

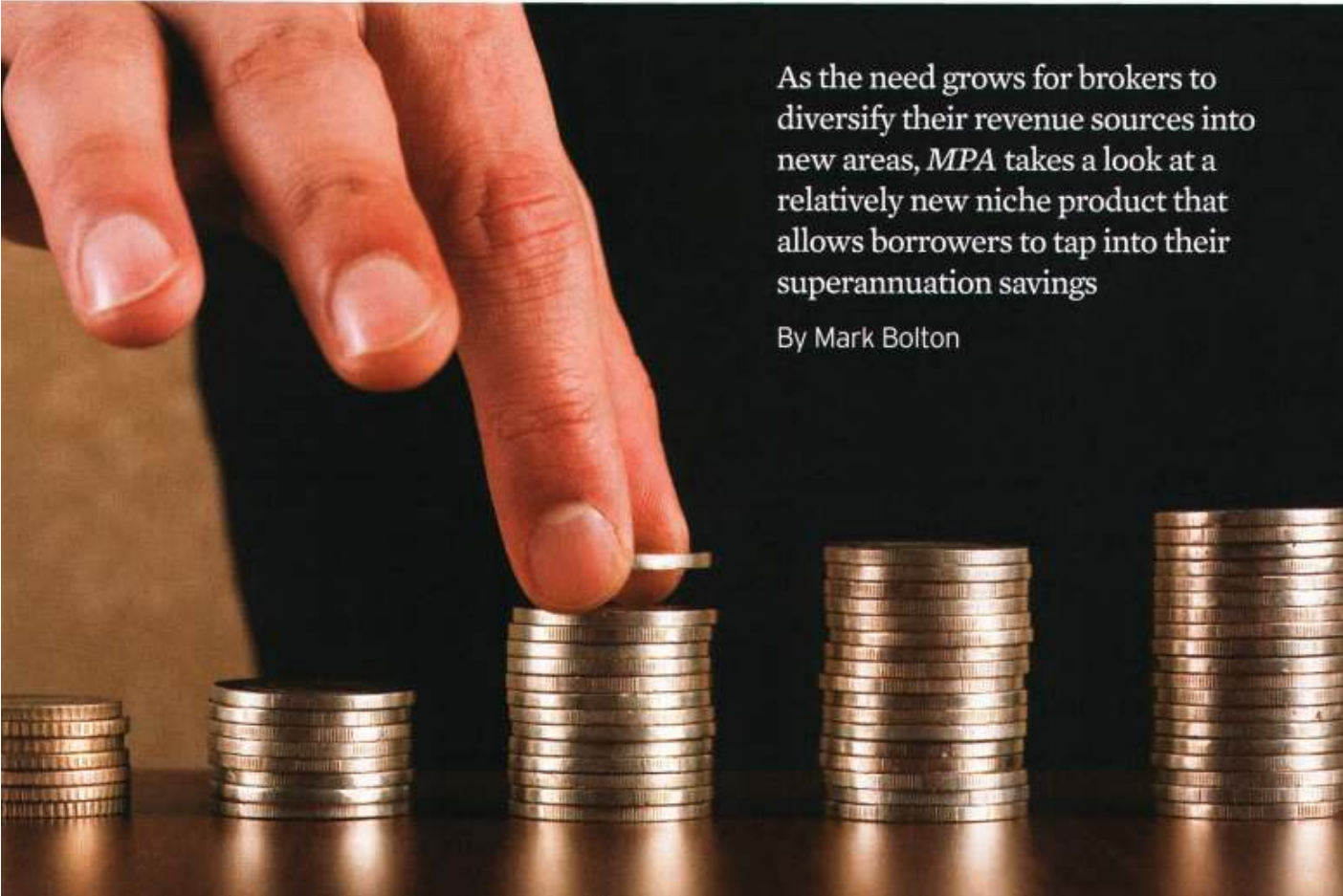


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DIVERSIFY
SMGFLOANG

A super opportunity



As the need grows for brokers to diversify their revenue sources into new areas, *MPA* takes a look at a relatively new niche product that allows borrowers to tap into their superannuation savings

By Mark Bolton



There are around 360,000 self-managed super funds in Australia representing the interests of around 690,000 people, with over 40,000 new self-managed super funds registered every year.

Then, in September 2007, changes were made to the Superannuation Industry Supervision Act (SIS Act) to allow self-managed superannuation funds (SMSFs) to borrow money to purchase assets.

And with credit markets drying up and funding hard to come by, the billions of dollars sitting in self-managed super combined with the voracious Australian appetite for property, it represents an opportunity for brokers that be should be considered closely.

Gaining acceptance

Having only been around a short time, SMSF loans are slowly gaining acceptance within the industry. Initially, there was a big push for these products in the commercial property market, targeted at business owners wanting to extract the capital out of their business residence or those trying to gain control of it. There is now more of a lean towards residential-backed SMSF loans.

"We're now seeing families look at this legal structure to see if mum and dad and the two siblings can aggregate all of their superannuation and actually wrap that around an estate plan where there's a retirement plan for the parents and a succession plan for the kids, all centred on a property investment strategy," says Drew Innes, director of SMSF Loans.

Which lenders are providing it and what commission is on offer?

Some of the big banks that are offering SMSF loans through the broker channel are St. George, BankWest, Westpac and NAB. Trails vary from an upfront of 0.55–0.7% and trails of 0.15–0.25%.

A number of non-bank lenders have also got involved including Firstfolio. Its mortgage manager, New Loan, offers an "SMSF Property Gear" product suitable for a "limited class of investment assets, including real estate property".

Then there is the option offered by SMSF Loans. It works on a referral basis. It has a large suite of products from a variety of lenders. If a broker refers a client, SMSF will take care of everything from coordinating the bare trust document to providing the funding facility and settling the loan. In return for the referral, SMSF Loans will pay brokers 25% of the available upfront and trail commission.

What knowledge/skills do you need to sell it?

The first step is to get accredited with the respective lenders to sell their product. Most are running them through their commercial arm, so



case study:

Mike Mall, finance broker

Mike Mall, a finance broker with X Inc Mortgage Brokers in Sydney's inner west, was quick to get involved with SMSF loans. Being self-employed, he had an interest in superannuation from a personal perspective.

So when he heard about SMSF loans, he started investigating. He got to know a financial planner who was already involved with the products, setting up trust deeds and the like. He then researched the various products on the market and put considerable effort into gaining the understanding and confidence needed to take them to the streets.

One of the big challenges has been understanding the technicalities of the product.

"It's a fair bit more involved than an ordinary home loan," he says. A distinct difference Mall has found is that SMSF loans are done through the banks' commercial arms. It has allowed him to further hone his commercial lending skills.

While Mall does understand some of the finer details, he makes sure he does not extend himself beyond his role of being the broker. "Don't be afraid to tell clients they need legal advice," he says. "You can't set these things up yourself."

Another obstacle is simply finding products to sell. He says it took a lot of work to find lenders who were offering the product.

While this product has worked well for Mall so far, he is unsure whether it will be the next boon for the broker industry. "I don't think it'll be huge for every broker," he says. "There's a lot of lead time, and a lot of brokers will find it frustrating to do one of these every six months."

Despite these challenges, Mall is still happy with his decision to add this to his repertoire. He has used the opportunity to offer a further service to his clients, and also build relationships with various accountants and financial planners.

The clients he is targeting are mainly the self-employed who have built up a contribution significant enough that they can have self-managed super.



ATO concerns

Being a new product, the Australian Taxation Office (ATO) is keeping a close eye on SMSF loans.

Assistant commissioner of super funds, Stuart Forsyth, is eager to promote good professional practice amongst brokers. While he says that most of the issues really fall on the shoulders of the trustees and their advisors, it is in everyone's best interests that the highest professional standards are adopted.

Forsyth explained that if a fund uses an SMSF loan to acquire an asset they are not legally entitled to buy - or breached superannuation rules - this would ultimately flow through to the broker, as the mortgage they are getting trailing fees from would have to be unwound.

One issue is that the loans will be oversold as part of a broker's strategy. "We're particularly concerned about people acquiring borrowings rather than property," says Forsyth.

The ATO also has a number of other concerns brokers should be wary of.

If the interest rate for the borrowing is less than or greater than a commercial rate, particularly when the lender is a related party, there could be a breach. If the money is less than a commercial rate, it could be characterised as a contribution to the SMSF.

This could result in the trustee/member having to pay excess non-concessional contribution tax. If the interest rate is greater than commercially acceptable, there could be a breach of the sole purpose test or a case of the trustee illegally giving the member financial assistance.

If the interest on the borrowing is able to be capitalised, there may be a breach of the requirement that money borrowed is applied to the acquisition of the asset.

A personal guarantee could also be in breach of the SIS Act, particularly where the guarantee is given by a member or related party. The rules allowing SMSFs to borrow are only supposed to apply to limited recourse borrowings.

Acquiring an asset that is prohibited under the SIS will also obviously be a breach. The in-house asset rules in the SIS Act generally prohibit super funds buying from a related party or for the property to be subject to a lease arrangement with a related party. Basically, you cannot buy grandma's house and then lease it back to her. There are some exceptions, however - a big one being if the property is a business premises.

Brokers are advised to stay vigilant when dealing with these products.

commercial accreditation is generally required. For those brokers not commercially accredited, this could be a great opportunity to further your skill set and take that next step towards becoming an advisor. "I think these products will create a general awareness with the smart brokers of the requirements or benefits of them getting better qualified and going down the track of PS146," says Mark Forsyth, CEO of Firstfolio.

Beyond accreditation is the need to have at least a reasonable understanding of the product and how it works. While brokers are advised to keep within the bounds of arranging the loan, a base knowledge is beneficial. "There's no formal training as yet," says Mike Mall, a finance broker with X Inc Mortgage Brokers, "but you have to be a little bit experienced to understand the technicalities of how the legal side of it all works."

Legal matters

It could be considered strange that the accreditation requirements for brokers to sell these products are relatively light considering the product's complexity. But one of the reasons for this, and it accompanies a big warning, is that the role of brokers in this process should be limited to selling the loan.

"It's most important to just keep within the scope of the things which brokers know about," says Forsyth. "Avoid any mention of tax strategies and the like. Keep to the actual details of the loan and leave strategising to someone else."

Jon Denovan, partner at Gadens Lawyers, also warns brokers to not overextend themselves. "There are a whole lot of things that can go wrong; it's really surprised us," he says. "There are so many little tricks of the trade associated with superannuation funds and these rules."

Denovan advises brokers to give the customer the idea of the product but not to get into the detail, "because there's a huge amount of devil in the detail."

Another issue Denovan warns brokers of is slipping into the financial product category. Generally, if you are selling a packaged product that includes both the trust structure and the loan then it is probably a financial product, says Denovan. "If the product and the credit are supplied by the same person, you might be in the financial product territory and therefore no broker can sell it."



Mark Forsyth



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So long as the brokers are arranging the credit only, then it should be fine. Another safety blanket for brokers is that most of the lenders require the consumer to receive independent financial advice before they will give the all clear.

Who are the typical clients of this product?

Forsyth suggests it is the high net-worth individuals – those in the upper-end of the borrowing spectrum – who are taking advantage of this product. Financial planner Phil Bamback agrees, saying that it is mainly the multi-property investors who are most likely to get involved.

Innes, though, has a broader opinion of who is getting involved. “We’re seeing a whole heap of different applications ... and it’s early days,” he says. The different types of people Innes has seen include family units wanting to create a combined succession plan and property portfolio. He has had clients in their mid-forties who have not been able to get into the property market conventionally, but have enough super to

get them going. He has also noticed a huge market for small- to medium-sized enterprises wanting to purchase their business premises and have the capacity to do so through their super.

And there are also those who already own their business premises but want to take the equity component out of the property and reinvest it back into their business.

How does a broker go about finding these clients?

Apart from your current client base, the next best place to look are the accountants and financial planners. Innes has found that people speak with their accountants and financial planners before considering their broker. “If the accountant can’t write the loan, he needs to have a relationship with a broker who can.”

Forsyth concurred, suggesting that brokers develop relationships with these financial service providers. “This is an opportunity for brokers to knock on those doors and show them a product they may not have access to at the moment.” **MPA**