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business real property

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Tom and Sue come to see you about purchasing the house next door. Sue runs a successful promotions business from her home office. With recent growth in the business and the need to take on new staff she has outgrown her space.

The house next door has just come on the market and Tom and Sue are plan to purchase it and turn it into an office for Sue's business.

As the property will be used as Sue's office, an accountant friend of the couple has told them they should purchase it using their self managed superannuation fund ("SMSF").

Tom and Sue are excited about the purchase, as are their three children, who can't wait to have a bigger backyard to play in. Tom and Sue plan to fence the two backyards into one. As Sue's business will not need all of the space available, Tom and Sue also plan to make one of the rooms opening onto the back yard into a rumpus room for their children and their friends to play in.

Tom and Sue are careful to point out their friend told them that as the owner of the property will be an unrelated party, as long as they put in place a lease between the SMSF and Sue's business the purchase will not breach any of the superannuation laws.

They also tell you that while the purchase will use up most of their superannuation balance they are happy that it will be a good long term investment for their retirement.

The conveyance settles without a hitch, you put in place a basic commercial lease between the SMSF and Sue's business and close the file.

## The sting

If Tom and Sue use the new property as suggested it will be an in-house asset of Tom and Sue's SMSF.

Under subs.71(1) of the Superannuation (Industry) Supervision Act ("The Act") an asset subject to a lease or lease arrangement between an SMSF and a related party of that SMSF is an in-house asset for the purposes of the Act. SMSF's are only allowed to have up to 5% of their investments in in-house assets.

However, s.71(1)(g) of the Act excludes business real property owned by a SMSF that is subject to an enforceable lease between the SMSF trustee and a related party of the SMSF from being an in-house asset.

Business real property is defined in the Act as any freehold or leasehold interest in real property where the real property, is used wholly and exclusively in one or more businesses (whether carried on by the entity or not).

The problem for Tom and Sue is that as soon as they use the property for anything other than the operation of Sue's business it is no longer business real property as it is not then being used wholly and exclusively in one or more businesses.

The ATO has set out its view on the meaning of business real property in Self Managed Superannuation Fund Ruling SMSFR 2009/1.

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Based on the ATO's view in that ruling Tom and Sue's plans would result in the property no longer being used wholly and exclusively for one or more businesses and therefore it would not be business real property.

As soon as the property stops being a business real property it becomes an in-house asset of the SMSF. As the property comprises more than 5 per cent of Tom and Sue's SMSF investments they would either need to stop the non business use or sell the property.

It is important to remember that the business real property test is an ongoing one and that if land owned by a SMSF is being leased to a related party the property must remain business real property at all times.

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For further information on this issue, please see the contacts below.

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