

smart smsf strategy #1: borrowing inside a smsf



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This month we start to delve into the wonderful opportunities that Self-Managed Super Funds (SMSFs) provide. The first strategy we will consider is borrowing.

In 2007 a change was made to legislation regarding super funds and borrowing to invest. An exemption was added to the SIS Act 1993 allowing super funds to borrow through an instalment warrant arrangement. This is a fairly basic concept whereby you pay an initial part payment upfront and then pay the remaining monies (plus interest) at a future date. The future payments could be a number of instalments (like your mortgage) or it could be as simple as one future payment.

It has taken a while for this strategy to gain momentum, but the Government has recently announced changes to these laws to make them easier to understand - particularly for property. In addition, as banks are seeing more of these loans, they are becoming much more competitive in terms of lending requirements and interest rates.

How does borrowing inside super work?

As mentioned, borrowing through a super fund must be done via an instalment

warrant arrangement. The SMSF borrows the money from a bank or another party (it could be themselves personally as the lender) and provides the money to a security trust (also known as a custodian trust). The security trust owns the asset on behalf of the SMSF until the loan is repaid. The SMSF receives all of the rent and pays all of the expenses. Once the last loan instalment payment has been made, the ownership of the asset is transferred from the security trust to the super fund.

Why is it an advantage to buy property through super?

The major advantage of borrowing through your super fund is the fact that if you hold on to the property until after you have started to draw down a pension (currently allowed once you reach age 55), and you then decide to sell it, there will be no capital gains tax. This is because there is 0% tax on all earnings once in a pension! Australia's own tax haven.

Secondly, one of the requirements for borrowing through a SMSF (as well as a benefit) is limited recourse. This means that should you default on the loan, none of the other super fund assets are at risk. A word of warning here, however - if you are borrowing from a bank, they are often seeking personal guarantees.

Finally, people have been frustrated by superannuation because they couldn't

buy the assets they wanted due to lower balances, and this limitation has now gone!

When would you use this strategy?

To grow your super fund at a faster rate with a much larger asset. The attractiveness of no capital gains tax is very compelling over a long period of time.

To buy the business property that your company operates out of. Your SMSF purchases the property and leases it back to your business.

For a seachange/ treechange. For those starting to think about where they want to live in retirement, they are securing their future home now via their super fund. Once they reach age 60, they will make a lump sum withdrawal (of the property) and start to live in it.

What are the traps of this strategy?

There are many things you need to be aware of with this strategy and getting it wrong can be costly. From ensuring your super fund trust deed allows the strategy, ensuring the loan and asset is held in the right name through to getting the paperwork right.

In addition, this strategy is not for everyone as borrowing always comes with risks (even for property).

The key is to seek advice from a SMSF Specialist Advisor® to work out whether this strategy might be right for you. **E**

How SUPER is your Self Managed Super Fund?



Make the most out of your SMSF, talk to
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