

SMSF Borrowing – Rulings and Releases



With Super Borrowing still in its infancy stage, the regulatory bodies associated with these transactions have released a number of rulings, draft rulings, alerts and publications clarifying their positions in relation to SMSF instalment warrants.

In this article we summarise some of the more pertinent rulings and releases from the ATO and the State Revenue Offices to provide you with a general overview of their respective positions.

ATO Alerts, Rulings and Draft Rulings

- Tax Payer Alert TA 2008/5
- GST Ruling GSTR 2008/3
- Draft Taxation Ruling TR 2009/D3
- Instalment warrants & super funds – questions and answers

Tax Payer Alert TA 2008/5

In this tax payer alert, the ATO raises concerns about certain features that an instalment warrant may exhibit. The features that are noted as raising concern for the ATO are as follows:

- 1. Rates of interest, especially in the case of related party loans.**
Summary: loans to the Fund, especially in regards to related party lenders, must be on commercial terms.
- 2. Capitalisation of Interest on the borrowing**
Summary: The capitalisation of interest may result in the instalment warrant failing to meet the requirement of paragraph 67(4A)(a) of the SIS Act which states the loan proceeds must be applied for the acquisition of an asset.
- 3. A personal guarantee for the borrowing is given by a third party, particularly where the guarantee is given by a member or a related party of the SMSF**
A personal guarantee given in the manner above may result in the lender having a recourse against assets of the super fund other than the asset being acquired, which is “contrary to the intent that the exception in subsection 67(4A) of the SIS Act only applies to limited recourse borrowings”.
- 4. The asset acquired is one that a trustee is prohibited from acquiring under SISA, or the SMSF's governing rules (eg, residential property, which is not business real property, from a related party)**
Summary: The Asset being acquired by the Fund must be one that the Fund could acquire if purchased outright as determined by SISA and the Fund's Trust Deed.

View this Tax Payer Alert in full

<http://law.ato.gov.au/atolaw/view.htm?docid=TPA/TA20085/NAT/ATO/00001>

GST Ruling GSTR 2008/3

This ruling applies to “supplies of real property involving bare trusts and similar trusts where the trustee has limited active duties and acts solely at the director of the beneficiary or beneficiaries”.

The ruling states that it is the super fund Trustee, and not the Custodian Trustee, that bears the liability for GST where the supply is a taxable supply in the following circumstances

- There is a supply of real property.
- The trustee of a bare trust acquires the real property to be held in a bare trust.

- The trustee has limited active duties, acts solely at the direction of the beneficiary and has no independent role in respect of the trust property.
- The SMSF beneficiary carries on an enterprise for GST purposes.
- The SMSF beneficiary arranges for the real property to be used in its enterprise.
- The real property is therefore acquired by the trustee to hold upon a bare trust for the SMSF beneficiary (subject to an obligation to transfer the legal title to the property to the beneficiary)
- The SMSF beneficiary carries on an enterprise in respect of the real property even though the legal title to the property is registered in the name of the bare trustee.
- The SMSF beneficiary makes supplies for consideration in relation to its enterprise.
- The consideration is received by the bare trustee who is bound to pay the consideration to the SMSF beneficiary.
- Because the trustee of the bare trust holds the real property on behalf of a SMSF beneficiary, the trustee does not carry on an enterprise for GST purposes as the trustee deals with the property at the direction of the SMSF beneficiary.
- Therefore, the SMSF as the beneficiary, and not the bare trustee, bears the liability for GST where the supply is a taxable supply.

View the full details of this Ruling

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

Draft Taxation Ruling TR 2009/D3

This draft ruling is relates to contributions to a superannuation fund, and is relevant to the issues of guarantees and instalment warrants. Clause 13 of this draft ruling reads as follows:

“A person may pay an amount to a third party to satisfy a liability of a superannuation provider on behalf of the provider. The person will usually be a member of the fund or an employer (or associate of the employer) of a member of the fund. The payment to the third party is treated for all tax purposes as though the person had made a contribution to the superannuation provider and the provider had separately paid an equal amount to the third party.”

The effect of this draft ruling is that, according to the ATO, if a member makes a payment under a guarantee relating to an SMSF borrowing, and they forgo their right of indemnity to assets of the Fund, then the payment is regarded as a contribution to the Fund.

View this Draft Ruling in full

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

Instalment warrants & super funds – questions and answers

The ATO released this publication to provide “general guidance on the Tax Office’s current views regarding the application of the superannuation law (specifically the Superannuation Industry (Supervision) Act 1993 and related superannuation rules) to instalment warrant type arrangements”. The key points to come from this publication are:

Related Party Transactions:

- “The exemptions provided for in the rules against acquisition of assets from related parties, such as those allowing for the market value acquisition of listed securities or business real property” apply to instalment warrants.
- A SMSF can borrow from a related party of the Fund for the purposes of an instalment warrant if the loan terms are on a commercial basis.

Conditions of the borrowing:

The instalment warrant borrowing arrangement must satisfy the following conditions:

- “The borrowed monies are used to acquire an asset which the fund is not otherwise prohibited from acquiring.
- The asset acquired (or a replacement asset) is held on trust so that the fund receives a beneficial interest in the asset.

- ii. The super fund has the right to acquire legal ownership of the asset (or, if applicable, the replacement asset) by making one or more payments after acquiring the beneficial interest.
- iii. Any recourse that the lender has under the arrangement against the super fund is limited to rights relating to the asset acquired (or, if applicable, the replacement asset). That is, the lender is able to have the right to recover monies where there is a default on the borrowing by repossessing or disposing of the asset acquired, but cannot have the right to recover such monies through recourse to the fund's other assets."

Borrowing situations that are not compliant

- i. The Trust that holds the asset on trust for the super fund cannot be a Unit Trust.
- ii. The Fund is not allowed to put an existing asset of the Fund into an instalment warrant arrangement.

Other pertinent issues

- i. Provided the borrowing arrangement complies with the relevant law, the granting to the lender of a mortgage over the asset being acquired will not contravene the prohibition against giving a charge over a Fund asset.
- ii. The Fund cannot enter into an instalment warrant arrangement if its Trust Deed does not allow for it.

Issues not resolved by this publication include:

- i. "Does an arrangement where a borrowing is guaranteed by a third party satisfy the new laws, particularly where the personal guarantee is provided by a member or a related party? – for more clarification see Draft Taxation Ruling TF 2009/D3 (below).
- ii. Does an arrangement that permits re-financing satisfy the new laws?
- iii. Does an arrangement that permits capitalisation of interest satisfy the new laws?
- iv. Can multiple drawdowns from a single loan facility satisfy the new laws?"

View the full details of this publication

<http://www.ato.gov.au/superfunds/content.asp?doc=/content/00132054.htm>

Victorian State Revenue Office

The Victorian State Revenue Office (SRO) has published its view on the Stamp Duty exemptions available for instalment warrant transactions via Self Managed Superannuation Funds (SMSFs) in a document titled "Instalment Warrant Arrangements – Use of instalment warrant arrangements by self managed superannuation funds'. A summary of the SRO release is as follows.

The SRO basis its view on the 'more common structures' used to facilitate an instalment warrant (or SMSF Loan) arrangement, which have as their basis:

1. "The SMSF provides all of the deposit monies and the balance of the purchase price for the land (the Property) from a combination of SMSF assets and borrowings from a financial institution (the Lender).
2. The trustee of the SMSF is the only borrower under a finance agreement.
3. A person other than the trustee of the SMSF (the Custodian) acquires the Property using the money provided by the SMSF, pays duty on the acquisition and is registered as the legal freehold owner on title." (Topdocs notes that the duty payable will be paid by the Custodian on behalf of the SMSF with the proceeds coming from the SMSF account)
4. "The Custodian executes a declaration/acknowledgment of trust that the Custodian holds the Property on a fixed trust or bare trust for the SMSF.
5. The Custodian grants the Lender a limited recourse mortgage on the terms required by the Lender over the Property.
6. The Custodian retains legal title to the Property until the borrowing from and mortgage to the Lender is fully discharged by the SMSF and then the unencumbered title is transferred absolutely to the trustee of the SMSF.
7. The Property is post-2006 land as defined in section 3 of the [Land Tax Act 2005](#), as section 67A(4A) of the SIS Act only came into effect from 24 September 2007. "

Duty payable at the purchase of the Property

Summary:

The property will attract ad valorem duty payable by the Custodian on behalf of the super fund as per a normal property purchase.

The SRO requires the Custodian Trust Deed (declaration of trust) to be registered with the SRO. The Custodian Trust Deed will be exempt from duty if its structure shows that the Custodian Trustee is merely holding the property on trust for the SMSF under a fixed or bare trust structure. Part of this requirement is demonstrating that the SMSF provided all monies for the purchase of the property. If the transfer of the property to the Custodian and the declaration of trust occurred 'contemporaneously' then the Custodian Trust Deed may be exempt from duty under section 17 of the Duties Act.

Duty payable upon transfer of the property from the Custodian to the SMSF Trustee

It should be noted that the SMSF Trustee has the right, but not the obligation, to transfer title of the property from the Custodian Trustee to the SMSF Trustee. Should the SMSF wish to exercise its right to transfer, there two possible exemptions that may apply:

1. If the Custodian Trust Deed was classified as exempt from duty when lodged with the SRO on the basis that the Custodian Trustee is merely holding the property on trust for the SMSF under a fixed or bare trust structure, then the transfer of the Property from the Custodian Trustee to the super fund Trustee will be exempt from duty.
2. Alternatively, if it can be evidenced that:
 - i. "duty was paid when the Property was acquired by the Custodian, and
 - ii. for the whole period from the time the trust was declared by the Custodian to the time when the Property was transferred to the trustee of the SMSF:
 - a. the trustee of the SMSF was always the only beneficiary, and
 - b. the beneficiaries (who are natural persons) of the SMSF were always the only beneficiaries of the SMSF. "

the transfer will be exempt from duty. However, before this exemption applies, the Commissioner of State Revenue would have to be satisfied that "the transfer is not part of a sale or other arrangement under which there exists any consideration for the transfer."

View the full details of this publication

<http://www.sro.vic.gov.au>

For more information on SMSF borrowing, please contact a Topdocs consultant on 1300 659 242 or visit our website at www.topdocs.com.au