SUPERMATTERS
SUPERANNUATION STRATEGIES FOR YOU AND YOUR BUSINESS

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Super Wise
SMSF SPECIALISTS

Risks of SMSF property gearing

A self-managed super fund (SMSF) is often considered an attractive option to purchase property, but it is important to beware of the involved risks and complications before deciding if it is the right investment choice for you.

The *Superannuation Industry (Supervision) Act 1993* (SIS Act) sets out stringent rules so that you may only borrow from your super to buy property under strict and complex borrowing terms known as a limited recourse borrowing arrangement (LRBA).

These terms are specific and also hold many potential risks for the trustee.

'Single acquirable asset'

Under an LRBA you can only purchase one "single acquirable asset" (i.e., a residential or commercial property) by taking out a loan with a third-party lender. The purchased asset must then be held in a separate trust called a bare trust. The bare trust holds the legal title to the asset on behalf of the SMSF.

Higher expenses

LRBAs generally have higher setup costs, interest and fees attached, which could potentially take away from any profits to be made from the investment. Banks also typically lend smaller amounts in LRBAs than for personal loans.

Can not reside in purchased property

Neither you nor your family will be able to take up residence in the property. However, you may use it for business purposes and pay rent at market rate prices back to your SMSF.

No 'capital improvements'

You can use borrowed funds to maintain or repair the property, but you can not make any capital improvements using the funds until after the loan is paid off. Using other SMSF savings to make changes to the property is permitted.

Fewer tax deductions

It is important to know that should you incur any tax losses through your investment you will not be entitled to offset these losses against your taxable income earned outside your SMSF.

Repayments

Loan repayments will be paid out of your SMSF, so it is important to check whether there will be sufficient capital to cover each payment.

Incorrect arrangements

Get professional advice to ensure your documentation is set up correctly. If your LRBA is structured inaccurately, it can significantly affect your SMSF, i.e., you may be required to sell the property (producing a loss of capital for your SMSF).

Defaulting on the loan

Should you default on the loan, the lender may only seize the property purchased through the LRBA. Any other retirement assets in your SMSF will remain protected.

Before buying property through your SMSF, it is essential to consider how the potential implications will affect your overall investment strategy.

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Boost your super by downsizing your home

Older Australians will soon be able to contribute the sale proceeds of their home to their superannuation when downsizing.

From 1 July 2018, eligible individuals can make a contribution into their super of up to $300,000 from the proceeds of the sale of their home. Fortunately, individuals are not required to purchase another home to access this measure.

Those aged 65 and over must meet the following eligibility requirements to make downsizer contributions into their super:

- the contract of sale must be exchanged on or after 1 July 2018;
- an individual or their spouse has owned the home for 10 or more years before the date of settlement of the sale;
- the home is located in Australia and is not a caravan, houseboat or other mobile home;
- the sale proceeds are exempt or partially exempt from CGT under the main residence exemption or entitled to an exemption if the home was a CGT rather than a pre-CGT asset.

If you meet the aforementioned requirements, you must make your downsizer contribution within 90 days of receiving the proceeds of the sale - usually the date of settlement. Additionally, you will need to provide your super fund with the downsizer contribution form either before or at the time of making your contribution.

Individuals can make multiple downsizer contributions as long as they do not exceed $300,000 or the total sale proceeds less any other downsizer contributions that have been made by a spouse.

It is important to note that you can only make a downsizer contribution to your super from the sale of a single home. Therefore, if you sell another home in the future and you have previously used the downsizer contribution, you will no longer be able to access this measure.

The downsizer measure is available for those with a total super balance greater than $1.6 million. It will not affect your total super balance until your total super balance is recalculated to include all your contributions, including your downsizer contributions, on 30 June (at the end of the financial year).

Cautions

- The measure will, however, count towards your transfer balance cap - set at $1.6 million.

This cap affects you when you move your superannuation into the retirement phase.

- The downsizer contribution will also be considered for determining eligibility for the age pension.
- If you cannot make your contribution within 90 days of settlement due to factors outside of your control, you will need to apply for an extension of time with the ATO.
- Contributions that are incorrectly declared eligible may be subject to false and misleading penalties.

Before making a downsizer contribution, ensure you meet the eligibility requirements, check that your super fund accepts downsizer contributions and that the contribution will not conflict with your future retirement plan, i.e., exceed the transfer balance cap or affect your eligibility for the age pension assets test.

Accessing the First Home Super Saver Scheme

From 1 July 2018, eligible individuals can apply to release their voluntary super contributions and associated earnings to purchase their first home under the First Home Super Saver (FHSS) Scheme.

The FHSS Scheme was introduced in the 2017-18 Federal Budget and allowed individuals to make voluntary concessional and non-concessional contributions to their super to save for their first home from 1 July 2017.

Voluntary contributions made from 1 July 2017 of up to a maximum of $15,000 from any one financial year, or $30,000 across all years can be applied for release.

Eligible individuals include those who are 18 years and over and:

- have never owned property in Australia or a company title interest in land in Australia (unless the Commissioner determines they have suffered a financial hardship)
- have not previously requested the Commissioner to issue an FHSS release authority in relation to the scheme.

Before deciding to use the Scheme, check that your nominated super fund/s will release the money and ask your fund about any fees, charges and insurance implications that may apply. Individuals should also be aware that receiving FHSS amounts will affect their tax for the year in which the request to release is issued.

Tax deductible super contributions

More taxpayers can now claim a personal super contributions deduction this tax time due to the removal of the 10 per cent maximum earnings condition that came into effect from 1 July 2017.

Eligible individuals include those who earn their income from:

- Salary and wages
- A personal business (self-employment)
- Investments such as interest, dividends, rent and capital gains
- Government pensions or allowances
- Super
- Partnership or trust distributions
- A foreign source

Those who wish to claim a deduction need to:

- Meet the age restrictions and conditions.
- Ensure the contribution is made to a complying super fund or a retirement savings account that is not a Commonwealth public sector super scheme in which they have a defined benefit interest; CPF or other untaxed fund; or a super fund that notified the ATO before the start of the income year that they elected to treat all member contributions to the super fund as non-deductible, or the defined benefit interest within the fund as non-deductible.
- Make personal after-tax super contributions directly to their super fund before 30 June 2018, if they have not already contributed this financial year.
- Provide their fund with a 'notice of intent to claim or vary a deduction for personal super contributions.'
- Obtain acknowledgement from their fund of their notice of intent before their 2018 tax return can be lodged.

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