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BENEATH THE SURFACE

Superannuation Alert

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Super Simplification - Are You Ready?

The changes to super from 1 July 2007 mean that superannuation continues to be a very attractive proposition particularly for self managed superannuation funds (SMSFs). There are now over 320,000 SMSFs which control investments of over $210 billion.

What is a Self-Managed Superannuation Fund?

A superannuation fund is a self managed superannuation fund if it meets the following conditions:

- has fewer than 5 members
- each individual trustee of the fund is a fund member
- each member of the fund is a trustee
- no member of the fund is an employee of another member of the fund, unless those members are related

An SMSF can also have a company as a trustee (known as a corporate trustee) if:

- the fund has fewer than 5 members
- each director of the company is a member of the fund
- each member of the fund is a director of the company
- no member is an employee of another member (unless related), and
- the trustee does not receive remuneration for their services as a trustee.

Single Member SMSFs:

It is possible to have an SMSF with only one member. If the single member fund has a corporate trustee, the member can be the sole director of the trustee company. If the single member fund does not have a corporate trustee, the fund must have two individuals as trustees with the member being one of them.

SMSF Examples:

- Ivan and Antoine have been good friends for many years and decided to set up their own small superannuation fund. They used the services of Beneath the Surface to set up the fund with themselves as individual trustees. It is usually recommended that you start an SMSF with $250,000 minimum but Ivan and Antoine did not have this much. Yet as hard-working self employed people, they felt strongly that they wanted to take control of their retirement funds and move them away from the public trustees. They started their SMSF in 2003 with $85,000, mostly rolled over from their public funds plus some cash contributions. An SMSF cannot borrow money, so their initial major investment was a vacant block of land in a seaside village. Over the years they continued to make contributions. Today their fund is valued at $200,000 being some cash, a share portfolio ($25,000) and huge capital growth on their land.

- Sally's business premises, which she leased, went on the market for sale in 2004. She paid a visit to her financial advisor to discuss purchasing the suite and was advised to do so in an SMSF. She came to Beneath the Surface to discuss this advice and to learn about SMSFs and their tax advantages. Subsequently, Sally decided to proceed and Beneath the Surface helped her set up the fund as a sole member with a corporate trustee and Sally appointed as the only director. She rolled over her public super funds and bought the professional suite. Then she sought the advice of an experienced independent sharebroker to place the extensive balance of her super investments,

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mainly in direct shares. Sally runs her business from the professional suite. As such she gains a tax deduction for her rental payments and at the same time accumulates income in her superannuation fund for further investment. This, combined with self employed superannuation contributions, has allowed her to increase her fund's value by more than $150,000 in two years.

"… if you do not have an SMSF now could well be the most opportune time to start one…"

◊ Wolfgang and Sabrina run their business in a company structure. As such they are employees and the company contributes their compulsory superannuation payments to their SMSF which they set up four years ago. They approached Beneath the Surface to provide annual accounting, audit and taxation services for their fund. Being pro-property investors, they continued to add to their rolled over funds until they had sufficient to pay cash for a rental investment property.

With early and sound planning and advice sought from Beneath the Surface, Wolfgang and Sabrina were able to meet the eligibility criteria for the small business capital gains tax concessions when they sold a business asset. This meant that the whole capital gain was not only tax-free, but 25% of it was able to be

SUPER SIMPLIFICATION PROPOSALS - Still Not Law But Released in Draft Form

From 1 July 2007, for taxpayers who are 60 and over and receive payments from a taxed superannuation fund, there will be:

◊ no tax on a lump sum
◊ no tax on a pension (segregated assets and income to support a pension are also tax free).

In addition, from 1 July 2007:

◊ the reasonable benefit limits will be abolished which means there will be no limit on the amount that can be accumulated within super, including life insurance and permanent disability insurance payouts on fund policies

◊ the age based limits will be abolished

◊ uniform contribution limit of $50,000 will be introduced (transitional rule: if 50 years of age, or over, can contribute $100,000 per year up to 30 June 2012)

◊ death benefit
- ✧ lump sums paid to dependants will be tax free
- ✧ lump sums (excluding concessional components) paid to non-dependants such as children of the deceased who are over 18 and not dependent on the deceased for support, will be taxed at 15% plus Medicare
- ✧ may be paid as pensions to a dependant child – however, when the child reaches age 25 the pension must be converted to a tax free lump sum except where the child is permanently disabled
- ✧ a death benefit paid to a non-dependant must be paid as a lump sum

◊ self employed
- ✧ will be entitled to a full deduction for their contributions
- ✧ will be entitled to the super co-contribution

◊ undeducted, or after-tax, contributions:
- ✧ allowed up to age 75
- ✧ will be limited to $150,000 per annum or $450,000 maximum, averaged over 3 years for people who are younger than age 65 whether they are working or not
- ✧ those aged 65 to 75 will be able to make after tax contributions of up to $150,000 provided they are working at least 40 hours in 30 consecutive days in the financial year of contribution
- ✧ any excess contributions will be taxed at the top marginal rate plus Medicare and the net amount will remain within superannuation
- ✧ it is intended that the thresholds will be indexed
- ✧ transitional rule: can contribute up to **$1 million from 10 May 2006 to 30 June 2007** – this provides a window of opportunity for all persons under age 75 and eligible to contribute to super.

CONVERSION OF EXISTING ALLOCATED PENSIONS AFTER 1 JULY 2007

◊ A new type of pension will be permitted – these pensions will provide a minimum pension payment but will have no maximum, *except in the case of Transition to Retirement pensions which have a maximum drawdown equal to 10% of the pension balance.*

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STRATEGY SUGGESTIONS

Now is the time to review your existing superannuation and/or SMSF and make plans to ensure that you are utilising the most current financial planning strategies available to you. Alternatively if you do not have an SMSF now could well be the most opportune time to start one as we believe that these changes will make superannuation and SMSFs an even more attractive proposition than it is today. Please note that Beneath the Surface actively encourages a close working relationship with you, your financial advisor, solicitor and family members, as a team:

- ◊ clients with several funds should consider rolling into one fund prior to 1 July 2007 so as to maximise any pre-July 1983 components - these will become a fixed dollar amount but, like undeducted contributions can be withdrawn tax free, subject to any applicable preservation rules
- ◊ as there is no limit on the amount that can be taken out tax free after age 60, it is desirable to get as much in there as possible
- ◊ a significant incentive to consider paying a minimum standard pension, so that the fund itself is tax free – thereafter, a beneficiary benefits from all income and all growth in capital on a tax free basis
- ◊ if the fund has substantial unrealised capital gains, consider commencing a pension prior to sale of the assets.

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- ◊ Allocated pensions which commenced prior to 1 July 2007 can convert to the new type of pension without the need for a formal commutation and rollover
- ◊ There will be some form of reporting required by the tax office.

CASH CONTRIBUTIONS

- ◊ Where a contribution is made by a transfer of investments, ensure the value transferred falls within the relevant contribution levels
- ◊ Abolition of previous compulsory cashing rules on cessation of work or reaching retirement age – the change means that there is no requirement to pay superannuation benefits except on a person's death
- ◊ There is no limit to the amount that can be transferred to superannuation from settlements for injuries resulting in permanent disablement
- ◊ Small business owners will be able to transfer up to $1 million to superannuation where it relates to certain capital gains earned on business assets – the benefit of this concession is that a person's capital gains tax liability is reduced and the amount is not counted as a contribution to superannuation, nor is it subject to the limit on contributions that applies to deductible and after-tax contributions.

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