

“How to Borrow Without Sorrow”

How to use your super fund to borrow money to purchase property and not fall foul of the rules

Mackay

McKays Law Centre
34 Wood Street
PO Box 37
Mackay Qld 4740
DX 41389
mackay@mckayslaw.com
www.mckayslaw.com
Facsimile 07 4963 0889
Telephone 07 4963 0888

“The Law Firm of Choice”

McKays

Solicitors

Brisbane

Level 26
239 George Street
PO Box 12275, George Street
Brisbane Qld 4003
DX 40138
brisbane@mckayslaw.com
www.mckayslaw.com
Facsimile 07 3221 5379
Telephone 07 3223 5900

How to Borrow Without Sorrow

1. Can a Self Managed Superannuation Fund (“SMSF”) borrow?

1.1. General Prohibition

The trustee of a SMSF is prohibited from borrowing money or maintaining an existing borrowing of money except in limited circumstances.¹

1.2. Exemptions

- (a) Maximum 90 days to meet benefit payments due to members² or the surcharge liability³ provided borrowing does not exceed 10% of Fund’s total assets;
- (b) Short-term borrowing for 7 days to cover settlement of security transactions provided borrowing does not exceed 10% of Fund’s total assets;⁴
- (c) From 24 September, 2007, borrowings under Limited Recourse Borrowing.⁵

2. Limited Recourse Borrowing Arrangements

2.1. Recent Changes

On 6 July, 2010, the Superannuation Industry (Supervision) Amendment Bill 2010 received Royal Assent.

The purpose of the amendments was to:

- (a) reduce the risks to superannuation funds undertaking limited recourse borrowing; and
- (b) resolve some uncertainty about the borrowing exemption.⁶

The changes were sparked by developments in the superannuation borrowing market which had led to products and practices which raised prudential concerns for superannuation funds. These included:⁷

- (a) the use of personal guarantees to underwrite the lender's risk in the borrowing arrangement;

¹ *Superannuation Industry (Supervision) Act 1993* (Cth) s 67(1).

² *Superannuation Industry (Supervision) Act 1993* (Cth) s 67(2).

³ *Superannuation Industry (Supervision) Act 1993* (Cth) s 67(2A).

⁴ *Superannuation Industry (Supervision) Act 1993* (Cth) s 67(3).

⁵ *Superannuation Industry (Supervision) Act 1993* (Cth) s 67A.

⁶ Explanatory Memorandum, *Superannuation Industry (Supervision) Amendment Bill 2010* (Cth).

⁷ Explanatory Memorandum, *Superannuation Industry (Supervision) Amendment Bill 2010* (Cth).

- (b) borrowing arrangements over multiple assets which can potentially allow the lender to choose which assets are sold in the event of a default on the loan; and
- (c) arrangements where the asset subject to the borrowing can be replaced at the discretion of the trustee or the lender.

The changes to the Superannuation Industry (Supervision) Act 1993 (Cth) ("SIS Act") are summarized in the table below:⁸

Previous	Current s 67A
Act referred to "asset" in the singular, was possible to interpret "asset" in the plural.	Explicitly defines the interpretation of acquirable asset in the singular. (Single Acquirable Asset)
The Act limited the rights over the original asset in terms of the direct lender and associated borrowing only.	Ensures that the recourse of the lender or of any other person against the superannuation fund trustee for default on the borrowing is limited to rights relating to the acquirable asset.
Allowed borrowing arrangements over multiple assets which may permit the lender to choose which assets are sold in the event of a default on the loan.	Limits borrowing arrangements to a single asset or a collection of identical assets together treated as a single asset.
Allows arrangements where the asset subject to the borrowing can be replaced at the discretion of the trustee or the lender.	Clearly defines circumstances under which assets can be replaced.

2.2. s 67A SIS Act Exemption (Current):

The SMSF may enter into a borrowing arrangement where:⁹

- (a) the money is or has been applied for the acquisition of a **single acquirable** asset including:
 - (i) expenses incurred in connection with the borrowing or acquisition, or in maintaining or repairing the acquirable asset (but not expenses incurred in improving the acquirable asset). *Example: conveyancing fees, stamp duty, brokerage or [loan](#) establishment costs*; and
- (b) the acquirable asset is held on trust so that the SMSF trustee

⁸ Ibid.

⁹ Superannuation Industry (Supervision) Act 1993 (Cth) s 67A(1).

acquires a beneficial interest in the acquirable asset (aka “Holding” “Security” or “Custodian” Trust;

- (c) the SMSF trustee has a right to acquire legal ownership of the acquirable asset by making one or more payments after acquiring the beneficial interest; and
- (d) the rights of the lender or any other person (e.g. guarantor) against the SMSF trustee for, in connection with, or as a result of, (whether directly or indirectly) default on:
 - (i) the borrowing; or
 - (ii) the sum of the borrowing and charges related to the borrowing;
 - (iii) **are limited to rights relating to the acquirable asset;**

Example: Any right of a person to be indemnified by the SMSF trustee because of a personal guarantee given by that person in favour of the lender is limited to rights relating to the acquirable asset.

- (e) if, under the arrangement, the SMSF trustee has a right relating to the acquirable asset (other than a right described in paragraph (c))-- the rights of the lender or any other person against the SMSF trustee for, in connection with, or as a result of, (whether directly or indirectly) the SMSF trustee's exercise of the SMSF trustee's right are limited to rights relating to the acquirable asset; and
- (f) the acquirable asset is not subject to any charge (including a mortgage, lien or other encumbrance) except as provided for in paragraph (d) or (e).

2.3. What is a Single “Acquirable Asset”

A single acquirable asset cannot be money nor can it be an asset prohibited by being acquired by a superannuation fund.¹⁰ It could be a collection of assets where:

- (a) the assets in the collection have the same market value as each other; and
- (b) the assets in the collection are identical to each other.¹¹

For example - a collection of shares of the same class in a single company.

The asset must be a new asset – it is not possible to mortgage an existing asset of

¹⁰ Superannuation Industry (Supervision) Act 1993 (Cth) s 67A(2).

¹¹ Superannuation Industry (Supervision) Act 1993 (Cth) s 67A(3).

the fund.¹²

2.4. Potential Traps

Multiple Titles:¹³

Real property can encompass numerous legal titles - e.g. a strata title unit with an accessory car park.

Commercial premises that are effectively one asset but comprise several titles for historical or other reasons are often sold via a single Contract of Sale between the seller and the buyer as part of the same transaction. A narrow interpretation of “single acquirable asset” would mean that a SMSF trustee would need to take out a separate loan for each title (and there would need to be a separate declaration of trust for each title).

- **Industry views/suggestions** – submitted that an ‘in substance’ meaning should be adopted ie. where strata title with accessory car park or commercial premises encompassing multiple titles, is practically and commercially treated as one asset, it is arguably not the intention of SIS Act to require parties to maintain separate borrowings. A narrow interpretation of the legislation produces an extreme outcome.
- **Australian Taxation Office (ATO) initial response** – Agree practical test should be taken but proceed with caution. Where assets are for practical purposes inseparable or where there is an incidental ancillary asset of a very small value, the test for “single acquirable asset” will not be violated. However, by contrast do not think that sub-divided land will satisfy the test, whatever the terms of the borrowing.

The ATO accepts that the fact that a property acquired is subject to a lease should not be taken to cause the arrangement to fail the requirements of s 67A. The lease itself should not be considered as a separate asset as long as it is dealt with together with the property under the arrangement (and therefore does not need to satisfy the requirements of section 67A(3)). Similarly, the ATO takes the view that the existence of a lease in these circumstances should not be taken to cause the 'only property' test in paragraph 71(8)(c) to be failed.

Consider each situation on its facts - where tests are not satisfied, there will need to be separate limited recourse borrowing arrangements in respect of each asset.

¹² *Limited Recourse Borrowing Arrangements by Self-Managed Super Funds – Questions and Answers* (2010), Australian Taxation Office <
<http://www.ato.gov.au/superfunds/content.aspx?menuid=0&doc=/content/00132054.htm&page=1&H1>>
at 15 May, 2011.

¹³ National Tax Liaison Group (NTLG), *Superannuation Technical Minutes, September 2010* (2010) Australian Taxation Office
<<http://www.ato.gov.au/super/content.aspx?doc=/content/00260683.htm&page=11&H11>> at 15 May, 2011.

Off the Plan:¹⁴

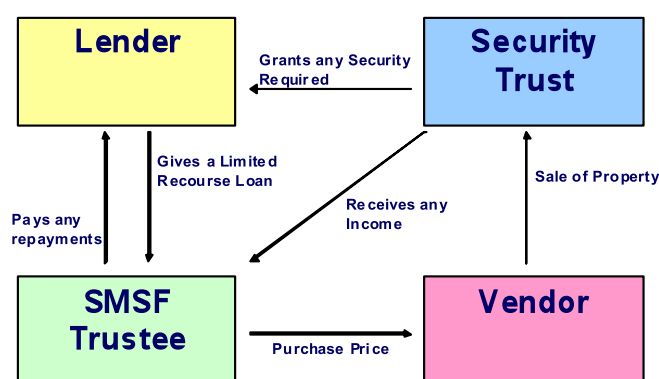
An “off the plan” purchase usually involves a superannuation fund signing a contract for a completed apartment to be delivered by the Seller at settlement. The Seller would then contract a builder to build the apartment separately and attend to other matters such as sub-dividing the title.

The ATO has not provided a definitive view on these arrangements due to lack of clarity of detail, but has commented that any arrangement would need to bear in mind the following requirements:

- (a) The asset must be transferred into the holding trust at the start of the borrowing and held in trust throughout the duration of the borrowing.
- (b) If the asset is replaced by another asset in circumstances which do not comply with the superannuation borrowing laws, then the arrangement must be terminated before a breach occurs.

The ATO has suggested that if the borrowing is made to fund the deposit and to acquire what at that stage is merely a contractual right to acquire title in future property, then there is a risk that the replacement of that “right” by the actual asset would be a contravention of the limited recourse borrowing arrangement provisions.

3. Basic Outline of Limited Recourse Structure



4. Preliminary Considerations

4.1. Compliance with SMSF Investment Rules

- (a) Has the investment strategy for the SMSF been complied with?
- (b) Does the investment strategy comply with s 52(2f) of the SIS Act?
 - (i) Risk;
 - (ii) Diversity;

¹⁴ Ibid.

- (iii) Liquidity;
- (iv) Ability to discharge liabilities.¹⁵
- (c) Is the investment the type of investment that a prudent person would make?¹⁶
- (d) Does the transaction comply with the sole purpose test?¹⁷
- (e) Does the transaction comply with in-house asset rules?¹⁸
- (f) Does the transaction comply with the rules relating to acquisition of assets from related parties?¹⁹
- (g) Is arm's length rule satisfied?²⁰
- (h) What is the intention with the asset? – ie. could cause breach of SIS Act if related persons are allowed to live in property or if commercial property, non-commercial rates are charged.²¹

4.2. Practical Considerations

- (a) Have you done a cash-flow analysis - is there sufficient cash-flow to make the interest payments over time?
- (b) if the Fund is in pension mode, then you need to ensure that the investment will leave enough money in the SMSF to keep paying the pension, plus make the interest payments;
- (c) are there enough funds in the SMSF to pay balance purchase price and related costs – lenders generally only lending 60-65%. If not, does a member need to make a contribution? Check contribution limits to ensure amount that can be contributed.
- (d) **Does the trust deed have the power to borrow and the power to make such an investment?** May need to update:
 - To engage in borrowing, need to ensure that SMSF trust deed contains:
 - Power to borrow
 - Power to charge assets and give security

¹⁵ *Superannuation Industry Supervision Act 1993* (Cth) s 52(2f).

¹⁶ *Superannuation Industry Supervision Act 1993* (Cth) s 52(2b).

¹⁷ *Superannuation Industry Supervision Act 1993* (Cth) s 62.

¹⁸ *Superannuation Industry Supervision Act 1993* (Cth) Part 8.

¹⁹ *Superannuation Industry Supervision Act 1993* (Cth) s 66.

²⁰ *Superannuation Industry Supervision Act 1993* (Cth) s 109.

²¹ *Superannuation Industry Supervision Act 1993* (Cth) Part 8; s 66, s 109, s 62.

- Power to appoint an agent/security trustee

5. Holding/Security Trust

5.1. Fundamental Elements

The Security Trust could be formed over original asset using the borrowings from the lender or over a settlement sum with the ability to have sub-trusts for each original asset purchased. The trustee of the SMSF will be the only beneficiary of the Security Trust.²² The Security Trust must have the ability to distribute the asset to the SMSF upon repayment of the loan.²³

5.2. Formation using Settlement Sum

If settlement sum used to form Security Trust, then possible that original asset will not be the only asset of the Security Trust and in-house asset exemption may not apply.²⁴

Example: Although \$10 settlement sum will likely be below 5% of Fund's total assets, the added purchase of an investment property held in the Security Trust would likely push the value of the Security Trust above that 5% threshold. Trustee would then be required to dispose of interest in the Security Trust before end of financial year.

However, have seen some examples of this used where firms have taken the view that it does not breach the borrowing rules.

5.3. Sub-Trust Strategy

An alternative strategy is to allow clients to have one Security Trust but multiple borrowings, without having to have a new Security Trust deed (ie. for investments in shares which may happen more than once). This would allow a settlement sum to be used to create the trust deed.

The general idea is that the security trust is set up and then distinct and separate sub-trusts are created for each purchase, with the trustee of the SMSF appointing the security trustee as agent for the purchase of each asset and sub-trusts being named in that document.

It is recommended that the trust deed should have clauses in it stating:

- (a) That each asset acquired under a sub trust will be kept separate and distinct and capable of identification by the Security Trustee;
- (b) That a separate bank account, or at least separate accounting records and books, will be kept by the Security Trustee;
- (c) May be worth having separate names for each sub-trust – with a

²² *Superannuation Industry Supervision Act 1993* (Cth) s 67(1)(b).

²³ *Superannuation Industry Supervision Act 1993* (Cth) s 67(1)(c).

²⁴ *Superannuation Industry (Supervision) Act 1993* (Cth) s 71(8).

clause saying that each sub-trust will have the same name as the original Security Trust but be consecutively numbered (ie. Security Trust 1, Security Trust 2 etc)

- (d) That the sub-trust will be governed by the terms of the Security Trust Deed.

5.4. Is it a “Related Trust” for In-House Asset Test?

Section 67A(1)(b) contemplates that the SMSF will become a beneficiary in a related trust.²⁵

An “in-house asset” of a superannuation fund is an asset of the fund that is a loan to, or an investment in, a related party of the fund, an investment in a *related trust of the fund*, or an asset of the fund subject to a lease or lease arrangement between a trustee of the fund and a related party of the fund.²⁶

“Related Trust” of a superannuation fund, means a trust that a member or a standard employer-sponsor of the fund controls *other than an excluded instalment trust of the fund*.²⁷

However, the in-house asset exemption provides:

“If, at a time:²⁸

- (a) an asset (the investment asset) of a superannuation fund is an investment in a related trust of the fund; and
- (b) the related trust is one described in paragraph 67A(1)(b) in connection with a borrowing, by the trustee of the fund, that is covered by subsection 67A(1); and
- (c) the only property of the related trust is the acquirable asset mentioned in that paragraph;

the investment asset is an in-house asset of the fund at the time only if the acquirable asset mentioned in that paragraph would be an in-house asset of the fund if it were an asset of the fund at the time.”

The result of the exclusion is that the investment in the Security Trust will not be taken to be an in-house asset (provided conditions complied with).

If borrowing undertaken by the trustee of the SMSF which does not comply with the rules, then the investment in the security trust will be a breach of the in-house asset rules if the investment is more than 5% of the total value of the SMSF.²⁹

²⁵ *Superannuation Industry (Supervision) Act 1993* (Cth) s 67A(1)(b).

²⁶ *Superannuation Industry (Supervision) Act 1993* (Cth) s 71(1).

²⁷ *Superannuation Industry (Supervision) Act 1993* (Cth) s 10.

²⁸ *Superannuation Industry (Supervision) Act 1993* (Cth) s 71(8).

²⁹ *Superannuation Industry (Supervision) Act 1993* (Cth) s 75.

6. Lending Process

6.1. The Lender

Section 109 of the SIS Act prohibits a SMSF from making an investment, unless the investment is at 'arm's length'.³⁰ In most cases, the Lender will be a bank or independent financier. Accordingly, the 'arm's length' rule will be complied with.

Presently, there is no restriction on the lender being a related party. However, care would need to be taken to ensure compliance with the superannuation rules. For example, payment of an excess rate of interest to a relative may contravene the rule against providing financial assistance to members or their relatives.³¹

It should be noted that if the lending involves a private company, then Division 7A of the *Income Tax Assessment Act 1936* (Cth) may still apply.

The lender's fees (ie stamp duty, brokerage and loan establishment costs) can be paid from the borrowed funds.³²

6.2. Potential Changes – Consumer Protection

On 10 March 2010, the Minister for Financial Services, Superannuation and Corporate Law, the Hon Chris Bowen MP, announced that the government will extend the consumer protection framework to include limited recourse borrowing arrangements by superannuation fund trustees.³³ Accordingly, these arrangements would become "financial products" under the *Corporations Act 2001* (Cth).

The impact of these changes would mean that only appropriately licensed financial services providers would be able to offer lending to superannuation funds.³⁴

6.3. Charging Assets

Superannuation funds are prohibited from giving charges over their assets, except for where the charges are required or implied by the SIS Act or Superannuation Industry (Supervision) Regulations 1994 (Cth) ("SISR").³⁵

Whilst the regulations have not been amended to cater for the superannuation borrowing exception, the Australian Prudential Regulation Authority ("APRA") and the ATO have not raised this as an issue of concern. If the borrowing rules under the

³⁰ *Superannuation Industry (Supervision) Act 1993* (Cth) s 109.

³¹ *Limited Recourse Borrowing Arrangements by Self-Managed Super Funds – Questions and Answers* (2010), Australian Taxation Office <<http://www.ato.gov.au/superfunds/content.aspx?menuid=0&doc=/content/00132054.htm&page=1&H1>> at 15 May, 2011.

³² *Superannuation Industry (Supervision) Act 1993* (Cth) (1)(a)(i).

³³ Chris Bowen, Minister for Financial Services, Superannuation and Corporate Law, 'Financial Services Consumer Protection Framework Extended to Superannuation Borrowing Arrangements' (Press Release, 10 March, 2010) <<http://www.treasurer.gov.au/DisplayDocs.aspx?doc=pressreleases/2010/020.htm&pageID=003&min=ceba&Year=&DocType=0>> at 15 May, 2011.

³⁴ *Ibid.*

³⁵ *Superannuation Industry (Supervision) Regulations 1994* (Cth) reg 13.14.

SIS Act are complied with, then the arrangement should fall within the exception for charging assets.

6.4. Instruments

The loan documentation should list the trustee of the superannuation fund as the borrower. The arrangement must be a limited recourse loan.³⁶ It is crucial that security is only taken over the original asset or replacement asset acquired, pursuant to the borrowing arrangement.

Any guarantees should be reviewed to ensure that they do not breach the borrowing rules and that no security is taken over the assets of the SMSF.³⁷

6.5. Member Guarantees

Since the changes in 2010, there has been clarification around members providing guarantees:³⁸

24 September, 2007-7 July, 2010	Current (Since 7 July, 2010)
Members can give guarantees and put up their own assets as a guarantee to provide additional security to the lender	Members can give guarantees provided rights against the principal debtor (the SMSF trustee) are limited to rights relating to the asset being acquired under the arrangement.
Recourse of the lender against the SMSF trustee in event of a default must be limited to the Asset	...the recourse of the lender or any other person against the SMSF trustees... must be limited to rights relating to the asset that is being acquired under the arrangement.
No requirement that guarantor waive their usual rights of indemnity against the SMSF trustee.	The guarantor must not have general rights of indemnity against the SMSF. The guarantor may have rights of subrogation of the lender's rights (that is, the right to exercise the lender's limited rights of recourse to the asset being acquired under the arrangement).

³⁶ *Superannuation Industry (Supervision) Act 1993* (Cth) s 67A(1)(d).

³⁷ *Superannuation Industry (Supervision) Act 1993* (Cth) s 67A(1)(d).

³⁸ Explanatory Memorandum, *Superannuation Industry (Supervision) Amendment Bill 2010* (Cth).

Beware of deemed contributions:³⁹

If a guarantor makes a payment to the lender under an arrangement where they have foregone their usual rights of indemnity against the SMSF, this is a contribution to the SMSF if it satisfies a liability of the SMSF – e.g. where the guarantor paid the borrowing and the acquirable asset was transferred to the SMSF trustee under the arrangement.

However, there would be no deemed contribution if the SMSF trustee has exercised a right to 'walk away' from the arrangement (and has lost the acquirable asset to the lender) and has no further liability, but the lender still exercises a right to call on the guarantee for a shortfall.

6.6. Loan Drawdown

The borrowing arrangement must be for the acquisition of a single acquirable asset.⁴⁰

Arguably, the SMSF could not draw down the loan and hold it pending completion of the contract. If funds are provided to SMSF who provides them to security trustee to hold on account prior to settlement (gathering interest), then this may itself, breach the borrowing rules, as the money would have been applied firstly to the security trustee and accrued interest. It is best to have the lender fund directly on the day of settlement to the SMSF who can provide the cheque directly to the vendor.

7. Contract of Sale

7.1. Buyer on Contract

When preparing the Contract of Sale, the purchase should be the trustee of the Security Trust.

If the Security Trust has not been established at the time of the Contract being signed, then a special condition should be inserted whereby the seller agrees, that upon the request of the buyer, the Contract can be rescinded (upon request by the buyer) and a new Contract entered into, with the buying entity being the trustee of the Security Trust. In this instance, it is strongly recommended that the buying entity is not just simply amended or crossed out and replaced, as this may cause stamp duty to be assessed twice.

7.2. GST Considerations

It is important to consider whether the security trust needs to be registered for GST.

Generally, GST registration is required where an enterprise is carried on and the turnover is \$75,000 or more.⁴¹ If the turnover is less than \$75,000, then GST

³⁹ See above n 12.

⁴⁰ *Superannuation Industry (Supervision) Act 1993* (Cth) s 67A(1)(a).

⁴¹ *A New Tax System (Goods and Services Tax) Act 1999* (Cth) s 23.5; *A New Tax System (Goods and Services Tax) Regulations 1999* (Cth) reg 23.15.01.

registration is optional.⁴²

An enterprise can be, among other things, an activity, or series of activities done on a regular or continuous basis, in the form of a lease, licence or other grant of an interest in property by a trustee of a complying superannuation fund or other person who manages the fund.⁴³

Accordingly, in a superannuation borrowing, it is important to consider whether the security trustee needs to be registered for GST. Is the superannuation fund going to be receiving \$75,000 or more in rent over the year?

A popular choice for structuring the borrowing arrangement is through a bare trust. The advantage of a bare trust is that a “look through” approach would be adopted by the ATO.⁴⁴ This would mean that there is no need to separately register the holding trust for GST as the beneficiary (superannuation fund) would be liable for the GST and able to claim input tax credits.⁴⁵ Further, if it is a bare trust, then there would be no CGT on the transfer of assets to the SMSF.⁴⁶

However, recently there has been much debate over whether or not a holding/security trust can ever be a “bare trust”. The ATO has indicated that a holding trust is not a bare trust.⁴⁷

If a holding/security trust is not a bare trust, then the security trust may need to be separately registered for GST. If the security trust is not separately registered for GST, then the Going Concern Concession may be at risk (as both the Buyer must be registered or required to be registered for GST for the concession to apply).⁴⁸

Regardless of whether or not a holding trust is a bare trust, the Government has announced that legislation will be amended so that the trustee of superannuation funds will not face CGT obligations at the time of the last installments being paid and the property is transferred to the SMSF trustee.⁴⁹ The legislation is proposed to have retrospective effect from the 2007-08 income year.⁵⁰

8. Repairs, Maintenance and Improvements

Borrowed monies can be applied towards maintaining or repairing the asset, but not expenses incurred in improving the asset.⁵¹ This means that borrowings could not be used to renovate an asset or build a house on vacant land owned by the fund.

⁴² *A New Tax System (Goods and Services Tax) Act 1999* (Cth) s 23.10.

⁴³ *A New Tax System (Goods and Services Tax) Act 1999* (Cth) s 9.20.

⁴⁴ Australian Taxation Office, *GSTR 2008/3- Goods and Services Tax: Dealings in Real Property by Bare Trusts* (2008), Australian Taxation Office

<<http://law.ato.gov.au/atolaw/view.htm?docid=GST/GSTR20083/NAT/ATO/00001>> at 15 May, 2011.

⁴⁵ *Ibid.*

⁴⁶ *Ibid.*

⁴⁷ See above n 13.

⁴⁸ *A New Tax System (Goods and Services Tax) Act 1990* (Cth) s 38.325.

⁴⁹ See above n 33.

⁵⁰ See above n 33.

⁵¹ *Superannuation Industry (Supervision) Act 1993* (Cth) s 67A(1)(a)(i).

8.1. Repair v Improvement

Taxation Ruling 97/23 provides some guidance on what constitutes a “repair”.⁵² It says that a repair, on its ordinary meaning, is remedying or making good of defects in, or damage to, or deterioration of, property to be repaired. Repairs may be necessitated by fair wear and tear, accidental or deliberate damage, or by the operation of natural causes. Work done though to prevent or anticipate defects, damage or deterioration may not a repair unless it is done in conjunction with remedying or making good defects in, or damage to, or deterioration of, the property. Repair for the most part is occasional and partial. It involves restoration of the efficiency of function to the property being repaired without changing its character.⁵³

By extension therefore, an improvement is bringing a thing or structure into a more valuable or desirable form, state or condition than a mere repair would do. It would provide greater efficiency or function in a property. Some factors that point to work done to property being an improvement include whether the work will extend the property's income producing ability, significantly enhance its saleability or market value or extend the property's expected life.⁵⁴

8.2. Creation of Replacement Asset

Section 67A of the SIS Act expressly provides that monies borrowed pursuant to a limited recourse arrangement must not be used to improve a property.⁵⁵ Making improvements to a property (whether or not funded by the borrowed monies), may cause the asset to become a “replacement asset” and cause a breach of the rules.⁵⁶

For example, if a house was completely destroyed by a flood, then technically, the fund would not be permitted to use the insurance money to rebuild the dwelling as this would be making ‘improvements’ rather than repairs and be a “replacement asset”.

This issue has become particularly pertinent as a result of the floods and fires experienced in Australia this year. However, it is pleasing that the taxation commissioner, Michael D’Ascenzo has announced that he will use his discretionary powers under the SIS Act to allow SMSF trustees to use limited recourse borrowings to repair the asset damaged by the recent natural disasters.⁵⁷ In many instances, the type of repairs that would need to be made would ordinarily be classified as “improvements” to the asset or even a replacement asset, neither of which can be

⁵² Australian Taxation Office, *TR97/23- Income Tax: Deductions for Repairs* (1997), Australian Taxation Office < <http://law.ato.gov.au/atolaw/view.htm?docid=TXR/TR9723/nat/ato/00001>> at 15 May, 2011.

⁵³ *Ibid.*

⁵⁴ *Ibid.*

⁵⁵ *Superannuation Industry (Supervision) Act 1993* (Cth) s 67A(1)(a)(i).

⁵⁶ *Superannuation Industry (Supervision) Act 1993* (Cth) s 67B.

⁵⁷ Darin Tyson-Chan, ‘ATO provides SMSF disaster relief – Discretion exercised over borrowing arrangements’, *Investor Daily*, 23 March, 2011. <<http://www.investordaily.com.au/cps/rde/xchg/id/style/11291.htm?rdeCOQ=SID-0A3D9632-077F92AC&rdeCOQ=SID-0A3D9633-349AC214>> at 15 May, 2011.

funded through a limited recourse borrowing.⁵⁸

He has stated that “in financing repairs or incurring other costs, trustees may need to borrow funds and if trustees contravene the limited recourse borrowing provisions due to the natural disasters experienced Australia-wide, we would be favourably inclined to exercise the commissioner's discretion under section 42A(5) of the Superannuation Industry (Supervision) Act 1993 to continue to treat the super fund as complying. We are currently reviewing this matter with APRA (Australian Prudential Regulation Authority) and Treasury to ensure no unintended consequences arise.”⁵⁹

9. Stamp Duty on Transfer of Asset

There may be potential stamp duty issues on transfer of the asset from the trustee of the holding/security trust into the SMSF. Though many advisors do not believe that stamp duty should be payable, it is our understanding that the Queensland Office of State Revenue believe otherwise. Most advisors rely on section 123 of the *Duties Act 2001* (Qld) that states that the trustee of a bare trust may distribute the property to the beneficiary (if it was absolutely entitled to the asset) without duty. Other commentators rely on the agency provisions in section 22(3) of the *Duties Act 2001* (Qld).⁶⁰

On discussing this matter with the duties' officials, they have repeated the Office of State Revenue's position that the final payment of the loan and the transfer of the property from the Security Trust to the SMSF will be assessed as a dutiable transaction.

10. Questions?

Presenter: Suzanne Brown (LLB Hons) - Senior Solicitor
 McKays Solicitors, 34 Wood Street, MACKAY QLD 4740
 Ph: (07) 4963 0820
 Email: sbrown@mckayslaw.com

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- This information is current as at 15 May, 2011. The law may change and we take no responsibility for notifying or updating you on any changes.
- This information is only of a general nature and should not be applied to individual situations without seeking further advice.
- The information presented is focused on particular issues and is not intended to be an exhaustive representation of the different legal issues.
- We do not provide any accounting, taxation, financial advice – you should seek advice from the appropriate professional.
- This information applies only to Queensland – laws may differ between states.

⁵⁸ Ibid.

⁵⁹ Ibid.

⁶⁰ Paul Ellis, *Stamp duty and SMSF Limited recourse borrowing arrangements (formerly instalment warrants): is there a double duty jeopardy?* (2010) Cleardocs
 <<http://www.cleardocs.com/clearlaw/superannuation/double-duty-jeopardy.html>> at 15 May, 2011.