2017

GUIDE TO SELF-MANGAED SUPER FUND BORROWING

Address
Suite 1, Level 1, 204 Merrylands Road MERRYLANDS NSW 2160
Sekou: 0432 674 668 **Nick**: 0408 617 950 **E**: info@epicpm.com.au

Table of contents

NO ADVICE WARNING 2
Letter from us 3
What is a super fund? 4
Taxation of superannuation 5
What is Self-Managed Superannuation Fund (SMSF)? 5
Why own an asset in super? 6
Case Study 7
Borrowing to invest in super? 8
The required documents 10
The process 11
How we can help? 12
How do you contact us? 12

SEKOU SEASAY: CFP®, CTA® M: 0432 674 668 E: sekou@epicpm.com.au

NICK VOUTOS …M: 0408 617 950 E: nick@epicpm.com.au

NO ADVICE WARNING

The information in this eBook is of a general nature only. This information was prepared without taking into account your personal circumstances and goals. You **should not** rely on or act on information provided in this eBook without seeking advice from a qualified financial planner. Epic Property Partners and related entities will not accept responsibility for any loss suffered as a result of reliance on information contained in this eBook. The information provided does not constitute a Statement of Advice. Specifically, by reading this eBook, you are aware and accept that although reasonable care has been taking in preparing all information provided you should not rely on this information when making a decision to purchase property. In particular:

a) The information contained in this eBook is general in nature and is not intended to be and should not be used as financial advice. You should seek independent financial advice before proceeding with any investment decision.
b) all content, including all information yielded by an investment search, is historic data and is not predictive of future investment performance. Such information does not take into account your personal financial circumstances.
c) By reading this eBook, you acknowledge the terms stated above and that although reasonable care has been taken to ensure the accuracy of data, Epic Property Marketing makes no warranty as to the accuracy of the information displayed and therefore you should not rely on it. You should obtain your own financial and legal advice before making any investment decisions.

SEKOU SEASAY:CFP®, CTA® M: 0432 674 668 E: sekou@epicpm.com.au

NICK VOUTOS …M: 0408 617 950 E: nick@epicpm.com.au

Letter from us

Dear Reader,

We are delighted to provide you with a free copy of this eBook and hope that you will find it very useful.

At Epic Property Marketing, we believe in empowering you with the information you require to make sound and reasonable decisions about your wealth and financial future.

As an investor, the structure you choose to own your investments affects the ongoing income generated by your investment as well as terminal taxes paid through the capital gains taxation system. As a result, superannuation ownership has become an effective way of holding valuable income and growth assets. The interest in superannuation asset ownership and borrowing has, broadly speaking, increased since changes to superannuation laws in September 2007 and subsequent amendment in 2010. This means that, as long as certain conditions are met, superannuation funds can borrow to invest in virtually all asset classes available to individual investors.

This complimentary eBook provides you a basic set of information that you will find helpful as a starting point in exploring this seemingly green and growing area of investment. The guide provides general information about a superannuation fund; the purposes of it, Self-Managed Superannuation Fund (SMSF) and borrowing arrangements. It is not intended to substitute tailored and personalised advice and research. The reader is therefore strongly encouraged to seek professional advice tailored to their situation.

Should you require advice, please contact us. Our in-house Certified Financial Planners™ and Chartered Tax Advisers™ work as a team, to help you optimise your future financial outcomes.

Have a great day and we hope to talk to you soon.

Best regards,

Sekou Seasay (CFP®, CTA®)
Director

Epic Property Marketing

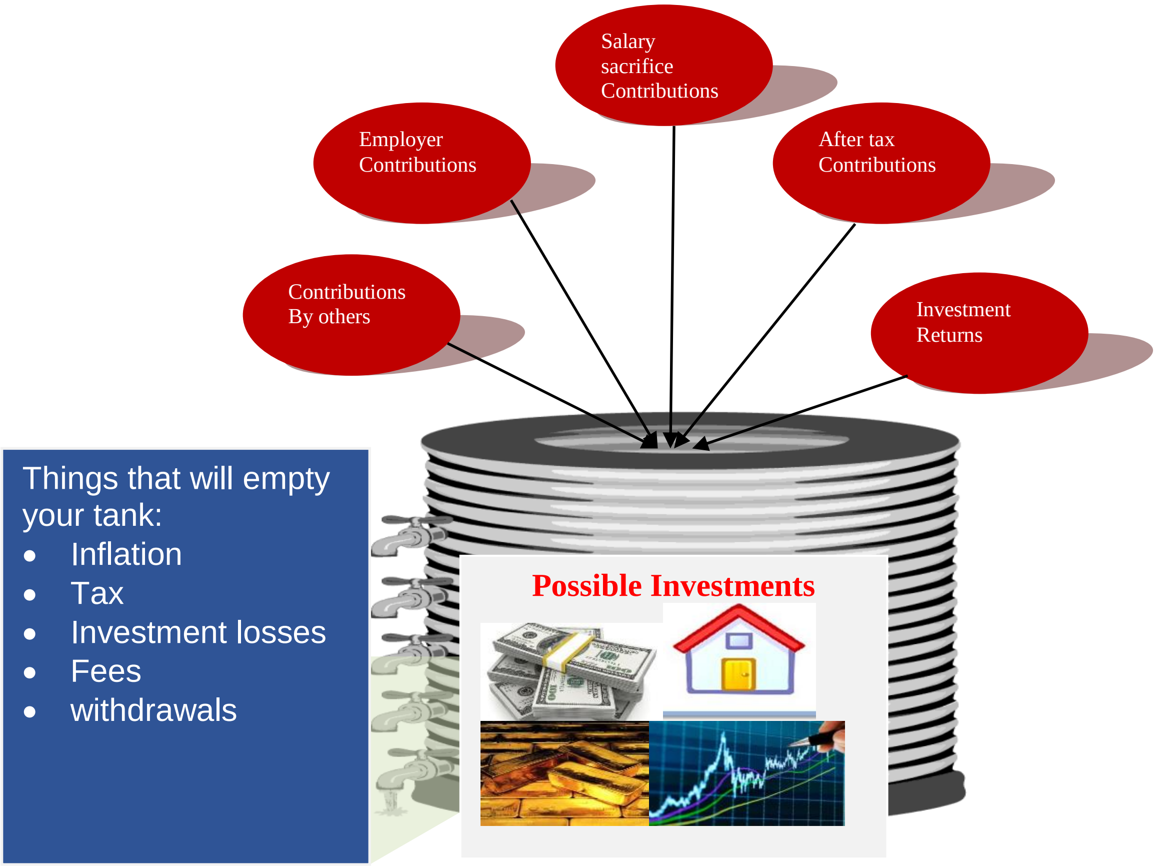
What is a super fund?

Many people think that superannuation (super) is in itself an investment. This is not the case, super is an account into which money can be contributed, and invested on your behalf to fund your retirement and/or provide death and disability benefits to you and your loved ones when you reach retirement age or suffer the unfortunate event of death or disability. As an investor, the best way is to imagine your super as a rain tank. Your challenge is to fill up the tank as much as possible for a “rainy day”; your retirement. Contributions and returns made on them help to fill up your super tank. On the other hand, losses, fees and withdrawals detract from the tank.

Contributions into a superannuation account can come from one of three sources:

- You, the investor,
- Your employer,
- The Australian Taxation Office (e.g super co-contribution), and
- Someone else (e.g your spouse)

The following diagram illustrates the concept.



How your super is invested entirely depends on you, the account owner. Where you fail to make an investment election, the trustee of the fund will decide on your behalf by investing your capital in the fund's default investment strategy, usually a premixed portfolio depending on your age.

It is also important to note that superannuation funds are set up as trusts, wherein someone called the trustee, holds your benefits in trust until you meet a condition of release. With very limited exceptions, you do not meet a condition of release until you retire at your preservation age.

Taxation of superannuation

Taxation laws apply to superannuation funds in as much the same way as they apply to individuals or companies, but at concessional rates. This means that the fund pays tax on its net income after expenses just like individuals. The income of a superannuation fund includes interest income; dividends; distributions from managed investments and rental income if the fund invests in property. However, the definition of the income for super funds is extended to include contributions made to the fund. These contributions, broadly speaking, can come either from a pre-tax source, like those paid by your employer, or an after tax source, like those paid by you from your bank account. If the contributions are funded by pre-tax money, they are referred to as “Concessional Contributions”. On the other hand, if funded by after tax money, they are called “Non Concessional Contributions”.

Concessional contributions pay tax at a maximum rate of 15%. Non concessional contributions by their nature are paid into a super fund after paying a marginal rate of tax at the individual level. Therefore, upon contribution to the fund, they are not subject to the super contributions tax.

What is Self-Managed Superannuation Fund (SMSF)?

In a nutshell, Self-Managed Superannuation Fund (SMSF) is a superannuation fund run by members for their own benefit. As such, it provides members greater control over their retirement savings than any other superannuation funds. A SMSF can invest in any of the following assets as long as allow by the law that governs the SMSF, called the trust deed:

- Bank deposits (savings accounts and term deposits)
- Fixed interests,
- Direct shares
- Managed funds
- Residential property
- Commercial property
- Gold
- Silver
- Collectables.
- Any other assets

The SMSF’s ability to pay retirement benefits, such as pensions and annuities directly from the fund means that the SMSF can be retained well into your retirement. This then provides the flexibility to determine the timing of disposal of growth assets during the pension phase when they are generally **exempt** from CGT provisions upon the members transfer balance cap ($1.6 mil) - a strong tax planning proposition.

Like any other superannuation funds, SMSFs must be established for the sole purpose of providing benefits to fund members on retirement. They must adhere to strict provisions regarding contributions, taxation, benefit payments, annual reporting, compliance regime, etc. Our in house advisers and professional associates are well experienced in all aspects of superannuation including setting up SMSFs and recommending an investment strategy to suite your financial circumstances.

Because the tax rate we pay in Australia is affected by the choice of legal entity chosen to own the income generating asset, superannuation is very attractive as it pays both income and capital gains tax at lower rates.

Why own an asset in super?

It is logical to suppose that every rational investor invests to increase:

- actual net income
- asset; or
- expected income and/or assets

Net income of a taxpayer and therefore, surpluses that can be converted into capital is affected by tax. Because the tax rate we pay in Australia is affected by the choice of legal entity chosen to own the income generating asset, superannuation is very attractive as it pays both income and capital gains tax at lower rates, being 15% and 10%, respectively. This is illustrated in the table below.

Taxable Income	Marginal Tax Rate (includes Medicare levy)	Effective Tax Rate on Capital Gains (Medicare Levy Included)
$18,201 - $37,000	19%	10.5%
$37,000 - $80,000	34%	17%
$80,001 - $180,000	38.50%	19.25%
More than $180,000	46.50%	23.25%
Self-Managed Super Funds		
Accumulation	15%	10%
Pension	Nil (subject to transfer balance cap)	

As evident from the table above, individuals pay tax on income and capital gains at a rate of 46.50% and 23.25%, respectively, as compared to 15% and 10% for superannuation funds.

SEKOU SEASAY:CFP®, CTA® M: 0432 674 668 E: sekou@epicpm.com.au

NICK VOUTOS …M: 0408 617 950 E: nick@epicpm.com.au

We are a one-stop-shop property services entity that can help you to:

- Establish an SMSF
- Source an SMSF loan
- Provide technical guidance over the borrowing process
- Help you source a property
- Deal with the auditing, accounting, and compliance of your SMSF.

Call Us Now On 0343 674 668 Sekou
0408 617 950 Nick
Email: info@epicpm.com.au

Case Study

$480,000 borrowed
To buy $600,000
Property

Super vs. Outside Super
If we assume the following:

- rental yield of 4.5% p.a
- interest rate of 6% p.a
- property management cost of $2,200 per year
- marginal tax rate of 47% p.a (includes Medicare Levy)

Outside Super

Rent		$27,000
Less:		
Interest expenses	$28,800	
Management cost	$2,200	($31,000)
Income Loss		($4,000)

As the tax payer's marginal tax rate is 47%, they will get a tax refund of 0.47
$4,000 = $1,880. This reduces the income loss to $2,120 per year.

Inside Super

Rent		$27,000
Less:		
Interest expenses	$28,800	
Management cost	$2,200	($31,000)
Income Loss		($4,000)

As the tax rate is 15%, the super fund will get a tax refund of 0.15 x $4,000 =
This reduces the income loss to $3,400 per year, which is 60% more than the
the property was held individually.

Now let's assume the property is held and sold after 5 years. Annual growth rate was 4%, over the same period; rent escalation was 3% and a loan balance of $300,000 at 7% interest.

Outside Super

Rent		$31,300
Less:		
Interest expenses	$28,800	
Management cost	$2,200	($31,000)
Net Income		*300*

The tax payer will pay an additional tax of $141 on this amount. If the property was held inside superannuation, the tax payable would be a maximum of $45.

Capital Gains Tax

Total assessable capital gains would be approximately $130,000. As an individual, capital gains tax (CGT) would up maximum of $30,550. If held

From the above analysis, it is evident that superannuation ownership can be an attractive proposition depending on the tax payer's tax status. However, every individual is different. Thus personalised financial as well as tax advice is recommended before this sort of strategy is pursued. Oour resident Certified Financial Planners™ as well as our Chartered Tax Advisers™ are SMSF and taxation experts who can work with you to determine the most suitable strategy.

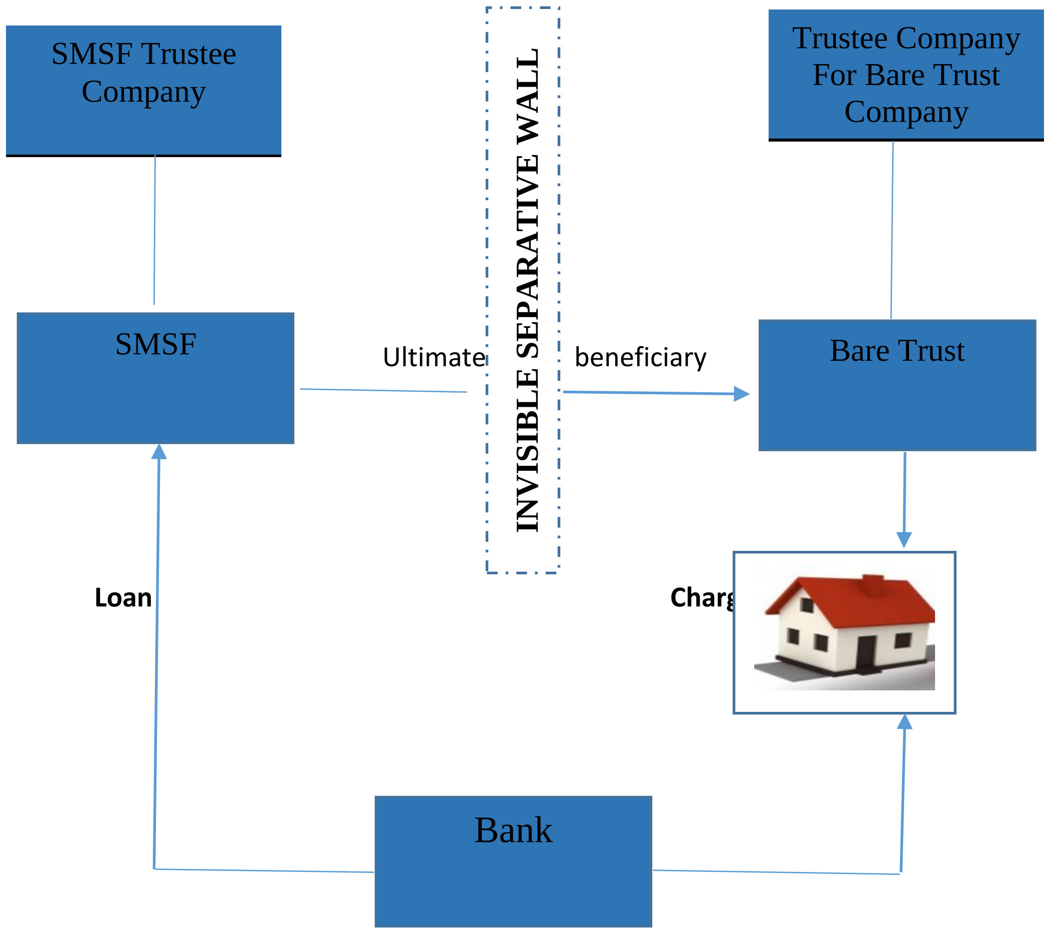
Borrowing to invest in super?

You want to buy a residential property through your proposed SMSF but it will not have enough funds for an outright purchase. It will, however, have enough funds to pay the deposit. One solution is for the SMSF to pay the deposit and borrow funds to pay the balance plus acquisition costs. To execute the transaction, the property must be held in a special type of trust called a custodian or bare trust. The purpose of such a trust is to own property on behalf of the SMSF as long as a loan exists and convey title to the SMSF once the loan is paid off. The lending arrangement is known as a "Limited recourse borrowing arrangement, LRBA". In the event of default, the lender will only have recourse to the property and cannot claim any other SMSF assets. Your SMSF makes the loan repayments; after the loan is repaid, the legal ownership of the property can be transferred to the SMSF.

SEKOU SEASAY: CFP®, CTA® M: 0432 674 668 E: sekou@epicpm.com.au

NICK VOUTOS …M: 0408 617 950 E: nick@epicpm.com.au

A graphical summary is provided below



THIS STRATEGY WORKS BEST IF:

- You have a long term investment timeframe;
- The SMSF members are working or actively making contributions
- You want to invest in a residential property within superannuation;

THE BENEFITS OF THIS STRATEGY

- You can pool together super assets of up to 4 members to increase deposit capital.
- Your SMSF can acquire property through instalments over the long-term.
- SMSF's other assets are secured as the lender does not have recourse to your SMSF's assets.
- Your SMSF receives all income and capital growth of the property during loan term.
- The SMSF will use rent from the property & super contributions to service the loan.
- Interest and other property expense may be claimed as tax deductions by the SMSF.

SEKOU SEASAY:CFP®, CTA® M: 0432 674 668 E: sekou@epicpm.com.au

NICK VOUTOS …M: 0408 617 950 E: nick@epicpm.com.au

- You may eliminate CGT if property is sold in the retirement (income) phase and proceeds do not exceed member's transfer balance cap

SERIOUS ISSUES TO CONSIDER

- Your SMSF trust deed must allow borrowing under an instalment arrangement.
- You must purchase the property from an unrelated party. Arrangements must be at arm's-length and transacted at market rates.
- You should weigh the benefits of the strategy against the costs of setting up and maintaining the instalment arrangement.
- Investment in residential property must be consistent with your SMSF's investment strategy.
- You should consider risk, return, diversification issues as well as loan interest rates.
- The instalment arrangement must meet certain requirements to ensure that the SMSF remains complying.
- As trustee, you must be acting in the best interests of the SMSF beneficiaries and the ability of the SMSF to make the instalments over the term of the loan.
- Cash flow may be sourced from investment earnings or member contributions. Consider limits to contributions that are eligible for concessional tax treatment.

THE IMPORTANCE OF FINANCIAL PLANNING

There are a number of rules and regulations surrounding superannuation and planning for retirement. Our in-house advisers and professional associates can provide advice on borrowing strategies for SMSFs that is personalized to your situation and goals. You should also consider seeking professional tax and legal advice.

THINGS TO CONSIDER

- **Be careful**: Do not rollover your capital to the SMSF before you make adequate provisions to replace your current personal insurance policies.
- **Liquidity**: you should ensure sufficient amount of liquid cash (say $10,000) is maintained in the fund to pay for ongoing fees, tax and rental shortfalls.
- **Deposit**: ensure the fund has enough money to fund deposit, set up costs, stamp duty and all other costs.

THE REQUIRED DOCUMENTS

To implement a Limited Recourse Borrowing Arrangement, you need the following:

1. A financial plan that deals with suitability of the strategy to you as well as the affordability of the strategy from a cash flow perspective. Banks will ordinarily require your planner to sign a form to this effect.
2. A deed giving life to the Self-Managed Super Fund and Custodian/Bare Trust.

3. A trustee structure for your self-managed super fund. Whilst an SMSF can have individual trustees, the custodian trust must always have a corporate trustee.

This means that you will have to pay for the cost of deeds for the SMSF and custodian trust, as well as trustee structures.

THE PROCESS

Steps	What does this entail
Step 1: **Pre-approval**	This is basically where we contact a bank to find out if it can lend money based on facts provided. We believe this should be a first step as setting up SMSF costs money. If the purpose is to borrow and buy property, we do not want you to pay set up costs for the SMSF only to find out that you cannot get the loan. So the remainder of the steps are entirely voided and revisited if you cannot get a loan. For example, we might then look at an alternative strategy using traditional super funds.
Step 2: **Get financial advice**	This will be a personalised financial plan outlining your strategy and how it benefits you.
Step 3: **Set up and execute SMSF**	Establish SMSF and associated structures: • SMSF deed • Bare trust deed • Corporate trustee for SMSF, where applicable • Corporate trustee for custodian trust This is a very involving process which involves signing various pages of the SMSF deed as well as associated minutes, including the ATO's SMSF trustee declaration. We help you with the entire process and let you know where to sign.
Step 4: **Apply for ABN and TFN for super fund**	This may take up to 28 days. We do all this in-house. So you do not have to worry.
Step 5: **Set up your SMSF Cash Account**	We do this for you at no additional cost. We use the Macquarie CMT for this purpose.
Step 6: **Rollover your super benefits**	This involves the rollover and consolidation of all your super benefits into your new SMSF.
Ste 7: **Buy property**	At this stage, you can engage Frontier Direct Property Pty Ltd to help you find an investment grade property. When a property is found, you will have to pay a holding deposit. All funds will be paid from the SMSF's account.
Step 8: **Formal approval**	At this stage, you sign the loan offer documents and return them to the bank for final approval.
Step 9: **Loan settlement**	This involves liaising with your solicitor; we will support you on financial matters in this process.
Step 10: **Stamp Bare Trust**	Once you have settled on a property, you will need to arrange the stamping of the Security Custodian Trust with the State Revenue Office if required. Your solicitor will do this for you.
Step 11:	Throughout the process, we keep records of your SMSF transactions and give you an

SEKOU SEASAY:CFP®, CTA® M: 0432 674 668 E: sekou@epicpm.com.au

NICK VOUTOS …M: 0408 617 950 E: nick@epicpm.com.au

Finalise your SMSF admin	individual login where you can track your balances. However, individual balances are not likely to be fully completed until you have found a property. Once you have settled on a property, we provide you balances of each individual member and give you an online access code where you can monitor your individual super balances.

HOW WE CAN HELP?

At Epic Property Marketing, we can help to:	
• **Explain the SMSF investment and borrowing process**	√
• **Provide you full financial advice regarding an SMSF investment strategy**	√
• **Set up your SMSF**	√
• **Help you execute your SMSF deeds and minutes**	√
• **Source a Limited Recourse Borrowing Loan**	√
• **Help you source an investment grade investment property**	√
• **Administer your SMSF**	√

HOW DO YOU CONTACT US?

At any time where you would like to discuss your situation and how find out how we can help you, please contact us on the following:

Business Address	Suite 1 Level 1, 204 Merrylands Road MERRYLANDS NSW 2160
Phone	02 9897 9711
Mobile	Sekou Seasay: (+61) 432 674 668 Nicolas Voutos: (+61) 0408 617 950
Email	info@epicpm.com.au
Contact Hours	9:00am – 5:00pm (Sydney time)