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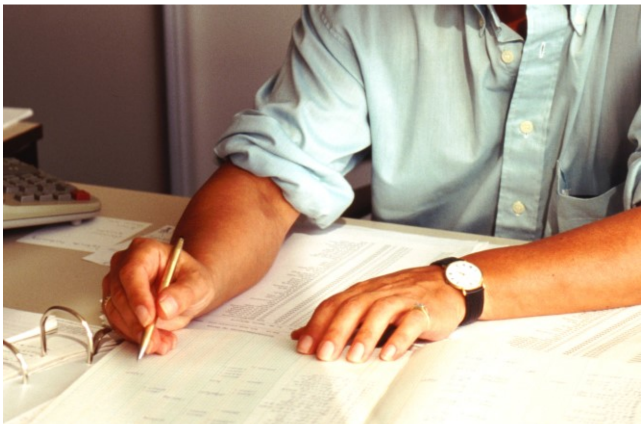

Treasury amends LRBA requirements for SMSFs – again

As if the new transfer balance cap rules were not complicated enough, the government has passed legislation that complicates it further where an SMSF starts a limited recourse borrowing arrangement (LRBA) from 1 July 2017.

Treasury was concerned that some trustees would try to get around the $1.6 million transfer balance cap (TBC) through the ingenious use of an LRBA. Thankfully the new rules do not affect LRBAs entered into before that date.

There was concern raised by some that the new rules would apply to refinancing existing loans, however guidance from the ATO makes it clear the new rules do not apply to existing loans that are refinanced or to contracts entered into before 1 July 2017 but not finalised until on or after that date.

New rules in plain English

What the new rules do in effect is ensure that a particular member of a fund is not able to manipulate arrangements to get around the TBC. The changes guarantee that the TBC rules apply appropriately where there is a repayment of an LRBA that transfers value from accumulation interests into retirement phase interests. It does this by creating an additional transfer balance credit. The credit is the amount equal to the increase in the value of a particular member's retirement phase superannuation interests that they receive. These rules only apply to SMSFs and complying superannuation funds with less than five members.

The particular member will receive a transfer balance credit when the superannuation provider (the SMSF) transfers a payment in regard to an LRBA that creates an increase in the value of the superannuation interest that is supporting the income stream they are receiving in retirement phase.

The timing of the credit arises at the time that the payment is made, however, the amount of the credit is only the amount by which the superannuation income stream has increased in value. The reason for this is to ensure that a member's transfer balance account reflects shifts of value between a fund's retirement phase and accumulation assets. This is no different to the way a transfer from an accumulation phase is dealt with at the time that a superannuation income stream is created.

Any repayment amount of an LRBA has the effect of increasing the value of the underlying superannuation interest. For this reason, where the repayment of the LRBA is sourced from the same assets that support the particular superannuation interest, it does not change the overall value of the superannuation interest because the reduction in the LRBA liability is offset by a corresponding reduction in cash. This, therefore, does not create a transfer balance credit. It is only when part or all of the income paying off the LRBA comes from an accumulation interest also held by the member that the credit applies.

What about excess transfer balance?

It is clear from the new rules that this new form of transfer balance credit may cause a member to also have excess transfer balance. If this is the case, the member can roll back an amount equal to the credit through a commutation or partial commutation of the superannuation income stream. This commutation of the income stream will allow the member to have a transfer balance debit. When this causes a commutation of the superannuation income stream this does not necessitate any changes to the underlying assets in the fund. However, the fund's access to the various earnings tax exemptions may be affected by doing so.

TBC credit transactions

There is a real concern the new rules will create a reporting nightmare. The problem is that every repayment will cause a TBC credit transaction to arise. Since every new TBC credit transaction must be reported to the ATO, this could create the situation of a large amount of reporting, which would be a nuisance to both the fund administrators and the ATO. This would also seem to go against the intent of the legislation.

For example if the fund made fortnightly payments to pay off the LRBA and part of that repayment comes from accumulation interest, then the fund must report to the ATO every fortnight.

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LRBAs proposed to count towards total superannuation balance

The original proposal was for LRBAs to count towards the "total superannuation balance" so that it was increased by the amount of the asset that supports one or more of their superannuation interests that are subject to an LRBA. It was proposed that the amount by which an individual's total superannuation balance is increased is equal to a proportion of the outstanding balance of the LRBA.

The concern was that by including the LRBA in the total superannuation balance, it would in effect make LRBAs pointless for the majority of those that wanted to use them. SMSF advisers lobbied the government hard to change its mind, and at least for the moment this proposal has not been progressed.

Conclusion

If you currently have an LRBA in place, rest easy. The government has made it clear that the new rules do not apply if you are refinancing an existing LRBA.

Contact us to get a full understanding of how these new rules apply and whether or not you need to be concerned by them. The simplest way to avoid the new rules is to ensure that any LRBA asset transferred to the assets underlying a superannuation pension are paid off from either or both of the income from the LRBA asset and cash in the superannuation pension, not from an accumulation asset