Financial Focus

Spring 2010

Welcome to Financial Focus, the newsletter that provides you with the latest news and information on significant financial planning topics. I hope you find the articles in this issue interesting and informative. If you have any comments, questions, or would like a review of your financial plan, please call or email me.

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Split your way to a better retirement

If you have a spouse, you may want to split some of your super contributions into their account.

By doing this, you could pay less tax on your super before age 60, access your combined benefits earlier and make insurance more affordable for your spouse.

You may even be able to take greater advantage of the recent changes the Government has proposed regarding the super contribution caps.

The benefits of splitting

Pay less tax on withdrawals before 60

If you make a lump sum withdrawal from your super between age 55 and 60, no tax is payable on the first $160,000[1]. Splitting super contributions into your spouse's account could therefore enable you to collectively withdraw up to $320,000 tax-free before you turn 60.

Pay less tax on income payments before 60

If you use your super to start an income stream investment (such as an account based pension), tax may be payable on the income payments you receive before age 60[2]. However, if you use contribution splitting to 'equalise' your account balances, you could reduce (even eliminate) the amount of tax you pay as a couple[3].

Access super benefits earlier

If you're younger than your spouse, splitting contributions into their super account can enable them to access the money earlier and/or receive unlimited tax-free benefits before you (when they reach age 60 or over).

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Concessional contribution cap for people aged 50+	Current cap	Proposed cap if < $500,000 in super
Up to 30/6/2012	$50,000	$50,000
From 1/7/2012	$25,000	$50,000
Up to 30/6/2012	$50,000	$50,000
From 1/7/2012	$25,000	$50,000

Get more Age Pension

If you're older than your spouse, splitting contributions into their super account can reduce the amount that will count towards the Assets test when you reach Age Pension age[4]. This could enable you to qualify for (or increase your entitlement to) Age Pension benefits.

Purchase insurance tax-effectively for your spouse

If your spouse is not working, you may want to:

- make salary sacrifice or personal deductible contributions into your super fund
- split some of these contributions into your spouse's super account, and
- arrange for your spouse to purchase Life, TPD and/or (in limited circumstances) Income Protection insurance in their super account.

By doing this, you could make some significant tax savings that could help reduce the cost of insurance for your spouse.

Provide protection against adverse law changes

Splitting could enable you to reduce your combined tax bill if the Government was to (for example) re-introduce:

- some form of tax on benefits received from a super fund at age 60 or over, and/or
- a limit on the amount of concessionally taxed super benefits you can receive over your lifetime.

Benefit more from the contribution cap proposal

Currently, the cap that applies to concessional super contributions[5] is $25,000 pa or, if you're aged 50 or over, it's $50,000 pa until 30 June 2012 and $25,000 pa thereafter.

However, the Government recently proposed that the cap will be maintained at $50,000 from 1 July 2012 for people aged 50 or over with super account balances under $500,000 (see table above).

If this change is legislated, splitting super contributions could enable you to keep your balance below $500,000 for as long as possible and allow you to make larger super contributions in the lead-up to your retirement.

That said, we don't know at this stage whether split amounts will count towards the $500,000 threshold. In other words, until any detail is known, splitting super contributions may not be worthwhile for this purpose alone.

But given the other potential benefits outlined above, splitting could still be a powerful pre-retirement strategy.

What contributions can be split?

It may be possible to split up to 85% of your employer's super contributions (including salary sacrifice) or your personal deductible super contributions, provided the split amount doesn't exceed your concessional contribution cap (see table on page 2).

Furthermore, you can generally only split contributions in a given financial year that were made or received in the previous financial year.

However, if the super account is closed, or the full proceeds are rolled over to another fund, some funds may allow you to split contributions received during the financial year up until the point of closure or rollover.

Who can receive contribution splits?

You can split super contributions into your spouses account if they are legally married to you or, if not, they live with you on a genuine domestic basis in a 'relationship as a couple' (regardless of whether they are of the same or opposite sex). They also need to be under age 55 or, if between 55 and 65, they must not have fully retired.

Key issues to consider

Not all super funds offer contribution splitting and some have their own rules and limits.

To split super contributions you will need to complete a valid application form.

If you want to claim a tax deduction for any contribution you want to split, you should correctly specify the amount on a valid 'Notice to Claim a Deduction' form before (or at the time of) submitting a splitting application form.

The contribution split will be fully preserved when transferred to your spouse's account and they cannot access the money until they meet a 'condition of release'.

To find out more about contribution splitting (and see whether it suits your goals and circumstances) you should speak to a financial adviser.

1 This threshold applies to the taxable component of lump sum withdrawals in 2010/11 and is indexed periodically in $5,000 increments.

2 When a super benefit is received as an income payment between 55 and 59, the taxable component is taxed at your marginal rate, however, the actual tax payable will be reduced by a 15% tax offset and any other offsets available (eg the low income tax offset).

3 This is because you'll be able to benefit more from the tax-free threshold and low income tax offset, as well as make better use of the progressive marginal tax rate scales.

4 Age Pension age is currently 65 if male and between 60 and 65 if female (depending on your date of birth).

5 Concessional contributions include salary sacrifice and all other employer contributions, personal deductible contributions and certain other amounts.

Tax alert: New rules for employee shares

Do you receive shares from your employer as part of your salary? If so, be aware the tax rules have changed.

Employee share plans are popular in Australia, mostly among publicly listed companies. The idea is they give 'ownership' of the company to its employees, therefore increasing productivity by making employees more invested and responsible for the company's success.

However, what many employees fail to adequately grasp is that these shares are a part of your salary, and are taxed accordingly.

In the past you could defer paying tax on those shares to a future financial year. However, according to the Australian Tax Office (ATO), there was scope for people to underpay tax. As of 1 July 2009, the rules have changed, impacting every employee that receives company shares.

New upfront taxation

Basically, employees can no longer choose whether they want to be taxed upfront or defer tax to a future financial year. This decision is now determined by the nature of the employee share plan.

All plans will pay tax upfront unless the plan includes a 'real risk of forfeiture' or the shares are acquired under certain salary sacrifice arrangements.

Exemptions

Employees who earn $180,000 or less will receive a $1,000 tax exemption when tax is paid upfront. This means the employee doesn't need to pay tax on the $1,000 worth of shares when they're issued, however they may be subject to capital gains tax in the future.

One issue to be aware of is that in order to receive the tax exemption the shares must be held by the employee for three years, except where the employee leaves the employer. This means that the employee can't sell or transfer the shares during this period.

These shares are subject to capital gains tax. Any potential capital gain will be the market value of shares when they are sold less the value of the shares when they were first given to the employee (less any original amount paid).

Deferred taxation

There are two types of employee share plans where tax is deferred to a future year. The first is where there's 'a real risk of forfeiture' and the second is where the shares are acquired under certain salary sacrifice arrangements.

1. **A real risk of forfeiture** means there's a risk the employee will lose their entitlement to the shares. For example, if the employee leaves the company before shares they're entitled to are issued, or a performance hurdle where the company must increase market share over a certain period of time.

   An employee committing fraud or dismissed for gross misconduct is not a real risk of forfeiture.

2. Employers can also offer a **salary sacrifice plan** that allows employees to direct some of their salary to purchase shares, normally at a discount to the arket price. This discount amount is then included in the employee's assessable income at a deferred point in the future. Employees can defer paying tax on the discount for up to seven years.

At the end of the deferral period, the difference between the market value of the shares and any original amount paid is included in the employee's assessable income for that financial year.

To work out any capital gains, the employee can take the market value of the shares when they sell them, then subtract the market value of the shares when the deferral period finished. If the employee is entitled to the 50% discount then the 12 month period will commence from after the deferral period has finished.

Shared responsibility

These new rules represent an important change to employee share plans, with the potential to impact many people.

If you're on an employee share plan and unsure how this impacts you, speak to your financial adviser.

Important Note:

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