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Manager

Melbourne Unit

Retirement Income Policy Division

The Treasurer

Langton Crescent

**PARKES ACT 2600**

Via email: superannuation@treasury.gov.au

CC: SMSF Association - trustees@smsfassociation.com

Dear Sir/Madam,

# SUBMISSION – SUPERANNUATION – INTEGRITY OF LIMITED RECOURSE

# BORROWING ARRANGEMENTS

We provide this submission in response to the recently released Treasury Laws Amendment (2017 Measures No. 2) Bill 2017: Limited Recourse Borrowing Arrangements (“LRBAs”).

We note, significant concern remains about the draft legislation, despite the subsequent recent inclusion of small amendments. The slight change that has been made is that this new LRBA treatment only apply to LRBAs entered into after the amended legislation receives royal assent.

Although this is of course welcome (and logical) – unfortunately the reality is that it will be extremely difficult for future LRBAs to be paid off.



By way of demonstration/example, we provide the following Case Study: -

|  |  |  |
| --- | --- | --- |
| **Fund Profile** |  |  |
|  |  |  |
| Number of Fund members: |   | 1 |
| Mode: |   | Accumulation |
|  |  |  |
| **Fund Asset Profile** |  |  |
| Cash  |  | 20,000 |
| Property  | 2,000,000 |  |
|  Limited Recourse Borrowing facility | (1,200,000) |  |
| Net property Asset |  | 800,000 |
|  |  |  |
| **Member's Balance** |  | **820,000** |
|  |  |  |
| **Fund Property-related inflows & outgoings** |  |
|  |  |  |
| Gross annual rent received @ 7% | 140,000 |  |
| Concessional contributions made by member | 25,000 | 165,000 |
|  |  |  |
| Yearly interest on loan @ 6.2% |   | (74,400) |
|  |  | 90,600 |
|  |  |  |
| Rates | (2,500) |  |
| Insurance | (1,000) |  |
| Repairs | (1,500) |  |
| Water | (500) |  |
| Administration | (4,000) | (9,500) |
|  |  | 81,100 |
|  |  |  |
| Contributions & Income Tax |  | (12,165) |
|  |  |  |
| **Net Cashflow**  |  | **68,935** |

As per the above case study, the existing rules define the member’s balance as being $820,000 and therefore, (easily) passing the $1.6m total balance cap test and hence, the member is able to make non-concessional contributions to assist in paying down the LRBA principal.

However, under the proposed Bill - the members balance is now deemed to be $2,020,000 (i.e. the gross value of the property + the cash component … despite the fact that on any measure, the net asset position of the fund is still only $820,000) and therefore will now breach the $1.6m balance cap test.  The important flow–on effect of this new deemed fund balance is of course that the member will no longer be able to make non-concessional contributions to assist in paying down the LRBA principal.

The Bill manifestly restricts the ability of the member to ever repay the LRBA principal.  Given the LRBA term is generally 10 years in duration, we ask the legislature as to how they propose the member repay the LRBA principal upon maturation of the term?  Moreover, this Bill also makes the LRBA strategy one that is both commercially unwise and legislatively unworkable for those member(s) potentially looking to utilise permitted bank finance to facilitate the acquisition of appropriate assets – investments which are intended to perform well enough over time to increase the value of the SMSF in order to self-fund the eventual retirement of the member.

Hence, it is our recommendation that the Treasury Laws Amendment (2017 Measures No. 2) Bill 2017: Limited Recourse Borrowing Arrangements be withdrawn immediately until such time as the legislature contemplates the above very real-world impacts of the proposed legislation.

We also note that the introduction of the $1.6M cap in relation to pension streams is acknowledged and it is a policy measure that future retirees will become accustomed to. However, to hamper legitimate investment strategies and to restrict finance arrangements is extremely harsh, and we hope was unintended.

Please contact either myself or Mr Sanyin Geljic directly should you wish us to speak further to our submission.

Yours sincerely,

# KOUSTAS & CO PTY LTD

**HERC KOUSTAS DIRECTOR**