

TAX TIME – PLANNING FOR JUNE 30

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The end of financial year is fast approaching, and you may be entering one of your busiest business periods. Here are some common year-end strategies as well as points to consider when making recommendations on superannuation, self-managed super funds, and discretionary trusts.

COMMON YEAR-END STRATEGIES



Investments

Review capital gains & losses: When reviewing clients' investment portfolios, identify those who have crystallised a capital gain during the financial year and consider crystallising capital losses to help reduce the tax liability. However, you must ensure that you do not recommend selling and re-purchasing the same or similar asset as the Australian Taxation Office (ATO) may deem this to be a 'wash sale' and disallow the loss.

Pre-pay interest on investment loans: If clients have investment or margin loans, they can pre-pay the interest for the year in advance and claim a tax deduction this financial year.

Consider ownership: When recommending new investments to couples, consider whose name the investment is in so that the clients can benefit from income splitting.

Super vs non-super: To reduce/eliminate tax on benefits paid to non-tax dependants in the event of a client's death (and to minimize legislative risk), substantial funds can be invested outside superannuation without clients being subject to tax via the use of franking credits and tax offsets. Re-consider the need for super and pension structures for clients with lower asset levels, as the effective tax-free threshold for clients aged 65 or more is:

- **\$33,898 for singles**, and
- **\$30,593 for couples (each)**.



Insurance

Pre-pay deductible premiums: Remind clients of the importance of income protection and how it can be held in either their own name and be tax deductible, or if cashflow is an issue, it can be held within superannuation. Premiums can be pre-paid in advance for the next 12 months to increase the tax deduction available in the current year.



Charitable giving

By making a tax-deductible donation to a charity or non-profit organisation, clients may be able to offset income and/or a capital gain made during the year. Compared to a one-off donation, setting up a charitable trust can be a better solution for individuals, families or businesses and generally offer long-term tax advantages. A charitable trust also provides a sustainable gift that grows over time to keep giving in perpetuity, allowing clients to leave a lasting legacy for the community.

TIPS FOR SUPERANNUATION

Tax time is very different this year

Superannuation in the lead-up to June 30 is unique this year in that clients may be better off delaying until the new tax year certain strategies that you would normally have them implement now.

From July 1, the general transfer balance cap (TBC), the contribution caps and the total superannuation balance (TSB) test limiting certain contributions, are all increasing, which may give a client the opportunity to get more into super – and keep more in it – if they put off doing certain things until after June 30.

Concessional contributions

The total amount that can be contributed as a personal deductible contribution and/or compulsory employer Superannuation Guarantee (SG) contributions and voluntary employer (salary sacrifice) contributions is generally \$25,000 before additional tax applies.

A client's TSB has nothing to do with concessional contributions (CCs) other than determining their eligibility:

- to make catch-up CCs, and/or
- to make them under the work test exemption (WTE).

If a client wishes to make a personal deductible contribution, they must provide their super fund with a section 290-170 notice of intent (NOI) to claim a tax deduction for the contribution and have it acknowledged by the fund trustee – usually done around tax time. Whatever you do, do **not** touch the contribution – e.g. roll it over to another fund, withdraw it, or start an income stream – before first lodging the NOI and having it acknowledged.

Remember, when recommending personal deductible contributions that the effective tax-free threshold for clients not eligible for the seniors and pensioners tax offset is **\$23,226**. You do not want a client paying for the privilege of getting money into super – 15 per cent tax – by reducing their income below this amount.

Catch-up concessional contributions

If a client did not utilise the full \$25,000 CCs cap in 2018-19 and/or 2019-20 then the unused amount(s) may be contributed this financial year provided their TSB at 30 June 2020 was less than \$500,000.

Increasing a client's tax deduction

Consider a 'contribution reserving strategy' – an arrangement whereby a contribution made to an SMSF in June is allocated in July.

Contributions must be allocated to members' accounts within 28 days after the end of the month in which they are received, but they do not count towards the client's contributions cap until allocated by the trustee. Importantly, a tax deduction is permitted in the year the CC is made, despite it not being allocated until the following financial year.

Please refer to 'Contribution reserving strategy – increasing a client's tax deduction' in the 'TIPS TO CONSIDER FOR SELF-MANAGED SUPER FUNDS (SMSFs)' section below.

Non-concessional contributions

Step 1. Know your client's total superannuation balance at 30 June 2020

If a client's TSB was \$1.6 million or more at 30 June 2020 then they cannot make a non-concessional contribution (NCC).

The following after-tax contributions are not treated as NCCs and can be made regardless of a client's TSB.

- CGT cap contributions – up to \$1.565 million
- Downsizer contributions – up to \$300,000
- Certain contributions made with the proceeds of a qualifying structured settlement, order for a personal injury payment or lump-sum workers' compensation payment.

Step 2. Determine if your client previously triggered the bring-forward rule

If a client's TSB was less than \$1.6 million at 30 June 2020 then look at their NCCs made in 2018-19 and 2019-20 to ascertain whether a bring-forward arrangement was triggered back then.

The bring-forward rule was triggered if the client contributed more than \$100,000 in either tax year.

Ensure to count as NCCs any excess CCs not withdrawn from super.

Also, be careful if you find a client contributed more than \$100,000 back then that it was not the tail end of a bring-forward period.

Bring-forward rule triggered in 2018-19 or 2019-20

If the client contributed more than \$100,000 in either the 2018-19 or 2019-20 financial years, determine the bring-forward arrangement under which they contributed – \$300,000 over 3 years or \$200,000 over 2 years?

The former applies if their TSB was less than \$1.4 million at the 30 June just prior to the year they triggered the bring-forward rule. In this case, the maximum they can contribute in 2020-21 is any remaining balance to \$300,000.

The latter applies if the client had \$1.4 million to less than \$1.5 million and the maximum they can contribute now is any remaining balance to \$200,000.

Step 3. Bring-forward rule not triggered in past two years

If a client's TSB was less than \$1.4 million at 30 June 2020 then they can contribute up to \$300,000.

If their TSB was \$1.4 million to less than \$1.5 million, they can contribute up to \$200,000.

Otherwise, the maximum they can contribute is \$100,000 only.

Age 67 or more

Generally, a client aged 67 to 74 must have met the work test before they can contribute CCs, NCCs and CGT cap contributions.

A client who will not meet the work test in 2020-21 can make a voluntary contribution under the WTE provided they satisfied the work test in 2019-20 and had a TSB at 30 June 2020 of less than \$300,000. Clients aged 74 have up until 28 days after the end of the month they turn 75 for the trustee to receive their contribution.

So, if a client has met the work test or WTE and wishes to make an NCC before June 30 then steps 1 and 2 still apply. However, step 3 differs in that if they did not trigger the bring-forward rule in either 2018-19 or 2019-20 and were aged 65 to 74 at 1 July 2020 then the maximum they can contribute is \$100,000 only.

At time of writing, the bring-forward rule had not been extended to clients aged 65 and 66. The Government remains committed to passing this legislation.

NB. The work test and age restriction do **not** apply to downsizer contributions.

But wait ...

From July 1, the CCs cap is increasing to \$27,500 and as the NCCs cap is four times the CCs cap, it is increasing to \$110,000.

With the general TBC increasing, clients may be able to make an NCC next financial year if their TSB at June 30 this year is less than \$1.7 million.

Combining the higher TSB and NCCs cap from July 1 means that if a client did not trigger a bring-forward arrangement in 2019-20 or 2020-21 and their TSB is less than \$1.48 million at 30 June 2021 then they may be able to contribute up to \$330,000. If a client has \$1.48 million to less than \$1.59 million then they may be able to contribute up to \$220,000, otherwise the maximum they can contribute is \$110,000.

Accordingly, if you are looking to get as much money into super as possible for a client, you should consider avoiding triggering the bring-forward rule this financial year by limiting their NCCs to \$100,000, thus giving them the ability to trigger it next year to contribute more.

THINGS TO CONSIDER WHEN MAKING SUPERANNUATION CONTRIBUTION RECOMMENDATIONS

- Ensure a client's salary sacrifice arrangement and/or personal deductible contributions will not exceed their CCs cap.
- Clients earning more than \$263,158 pa receiving SG contributions from two or more employers can ask an employer to stop paying SG for one or more quarters, provided at least one employer continues to make SG contributions. Clients should discuss this with their employer before making any changes.
- Be aware of SG on any bonus payments and bonuses that have been salary sacrificed into super as they count towards the CCs cap. It is worth asking a specific question on bonuses.
- Where the employer pays the administration expenses and/or insurance premiums of the fund, include these payments in the client's CCs cap.
- Businesses need to pay SG (and other contributions) by June 30 to be able to claim a tax deduction in the current year.
- When splitting spouse contributions, the amount split counts towards the contributing spouse's CCs cap – not the receiving spouse's cap. CCs made in 2019-20 must be split before 30 June 2021.
- Check a client's contribution history and TSB for 2020-21 and 30 June 2020 respectively, and for the previous two income years and preceding June 30's. This information allows you to see if the client:
 - is eligible to make CC catch-up contributions,

- is eligible for the WTE,
- has – maybe unknowingly – invoked the NCC bring-forward rule.
- The following contributions are exempt from the contribution caps.
 - CGT cap contributions.
 - Downsizer contributions.
 - Certain contributions made with the proceeds of a qualifying structured settlement, order for a personal injury payment or lump-sum workers' compensation payment.
 - Government co-contributions.
- The work test or WTE must be satisfied **before** making a contribution if a client has turned age 67.
- Consider transferring assets into super via in-specie transfer or realising the asset. If a loss is realised, it can be carried forward to offset any future capital gains. If a gain is realised, this may be offset with a personal deductible contribution, but make ensure client is eligible.
- If an asset is sold and a capital gain realised, make sure where a deductible contribution is being made to offset the gain that it occurs in the same financial year as the asset disposal – date of contract (not settlement) is the crucial date!
- If a client's spouse has total income less than \$40,000, the client may be eligible for a tax offset of up to \$540 for an NCC of up to \$3,000 for their spouse.
- If a client has total income less than \$54,837 with at least 10% of their income coming from employment or business, they may be eligible for a co-contribution of up to \$500 for a personal NCC.
 - Total income is assessable income, reportable fringe benefits, reportable employer super contributions less certain business deductions.

Remember, a contribution is made when the fund receives it and counts towards the client's contribution cap in the year of receipt. Allow sufficient time for funds to be transferred by June 30 if using electronic payment methods – 30 June falls on a Wednesday!

ISSUES WITH PERSONAL DEDUCTIBLE CONTRIBUTIONS

A client may be eligible to claim a tax deduction for a personal contribution. To claim the deduction, the client must lodge an NOI with their fund and have it acknowledged by the trustee. A misunderstanding of the process can lead to the deduction being disallowed and the NCCs cap exceeded.

NOI not completed within required timeframe

To be valid, NOI must be completed by earlier of the time the client lodges their tax return for the year in which they made the contribution, or by June 30 of the following year.

The NOI **must** be completed before any rollover of contributions into another super fund occurs, a lump sum withdrawal is made, or a pension is commenced from the account. Lodging the NOI after any of these events may render it invalid and the tax deduction will be reduced or denied.

Where the NOI requirements are not completed properly:

- the contribution will continue to be an NCC, instead of being a CC
- the client will be ineligible for a tax deduction, and
- the contribution will be assessed against their NCCs cap which may invoke the two or three year bring-forward rule potentially resulting in an excess NCC.

NOI completed but client has insufficient income

The amount a client can claim as a deduction is limited by their level of taxable income – not the CCs cap.

For example, a client can make CCs of up to \$25,000 without issue, but if their taxable income (excluding the contribution) is only \$20,000 then they can only claim a deduction of \$20,000.

Until the date of lodging the tax return or the following June (whichever is earlier), an NOI can be varied. So, the NOI can be varied down to \$20,000. Thus, 15% tax is levied on the \$20,000 only and the remaining \$5,000 is an NCC. Apart from being tax inefficient, it may create issues for the NCCs cap.

Where the client is out of time to make the variation:

- *the \$25,000 contribution remains subject to 15% tax in the fund*
- *counts in full towards the CCs cap*
- *the client is entitled to a tax deduction for \$20,000 only, and*
- *the \$5,000 difference is assessed as an NCC.*

TEMPORARY REDUCTION IN MINIMUM PENSION DRAWDOWN RATES

The Government reduced the minimum pension drawdown rates by 50 per cent for the 2019-20 and 2020-21 financial years as part of the response to the coronavirus pandemic.

Now, this temporary reduction has been extended to the 2021-22 financial year. Accordingly, the minimum pension drawdown rates will remain halved until 30 June 2022. Consequently, clients wishing to continue with a reduced drawdown rate from July 1 may need to act now to reset their pension payments which may otherwise be set to go back up to the normal drawdown rate.

Reduced minimum pension drawdown rates apply to:

- account-based pensions (ABPs)
- transition-to-retirement pensions
- allocated pensions, and
- market linked pensions, e.g. term allocated pensions (TAPs).

Remember, should a client need more income than what the reduced minimum pension drawdown provides, consider taking the excess as a partial commutation to benefit their TBC, but ensure that the documentation – a valid election from the client (as a fund member) – is in place before the payment is made. But be careful doing this with Centrelink clients with grandfathered ABPs who's entitlements are determined under the income test, as partial commutations impact the non-assessable portion – deductible amount – of their pension income and may lead to reduced entitlements.

MAXIMISING TAX-FREE PENSIONS

As you know, the general TBC is increasing from \$1.6 million to \$1.7 million – but everyone will have their own TBC between these amounts.

It could mean a client may be able to get more into a tax-free income stream from July 1 – but it all depends on what they have done up to June 30. The more they have used up of the current \$1.6 million cap before June 30, the less of this increase they'll get.

A client will only benefit from the full \$100,000 increase where they have not transferred any super into retirement phase, nor received a death benefit income stream before July 1. If they've used the entire \$1.6

million TBC, then they get no increase, and they will receive some increase where they've had super in retirement phase but haven't used the full \$1.6 million cap.

Conventional wisdom has it that if a client is eligible to start a retirement phase pension, then they should do so. Generally, the aim is to have money invested in a tax-free income stream as soon as possible. However, with the TBC increasing, it may be worthwhile waiting until after June 30 to commence a pension – or move more money into retirement phase – to have more in the tax-free environment for the long term.

A common strategy for a client wanting the tax break but not the income is to commence a retirement phase pension on June 1 because a pension payment is not required before June 30 and may be delayed even until the end of the following financial year. However, starting a pension on June 1 this year will use up some of the \$1.6 million cap leading to less increase in their TBC. Depending on the value of the pension and other pension(s) a client may have, it could eat up the entire amount resulting in no increase in their TBC.

Accordingly, it may be worthwhile waiting until after June 30 to commence a pension.

If a client has never had a retirement phase pension but wants to start one 'now', you need to determine whether the tax benefits of doing so now are greater than the downside of getting less increase in their TBC.

TIPS TO CONSIDER FOR SELF-MANAGED SUPER FUNDS (SMSFs)

- **Contribution reserving strategy – increasing a client's tax deduction:** An opportunity this financial year arising from the increase in the CCs cap on July 1 involves the 'contribution reserving strategy'. A deduction of \$52,500 – plus any unused cap amounts from 2018-19 and/or 2019-20 – may be available because the second contribution is \$27,500 as it will be tested against the cap in 2021-22. To do this right, the SMSF trustee must resolve to defer the allocation of the contribution until the new financial year and lodge a Request to Adjust Concessional Contributions form with the ATO by the time the fund's annual return and client's tax return are lodged – otherwise it could be treated as an excess contribution.
- **Transferring assets into an SMSF:** Assets must be transferred at an arm's length value, otherwise the difference between the market value and transferred value may be treated as a contribution.
- **Expenses paid on behalf of an SMSF:** All SMSF expenses must be paid directly from the fund's bank account. If for some reason a client has paid a fund expense from their personal account, they should seek reimbursement immediately or the amount will be treated as a contribution to the fund.
- **Loans forgiven or guarantees paid for:** If an SMSF has borrowed under a limited recourse borrowing arrangement and the lender has forgiven part of the loan, or a guarantor has made a payment on behalf of the trustee, this may be treated as a contribution.
- **Certain allocations from reserves:** An allocation from reserve counts towards the member's CCs cap, unless the allocation is **less than 5%** of member's total interest in fund and is done on a fair and reasonable basis to all members – and cannot be allocated to an ABP!
- **Ensure minimum pension paid:** For clients in pension phase, ensure at least the reduced minimum is paid before June 30. If less than the minimum is paid, then generally the pension will lose the tax exemption for the entire year.
- **Before commencing a pension:** Claim all deductions and offset any capital gains with any capital losses because once the pension has commenced there may be no benefit in having any deductions or losses if the fund does not pay tax.
- **Check the value of any in-house assets (IHAs):** If, at the end of the tax year, the level of IHAs of an SMSF exceeds 5% of a fund's total assets, the trustees must prepare a written plan to reduce the market ratio of IHAs to 5% or below. This plan must be prepared before the end of the next tax year. If asset values have fallen to the extent that IHAs may exceed 5%, consider making additional contributions to remain within the allowable limit. However, if an SMSF exceeds the 5% IHA threshold at 30 June 2021, a plan must be prepared and implemented on or before 30 June 2022. The ATO has advised that due to

COVID-19, they will not undertake compliance activity if the rectification plan was unable to be executed because the market has not recovered or it was unnecessary to implement as the market had recovered.

- **Segregating pension assets (SMSFs with no disregarded small fund assets):** If a fund is contemplating selling an asset that has a significant capital gain, consider segregating that asset to a pension, where eligible, as no capital gains tax is payable. However, ensure the purpose of this strategy is to run an income stream. Commencing a retirement phase pension purely to realise a capital gain before commuting it back to accumulation phase is fraught with danger and should not be undertaken.
- **Investment strategy:** An SMSF's investment strategy must be reviewed regularly – at least annually and when circumstances change significantly – to ensure it continues to reflect the purpose and circumstances of the fund and its members, and must take into account:
 - risk and return
 - diversification
 - liquidity
 - the fund's ability to discharge its existing and prospective liabilities, and
 - whether the trustees should provide insurance cover for members.

Ensure the SMSF's investments are consistent with the fund's investment strategy – the two should go 'hand-in-glove'!

NB. SMSF investment strategies have come under the spotlight of the ATO and consequently greater scrutiny from fund auditors, particularly in respect to investment diversification. Accordingly, it is wise to pay close attention to a fund's investment strategy to ensure it is compliant and will not fall short of the ATO's expectations – no one wants a fight on their hands with the ATO!

TIPS TO CONSIDER FOR DISCRETIONARY TRUSTS

- Trustees should ensure resolutions are made **before** the date required in the trust deed – but no later than 30 June – and should prepare written evidence of what was resolved.
- Trustees should ensure resolutions are appropriately drafted. Before resolving to distribute income to individuals and/or entities:
 - the trust's **definition of beneficiary** should be reviewed to confirm the individual/entity falls within the definition
 - the trust's **definition of income** should be reviewed – if streaming certain types of income (e.g. capital gains), ensure the deed provides the power to that stream income and that the intended beneficiaries are made specifically entitled to those amounts.
- To give proper effect to the resolution, trustees should ensure beneficiaries' entitlements are either physically paid by 31 August, or the liabilities due to the beneficiaries are reflected in the records of the trust by this date.
- If the beneficiary is a tax-exempt entity, ensure they are paid their entitlement, or notified of the amount due by 31 August.
- Where the trust has franking credits available for distribution, ensure a Family Tax Election (FTE) is made and the intended beneficiaries are within the defined family group associated with the test individual specified in the FTE.
- Be aware of the TFN withholding rules for closely held trusts – if a beneficiary receiving a payment or distribution has not provided their TFN, the trust may be obliged to withhold and remit to the ATO at the top marginal rate plus Medicare levy.
- Good practice at year-end – confirm the vesting date of trust to ensure the rule against perpetuities is not breached. Generally, a trust cannot exist forever, so if it is an old trust it may be due to vest and the trustee could be unaware of this.

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