

TAX TALKS

Australia's Tax News Podcast - The Podcast for Australian Tax Professionals

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LRBA stands for Limited Recourse Borrowing Arrangement. An SMSF can only borrow money through an LRBA.

LRBA

How does an LRBA actually work? In episode 177 we already touched on LRBAs and you sent in a huge amount of questions. So in today's episode Peter Bobbin of [Argyle Lawyers](#) in Sydney will try and give you an answer to 16 of your questions.

Here is what we learned but please listen in as Peter Bobbin explains all this much better than we ever could.

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1 Do most SMSF deeds allow an LRBA?

Yes, they do. Most modern SMSF deeds give the SMSF trustee the power to borrow.

However, if the trust deed is silent on this point, then there is no power to borrow. Under common law, trustees do not have the ability to borrow. It is not that they are restricted or prohibited. The courts just didn't vest trustees with the power to borrow.

So for an SMSF to be able to borrow, the trust deed must specifically give this power to its trustees. So the first thing a lender usually does is to check the deed.

2 Can anybody be an LRBA lender?

Yes, they can. Anybody can be a lender. The lender can be a bank or somebody else like an individual or another SMSF or a family trust. Any legal entity can be a lender.

3 What is a bare trust?

Like any trust, a bare trust has a trustee. And this trustee is usually a company, so a corporate trustee. Some call this corporate trustee a custodian company or a nominee company or a bare trustee company. It all means the same.

By law the asset subject to the loan can't be held within the super trust itself, but must be held in a bare trust. The bare trustee is merely the title holder. Hence the name bare trust.

4 Does the custodian company need a constitution?

No, not necessarily. Either constitution or replaceable rules is fine, since the custodian company is not a special purpose company anyway.

Technically the bare trustee doesn't even need to be a company. But having a corporate trustee keeps clarity and keeps the asset separated from individual interest.

5 Why a bare trust?

Because the legislation says so. It is a specific section of the SIS Act that requires an asset subject to a loan to sit in a separate trust.

6 Who should be shareholders / directors of the bare trustee?

It could be anybody. The most common approach is that the directors of the SMSF will also be the directors of the custodian company. Different to an SMSF there is no requirement that all parties also act as directors or shareholders of the bare trustee company.

7 Who signs the purchase contract?

The contract is in the name of the custodian company. For all jurisdictions other than Queensland you would just identify the custodian company and its name and its name only on the purchase contract.

In Queensland you can identify someone as the holder of the real estate and the capacity in which they are holding it, for example as a trustee.

8 What name for the custodian company?

It can be any name whatsoever. There is no need to specify that this is a bare trustee or nominee company etc

9 What is the timeline?

In Victoria you can re-assign the contract, but in NSW you can't. So in states like NSW you need to have the custodian company in place to sign the purchase contract of the property.

10 What rules apply to the LRBA?

The LRBA needs to comply with the ATO's safe harbour rules if you want to rely on the safe harbour rules. The money for an LRBA often comes out of a bucket company, and then you also need to comply with the Div 7A regulations.

11 Who signs the loan agreement?

The SMSF trustee signs the loan agreement. The bare trustee actually buys the property.

12 Who is actually the borrower?

The borrower is the super fund itself. The super fund trustee will have its name on the loan agreement. The agreement will then refer to the fact that the loan is in respect of the particular property, title of which will go into the bare nominee company name.

For an LRBA you need the purchase contract and the loan agreement. The purchase contract commonly is in the name of the nominee custodian or bare trustee company. And the loan agreement most commonly in the name of the super fund. One or both or maybe a third document will reflect the fact that those particular parties

are working cooperatively. One being the real estate holder and the other being the borrower and that they are working cooperatively under one transaction.

13 Does an LRBA always require a mortgage?

Whether to register a mortgage or not is up to the parties involved, especially the lender. However, to meet the safe harbour rules for an LRBA the lender must register a mortgage.

14 What happens if the SMSF doesn't pay the interest due?

You have a breach. If the lender is a bank, they will take action sooner or later, ranging from additional interest to repossession.

With a non-bank lender who is usually a related party, you very quickly slip into non-arm's length territory. And then you risk the ECPI status of the entire asset.

15 Can the LRBA set a fixed interest rate for 30 years?

If it is a third party lender, the answer is yes. If it is a related party lender, then you need to show that a third party lender would have offered the same terms and conditions.

16 Why are LRBA documents more expensive?

LRBA documents are quite labour intensive. They take time. The devil is in the detail.

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