



CHRIS GABRIEL OUTLINES REGULATORY CHANGES THAT NOW ALLOW SELF-MANAGED SUPERANNUATION FUNDS TO BORROW FOR REAL ESTATE.

The History of Installment Warrants.

Installment warrants have been used for many years for the acquisition of publicly listed shares. The warrants are listed separately on the Stock Exchange.

Under a warrant, the applicant pays an initial deposit for a particular listed security with an obligation to pay the balance of the purchase price by installments at a future dates and at a pre-determined amount. The shares are held by the grantor of the warrant as trustee for the applicant. The unpaid amount of the purchase price is treated as a loan and interest is paid by the applicant and the applicant receives the full dividend declared on the security.

Should the market value of the listed share fall below the agreed purchase price, the applicant can terminate the warrant and the grantor may sell the shares to repay the loan, however, there is no right of recourse against the applicant for any loss sustained by the grantor of the warrant.

The position of installment warrants was questioned as far back as the 1990's when the Commonwealth Bank and Telstra were floated by way of installment warrants. Under the SIS Act, superannuation funds are unable to borrow; the question then arose as to whether a warrant was a "borrowing".

In 2002 APRA and the ATO put out a statement saying that installments were not borrowings.

The Current Position.

After the Government's review of installment warrants, last September, Section 67 (4A) of the SIS Act was amended to allow warrant style borrowings but the amendments were not restricted to the purchase of publicly listed shares, thus opening the door for borrowing (or gearing) for SMSF's for other assets including real estate.

It is not known whether legislative drafting was intentionally broad or whether it was an unintended consequence of the legislator.

In any event, there are currently many promoters and financiers offering specialized loans to accommodate the new regime.

The following conditions apply to SMSF borrowing:

- Recourse of the lender against the SMSF is limited to the asset itself;
- The asset is an asset the SMSF could otherwise legally acquire (if it had the funds);
- The assets is held on trust for the SMSF;
- The SMSF acquires a beneficial interest in the asset from the outset, and
- The SMSF has the right to acquire legal title on making one or more payments.

Can Superannuation Funds Now Borrow?



Benefits of Gearing.

We believe that gearing through a superannuation fund is not for everyone, however, we can see situations where the ability to use the value of the asset may give the opportunity to purchase, say, a factory or business premise for the employers use that would otherwise be lost because of the lack of other equity.

Interestingly, the current ability of a SMSF to borrow revives the gearing possibilities available prior to May, 1998.

Trustee Considerations.

The fund's trust deed must allow the fund to borrow, otherwise the deed would need to be professionally amended.

The investment strategy should cover gearing.

The loan structure should be reviewed by your legal advisors to ensure the structure complies with the SIS rules and provides appropriate choice of trustee, property managers, management fees etc.

Whilst the lender has no recourse against the SMSF, the lender may require personal guarantees to be provided by the trustees. Advice needs to be considered in this situation.

Will it last?

We believe that the Government was lobbied in 1998 by the major superannuation fund managers before the borrowing prohibition was introduced.

Currently, there is a frenzy of activity of promoters of loan products offering gearing to SMSF's. This activity must be attracting the attention of the Government and the major fund managers.

If the breath of the amendments was not intended, then there may be future restrictions, however, if there are future restrictions, they are unlikely to be retrospective.

Please contact us should you require detailed advice.

Volatile Share Markets & Tax by Victor Jarmusz

Recently, the Australian share market has experienced a lot of uncertainty. One certainty of life we can control, however, is tax. As a basic **rule of thumb**, in a rising market, you are better off being a **share investor**, and in a falling market, you are better off being a **share trader**.

Share investors are motivated by factors such as **long term growth** and dividends. Losses or gains are capital in nature. Losses are carried forward and can only be used to offset against other capital gains, while gains can be subject to the **50% discount**. Costs of buying and selling (e.g. broker's fees) are **not tax deductible** and are only taken into account when calculating gains and losses.

A **share trader** carries on a **business** of making money from shares, and is usually motivated by **short term profits**. Losses can be used to offset against ordinary taxable income, and gains do not get the 50% discount. Shares held are **trading stock**, and costs of buying and selling shares are **tax deductible**. In certain circumstances, a trader can even claim back GST in brokerage fees.

Let us look at an example.
We have an investor and trader, they both;

- hold \$10,000 in shares at the start of the year,
- sell \$2,000 worth of shares (original cost \$1,500),
- buy another \$5,000 in shares, and
- the remaining shares are worth \$20,000 at the end of the year.

The **investor** will have a **capital gain** of \$250, being \$2,000 received, less \$1,500 cost, less the 50% discount (assuming the shares were held for more than a year). The **trader** will have a **taxable income** of \$7,000, being \$2,000 received, \$10,000 for the rise in stock value, less \$5,000 for the extra purchases. Clearly, in this case, **the investor is better off** (from a tax point of view) in a **rising market**.



Let's use the same facts, except that the share value at the end of the year is \$7,000 instead of \$20,000. The **investor** still has a capital gain \$250. The **trader**, however, will have a **tax loss** of \$6,000, being \$2,000 received, less \$3,000 for the fall in stock value, less \$5,000 for the extra purchases. This loss can be used to offset against other income sources. Clearly, in this case, **the trader is better off** (from a tax point of view) in a **falling market**.

To determine whether someone is a trader instead of an investor, we need to see if a **business is being carried on**. Some factors are;

- A trader will be more systematic, operating to a plan and keeping detailed records
- A trader will generally have a much larger frequency and scale of transactions
- A trader will spend a lot more time on buying and selling than an investor
- The intention is important

The ATO stance with **superannuation funds** is that they are unlikely to be a share trader. This is because superannuation funds have a purpose to provide for the retirement of their members, and accordingly, the trustees would not be engaged in speculative activities.

Overall, it is a question of fact.

Please contact us should you require detailed advice.



Marion to take maternity leave...

Marion Gregorace CA (now Marion Mejias) is expecting twins in mid May. We at Gabriel & Partners are very excited for Marion and her husband, Ric, with the immanent arrival of a "family".

Marion has been with the firm since December, 1999 and plays a very important role at Gabriel & Partners as business services manager being responsible for a large and diverse group of clients.

Marion will take maternity leave from late April until her expected return in early 2009.

Everyone at Gabriel & Partners and all her clients wish Marion & Ric nothing but the best for double parenthood.



A firm providing a high standard of performance and personalised service over a range of specialities.

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The fact that we are required under the Corporations Act 2001 to provide this warning does not in any way affect our ability to provide taxation advice and, in particular, the specific tax advice in this letter.