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SMSF STRATEGIES SPECIALIST SMSF ADVISER TRAINING

Module 9 – SMSF Investment Strategies, Lending by SMSFs
and In-House Assets

MODULE 9 OVERVIEW

- ❖ Investment Strategy S52(2)(F)
- ❖ In-house Assets S84
- ❖ Ungeared Trust
- ❖ S65(1) SISA 1993
- ❖ Lending \$ to Related Parties
- ❖ Limited Recourse Borrowing Arrangements
- ❖ PCG 2016/5



PREVIEW OF MODULE 9

QUIZ QUESTIONS (MULTIPLE CHOICE ANSWERS)

- ❖ What section of SIS deals with investment strategies in a superannuation fund?
- ❖ If a financial planner recommends an investment that breaches the fund's investment strategy then ...
- ❖ Section 65(1) of the SIS Act 1993 allows ...
- ❖ The Trustee of a SMSF has a holiday vacation home let on short term rentals. During December they have three days free and stay in the home to repair and relax. The home is worth \$400,000. The fund has no in-house assets. The result?
- ❖ Which of the following is not an in-house asset?

INVESTMENT STRATEGY S52(2)(F)

- A compulsory and vital document
- Describes Asset Classes based on risk profile of the members
- Issues to consider
 - Liquidity
 - Risk
 - Return
 - Gearing
 - Diversification
 - Insurance



CONSEQUENCES OF IGNORING THE INVESTMENT STRATEGY

- What are the consequences if an adviser recommends an investment that breaches the investment strategy?
- Members of the fund can sue the adviser for any losses that result





IN-HOUSE ASSETS S83

- In-house assets rule: < 5% of your fund
- An in-house asset is any of the following:
 - a loan to, or an investment in, a related party of your fund
 - an investment in a related trust
 - an asset of your fund that is leased to a related party.
- Exceptions, include:
 - business real property that is leased between your fund and a related party of your fund
 - some investments in related non-g geared trusts or companies

Discussion:

- 2 members have an SMSF
- Fund owns machinery that is leased to a member but only 4% of the total fund
- One member retires and takes a lump sum
- That member had 75% of the fund!
- SISA s84 – Trustees **MUST** comply

GROUP CASE STUDY

James has found the perfect holiday house and wants to buy it inside his SMSF. He will stay there during the holidays and otherwise rent it out casually. It's really his house, so he won't pay rent.

1. Can he buy it?
2. Can he stay there?
3. What if he pays rent?
4. What if he does some maintenance while he and his family stay there?

GROUP CASE STUDY

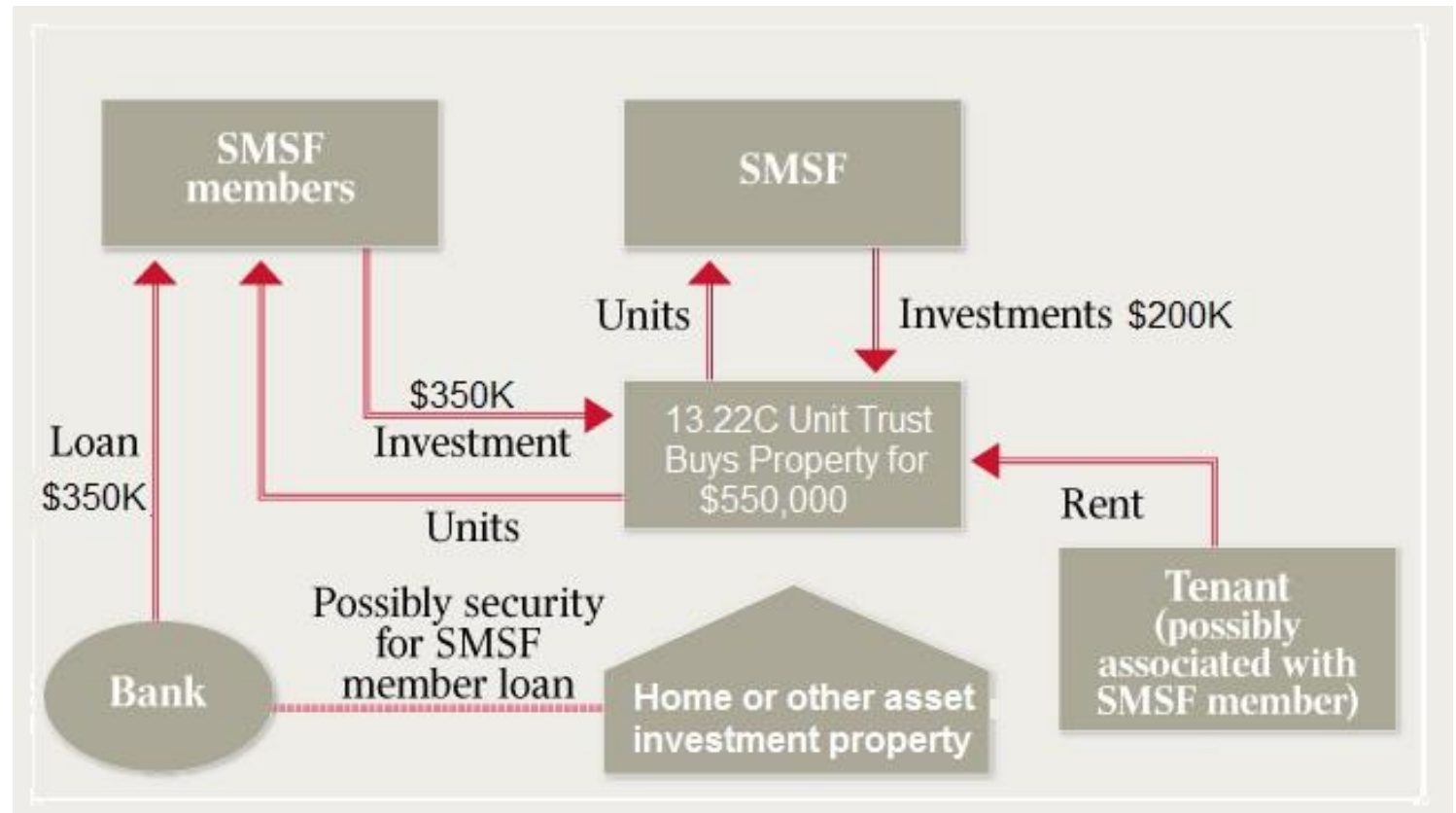
James has found the perfect holiday house and wants to buy it inside his SMSF. He will stay there during the holidays and otherwise rent it out casually. It's really his house, so he won't pay rent.

1. **Can he buy it?** *Yes, but check the trust deed, investment strategy*
2. **Can he stay there?** *Present personal benefit – clear breach*
3. **What if he pays rent?** *In-house asset for the period, breaches rule if > 5% of fund value (example taken from Explanatory Memorandum)*
4. **What if he does some maintenance while he and his family stay there?** *Incidental use (SMSFR2010/1); but personal use by other family members may still put the fund into breach*



REG 13.22C UNGEARED TRUSTS

- A related trust that meets the conditions of SIS Reg 13.22C is not an in house asset.
- Investment goal: transfer of ownership to SMSF over time





LENDING TO RELATED PARTIES

SUPERANNUATION INDUSTRY (SUPERVISION) ACT 1993

(S 65) Lending to members of regulated superannuation fund prohibited

Prohibition

(1) A trustee or an investment manager of a regulated superannuation fund must not:

(a) lend money of the fund to:

- (i) a member of the fund; or
- (ii) a relative of a member of the fund; or

(b) give any other financial assistance using the resources of the fund to:

- (i) a member of the fund; or
- (ii) a relative of a member of the fund.

- Trustees of SMSFs **cannot** lend money to members of the SMSF or their relatives.
- Trustees **can** lend to related parties of the SMSF e.g., family trust.
- SIS Act limits investments in 'in-house' assets (includes loans to related parties) to 5% of the fund.
- Have to observe sole purpose test: adequate security, commercial terms.



PCG 2016/5 – SAFE HARBOUR

A trustee can ignore the safe harbour provisions & argue that the terms of a related party loan are on a Commercial footing.

- Loan Agreement
- Interest Rate (5.75% or 7.75%)
- Interest Terms
- Loan Term (15 years)
- Loan Repayments (No I/O)
- LVR (70%)
- Security (Register Mge)
- 2015/16 – Catch up

- What about non-real estate or listed share investments?

LIMITED RECOURSE BORROWING ARRANGEMENTS

Most common form of investment inside an SMSF for **accountants** is **purchasing property**



Starting Point: Deed and Investment Strategy

- Property is owned by a Custodian
- Loan is made to the SMSF
- Rent paid to SMSF
- Expenses paid by SMSF
- A Custodian can only have one obligation
- Once loan is repaid then the property transfers from Custodian to the SMSF
- Can this loan be refinanced?

LRBA

Residential

- Appn Fee: \$500
- Valn: \$330
- Vetting Trust Deed: \$1500
- Rates – 3 yrs fixed: 4.29%
var: 5.18%
- Annual Fee/Monthly Fee: Rare
- No Broker Fee = additional 1%

Commercial

- Appn Fee: 1.5%
- Broker Fee: 1%
- Valn: \$1500
- Vetting Trust Deed: \$1300 - \$2500
- Rates: Varies widely – next slide
- Monthly/Qrtly Fee: \$187.50

ALWAYS SOMETHING NEW

Product	Post Settlement Capital Requirements	Property Age	Max Amount	Max LVR	Rates From
SMSF Residential	<60 y.o - 20% of original Superannuation Amount outside the SMSF	<2 years old OK	\$1,000,000	80%	5.49%*
SMSF Residential	>60 y.o - 40% original Superannuation Amount outside the SMSF	< 2years old OK	\$1,000,000	65%	5.49%*
SMSF Residential	Nil	➤ 2 years old	\$1,000,000	70%	5.6%*

SMSF Residential	>55-59+ y.o – independent financial advisors certificate to confirm that a SMSF investment suits your clients requirements	➤ 2 years old	\$1,000,000	70%	5.6%*
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QUIZ TIME

- Go online
- Take the Module 9 Assessment
- Ask us if you have any queries
- You will have TWO opportunities to take the quiz

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LRBAS & PENSION – CASE STUDY50

- Facts

James (50) pre 1/7/60 (55 Pres Age)

\$250,000 balance

Earns \$100k with \$12k going to super

Rolls into SMSF and buys property

PP - \$475k + \$25k costs

I/O Loan at 5.7%

Rental yield 3% Mment costs \$3500

Depn: \$40k at 20% & \$235k at 2.5%

Age	50	55	60
Rental Income	14250	15750	17250
Running Costs	-3500	-4500	-5000
Capital allowances	-13875	-8496	-6734
Interest expense	-14250	-13132	-11497
Net property tax income	-17375	-10378	-5981
Other Fund income			
Contributions	12000	12000	12000
Admin Costs	-5000	-5000	-5000
Net taxable income	-10375	-3378	1019
CFWD tax loss		-36656	-46165
Taxable income	-3375	-33034	-38146
Tax 15%	na	na	na
Net Cash flow	3500	5118	7753
Members balance less LRBA	228500	294612	373290
Min pension reqd		11784	14932
Cash flow shortfall		6666	7179

LRBAS & PENSION – CASE STUDY50

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GET THEM OUT OF THE MESS

Group Activity

Spend 5 minutes to outline the possible strategies to get the SMSF into a position where it can pay the pensions.

POSSIBILITIES

- Increase concessional contributions add \$23,000
- Make non-concessional contributions
- Make non-concessional contributions and pay down the debt
- Add other members
- Sell the property: hmm the issues here

- Conclusion – careful planning & implementation to ensure retirement strategies can be implemented

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