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What an SMSF should do after paying out an LRBA loan

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news By Keeli Cambourne 22 January 2024 — 3 minute read

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SMSF trustees have to decide on two key things after completion of repayments on a limited recourse borrowing arrangement, says a leading legal adviser.

Daniel Butler, director of DBA Lawyers, said navigating the transfer of a property from a bare trustee to an SMSF trustee involves careful planning and adherence to the correct steps.

"Careful execution of these steps ensures a smoother transfer and compliance with regulatory obligations," he said.

"Contraventions can give rise to significant penalties, so it is important to seek expert input and plan ahead carefully."

He said after paying out an LRBA trustees have to choose between whether the bare trustee transfers the property back to the SMSF trustee or continues to hold the legal title to the property.

"This decision can result in significant administrative and financial issues," Mr Butler said.

"Firstly, even though the legal title to a property under an LRBA remains in the bare trustee's name, beneficial ownership of the property rests with the bare trustee, otherwise known as a custodian. The SMSF continues to collect any rent and pays for expenses and reflects any net rental income in its tax return each financial year, regardless of the decision made."

Mr Butler said that transferring the legal title to the SMSF trustee can assist SMSF trustees in streamlining their fund's legal framework, especially if they wish to undertake an in-specie payment to a member later by way of transfer of the legal title.

He added if the decision is made to transfer the legal title to the SMSF trustee, adherence to a structured process is essential.

"Furthermore, it is important to document each step as SMSF trustees have the responsibility to retain trustee resolutions for a minimum of 10 years," he added.

There are six key steps to winding up an LRBA loan, with the first and perhaps most imperative being seeking expert advice.

Mr Butler said trustees should seek guidance from both property and SMSF legal advisers because failure to complete requisite steps and documentation may result in additional costs and complications during the transfer and the annual SMSF audit process.

He said there are specific areas where advice is critical including property law advice for potential stamp duty exemptions.

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"These may not be straightforward and vary between states and territories," Mr Butler said.

"If there is no duty concession or the transfer is likely to invoke duty, this may be a reason for the title remaining in the SMSF trustee's name."

Advice should also be sought on the impact of the transfer and documentation requirements, as these factors will depend on the governing rules and the bare trust agreement of the individual fund.

Additionally, there may also be superannuation law considerations to be made and specific documents to be drafted.

The second step to winding up an LRBA is confirming the complete repayment of the loan, and Mr Butler said the SMSF trustee should obtain written confirmation from the lender that the loan has been fully repaid and the mortgage has been discharged.

Step three is transferring the title. The SMSF trustee should initiate the transfer of the title into the SMSF trustee's name according to the laws in the relevant state or territory.

"Given the complexity that can arise in relation to these transfers, we recommend that a property lawyer be engaged in the relevant jurisdiction rather than a conveyancer who may not be experienced with the type of issues that can arise in these types of transactions," Mr Butler said.

Documenting the cessation of the bare trust arrangement is the next step in the process and should be prepared by an SMSF lawyer who will record the cessation of the bare trust and any related SMSF change.

All relevant parties must then be notified of the change in the title, which is usually carried out by a property lawyer.

Notifications should be sent to state revenue offices and local councils, as well as advisers and other interested parties such as power, water and other suppliers' services, which is particularly important for leased properties.

"The tenant should already be paying rent directly to the SMSF trustee or its nominated agent," Mr Butler said.

"However, the property lawyer should be asked to advise what is required to change the landlord from the bare trustee to the SMSF trustee under the relevant state or territory laws. A legal document assigning the lease to the new landlord and any related document might be needed."

The final step in the process is disbanding the bare trustee.

"If a bare trustee company was established solely to hold the legal title to the property, the directors of the bare trustee company may consider liquidating or deregistering the bare trustee company," Mr Butler said.

"However, they should exercise caution to avoid premature liquidation or deregistration, as it can be complex to reinstate a company if it is subsequently required. We generally recommend liquidation over deregistration for greater certainty to minimise any future risks."



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