

Buying Property Through Your SMSF is a Poor Strategy



One of the hottest topics right now is whether self-managed superannuation funds should be allowed to borrow to buy property.

However, it's become rather an academic question- even though the authorities have not ruled it out, any mortgage broker will tell you that in the aftermath of the Hayne royal commission, it is almost impossible for a self-managed super fund (SMSF) to get a loan.

It begs two questions. Do you need a SMSF? And, if you do, is SMSF borrowing for residential real estate a good strategy?

I have long been an opponent of it. Usually, those who do it have been talked into it by property spruikers, or they want to buy an investment property but the only capital available is through their super fund.

In any event, even though conservative borrowing is a great way to build wealth, if the property is negatively geared- as most are- the effectiveness of negative gearing is enhanced by a high marginal tax rate, which produces a large tax refund.

Even if your SMSF could borrow, I suggest it would be a poor strategy to go into negative gearing using a vehicle that pays 15 per cent tax, at most. You would be negating the tax benefits.

Therefore, a sound principle is to refrain from buying property in the name of your super fund. It is better to buy it in your own name, or that of a family trust, and gain the benefits of negative gearing in the names of the taxpayer with the highest marginal tax rate.

Next, let's consider the question of whether you should be running a SMSF at all.

There is no easy answer.

Running your own fund is not as simple as it sounds.

It involves three major jobs: administration (doing the paperwork), investment (deciding where to place the money); and insurance (arranging appropriate cover).

If you can handle these tasks with ease, you are well on your way, but you also need to take into account the assets the fund will hold. If these are not at least \$250,000, the setting up costs and annual expenses of a SMSF are probably not worth the exercise.

Unfortunately, judging by the huge number of queries I receive from SMSF trustees, people are still woefully ignorant of the rules.

As a SMSF is run by related parties, most breaches relate to acquiring assets from members or relatives, buying the wrong assets, getting the fund's money intermingled with personal money and providing financial assistance to members and relatives.

These are serious matters with heavy penalties.

One of the biggest areas of confusion is acquiring assets from a related party. With some specific exceptions, a fund cannot acquire assets from a related party because it could be seen to be enabling member to obtain access to their super funds before they are entitled to do so.

The main exceptions are listed securities from members or their relatives, provided the securities are acquired at market value, and business real property from a related party, again, provided the property is acquired at market value.

Given that much of the work of running the fund will happen after retirement- and probably will be done by one family member- there are two other questions to consider.

First, is this really how you want to spend your retirement? And second, who will run the fund if the person currently doing so dies or becomes incapacitated?

In summary, a SMSF is great for high net-worth individuals who want to run their own race and have the skills to do it.

However, you should not start your own fund just because the share market is down generally and you believe, "I could do better myself."

Taking control of the investment decisions for your life savings is a massive responsibility and making mistakes while learning with your own money could cripple you financially.

If you are not happy with your super, you may be better off to seek another fund with better returns and lower fees, rather than taking over the management yourself.

Article reproduced with the kind permission of Noel Whittaker, columnist for The Sun-Herald

31-03-2019

Noel Whittaker is the author of 'Making Money Made Simple' and numerous other books on personal finance. noel@noelwhittaker.com.au
