



MONEY DUE REWARDS:



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Super Fund Borrowing – Possible but not Easy

Earlier this year, some people in the finance industry were very excited about the possibility of self-managed super funds borrowing to invest. For those in the occupation of writing loans, it seemed like a great new source of new business, and as a result many articles were written and a number of new products were developed and marketed. The borrowing strategy had become legally possible in 2007, and the future seemed bright.

I think it is now fair to say that events have overtaken us, and we have seen the world's economic troubles multiply. As a consequence "debt" has become a little bit of a dirty word – at least where the level is high compared with the available assets. In the new environment, the very idea that superannuation could have some level of debt seems slightly alarming to many, and it has probably only been the brave and the foolish who have taken this course so far.

Nevertheless, the practice of borrowing within a self-managed superannuation fund does remain legal, provided the various legislative requirements are met. We should therefore give it due consideration. There are undoubtedly still some situations where it remains a good idea.

When entering into this kind of arrangement, the best course of action really depends on what the underlying asset is that you want to invest in. For shares, probably the most straightforward way is to purchase individual instalment warrants for each share that you wish to invest in on a geared basis. Instalment warrants are well established products with a debt component "built in", and which are available for investing in shares from a wide range of blue chip Australian companies. They are issued by a number of well known institutions, including Macquarie, UBS and Citigroup, and trade daily on the Australian Securities Exchange (ASX). When the Australian market begins to recover, they may actually be a good investment – at least during the "upward" portion of the investment cycle .

If you wish to invest in geared property, this can be a little more tricky. One way to arrange this is by having the super fund borrow directly from a bank or financier. A related complication is that the Australian Taxation Office (ATO) position does not allow the lender to take guarantees or security from a member of the fund – whereas the lender will generally require it. If a lender can be persuaded not to require the additional security, this may well involve a significantly higher interest rate being applied – and may detract from the commercial attractiveness of the arrangement.

Another possible complication is that the legal department of the lender may have very specific requirements in regard to the documentation of the arrangement. Another is that the documentation has to be very carefully crafted to avoid a second liability for stamp duty arising when the loan is finally paid out. These sorts of issues can easily create a sizeable legal bill.

If you have a property (e.g. your main residence) which is largely unencumbered, one way of avoiding some of the complications is to draw down your home loan, and then on-lend the cash to the super fund. While there are still some fairly stringent legal requirements to be met, this will at least give you an affordable interest rate as well as solving some of the hard issues concerning the lender's security requirements.

All told, geared property investment using a self-managed super fund remains complicated and difficult. Nevertheless, there are some situations, particularly when investing in business properties, where the benefits will outweigh these pitfalls. Speak to your professional advisor if you need further information.

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