



Safe Harbour terms for LRBAs & TD 2016/16

Important

The ATO released PCG 2016/5 – the safe harbour guidelines for arm’s length Limited Recourse Borrowing Arrangements (LRBAs). Originally the date to ensure all LRBAs were brought into line was before 30th June 2016. However on the 30th May 2016 the ATO extended the deadline until 31st January 2017.

The ATO are not asking for interest adjustments from commencement of the LRBA however the tables on the following pages show the interest rates that are required to be charged for the 2015/16 financial year and ongoing.

The extension means that the principal loan repayments for the 2015/16 year are to be paid prior to 31st January 2017.

Additionally, it is important to note that the length of the loan previously is taken into account for the calculation of principal repayments. For example, if a property LRBA has been running for 4 years the SMSF have 11 years to repay the remaining principal.

TD 2016/16

However subsequently the ATO released TD 2016/16 which is a shift in its position since it released the safe harbour guidelines.

The Taxation Determination is to show how the ATO determines whether the ordinary or statutory income of an SMSF be non-arm’s length income under subsection 295-550(1) of the Income Tax Assessment Act 1997 (ITAA 1997) when the parties to a scheme have entered into a limited recourse borrowing arrangement on terms which are not at arm’s length.

The ruling states:

“When parties to a scheme, that include a trustee of a self-managed superannuation fund (SMSF), have entered into a limited recourse borrowing arrangement (LRBA) on terms which are not at arm’s length, it is necessary to consider whether the SMSF has derived more ordinary or statutory income under the scheme than it might have been expected to derive if the parties had been dealing with each other at arm’s length in relation to the scheme. Non-arm’s length income (NALI) will only arise in those cases where the answer to this question is affirmative.”

The ruling also states that it is “necessary to identify what the terms of the borrowing arrangement may have been if the parties were dealing with each other at arms’ length (‘the hypothetical borrowing arrangement’). Having identified a hypothetical borrowing arrangement between the SMSF and the lender the terms of which are on an arm’s length basis, it is then necessary to establish whether it is reasonable to conclude that the SMSF could have and would have entered into the hypothetical borrowing arrangement. Where it is reasonable to conclude that the SMSF could not have, or would not have entered into the hypothetical borrowing arrangement, the SMSF will have derived more ordinary or statutory income under the scheme than it might have been expected to derive under the scheme with the hypothetical borrowing arrangement. In this instance, the ordinary or statutory income derived under the scheme is NALI.

Safe Harbour 1 – Real Property

The ATO will accept the LRBA is consistent with arm's length dealings if the terms of the borrowing are established and maintained throughout the LRBA as set out below:

Safe Harbour 1	The asset acquired is real property
Interest Rate	<p>RBA Indicator Lending Rates for banks providing standard variable housing loans for investors. Applicable rates:</p> <ul style="list-style-type: none"> • For the 2015-16 year the rate is 5.75% • For the 2016-17 and later years, the rate published for May (the rate for the month of May immediately prior to the start of the relevant financial year)
Fixed / Variable	<p>Interest rate may be variable or fixed.</p> <p>For variable use the above rate</p> <p>For fixed – Can be fixed for up to a maximum of 5 years using the fixed rate published for May (the rate for the May before the relevant financial year).</p> <p>The 2015-16 rate of 5.75% may be used for LRBA's in existence on publication of these guidelines, if the total period for which the interest rate is fixed does not exceed 5 years.</p>
Term of the loan	15 year maximum loan term. (for both residential and commercial).
Loan to Market Value Ratio (LVR)	<p>Maximum 70% LVR (for both residential and commercial)</p> <p>If more than one loan is taken out to acquire (or refinance) the asset, the total amount of ALL those loans must not exceed the 70% LVR.</p> <p>For an LRBA in existence on publication of these guidelines, the trustees may use the market value of the asset at 1 July 2015.</p>
Security	A registered mortgage over the property is required
Personal Guarantee	Not required
Nature & Frequency of repayments	<p>Repayment must be principal and interest</p> <p>Repayments are monthly</p>
Loan Agreement	A written and executed loan agreement is required

Safe Harbour 2 – Listed Shares or Units

The ATO will accept the LRBA is consistent with arm's length dealings if the terms of the borrowing are established and maintained throughout the LRBA as set out below:

Safe Harbour 2	The asset acquired is listed shares or units
Interest Rate	RBA Indicator Lending Rates for banks providing standard variable housing loans for investors plus 2%. Applicable rates: <ul style="list-style-type: none"> • For the 2015-16 year the rate is 5.75% + 2% = 7.75% • For the 2016-17 and later years, the rate published for May plus 2% (the rate for the month of May immediately prior to the start of the relevant financial year)
Fixed / Variable	Interest rate may be variable or fixed. For variable use the above rate For fixed – Can be fixed for up to a maximum of 3 years using the fixed rate published for May plus 2% (the rate for the May plus 2% before the relevant financial year). The 2015-16 rate of 7.75% may be used for LRBA's in existence on publication of these guidelines, if the total period for which the interest rate is fixed does not exceed 3 years.
Term of the loan	7 year maximum loan term. If you refinance you need to deduct the term of any previous loan(s).
Loan to Market Value Ratio (LVR)	Maximum 50% LVR If more than one loan is taken out to acquire (or refinance) the asset, the total amount of ALL those loans must not exceed the 50% LVR. For an LRBA in existence on publication of these guidelines, the trustees may use the market value of the asset at 1 July 2015.
Security	A registered charge / mortgage or similar security
Personal Guarantee	Not required
Nature & Frequency of repayments	Repayment must be principal and interest Repayments are monthly
Loan Agreement	A written and executed loan agreement is required