

>> PIS Tech Update 52

Professional Investment
Services Group of
Companies

8th April 2008

SUMMARY

- The ATO has issued clarification of their interpretation of the borrowing rules for super funds.

SMSFs and Borrowings

On Friday 4th April 2008, the Australian Taxation Office (ATO) issued a Taxpayer Alert (TA 2008/5) and a Q & A covering the use of installment warrants by SMSFs. The industry has been awaiting clarification of the ATO's position.

The key issues that arise from the ATO's releases include:

- The use of traditional style (tradeable) installment warrants issued over direct shares are deemed not to breach the borrowing restrictions as prescribed in SISA;
- An installment warrant type structure can be used to "wrap" around other assets the trustees of a SMSF are otherwise able to acquire, provided the conditions imposed by SISA sec 67(4A) are complied with;
- The law does not preclude a trustee from obtaining borrowings from a related party to the fund however a commercial rate of interest should apply. The ATO has interpreted an interest rate of zero or less than market rate as a potential attempt to circumvent the contribution caps, whilst an excessive interest rate may raise concerns about potential breaches of the sole purpose test.
- Where a lender requires a personal guarantee from the trustees, in addition to limited recourse against the underlying asset, the loan arrangement may not meet the requirements of sec 67(4A)(d) (i.e. the limited recourse nature of the loan).
- An official position is still to be determined by the ATO in relation to a number of key issues including:
 - Personal guarantees by a member or related party,
 - Re-financing,
 - Capitalisation of interest,
 - Multiple drawdowns from a single loan facility,

We expect to see further clarification of these and other issues.

A copy of the Taxpayer Alert and Q&A can be accessed via the following links. We urge authorised representatives and accountants engaged in providing advice to SMSF clients in relation to borrowings to familiarise themselves with the content of the ATO's releases.

Taxpayer Alert:

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

Q & A:

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

Whilst the ATO has now provided some guidance in relation to their interpretation of the application of the "installment warrant" exemption, we understand that this remains on the agenda as part of the review of SMSFs currently being conducted by the Minister for Superannuation and Corporate Law, Senator Nick Sherry.



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Professional Investment Services recognises there is an opportunity for SMSFs to engage in borrowings for the purpose of acquiring an asset, however when framing their advice, authorised representatives must consider all the risks associated with a geared investment strategy. In all cases where advice is being provided to a trustee of a SMSF that involves borrowings, a copy of the SoA must be submitted to PIS (to the attention of Peter Kelly) for review prior to being given to the client.

Any enquiries regarding the Tech Update should be directed to Peter Kelly at Head Office.

Regards

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