

Superannuation UNCOVERING HIDDEN GEMS

A little known and scarcely used tax law could make a huge difference to the legacy left behind by a family business owner. In the summer edition of *FBM*, The Superannuation Death Trap article addressed family businesses that use their self-managed super fund to hold and grow business real property. The key reason for doing this is to take advantage of the tax concessions within super and the opportunity to use those assets to fund a member's pension, tax-free. But if the member dies, the assets revert back to taxable status, creating a large and unwanted tax burden for loved ones.

No one likes paying more tax than they have to, not even multi-billionaires. Kerry Packer, when appearing at the Print Media Inquiry said, "... if anybody in this country doesn't minimise their tax they want their heads read because as a government, I can tell you you're not spending it that well that we should be donating extra". So, in the spirit of these words, let's uncover some hidden gems in the superannuation tax law minefield and find a solution to this problem.

Hidden gem #1

Sell assets with unrealised capital gains after the member starts a pension while the asset is tax-free Superannuation funds holding real property could sell assets with unrealised gains as soon as the business owner starts a pension. This may also be sensible to create liquidity to pay pension benefits.

Hidden gem #2

Pay out the ordinary death benefit along with an additional 'anti-detriment payment' as a lump sum to eligible dependants. When

the Hawke Government introduced a 15% tax on concessional superannuation contributions in 1988, the tax on lump sum payments from super was reduced by a corresponding 15%. At the time, the government argued the contributions tax was really just a 'bring forward' of lump sum payment taxes, rather than a new tax.

The only problem with this argument is that it didn't apply to lump sum death benefits paid to dependants, as these benefits were always paid out tax-free. Therefore the introduction of the 15% contributions tax would in fact be detrimental to dependants without the introduction of adequate compensation – hence the 'anti-detriment payment' was introduced.

How does an anti-detriment payment work?

An additional payment could be made to dependants of a deceased super member to compensate for the effect of contributions tax on the member's balance over their life.

An example of how this would work in practice is:

- Frank ran an auto parts dealership in South Australia. He retired 10 years ago to spend more time with his wife, Carla and his two sons, Stephen and Peter, who took over the business;
- They are all members of the family's self managed super fund, which holds a number of assets relating to the business, including business real property and warehouses acquired freehold 20 years ago;
- Frank's pension is paid from the rental income earned from the properties, which have appreciated considerably in value;
- On Frank's death, the trustee pays out his death benefit of \$2 million to his nominated beneficiary, his wife Carla;



Kerry Packer, when describing tax said, "... as a government I can tell you you're not spending it that well that we should be donating extra". So finding those hidden gems in the minefield of tax law is well worth the effort.

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- As Carla is an 'eligible' beneficiary for anti-detriment purposes, the trustee is permitted to make an additional payment to ensure the amount she receives is the same as it would have been if Frank's super contributions had not been subject to tax. Let's assume the additional amount is \$150,000;
- As a result of the payment, the super fund is entitled to an income tax deduction equivalent to the value of the payment divided by 15%, i.e. \$1 million. The value of this deduction may be used to offset taxable contributions, taxable capital gains and other assessable ordinary fund income. Any unused value of the deduction may also be carried forward to reduce future assessable income.

The effect of this, from the fund's point of view, is that it pays tax on Frank's behalf (on his taxable contributions) over the life of Frank's membership of the fund. When an additional anti-detriment payment is made on his death, the fund obtains an equivalent income tax deduction for the value of Frank's previously assessed contributions.

So, why doesn't everyone take advantage of anti-detriment payments? It's all in the timing, as they say. Because income is assessed early (at the time contributions are paid into the fund) and the deduction is only available much later (after the member dies), the timing mismatch makes the anti-detriment payment strategy largely ineffective as a tax management tool.

Why? Because generally, the deduction comes at a time when there is little or no assessable income to offset. However, in circumstances where the deceased family member is taxed on

their death for the value of unrealised capital gains, anti-detriment payments present a real opportunity to offset assessable capital gains that may occur as a result.

Additionally, because the deduction can be sizeable in some circumstances, the strategy may also be useful in creating a tax-free environment for surviving non-pension members to offset assessable contributions or other fund income.

Can all self managed super funds make anti-detriment payments? There are some basic requirements that must be met before a fund can pay an anti-detriment payment, including:

1. Anti-detriment payments must be specifically provided for in the fund's trust deed;
2. The additional payment must be made as a lump sum in addition to the ordinary death benefit; and
3. Only the deceased member's spouse, former spouse, or children can receive anti-detriment payments.

Like most tax legislation, this is a technically involved strategy, which has strict eligibility criteria, complex formulae and hefty penalties if you get it wrong. If you are considering implementing this strategy in your self managed super fund, it is best you consult with a specialist adviser who understands not only the super tax rules, but also inheritance rules. ●

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CLASSIC KERRY

"I don't want to be left behind. In fact I want to be there before the action starts."

"I've been to the other side, and let me tell you son, there's f...ing nothing there."

"Watch out that greed doesn't eat you up – a person's life does not consist in the abundance of his or her possessions."

"I'm a simple bloke – I only need a couple of hundred grand a year."

"There are two great moments in a man's life. One, when he buys his first yacht. Second, when he sells the thing!"

"Betting is like a disease which is not understood by those who do not have it."