

Submission on LRBA Exposure Draft

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1. The Australian SMSF Members Association - ASMA

ASMA was established in 2011 to protect and grow SMSFs on behalf of its membership. To date ASMA has attracted more than 2,000 SMSF Trustees to its membership and is growing at 200 or more per month. On the subject of Limited Recourse Borrowing Arrangements ("LRBA") - ASMA has recently surveyed its members who have overwhelmingly given support to the use of LRBA arrangements *for the acquisition of property* as compared to shares. In other words our member's preference is for limited recourse *property* borrowing arrangements as opposed to traditional share instalment warrants.

2. Comments on Exposure Draft - Corporations Amendment Regulations 2012 - Limited Recourse Borrowings by Superannuation Funds (Instalment Warrants)

ASMA would like to make the following comments on the LRBA Exposure Draft:

a) Property not Shares must be the focus for the Exposure Draft

The original instalment warrant laws contained in section 67(4A) of the SIS Act 1993 were for both shares and property allowing for replacement assets in the same Holding Trust. However changes made to section 67 with the introduction of section 67A and 67B of the SIS Act 1993 have resulted in the Limited Recourse Borrowing Arrangements being used by ASMA members for the purpose of acquiring residential, commercial and rural property. The single acquirable asset rule has made it very expensive to and impractical to enter into an LRBA over shares.

In that regard the typical LRBA property transaction involves the following three *parties*:

1. A Lender – whether a bank or related party lender as allowed under the SIS Act 1993 to lend for investment property purposes.
2. A Trustee of a Holding Trust pursuant to a section 67A which holds legal title to the property – the Trustee generally being a company associated with or member of the superannuation fund.
3. The Trustee of a superannuation fund.

The Explanatory Memorandum states as follows: – “The proposed Regulations would extend the Principal Act's consumer protections to superannuation funds when purchasing instalment warrants.” There is no reference to LRBA's but rather share instalment warrants.

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It appears from ASMA's point of view that the drafters of the proposed regulations were focused on commercial instalment share warrant arrangements offered by investment banks and not the limited recourse property borrowing arrangements that are generally found under section 67A and 67B of the SIS Act 1993 and used by SMSF Trustees in conjunction with commercial lenders including amongst others Westpac, St George, NAB, Bendigo Bank, ANZ and CBA .

As property is not a financial product – see sections 763A and 763B of the Corporations Act 2001, ASMA proposes that a carve out be given to property LRBA's whilst continuing the current proposed regulatory regime for instalment warrants.

b) All Parties deemed to be Issuers – proposed Corporations Regulation 7.1.04H

The draft regulations propose that each party to the legal arrangement is an issuer of the LRBA. As an issuer of a LRBA – which is deemed to be a financial product pursuant to proposed 7.1.04J of the Corporations Regulations 2001, each party must be licensed and provide a Product Disclosure Statement (“PDS”) in relation to the LRBA. For a property LRBA this would include the Lender, the Holding Trustee and also the Trustee of the SMSF. At this time the Trustee of a SMSF is exempt from the licensing laws – see section 911A(j) of the Corporations Act 2001 but not the PDS requirements.

The effect of proposed Regulation 7.1.04H would be to make all property LRBA's un-commercial as the related party Holding Trust is not in a position to financially obtain a license for essentially a one off investment property transaction. This is also the case for any related party lender.

Once again we emphasise that the proposed regulations appear to focus on share instalment warrants and not small scale property LRBA's. ASMA proposes that a carve out be given to property LRBA's whilst continuing the current proposed regulatory regime for instalment warrants.

c) Licensees to have Securities Financial Services Provision

The Explanatory Memorandum provides that “Regulation 7.6.01AB would provide that an AFSL which covers the provision of a financial service in relation to a “security” (as defined in section 92 of the Principal Act) or a “derivative” (as defined in section 761D of the Principal Act) is taken to cover limited recourse borrowings under sections 67A and 67B of the SIS Act.”

Following on from above, property is not a financial product and a LRBA – which is in essence an investment property transaction is clearly not a financial style product where a licensee if advising on an LRBA investment where the investor – the Trustee of the SMSF, does not have day to day control. ASMA emphasises that the proposed regulations appear to focus on share instalment warrants and not small scale property LRBA's. ASMA proposes that a carve out be given to property LRBA's whilst continuing the current proposed regulatory regime for instalment warrants.

The Board
The Australian SMSF Members Association