually required from the Court system.

For more information on any aspect covered in this article, please call SUPERCentral on 02 8296 6266 or email info@supercentral.com.au.