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When business real property counts

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Recent changes to the limited recourse borrowing arrangement rules have shifted the focus for SMSFs. The new challenge is whether the property can genuinely satisfy the definition of business real property (BRP), as that is where it will count.

From 10 August 2026, SMSFs using a new limited recourse borrowing arrangement (LRBA) for real property must ensure that the asset is business real property within the meaning of section 66 of the *Supervision Industry (Supervision) Act 1993* (SIS Act).

The practical effect is that new residential property LRBAs are excluded unless the property can satisfy the business real property test.

Existing arrangements entered into before that date, and refinances of those existing arrangements, are not affected by the change, regardless of whether the LRBA is financed through a bank, non-bank or related party lender.

It makes the definition of business real property more important than ever. The issue is not simply whether a property looks residential or commercial. The critical question is how the property is used at the relevant time and whether that use is wholly and exclusively in one or more businesses.

That distinction will be straightforward in many cases. A warehouse, factory, office suite, or retail premises used entirely for business will usually be easier to characterise. The difficulty arises where the property has residential features, mixed use, temporary vacancy, private occupation, or a business use that may be genuine but is not obvious from the property's appearance.

Those blurred-line cases are where trustees, advisers and auditors will need to be especially careful. The consequences of getting the classification wrong can be significant, particularly where the fund has borrowed to acquire the property, and the auditor is being asked to accept that the LRBA complies with the new law.

What has changed for LRBAs?

The LRBA rules have been narrowed so that, for real property, the acquirable asset must be business real property. This change does not prevent an SMSF from buying residential property outright. It affects new borrowing arrangements where the fund seeks to acquire real property under an LRBA.

The commencement date is critical. The new restriction applies to arrangements entered into on or after 10 August 2026. Arrangements already in place before that date are grandfathered, along with the ability to refinance an existing arrangement. The unanswered practical question, however, is how far that grandfathering extends where the original arrangement changes materially.

For example, what happens when a residential property held under an LRBA is transferred as part of a family law settlement, moved to another SMSF, or placed under a new bare trust with new finance documents?

The original borrowing may have been protected, but the new structure may appear to be a fresh arrangement, and these cases will require careful legal analysis rather than assumptions.

ATO guidance

The Australian Taxation Office (ATO) has released *Changes to limited recourse borrowing arrangements* (QC 107811) to address the practicalities of what constitutes an arrangement entered into before 10 August 2026. It states that an SMSF must have entered into a legally binding arrangement evidenced by the exchange of a binding contract, providing certainty for transactions such as a binding off-the-plan contract.

It is irrelevant whether the contract is settled or not, or even if the LRBA is entered into before that day. Contracts that are changed significantly, however, where the fundamental terms no longer exist, may be considered a new arrangement and no longer be able to rely on the grandfathering provisions.

Most importantly, those LRBAs commencing after 10 August 2026 must remain as BRP for the entire life of the LRBA. Where the asset no longer meets these requirements, the SMSF has breached section 67A SIS Act, and compliance action may apply.

Why business real property is not commercial property

Business real property is not defined by the property's label, zoning or appearance. A property is not automatically business real property because it is described as commercial, and a property is not automatically excluded because it has residential characteristics.

The key test is use.

Under SMSFR 2009/1: *Self-Managed Superannuation Funds: business real property for the purposes of the Superannuation Industry (Supervision) Act 1993,* the property must be used wholly and exclusively in one or more businesses. This requires a practical assessment of the facts and circumstances at the time of acquisition and at relevant times afterwards.

The question is whether the property's actual use satisfies the business-use test.

Where the lines become blurred

The new LRBA rules are likely to increase pressure on the definition of residential property and business real property. Trustees who can no longer gear ordinary residential property may be tempted to characterise marginal or mixed-use assets as business real property. That is where the risk sits.

Residential premises used wholly in a business

A house, terrace or apartment may satisfy the business real property definition if it is used wholly and exclusively in a business. Examples may include premises converted and used entirely as professional consulting rooms, a medical practice, a veterinary clinic, an office, or business premises where no part is used as a residence.

The risk is assuming that business use is enough. If part of the property is still used privately, or if residential occupation is more than minor or incidental, the "wholly and exclusively" requirement may not be met. Evidence of the actual business use will be crucial.

Mixed-use property

Mixed-use property is one of the most difficult areas. A shop with a residence upstairs, a rural property with a farmhouse, or accommodation attached to business premises can all raise questions about whether the non-business use is incidental or whether it prevents the property from satisfying the definition.

The analysis should focus on the overall property, the extent and purpose of any residential component, and whether that component is integral, incidental or separate from the business use. A private residence sitting alongside a business may be harder to justify than accommodation that is genuinely ancillary to the business operation.

Residential property held as part of a property business

Another blurred-line scenario is one in which residential properties form part of a genuine property business. The issue is not simply whether the owner receives rent.

Passive investment activity will not necessarily amount to carrying on a business. The analysis turns on ordinary business indicators such as scale, repetition, regularity, commercial organisation, record keeping, systems, time commitment, and profit-making purpose.

This distinction matters because a portfolio of residential rentals may be operated as a business in some circumstances, but many rental arrangements remain investments.

SMSF professionals should not assume that multiple properties, significant value, or regular rent alone will establish business real property.

Document before the transaction

The best protection is a documented business real property analysis prepared before the SMSF enters the transaction. The analysis should not be done after the event to justify a conclusion. It should show that the trustees considered the issue before acquisition and that there is a reasonable basis for treating the property as business real property.

A useful analysis should identify the property, describe its physical characteristics, explain its current and intended use, identify the vendor and tenant, address whether any related-party issues arise, and explain how the acquisition fits the fund's investment strategy.

It should also include evidence: leases, business records, photographs, zoning information, floor plans, valuation material, trustee minutes, and any other documents that support the conclusion.

The quote

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Shelley Banton, Super Clarity

Shelley is director of Super Clarity and an SMSF specialist adviser and auditor with more than two decades of experience in superannuation, compliance, and risk management. She delivers practical compliance solutions, risk management strategies, and technical education designed to empower SMSF professionals. A respected industry voice, Shelley is a sought-after speaker and commentator, recognised for her clear, pragmatic insights that cut through complexity.

The quote

Most importantly, those LRBAs commencing after 10 August 2026 must remain as BRP for the entire life of the LRBA.

Where the property is mixed-use or has residential characteristics, the analysis should directly address why those features do or do not affect the property's status as business real property.

Practical questions for SMSF professionals

The type of practical questions that SMSF professionals should ask before proceeding with an LRBA involving property that is not clearly BRP are:

- What is the property actually used for now?
- Is every part of the property used in one or more businesses?
- If there is residential use, is it genuinely incidental or does it undermine the "wholly and exclusively" test?
- Is the use supported by leases, business records and physical evidence?
- Is there any related-party acquisition, lease or financing issue?
- What happens if the tenant changes, the business stops, or the property becomes vacant?
- Has the trustee documented the analysis before committing to the acquisition?

Conclusion

The new LRBA rules do more than remove gearing for residential property. They bring the business real property definition into front-of-mind compliance where it counts most. More pressure is placed on the grey areas, particularly where residential property is used in a business, forms part of a broader property business or includes both business and private elements.

If the real property sits on the fence between residential property and BRP, the answer should be proven and documented.

The safest approach is to analyse the property by reviewing its actual use, document the reasons beforehand, and avoid stretching the definition to fit a desired borrowing outcome. **FS**