


# ***TA 2008/5 - Certain borrowings by self managed superannuation funds***

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# Taxpayer Alert

**TA 2008/5**

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**FOI status: may be released**

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*Taxpayer Alerts are intended to be an "early warning" of significant new and emerging tax planning issues or arrangements that the ATO has under risk assessment.*

*Taxpayer Alerts will provide information that is in the interests of an open tax administration to taxpayers. Taxpayer Alerts are written principally for taxpayers and their advisers and they also serve to inform ATO officers of new and emerging tax planning issues. Not all potential tax planning issues that the ATO has under risk assessment will be the subject of a Taxpayer Alert, and some arrangements that are the subject of a Taxpayer Alert may on further examination be found not to be of concern to the ATO.*

*Taxpayer Alerts will give the title of the issue (which may be a scheme, arrangement or particular transaction), briefly describe the issue and will highlight the features which the ATO considers give rise to taxation and superannuation regulatory issues. These issues will generally require more detailed analysis to provide an ATO view to taxpayers.*

*The developers and marketers of an arrangement which is the subject of a Taxpayer Alert should provide the full facts of the arrangement to the ATO to enable the ATO to finalise its view.*

*Taxpayers who have entered into or are contemplating entering into an arrangement similar to that described in this Taxpayer Alert might obtain their own advice or contact the ATO to seek guidance in relation to the superannuation regulatory issues covered in the Alert.*

*This Taxpayer Alert is issued under the authority of the Commissioner*

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## **TITLE: Certain borrowings by self managed superannuation funds**

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This Taxpayer Alert is concerned with arrangements under which the trustee of a self managed superannuation fund (SMSF) enters into certain limited-recourse borrowings, which may not meet the conditions in subsection 67(4A) and/or breach other provisions of the *Superannuation Industry (Supervision) Act 1993* (SIS Act), as well as related superannuation rules.

This Taxpayer Alert does not deal with taxation issues other than those relating to the application of the superannuation law.

## DESCRIPTION

The Alert applies to arrangements which have the following features:

1. The trustee of the SMSF ("the trustee") borrows money to acquire an asset.
2. The asset acquired (or any replacement asset) is held on trust so that the trustee acquires a beneficial interest in it.
3. The legal interest in the asset (or any replacement) is held by the trust as security for the borrowed money.
4. The trustee has the right to acquire legal ownership of the asset (or any replacement) by making one or more payments after acquiring the beneficial interest.
5. The borrowing is of a limited-recourse nature, noting particularly that any recourse that the lender has under the arrangement against the trustee must be limited to rights relating to the asset acquired (or any replacement). In other words, the lender is able to recover monies where there is a default on the borrowing by repossessing or disposing of the asset acquired (or any replacement), but cannot recover such monies through recourse to the SMSF's other assets.
6. The arrangement has one or more of the following features:
  - (a) The interest rate for the borrowing is zero or less than a commercial rate, particularly where the lender is a related party;
  - (b) The interest rate for the borrowing exceeds a commercial rate, particularly where the lender is a related party;
  - (c) Interest on the borrowing is able to be capitalised;
  - (d) 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;
  - (e) The asset acquired (or any replacement) is one that a trustee is prohibited from acquiring under the SIS Act or any other law, or under the SMSF's governing rules (for example, acquiring residential property, which is not business real property, from a related party).

## FEATURES WHICH CONCERN US

The Tax Office considers that arrangements which exhibit one or more of the features outlined in paragraph 6 above may give rise to taxation and superannuation regulatory issues, including whether:

1. monies advanced by a member or related party at zero or less than a commercial rate of interest could be characterised as a contribution to the SMSF. This may result in the trustee/member having to pay excess non-concessional contributions tax under Division 292 of the *Income Tax Assessment Act 1997*;
2. monies advanced by a member or related party at greater than a commercial interest rate of interest may result in:
  - a) a breach of the sole purpose test outlined in section 62 of the SIS Act, on the basis that the excessive interest rate may mean that the SMSF is not being maintained solely for the purpose of providing superannuation benefits, and/or
  - b) the trustee breaching paragraph 65(1)(b) of the SIS Act, which prohibits the trustee from giving financial assistance to a member of the SMSF or to a relative of such a member using the resources of the SMSF;

3. interest capitalised may result in the arrangement failing to meet the requirement that the money borrowed is or has been applied for the acquisition of an asset under paragraph 67(4A)(a) of the SIS Act;
4. a personal guarantee of the type outlined in paragraph 6 (d) above may result in recourse being made to the assets of the SMSF other than the asset acquired (or any replacement) in the event that the guarantee is enforced against the trustee as the principal debtor, contrary to the intent that the exception in subsection 67(4A) of the SIS Act only applies to limited recourse borrowings; and
5. an asset of the type outlined in paragraph 6 (e) may result in breaches of the SIS Act or SIS Regulations (for example, intentionally acquiring an asset from a related party, which breaches subsection 66(1) of the SIS Act).

Trustees are also reminded that existing fund assets cannot be placed into a limited recourse borrowing without breaching the SIS regulatory requirements.

*The Australian Taxation Office is examining these arrangements.*

For further information on the Tax Office's current views regarding the exception provided to certain limited-recourse borrowings under subsection 67(4A) of the SIS Act refer to *Instalment warrants and super funds – questions and answers*.

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**Subject References:**

self managed superannuation fund  
sole purpose  
personal guarantees  
limited recourse borrowings  
financial assistance  
borrowing  
instalment warrants

**Legislative References:**

*Superannuation Industry (Supervision) Act 1993*  
*Superannuation Industry (Supervision) Regulations 1994*  
*Income Tax Assessment Act 1997*

**Related Taxpayer Alerts:**

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