

# Smart strategies for your super 2009



# Make your super count

**Superannuation is still one of the best ways to accumulate wealth and save for your retirement. The main reason, of course, is the favourable tax treatment.**

When you invest in super, earnings are generally taxed at a maximum rate of 15%. A low tax rate means your money can grow faster than investments that are taxed at a higher rate.

Depending on your circumstances, there may be some other great incentives – like claiming a tax deduction for your own contributions or receiving a co-contribution from the Government.

Also, all benefits received from a taxed super fund at age 60 or over will generally be tax-free.

However, to get the most out of superannuation you need to be ‘super smart’. You need to understand how the rules work and use them to your advantage. You also have to keep up with the latest rule changes so you can take appropriate action.

In this booklet, we outline nine clever strategies that could help you achieve your lifestyle and financial goals. Each of these strategies has long-term implications, so by making the right moves now, you may benefit in the future.

This booklet serves as a guide only. To find out if a particular strategy suits your circumstances, we strongly recommend you see a financial adviser.

## **Important information**

The strategies covered in this booklet assume the superannuation fund is a complying fund (see Glossary). The information and strategies provided are based on our interpretation of relevant superannuation, social security and taxation laws as at 15 December 2008. Because these laws are complex and change frequently, you should obtain advice specific to your own personal circumstances, financial needs and investment objectives, before you decide to implement any of these strategies. The investment returns shown in the case studies are hypothetical examples. They do not reflect historical or future returns of any specific financial products.

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# Public offer versus self-managed superannuation

There are generally two types of super funds you could use to meet your living expenses in retirement.

	Public offer superannuation	Self-managed superannuation
<b>The key differences</b>	<ul style="list-style-type: none"> <li>• In a public offer super fund, a corporate Trustee takes care of all the fund's reporting, management, tax and investment responsibilities.</li> <li>• Public offer funds generally suit people who prefer to outsource the management of their super or have smaller account balances.</li> </ul>	<ul style="list-style-type: none"> <li>• A self-managed super fund, also known as a DIY fund, has fewer than five members. Generally all members are Trustees of the fund, and all the Trustees are members. If you set up a self-managed super fund, you take on all the responsibilities of a Trustee.</li> <li>• Self-managed super funds are generally more appropriate for people with larger account balances (upwards of \$250,000) who want to be actively involved in the management of their super.</li> </ul>
<b>The benefits</b>	<ul style="list-style-type: none"> <li>• You don't have to worry about the cost and legal hassle of setting up your own fund, or the ongoing responsibilities of running the fund.</li> <li>• You can choose from a range of managed investment options and in some cases direct shares.</li> <li>• Your investment receives concessional tax treatment.</li> </ul>	<ul style="list-style-type: none"> <li>• Because you're a Trustee of the fund, you can exercise more direct control over the investment strategy.</li> <li>• You have a choice of managed investments, direct shares and private assets<sup>1</sup> such as direct property.</li> <li>• Your investment receives similar concessional tax treatment to a public offer fund.</li> </ul>
<b>Tips and traps</b>	<ul style="list-style-type: none"> <li>• While you can only invest in the options offered by the fund, a broad choice of investment options is usually available.</li> <li>• Because the Trustee makes all the decisions in relation to the management of the fund, you can sit back and relax while someone else does all the hard work. Keep in mind this also means you typically have no say in the way the fund is managed.</li> <li>• Some public offer funds offer reduced management fees for larger account balances.</li> <li>• Most of the strategies in this book can be implemented through a public offer fund.</li> </ul>	<ul style="list-style-type: none"> <li>• The secret to successfully managing your own super fund is to get expert advice. Don't try to do it all yourself.</li> <li>• As Trustee of your own fund, you and the other Trustees are responsible for the administration of the fund and complying with regulatory requirements. This responsibility also applies to any tasks outsourced to third-party service providers.</li> <li>• There are many costs involved in setting up your own fund, including establishment costs, legal costs, ongoing administration costs and investment costs.</li> <li>• There are companies who can help you to set up and administer a self-managed super fund.</li> <li>• Most of the strategies in this book can be implemented through a self-managed super fund.</li> <li>• There are currently over 387,936<sup>2</sup> self-managed super funds in Australia. To find out whether a self-managed super fund is right for you, talk to your financial adviser.</li> </ul>

<sup>1</sup> There are specific restrictions on the types of assets you can acquire in a self-managed super fund. To find out more, speak to your financial adviser.

<sup>2</sup> APRA Quarterly Superannuation Performance – June 2008.

# Strategies at a glance

Strategy	Suitable for	Key benefits	Page
<b>1</b> Boost savings and minimise tax via salary sacrifice	Employees and employers	<ul style="list-style-type: none"> <li>• Pay less income tax</li> <li>• Make a larger after-tax investment</li> </ul>	<b>04</b>
<b>2</b> Divert cashflow from your home loan into super	Anyone with a home loan	<ul style="list-style-type: none"> <li>• Use your cashflow more tax-effectively</li> <li>• Increase your retirement savings</li> </ul>	<b>06</b>
<b>3</b> Grow your super without reducing your income	Anyone aged 55 or older and still working	<ul style="list-style-type: none"> <li>• Benefit from an income stream investment while you are still working</li> <li>• Increase your retirement savings</li> </ul>	<b>08</b>
<b>4</b> Split your way to a better retirement	Couples	<ul style="list-style-type: none"> <li>• Reduce tax on super benefits received before age 60</li> <li>• Retain more of your super</li> </ul>	<b>10</b>
<b>5</b> Invest non-super money in super	Anyone with non-super money	<ul style="list-style-type: none"> <li>• Reduce tax on investment earnings</li> <li>• Increase your retirement savings</li> </ul>	<b>12</b>
<b>6</b> Top-up your super with help from the Government	People who earn less than \$60,342 pa, of which at least 10% is from eligible employment or carrying on a business	<ul style="list-style-type: none"> <li>• Receive a Government co-contribution (up to \$1,500)</li> <li>• Increase your retirement savings</li> </ul>	<b>14</b>
<b>7</b> Contribute to super and offset Capital Gains Tax	Anyone selling an investment who is eligible to make tax-deductible contributions into super	<ul style="list-style-type: none"> <li>• Save CGT</li> <li>• Make a larger after-tax investment</li> </ul>	<b>16</b>
<b>8</b> Purchase Life and Total and Permanent Disability insurance tax-effectively	Employees who are eligible to salary sacrifice, people who are eligible to receive co-contributions, couples where one partner earns a low income and people who are eligible to make personal deductible super contributions	<ul style="list-style-type: none"> <li>• Reduce the cost of insurance premiums</li> <li>• Purchase more insurance cover</li> </ul>	<b>18</b>
<b>9</b> Convert business capital into tax-free retirement benefits	Small business owners planning for retirement	<ul style="list-style-type: none"> <li>• Save CGT</li> <li>• Increase your super benefits</li> </ul>	<b>20</b>

# Strategy 1

## Boost savings and minimise tax via salary sacrifice

**If you're an employee, you may want to sacrifice some of your pre-tax salary, wages or a bonus payment into your super fund.**

### What are the benefits?

By using this strategy you could:

- reduce the tax rate payable by up to 31.5%, and
- make a larger after-tax investment for your retirement.

### How does the strategy work?

Salary sacrifice involves getting your employer to contribute some of your salary, wages or a bonus payment directly into super before tax is deducted at your marginal rate (which could be up to 46.5%<sup>1</sup>).

The advantage of this strategy is that salary sacrifice super contributions are generally taxed at a maximum rate of 15% – a potential tax saving of up to 31.5%.

To use this strategy you need to make an arrangement with your employer that is prospective in nature. In other words, you can only sacrifice income that relates to future performance.

When sacrificing regular salary or wages, the arrangement should commence on the first day to which the next pay period relates.

However, you may only salary sacrifice a bonus payment to which you have no pre-existing entitlement.

In practice, this often means the arrangement must be made no later than the day before your employer determines your bonus entitlement.

In both cases, it's also important to have the agreement thoroughly documented and signed by both parties.

**Note:** Salary sacrifice contributions can't be accessed until you meet a condition of release (see FAQs on page 25).

<sup>1</sup> Includes a Medicare levy of 1.5%.

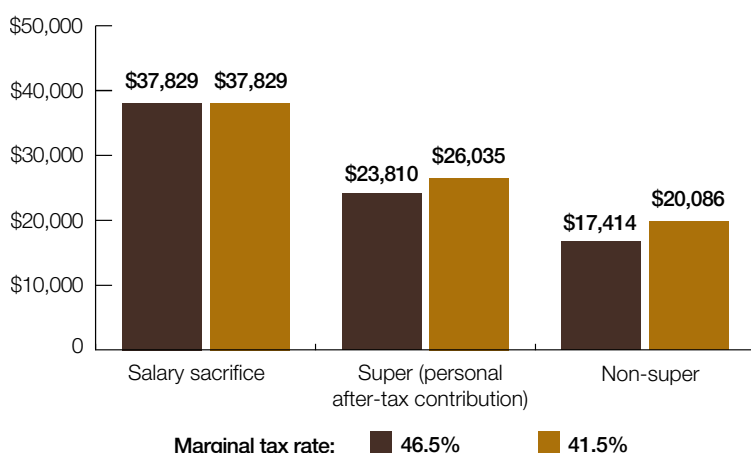
## Case study

**William, aged 45**, receives a salary of \$80,000 pa and anticipates receiving a bonus of around \$10,000. He negotiates with his employer to have any bonus paid directly into his super fund, rather than receiving the money as after-tax salary. This will enable him to invest an additional \$2,650.

	Bonus as after-tax salary	Bonus as salary sacrifice
Pre-tax bonus	\$10,000	\$10,000
Less income tax at 41.5% <sup>1</sup>	(\$4,150)	(N/A)
Less contributions tax at 15%	(N/A)	(\$1,500)
Net amount to invest	\$5,850	\$8,500
<b>Additional amount to invest</b>		<b>\$2,650</b>

If William retires in 20 years at age 65, the higher initial investment (plus a maximum tax rate of 15% on investment earnings) makes salary sacrifice a more powerful strategy than investing the after-tax bonus within super (as a personal after-tax contribution) or outside super. This is confirmed below at William's marginal tax rate of 41.5%<sup>1</sup>, as well as the highest marginal rate of 46.5%<sup>1</sup>.

### The long-term benefits of salary sacrifice (\$10,000 invested over 20 years)



**Assumptions:** A 20-year comparison based on a \$10,000 pre-tax bonus payment. Total return is 8% pa (split 3.5% income and 4.5% growth). The overall franking level on investment income is 30%. All figures are after income tax (at 15% in super and 41.5% or 46.5% outside super) and capital gains tax (including discounting). These rates are assumed to remain constant over the investment period.

**Note:** William pays no lump sum tax on his super benefit in 20 years, as he will be over age 60.

## Tips and traps

- A salary sacrifice arrangement may result in a reduction in other benefits such as leave loading, holiday pay and Superannuation Guarantee contributions, as these benefits are often calculated on your base salary.
- Before you arrange to make salary sacrifice super contributions, you should make sure you don't exceed the concessional contribution cap (see FAQs on page 23).
- It may be worthwhile converting your home loan to interest-only and contributing pre-tax salary into super via salary sacrifice (see Strategy 2).
- If you are aged 55 or over and still working, you may want to sacrifice a portion of your pre-tax salary into super and commence a transition to retirement pension to replace your income shortfall (see Strategy 3).
- If eligible, there may be an advantage in splitting some of your salary sacrifice (or other concessional super) contributions with your spouse (see Strategy 4).
- If you earn less than \$60,342 pa, of which at least 10% is from eligible employment or carrying on a business, you may want to consider making a personal after-tax super contribution. This may enable you to qualify for a Government co-contribution of up to \$1,500 (see Strategy 6).
- Although it is possible to sacrifice salary below the minimum entitlement under an industrial award, employers should be aware they may still be required to provide the minimum salary or wages under industrial law.

# Strategy 2

## Divert cashflow from your home loan into super

**If you're currently making principal and interest home loan repayments, you may want to switch to an interest-only loan and invest more in super.**

### What are the benefits?

By using this strategy you could:

- use your cashflow more tax-effectively, and
- retire with more super to meet your living expenses.

### How does the strategy work?

This strategy involves three key steps.

First, you need to convert your home loan to interest-only. This will reduce your repayments and increase your surplus cashflow<sup>1</sup>.

You then need to arrange with your employer to sacrifice some of your pre-tax salary into your super fund.

This will enable you to use your cashflow more tax-effectively because salary sacrifice super contributions (which are made from your pre-tax salary) are generally taxed in the super fund at a maximum rate of 15% – see Strategy 1.

Conversely, home loan principal repayments are made from your after-tax salary (ie after tax is deducted at your marginal rate of up to 46.5%<sup>2</sup>).

Finally, you need to pay off your outstanding home loan debt (in full) at age 60 or over by making a tax-free withdrawal from your super.

While you will pay more interest over the life of the loan, this strategy could enable you to increase your super and still pay off your home loan by the time you retire.

The results will depend on a range of factors such as your marginal tax rate, the home loan interest rate, the investment returns and your time horizon.

<sup>1</sup> In this context, surplus cashflow is your after-tax income from all sources, less your living expenses and home loan repayments.

<sup>2</sup> Includes a Medicare levy of 1.5%.

## Case study

**Tina, aged 50**, pays tax at a marginal rate of 41.5%<sup>2</sup>. Her home loan is \$250,000 and the current interest rate is 7% pa. She is making the minimum principal and interest repayment of \$2,903 per month over a ten-year term. She is looking to build her retirement savings, but currently doesn't have any surplus cashflow to do this.

If Tina switches to an interest-only loan at an interest rate of 7% pa, her repayment will reduce to \$1,458 per month. This will free-up \$1,445 in cashflow each month and enable her to invest a pre-tax amount of \$2,469<sup>3</sup> per month in super via salary sacrifice.

	Per month
Principal and interest repayment	\$2,903
Less interest-only repayment	(\$1,458)
Surplus cashflow created by refinancing	\$1,445
Pre-tax amount available to salary sacrifice	\$2,469 <sup>3</sup>

The next table shows the value added by this strategy in ten years, after cashing out her super and repaying the debt of \$250,000<sup>4</sup>. By using her cashflow more tax-effectively, Tina has accumulated an additional \$123,069 in super for her retirement, despite paying more home loan interest.

	In ten years
Value of salary sacrifice contributions (including earnings)	\$373,069
Less amount withdrawn from super to repay home loan	(\$250,000) <sup>4</sup>
Net value of salary sacrifice contributions (including earnings)	\$123,069

**Assumptions:** A ten-year comparison. The salary sacrifice super contributions earn a total return of 8% pa (split 3.5% income and 4.5% growth). The overall franking level on investment income is 30%. The home loan interest rate is 7% pa. All figures are after income tax of 15% in super, capital gains tax (including discounting), home loan interest and repayment of the home loan. These rates are assumed to remain constant over the investment period.

<sup>3</sup> The salary sacrifice amount of \$2,469 per month, less tax at her marginal rate of 41.5% (ie \$1,024) is the pre-tax equivalent of her surplus cashflow of \$1,445 per month.

<sup>4</sup> Tina pays no lump sum tax when she cashes out her super in ten years, as she will be aged 60.

## Tips and traps

- Most lending institutions offer interest-only home loans with a choice of fixed or variable interest rates. However, some may charge a fee to refinance your home loan.
- Salary sacrifice super contributions can't be accessed until you meet a condition of release; see FAQs on page 25.
- Before using this strategy, you should ensure your salary sacrifice and other concessional super contributions don't exceed the concessional contribution cap (see FAQs on page 23).
- There may be an advantage in splitting some of your salary sacrifice (or other concessional super) contributions with your spouse (see Strategy 4).
- If you have surplus cashflow before you refinance to an interest only loan, you could use this money to make additional principal repayments, or contribute an equivalent pre-tax amount into super via salary sacrifice. To find out the best option for you, seek financial advice.
- There is a risk that future Governments may restrict lump sum withdrawals from a super fund. This could limit your ability to pay off the loan unless you have other savings.
- You may need to pay lump sum tax if you withdraw money from a super fund prior to age 60 – see FAQs on page 26.

## Strategy 3

# Grow your super without reducing your income

**If you're aged 55 or over, you may want to sacrifice some of your pre-tax salary into a super fund and use a Transition to Retirement Pension to replace your reduced salary.**

### What are the benefits?

By using this strategy you could:

- take advantage of a tax-effective income stream investment while you are still working, and
- build a bigger retirement nest egg without reducing your current income.

### How does the strategy work?

This strategy involves:

- arranging with your employer to sacrifice part of your prospective pre-tax salary directly into a super fund (see Strategy 1)
- investing some of your existing preserved or restricted non-preserved super in a Transition to Retirement Pension (TRP), and
- using the regular payments from the TRP to replace the income you sacrifice into super.

By taking these steps, it's possible to accumulate more money for your retirement, due to a range of potential benefits, including:

- less tax on contributions, as salary sacrifice super contributions are generally taxed at up to 15%, rather than marginal rates of up to 46.5%<sup>1</sup>,
- less tax on investment earnings, as earnings in a TRP are tax-free, whereas earnings in a super fund are generally taxed at a maximum rate of 15%, and
- less tax on income, as the taxable income payments from the TRP will attract a 15% pension offset between age 55 and 59. Also, when you reach age 60, the income stream payments you receive are completely tax-free<sup>2</sup> and you don't have to include these amounts in your annual tax return (which could reduce the tax payable on your non-super investments).

While the magnitude of the tax savings will depend on your particular circumstances, combining salary sacrifice with a TRP could be a powerful pre-retirement strategy.

To find out more about how a TRP works (including the income limits and access restrictions) see FAQs on page 27.

**Note:** This strategy could also be used if you are self-employed (see Glossary). However, rather than making salary sacrifice contributions, you need to make personal deductible super contributions.

<sup>1</sup> Includes a Medicare levy of 1.5%.

<sup>2</sup> Assumes the income stream is commenced from a taxed super fund (see Glossary).

## Case study

**Craig, aged 55**, earns a pre-tax salary of \$90,000 pa and receives 9% Superannuation Guarantee (SG) contributions from his employer. He decides to reduce his pre-tax salary to \$55,000 pa and sacrifices \$35,000 pa into his super fund to build his retirement savings.

To receive the same after-tax income of approximately \$66,000 pa, he commences a TRP and elects to receive taxable income payments of \$27,313 in the first year.

**Note:** Assumes Craig continues to receive 9% SG based on his package of \$90,000 pa, even after he sacrifices \$35,000 pa into his super fund.

	Before strategy	After strategy
Pre-tax salary	\$90,000	\$55,000
TRP income	Nil	\$27,313
Total pre-tax income	\$90,000	\$82,313
Less tax payable	(\$23,350)	(\$15,663) <sup>3</sup>
After-tax income	\$66,650	\$66,650
SG contributions	\$8,100	\$8,100
Salary sacrifice contributions	Nil	\$35,000

While the after-tax income and SG contributions are exactly the same in both scenarios, this strategy has the potential to increase Craig's retirement savings.

This is partly because Craig will invest more money in super each year than he will withdraw from his TRP. For example, in the first year, while Craig will receive an income of \$27,313 from the TRP, he will invest a net amount of \$29,750 in his super fund (ie \$35,000 less 15% contributions tax = \$29,750). That's an extra \$2,437 in the first 12 months alone. Also, earnings in the TRP are tax-free, versus tax at up to 15% applying to earnings accumulating in the accrual phase in super.

If we assume Craig has \$325,000 in super (consisting entirely of the taxable component, see Glossary) and invests this amount in a TRP, the next table shows the value added by this strategy over various time periods. For example, if Craig uses this strategy for the next ten years, he will increase his retirement savings by a further \$97,120.

Value of investments			
After year	Before strategy (super only)	After strategy (super and TRP)	Value added by strategy
1	\$358,175	\$362,789	\$4,614
5	\$519,617	\$546,655	\$27,038
10	\$805,553	\$902,673	\$97,120

<sup>3</sup> Takes into account the Mature Age Worker Tax Offset (see FAQ on page 26).

## Tips and traps

- When using this strategy, you need to consider the following:
  - To replace large salary sacrifice contributions, you may need to invest a significant amount of super in a TRP.
  - The salary sacrifice (and other concessional) super contributions are subject to a cap (see FAQs on page 23).
  - If your SG contributions are based on your reduced salary amount, this strategy could erode your wealth.
- There may be an advantage in splitting some of your salary sacrifice (or other taxable super) contributions with your spouse (see Strategy 4).
- A TRP could also be used to top-up your salary when reducing your working hours.

**Assumptions:** Both the super and TRP investment earn a total pre-tax return of 8% pa (split 3.5% income and 4.5% growth). The overall franking level on investment income is 30%. Salary doesn't change over the ten-year period. Craig receives a tax-free income from the TRP from age 60. Neither the super nor TRP investment are cashed out.

# Strategy 4

## Split your way to a better retirement

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

### What are the benefits?

By using this strategy you could:

- receive your combined super balances in a more tax-effective manner prior to age 60, and
- keep more of your money to meet your living expenses in retirement.

### How does the strategy work?

Splitting some of the concessional super contributions you make (or receive) into your spouse's super account can enable you to accumulate super benefits in two names. As a result, this strategy could enable you to:

- access two low-rate caps (of \$145,000 per person in 2008/09) when making lump sum withdrawals from the taxable component (see case study) and/or
- start two income stream investments (such as an account based pension), where you can take advantage of two sets of personal tax thresholds and the taxable income payments will qualify for a 15% tax offset between age 55 and 59.

Concessional contributions include, but are not limited to:

- employer contributions, including salary sacrifice (see Strategy 1), and
- personal deductible contributions, which can generally only be made if you are self-employed (see Glossary).

The maximum amount you can split in any particular financial year is the lesser of:

- 85% of the concessional contributions you received in the previous financial year, and
- your concessional contribution cap (see FAQs on page 23).

However, if you close your account to commence an income stream or rollover the proceeds to another super provider, some funds may allow you to split up to 85% of the concessional contributions you receive during the financial year up until the point of closure or rollover.

To use a splitting strategy, you and your spouse must be in a married (or de facto) relationship. Also, to receive a contribution split, your spouse must be under 55 years of age or, if between 55 and 64 years, they may need to meet certain conditions (see FAQs on page 25).

## Case study

**Harry, aged 48**, is working full-time and is married to Ruth, aged 47, who is working part-time. They both plan to take their super as a cash lump sum in ten years (ie before either of them reaches age 60). Harry and Ruth currently have \$200,000 and \$10,000 in their respective super funds, consisting entirely of the taxable component.

Given Harry's super already exceeds the low-rate cap on the taxable component of \$145,000 in 2008/09, he arranges to split 85% of his employer's contributions into Ruth's super account in each of the next ten years until she reaches age 57<sup>1</sup>.

At the end of the ten year period, Ruth's super benefit is worth a total of \$135,000. This includes \$100,000 of contributions split into her account and related earnings. Because the total amount of \$135,000 is within the low rate cap, Ruth will pay no lump sum tax when cashing out her benefit<sup>2</sup>.

Conversely, if the \$100,000 in split contributions and related earnings had stayed in Harry's super account, he would have paid tax of 16.5%<sup>3</sup> when received as a cash lump sum before age 60. By using the splitting strategy, Harry and Ruth will save \$16,500 in lump sum tax as a couple.

	If received by Ruth	If retained by Harry
Split contributions and related earnings	\$100,000	\$100,000
Lump sum tax rate payable	Nil	16.5% <sup>3</sup>
Lump sum tax payable	Nil	\$16,500

Given the low rate cap is indexed each year, there is considerable scope for Ruth to accumulate additional tax-free benefits. This could be achieved, for example, if Harry makes salary sacrifice contributions into his super fund (see Strategy 1) and splits up to 85% of these amounts into Ruth's super account.

**Note:** There are other reasons why you might want to use a splitting strategy. These could include to:

- transfer contributions to an older spouse, who will reach age 60 earlier and be able to receive tax-free benefits upon reaching this age
- provide some protection against the legislative risk that a future Government will re-introduce some form of taxation on end super benefits for people aged 60 or over.

<sup>1</sup> Ruth is able to receive the contribution splits between age 55 and 57, as she will still be employed part-time.

<sup>2</sup> Ruth is able to access her super at age 57 as she will have reached her preservation age (see FAQs on page 26).

<sup>3</sup> Includes a Medicare levy of 1.5%.

## Tips and traps

- Not all funds offer splitting and some are not eligible to participate (eg the defined benefit component of any super interest is excluded).
- Funds offering splitting are likely to have their own rules and limits. For example, some funds may limit the split to ensure a minimum account balance remains.
- Certain amounts can't be split. For instance, once contributions have been rolled over to another fund, they cannot be re-directed to your spouse. Also, it's no longer possible to split personal after-tax (and other non-concessional) super contributions into your spouse's account.
- Before you split super contributions, you should determine whether the potential benefits outweigh the costs (including any splitting fees or capital gains tax that may be payable).
- After splitting super contributions, there may be tax or estate planning advantages if you (or your spouse) cash-out and re-contribute a portion of your super benefits before commencing an income stream.

# Strategy 5

## Invest non-super money in super

**If you hold an investment in your own name (outside super) you may want to cash it out and use the money to make a personal after-tax super contribution.**

### What are the benefits?

By using this strategy you could:

- reduce tax on investment earnings, and
- increase your retirement savings.

### How does the strategy work?

When you invest outside super, earnings are generally taxed at your marginal rate of up to 46.5%<sup>1</sup> (see FAQs on page 25).

However, if you cash out the investment and make a personal after-tax contribution, investment earnings in a super fund are generally taxed at a maximum rate of 15%; a potential tax saving of up to 31.5%.

This strategy can be particularly powerful if your money is currently invested in a term deposit or other asset where you don't have to pay capital gains tax (CGT) on the withdrawal.

But even if you have to pay CGT when selling assets like shares, investment properties and unit trusts, the lower tax rate on investment earnings could more than compensate for your CGT liability.

When getting money into super, there is a cap on the amount of personal after-tax and other non-concessional contributions (NCCs) that you can make.

This cap is \$150,000<sup>2</sup> a year (or up to \$450,000<sup>2</sup> in one year if you're under age 65 in that year and meet certain other conditions); see FAQs on page 22.

You should also keep in mind that super benefits are 'preserved' in the fund and cannot be accessed until you satisfy a condition of release (see FAQs on page 25).

**Note:** The results from this strategy will depend on a range of factors such as your marginal tax rate, any CGT payable on the sale of your non-super investment, your timeframe and the investment returns.

<sup>1</sup> Includes a Medicare levy of 1.5%.

<sup>2</sup> These figures apply in 2008/09.

## Case study

**Kate, aged 42**, earns a taxable income of \$80,000 pa. She has a share portfolio worth \$50,000 (including a taxable capital gain of \$10,000<sup>3</sup>) and wants to retire in 20 years.

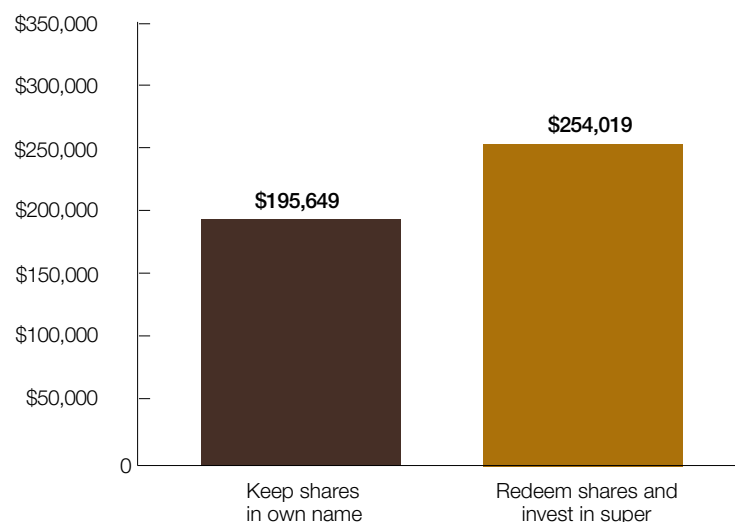
After speaking to her financial adviser, Kate:

- sells the shares
- keeps \$4,150 to pay CGT
- makes a personal after-tax super contribution of \$45,850, and
- invests the super money in a broadly diversified share portfolio.

Even though CGT reduces the amount Kate can invest in super, her investment will be worth an extra \$58,370 when she retires in 20 years when compared to keeping the shares in her own name.

In this example, the lower tax rate on investment earnings in super has compensated for her CGT liability.

### The long-term benefits of investing in super over 20 years



<sup>3</sup> This figure is after the 50% CGT discount (that is available because Kate has owned the shares for more than 12 months) and assumes she has no capital losses to offset her taxable capital gain.

### Tips and traps

- Making personal after-tax contributions could enable you to qualify for a Government co-contribution (see Strategy 6).
- If you meet certain conditions, you may be able to offset the taxable capital gain on the sale of an asset by claiming a portion of your super contribution as a tax deduction (see Strategy 7).
- There are other ways to reduce CGT on the sale of an asset. These could include using capital losses, selling in a low income year or selling the assets progressively.
- Getting non-super money into super could also enable you to receive unlimited tax-free benefits at age 60 or over.
- If you're a member of a self-managed super fund, or discretionary master trust, you may be able to transfer certain non-super investments (such as shares) into super as an *in specie* contribution (see Glossary). However, CGT and stamp duty may be payable.

**Assumptions:** Kate's salary (\$80,000 in year one) is indexed at 3% pa. Both the super and non-super investments earn a total pre-tax return of 8.5% pa (split 4% income and 4.5% growth). Investment income is franked at 75%. All investment income is reinvested. Both investments are cashed-out at the end of the 20-year period. All figures are after income tax (at 15% in super and 41.5% outside super) and capital gains tax (including discounting). These rates are assumed to remain constant over the investment period.

**Note:** No lump sum tax is payable on the super investment, as Kate will be aged 62 at the end of the investment period.

# Strategy 6

## Top-up your super with help from the Government

**If you are a low to middle income earner, you may want to make personal after-tax super contributions.**

### What are the benefits?

By using this strategy you could:

- qualify for a Government co-contribution of up to \$1,500, and
- take advantage of the maximum tax rate of 15% that is payable on super fund earnings.

### How does the strategy work?

If you earn less than \$60,342<sup>1</sup> pa (of which at least 10% is from eligible employment or carrying on a business) and you make personal after-tax super contributions, the Government may also contribute into your super account.

This additional super contribution, which is known as a co-contribution, could make a significant difference to the value of your retirement savings over time.

To qualify for a co-contribution, you will need to meet a range of conditions (see FAQs on page 24). But as a general rule:

- The maximum co-contribution of \$1,500 is only available if you contribute \$1,000 and earn less than \$30,342<sup>1</sup>
- A reduced amount may be received if you contribute less than \$1,000 and/or earn between \$30,342<sup>1</sup> pa and \$60,342<sup>1</sup>, and
- You will not be eligible if you earn \$60,342<sup>1</sup> or more.

The Australian Taxation Office (ATO) will determine if you qualify based on the data received from your super fund (usually by 31 October each year for the preceding financial year) and the information contained in your tax return.

As a result, there can be a time lag between when you make your personal after-tax super contribution and when the Government pays the co-contribution.

If you are eligible for the co-contribution, you can nominate which fund you would like to receive the payment.

Alternatively, if you don't make a nomination and you have more than one account, the ATO will pay the money into one of your funds based on set criteria.

**Note:** Some funds or superannuation interests may not be able to receive co-contributions. This includes unfunded public sector schemes, defined benefit interests, traditional policies (such as endowment or whole of life) and insurance only superannuation interests.

<sup>1</sup> Includes assessable income plus reportable fringe benefits. These thresholds apply in 2008/09 and are indexed periodically.

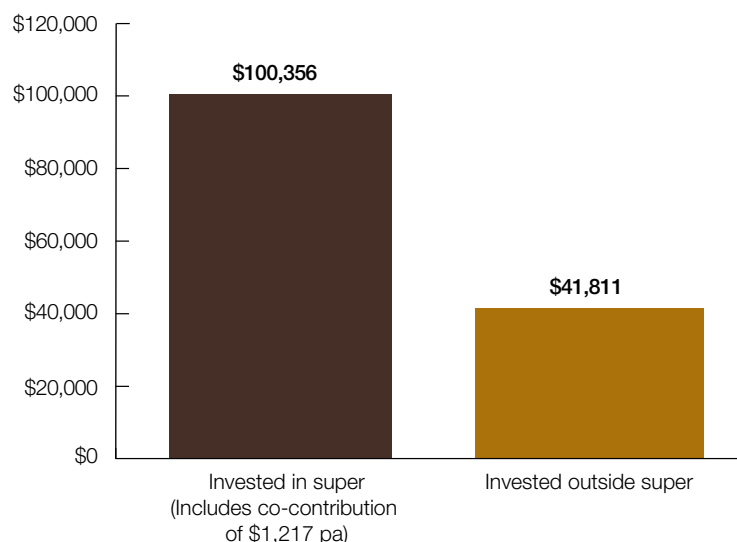
## Case study

**Ryan, aged 40**, is employed and earns \$36,000<sup>1</sup> pa. He wants to invest \$1,000 per year (from his after-tax salary) so he can build his retirement savings.

If he invests the \$1,000 outside super each year (in a unit trust, for example), the earnings will be taxable at his marginal rate of 31.5%<sup>2</sup>. Alternatively, if he invests the money in super as a personal after-tax contribution, the earnings will only be taxed at a maximum rate of 15%, and he will be entitled to a co-contribution of \$1,217 per year.

The graph below compares these two approaches if they are maintained over 20 years until Ryan is age 60. The combined effect of receiving co-contributions and the lower tax rate on investment earnings will make a big difference to his wealth in retirement.

### The long-term benefits of co-contributions (\$1,000 pa in after-tax salary invested over 20 years)



**Assumptions:** A 20-year comparison based on an after-tax investment of \$1,000 pa. The super investment (only) attracts a co-contribution of \$1,217 pa. Total return is 8% pa (split 3.5% income and 4.5% growth). The overall franking level on investment income is 30%. All figures are after income tax (at 15% in super and 31.5% outside super) and capital gains tax (including discounting). These rates are assumed to remain constant over the investment period.

**Note:** Ryan pays no lump sum tax on his super benefit in 20 years, as he will be age 60.

<sup>2</sup> Includes a Medicare levy of 1.5%.

## Tips and traps

- Personal after-tax super contributions (as well as any associated co-contributions) can't be accessed until you meet a condition of release; see FAQs on page 25.
- Make sure you supply your super fund with your Tax File Number so your fund can accept your personal after-tax contributions and the ATO can correctly determine your co-contribution entitlement.
- If you are a higher income earner and you are currently making salary sacrifice contributions (see Strategy 1), your lower income spouse (if applicable) may also want to make a personal after-tax super contribution so they can qualify for a co-contribution. If you have insufficient cash flow to do both, there may be an advantage if you forgo a portion of your salary sacrifice contributions and have your spouse invest the after-tax proceeds into their super account instead.
- If you want to maximise your eligibility for a co-contribution in 2008/09, salary sacrificing into super could enable you to reduce your income below \$60,342 pa (so you qualify for a part co-contribution) or \$30,342 pa (to qualify for a full co-contribution).
- A co-contribution could be used to purchase insurance through a super fund (see Strategy 8). Alternatively, insurance purchased through a super fund may attract a co-contribution that could be used to top-up your super investments or purchase even more insurance cover.
- You could also consider making an after-tax contribution of \$3,000 into a super fund on behalf of your spouse. If they earn less than \$13,800 pa, this may entitle you to a spouse offset of up to \$540 (see FAQs on page 24).

# Strategy 7

## Contribute to super and offset Capital Gains Tax

**When getting non-super money into super, you may want to claim a portion of your contribution as a tax deduction.**

### What are the benefits?

By using this strategy you could:

- reduce, or eliminate, capital gains tax on the sale of the non-super investment, and
- get more money into the concessional tax superannuation system.

### How does the strategy work?

Cashing out a non-super investment, paying capital gains tax (CGT) and using the remaining amount to make a personal after-tax super contribution can be a powerful strategy.

This is because the low tax rate payable on investment earnings in super could more than compensate for your CGT liability (see Strategy 5).

However, if you meet certain conditions, claiming a portion of your super contribution as a tax deduction<sup>1</sup> could enable you to offset your taxable capital gain and reduce (or eliminate) your CGT bill.

While the tax-deductible portion of your super contribution will attract a contributions tax of 15%, you may be able to make a larger super investment and retire with even more money to meet your living expenses (see case study).

To use this strategy you:

- must be eligible to contribute to super (see FAQs on page 22), and
- generally need to receive less than 10% of your assessable income (plus reportable fringe benefits) from eligible employment.

As a result, this strategy is usually only available if you are self-employed or are under age 65 and not employed.

**Note:** The amount of your super contribution you don't claim as a tax deduction will be classified as a non-concessional contribution (NCC). These contributions do not attract the 15% contributions tax in the super fund. However, amounts exceeding the NCC cap are subject to a penalty tax of 46.5%. The cap is \$150,000<sup>2</sup> a year (or up to \$450,000<sup>2</sup> in one year if you're under age 65 in that year and meet certain other conditions) see FAQs on page 22.

<sup>1</sup> Contributions claimed as a tax deduction will count, along with certain other amounts, towards your concessional contribution (CC) cap. In 2008/09, the CC cap is \$50,000 or, if you're aged 50 or over, \$100,000 pa until 30 June 2012. If the cap is exceeded, excess contributions will be taxed at a penalty rate of 31.5%, in addition to the contributions tax of 15%.

<sup>2</sup> These figures apply in 2008/09.

## Case study

**Lisa, aged 42**, is self-employed. Like Kate from Strategy 5, she earns a taxable income of \$80,000 pa, has a share portfolio worth \$50,000 (including a taxable capital gain of \$10,000<sup>3</sup>) and wants to retire in 20 years.

If she sells the shares, she could make a personal after-tax super contribution of \$45,850, after keeping \$4,150 to pay her CGT bill. However, if she claims \$10,000 of her super contribution as a tax deduction, she can offset her taxable capital gain and eliminate her CGT liability.

While the deductible contribution of \$10,000 will be taxed at 15% in the super fund, this strategy will enable her to invest an additional \$2,650 in super.

	Without claiming deduction	With claiming deduction
Value of shares prior to selling	\$50,000	\$50,000
Less CGT payable on sale	(\$4,150)	Nil
Less tax on deductible super contribution	Nil	(\$1,500)
Net super investment	\$45,850	\$48,500
<b>Additional super investment</b>		<b>\$2,650</b>

Let's now compare these two options when she retires in 20 years. By claiming a portion of her super contribution as a tax deduction, and making a larger initial investment in super, Lisa will have an extra \$14,681 to meet her living expenses when she is no longer working.

	Without claiming deduction	With claiming deduction
Value of investment in 20 years	\$254,019	\$268,700

**Assumptions:** Lisa's super is invested in a broadly diversified share portfolio, which earns a total pre-tax return of 8.5% pa (split 4% income and 4.5% growth). Investment income is franked at 75%. All investment income is reinvested. Both investments are cashed-out at the end of the 20-year period. All figures are after income tax and capital gains tax (including discounting). These rates are assumed to remain constant over the investment period.

**Note:** No lump sum tax is payable on the super investment, as Lisa will be aged 62 at the end of the investment period.

## Tips and traps

- This strategy could also be used when selling an investment property, unit trust or other investment where CGT is payable by you.
- To offset a capital gain, the super contribution needs to be made and the tax deduction claimed in the same financial year in which the investment is sold.
- To reduce the tax payable on other income sources (eg from self-employment) you may want to claim more of your super contribution as a tax deduction (subject to the cap on concessional super contributions; see FAQs on page 23).
- While personal after-tax contributions will be received tax-free by all your beneficiaries, in the event of your death, personal deductible contributions will form part of the taxable amount and are generally taxed at 16.5% if received by non-dependants for tax purposes (eg adult children).
- Rather than selling an asset and transferring the proceeds into super, it may be possible to contribute certain qualifying assets into super *in specie* (see Glossary). While the transfer may still result in CGT and stamp duty being payable, the CGT may be offset by claiming a portion of the *in specie* contribution as a tax deduction.

<sup>3</sup> This figure is after the 50% CGT discount (that is available because Lisa has owned the shares for more than 12 months) and assumes she has no capital losses to offset her taxable capital gain.

# Strategy 8

## Purchase Life and Total and Permanent Disability insurance tax-effectively

**If you want to protect yourself and your family tax-effectively, you may want to take out life and total and permanent disability insurance in a super fund, rather than outside super.**

### What are the benefits?

By using this strategy you could:

- reduce the premium costs considerably, or
- purchase a higher level of cover.

### How does the strategy work?

When you buy life and total and permanent disability (TPD) insurances in a super fund, you may be able to take advantage of a range of up-front tax concessions generally not available when insuring outside super.

For example:

- **If you're eligible to make salary sacrifice contributions** (see Strategy 1), you may be able to purchase insurance through a super fund with pre-tax dollars (see case study).
- **If you earn less than \$60,342<sup>1</sup> pa of which at least 10% is from eligible employment or carrying on a business and you make personal after-tax super contributions**, you may be eligible to receive a Government co-contribution (see Strategy 6) that could help you cover the cost of insurance.

- **If you make super contributions on behalf of a low-income spouse**, you may be able to claim a tax offset of up to \$540 pa (see FAQs on page 24) that could be put towards insurance premiums for you or your spouse.
- **If you earn less than 10% of your income<sup>1</sup> from eligible employment (eg you're self-employed or not employed)**, you can generally claim your super contributions as a tax deduction, regardless of whether they are used in the fund to purchase investments or insurance.

These tax concessions can make it cheaper to insure through a super fund, or enable you to purchase a higher level of cover.

Also, due to a recent change in legislation, if you purchase life cover through a super fund, your dependants for tax purposes (such as a spouse or young child) can now receive unlimited tax-free lump sum payments in the event of your death.

This change has made it more attractive to hold larger life insurance policies within the superannuation system.

**Note:** Lump sum tax may be payable when a death benefit is received by a non-dependant for tax purposes (eg an adult child), or a TPD benefit is received by a disabled fund member (see FAQs on page 26). However, to compensate for the potential tax liability, you could consider taking out a higher level of insurance. While this will generally increase the premiums, the after-tax cost may still be lower than insuring outside super, when you take into account the up-front tax concessions.

<sup>1</sup> Includes assessable income plus reportable fringe benefits. Other eligibility conditions apply.

## Case study

**Andrew, aged 38**, earns a salary of \$85,000 pa. He is married with young children, has a large mortgage and needs additional life cover.

In the event of his death, Andrew wants the insurance proceeds to be paid to his wife, so she can use the money to pay off their debts and replace his income. The premium for this additional insurance is \$1,170 pa.

If Andrew takes out the additional life cover through a personal insurance policy (outside super), he will need to pay the annual premium from his after-tax salary. The pre-tax cost will therefore be \$2,000 after taking into account \$830 in tax he would otherwise have to pay on his salary at his marginal rate of 41.5%<sup>2</sup> (ie \$2,000 – \$830 is \$1,170).

After speaking to his financial adviser, Andrew decides to take out an equivalent level of cover through his super fund. He arranges for his employer to sacrifice \$1,170 of his pre-tax salary into his fund and instructs the fund administrator to use this contribution to pay the insurance premiums.

Because super funds receive a tax deduction for insurance premiums, no contributions tax will be deducted from Andrew's super contribution. As a result, he will be able to purchase the insurance through his super fund with pre-tax dollars and make a pre-tax saving<sup>3</sup> of \$830 on the first year's premiums.

	<b>Insurance purchased outside super (with after-tax salary)</b>	<b>Insurance purchased within super (via salary sacrifice)</b>
Insurance premium (pa)	\$1,170	\$1,170
Plus income tax payable on salary at 41.5% <sup>2</sup>	\$830	Nil
Pre-tax cost of insurance	\$2,000	\$1,170
<b>Pre-tax saving<sup>3</sup></b>		<b>\$830</b>

<sup>2</sup> Includes a Medicare levy of 1.5%.

<sup>3</sup> Given Andrew pays tax at a marginal rate of 41.5%, the after-tax saving would be \$486.

## Tips and traps

- Insurance cover, purchased through a super fund is owned by the Fund Trustee who is responsible for paying benefits subject to relevant legislation and the fund rules. When insuring in super, you should be clear on the powers and obligations of the relevant Trustee in respect of paying benefits.
- When making contributions to fund insurance premiums in a super fund, you should take into account the cap on concessional and non-concessional contributions (see FAQs on pages 22 and 23).
- When insuring in super, you can usually arrange to have the premiums deducted from your account balance without making contributions to cover the cost. This can enable you to get the cover you need without reducing your cashflow.
- While critical illness insurance is generally not available within super, it is now possible to purchase income protection (or salary continuance) insurance in super with a choice of benefit payment periods up to age 65.

# Strategy 9

## Convert business capital into tax-free retirement benefits

**If you're aged 55 or over and selling your small business to retire, you may want to take advantage of the CGT Retirement Exemption.**

### What are the benefits?

By using this strategy you could:

- reduce, or eliminate, Capital Gains Tax (CGT) on the sale of your business, and
- get more money into the concessional tax superannuation system.

### How does the strategy work?

To use this strategy, you need to sell active business assets<sup>1</sup> that have been held for less than 15 years.

If eligible (see FAQs on page 23), you then need to claim the CGT Retirement Exemption no later than when you lodge your income tax return for the year in which the business is sold.

This exemption enables you to disregard up to \$500,000 in capital gains and keep more of the sale proceeds to meet your living expenses in retirement.

Finally, if you invest the CGT Retirement Exemption amount in super and elect to have this amount counted towards your CGT lifetime limit, you could potentially get more of the sale proceeds into super without incurring a penalty.

This is because super contributions made under the CGT lifetime limit are specifically excluded from the non-concessional contribution cap of \$150,000<sup>2</sup> a year (or up to \$450,000<sup>2</sup> in one year if you're under age 65 in that year and meet certain other conditions; see FAQs on page 22).

**Note:** If you held the active business assets for 15 years or more, you may be eligible to claim the 15 year CGT exemption (see FAQs on page 23). This exemption could enable you to disregard 100% of the capital gain and take advantage of a higher CGT lifetime limit of \$1,045,000<sup>2</sup>.

<sup>1</sup> Active business assets can include assets such as land and buildings used in producing assessable income, but not necessarily passive assets such as shares.

<sup>2</sup> These figures apply in 2008/09.

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## Case study

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**Jane, aged 64**, owns a business she wants to sell to fund her retirement. She has owned the business for the last ten years and has recently found a buyer who is willing to pay \$800,000 – providing a capital gain of \$700,000.

### Offsetting CGT

By claiming the 50% CGT discount<sup>3</sup> and a CGT Retirement Exemption of \$350,000, Jane is able to offset her taxable capital gain and receive the full sale proceeds of \$800,000 without paying any tax.

Sale proceeds received	\$800,000
Less cost base	(\$100,000)
Nominal capital gain	\$700,000
Less 50% CGT discount <sup>3</sup>	(\$350,000)
Net gain after discount	\$350,000
Less CGT Retirement Exemption claimed	(\$350,000)
<b>Net taxable gain</b>	<b>Nil</b>

### Getting more money into super

Jane also wants to get as much of the sale proceeds as possible into the concessional tax superannuation system. She therefore decides to invest the CGT Retirement amount of \$350,000 in super and notifies her fund that she wants this amount to be counted towards her CGT lifetime limit.

Because the amount claimed under the CGT lifetime limit is excluded from the non-concessional contribution cap (and she is under age 65), she is then able to invest a further \$450,000 in super as a personal after-tax contribution.

By using this strategy, she is able to get the full sale proceeds of \$800,000 into super and use this amount to commence a tax-effective income stream investment to meet her living expenses.

### Tips and traps

- If you're under age 55, you must invest the CGT Retirement amount in super to qualify for the CGT concession. Also, you won't be able to access the money (as a lump sum or income stream) until you meet a condition of release (see FAQs on page 25).
- If your capital gain is large, you may also want to claim the 50% Active Assets Exemption (see FAQs on page 23). If eligible, this exemption could also enable you to reduce a taxable capital gain on the sale of active business assets. However, the amount claimed cannot be counted towards the CGT lifetime limit when invested in super.
- If you use your super to start an income stream investment:
  - No tax will be payable on earnings within the fund,
  - The taxable income payments will attract a 15% tax offset between age 55 and 59, and
  - All income payments received at age 60 or over will generally be tax-free.

<sup>3</sup> If an asset has been held for more than 12 months, individual small business owners (eg sole traders and partners) can elect to be taxed on only 50% of the nominal gain.

# Frequently asked questions

## Who can contribute to super?

Subject to the fund rules, contributions to your super account in 2008/09 are allowed in the circumstances outlined in the following table:

Your age	Allowable contributions
< 65	<ul style="list-style-type: none"><li>Personal contributions, mandatory employer contributions, voluntary employer contributions (including salary sacrifice) and spouse contributions.</li></ul>
65-69	<ul style="list-style-type: none"><li>Personal contributions, voluntary employer contributions (including salary sacrifice) and spouse contributions, provided you have worked at least 40 hours over a consecutive 30 day period during the financial year.</li><li>Mandatory employer contributions.</li></ul>
70-74	<ul style="list-style-type: none"><li>Personal contributions and voluntary employer contributions (including salary sacrifice), provided you have worked at least 40 hours over a consecutive 30 day period during the financial year.</li><li>Mandatory employer contributions.</li></ul>
75 +	<ul style="list-style-type: none"><li>Mandatory employer contributions.</li></ul>

An existing super benefit can be rolled over at any time. You will also need to satisfy these conditions if you want to rollover an employment termination payment (if eligible) or invest the proceeds from the sale of a business in super.

## How much can you contribute to super?

Assuming you are eligible to make contributions, certain caps and limits apply. These include the non-concessional contribution cap, the concessional contribution cap and the CGT lifetime limit. Each of these caps/limits is outlined below.

### What is the non-concessional contribution (NCC) cap?

The NCC cap is a cap that applies to certain super contributions that include, but are not limited to, personal after-tax contributions made and spouse contributions received.

In 2008/09, the cap is \$150,000<sup>1</sup>. However, if you are under age 65, it is possible to contribute up to \$450,000 in 2008/09, provided your total non-concessional contributions in that financial year, and the following two financial years, do not exceed \$450,000.

If the cap is exceeded, excess contributions will be taxed at a penalty rate of 46.5%. Where penalty tax is payable, you must request your super fund to release sufficient benefits to pay the tax.

**Note:** Particular contributions are excluded from this cap. The main ones include:

- certain proceeds from the sale of small business assets up to a CGT lifetime limit of \$1,045,000<sup>1</sup> in 2008/09 (see page 23), and
- settlements received for injuries relating to permanent disablement.

<sup>1</sup> These figures are indexed periodically.

## What is the concessional contribution (CC) cap?

The CC cap is a cap that applies to certain super contributions that include, but are not limited to:

- all contributions from an employer (including salary sacrifice)
- personal contributions claimed as a tax deduction (where eligible), and/or
- Employment Termination Payments rolled over to super between 1 July 2007 and 30 June 2012 exceeding \$1 million<sup>2</sup>.

In 2008/09 the cap is \$50,000<sup>1</sup> or, if you're aged 50 or over, \$100,000 pa until 30 June 2012.

If the cap is exceeded, excess contributions will be taxed at a penalty rate of 31.5%, in addition to a contributions tax of 15%.

Where penalty tax is payable, you will be able to request your super fund to release sufficient benefits, or you can pay the tax out of your non-super money.

## What is the CGT lifetime limit?

The CGT lifetime limit is a limit of up to \$1,045,000<sup>1</sup> that is available to business owners when investing amounts from the following sources in super as a personal after-tax contribution:

- Capital proceeds from the disposal of assets that qualify for the 15 year CGT Exemption (see below), including capital proceeds that would have qualified for the 15 year CGT Exemption except that the disposal did not result in a capital gain or capital loss.
- Capital gains from the disposal of assets that qualify for the CGT Retirement Exemption (see below) up to a limit of \$500,000 per person.

## What CGT concessions are available to small business owners?

Small business owners have a number of CGT concessions available to them. Some can also take advantage of more than one CGT concession.

To qualify for these concessions, small business owners must have net income producing assets (excluding super) of less than \$6 million in 2008/09 (or be subject to the Simplified Tax System) and the assets disposed of must be active assets (eg land, buildings and goodwill) used in producing assessable income.

Where an entity (ie a trust or company) conducts the business, there are further conditions that must be met including the significant individual 20% small business participation percentage test.

There are various concessions available if a small business owner meets the relevant conditions, including the:

- **15 year CGT exemption** – This is a 100% CGT exemption available to all small business owners on the disposal of active assets held for 15 years or more. The assets must have been disposed of for the purpose of retirement, and the small business owner must be at least 55 years of age or incapacitated.
- **50% CGT Active Assets exemption** – This is a 50% exemption available to all small business owners on the disposal of active assets.
- **CGT Retirement exemption** – This is available to all small business owners up to a maximum lifetime limit of \$500,000. If the small business owner is less than 55 years of age, they must invest the proceeds in a super fund. However, if the small business owner is 55 or over, they can take the proceeds as cash, invest in super or purchase an income stream.

**Note:** Other conditions may apply for these concessions.

In addition to the small business concessions, the **50% CGT discount** is available to individuals and beneficiaries of trusts on all assets held for more than 12 months. This exemption is generally utilised before any other concession is claimed.

<sup>2</sup> The \$1 million is reduced by all other transitional Employment Termination Payments received between 1 July 2007 and 30 June 2012 (including those taken in cash).

# Frequently asked questions

## How is your super taxed?

### Tax on contributions

Employer contributions (including salary sacrifice) and personal deductible contributions form part of the super fund's assessable income and are generally taxed at a maximum rate of 15%.

### Tax on investment earnings

The investment earnings of a complying super fund are generally taxed at a maximum rate of 15%. The tax rate payable can be reduced with the use of dividend imputation credits and the CGT discount provisions. The one-third CGT discount means the effective tax rate on realised capital gains is only 10%, where the investments have been held for more than 12 months.

## What tax concessions are available when contributing to super?

### Tax deduction on super contributions

If you earn less than 10% of your income<sup>3</sup> from eligible employment (eg you're self-employed or not employed), you may be eligible to claim a full tax deduction for your super contributions.

However, you should keep in mind that any contributions you are eligible to claim as a tax deduction will count, along with certain other amounts, towards your concessional contribution cap (see page 23).

### Government co-contributions

You may be entitled to a Government co-contribution of up to \$1,500 pa if:

- your assessable income plus reportable fringe benefits is less than \$60,342 in 2008/09
- at least 10% of your assessable income plus reportable fringe benefits is attributable to eligible employment or carrying on a business
- you make personal after-tax contributions to your super account<sup>4</sup>
- you lodge an income tax return
- you are under age 71 at the end of the financial year that the personal superannuation contribution is made, and
- you are not a temporary resident.

The table below outlines the co-contribution you may be entitled to receive if you make personal after-tax super contributions in 2008/09.

Income <sup>3</sup>	Personal after-tax contribution <sup>5</sup>	Co-contribution available
\$30,342 or less	Any amount	Personal contribution x 1.5 (max \$1,500)
\$30,343 – \$60,341	\$0 – \$1,000	An amount equal to the lesser of: <ul style="list-style-type: none"> <li>• Personal contribution x 1.5, or</li> <li>• \$1,500 – [0.05 x (income<sup>3</sup> – \$30,342)]</li> </ul>
\$30,343 – \$60,341	\$1,000 or more	\$1,500 – [0.05 x (income <sup>3</sup> – \$30,342)]
\$60,342 or more	Any amount	Nil

### Spouse contribution tax offset

You may be able to claim a tax offset of up to \$540 pa when you make after-tax super contributions on behalf of your spouse. The amount of the offset will depend on your spouse's income<sup>3</sup> as follows:

Spouse's income <sup>3</sup>	Contribution amount <sup>6</sup>	You can claim an offset of:
\$10,800 or less	\$0 – \$3,000	18% of contributions
\$10,800 or less	\$3,000 or more	\$540 maximum
\$10,801 – \$13,799	Any amount	An amount equal to the lesser of: <ul style="list-style-type: none"> <li>• Spouse contribution x 18%, or</li> <li>• [\$3,000 - (spouse's income<sup>3</sup> - \$10,800)] x 18%</li> </ul>
\$13,800 or more	Any amount	Nil

**Note:** A spouse under the relevant legislation includes a married or de facto spouse, but does not include a partner (married or de facto) who lives in a different home or a same sex de facto spouse before 1 July 2009. The receiving spouse must also be under age 65 or, if between 65 and 70, must have worked at least 40 hours over 30 consecutive days during the financial year.

<sup>3</sup> Includes assessable income plus reportable fringe benefits.

<sup>4</sup> Salary sacrifice amounts do not qualify as personal contributions.

<sup>5</sup> The personal after-tax contributions (but not Government co-contributions) will count towards the non-concessional contribution cap outlined on page 22.

<sup>6</sup> The after-tax super contributions received by your spouse will count towards their non-concessional contribution cap; see page 22.

## Who can split super contributions?

To split super contributions, you and your spouse must be in a married (or de facto) relationship. Also, to receive a contribution split, your spouse must be under 55 years of age or, if between 55 and 64 years, they:

- are currently gainfully employed for 10 or more hours per week
- although not currently employed for 10 or more hours per week, they intend to resume gainful employment for 10 or more hours per week, or
- have never been gainfully employed for 10 or more hours per week.

## What are the current income tax rates?

### Marginal tax rates on income

The following table summarises the tax rates that apply to residents in 2008/09.

Taxable income range	Tax payable
\$0 – \$6,000	Nil
\$6,001 – \$34,000	15% <sup>7</sup> on amount over \$6,000
\$34,001 – \$80,000	\$4,200 + 30% <sup>7</sup> on amount over \$34,000
\$80,001 – \$180,000	\$18,000 + 40% <sup>7</sup> on amount over \$80,000
Over \$180,000	\$58,000 + 45% <sup>7</sup> on amount over \$180,000

**Note:** Changes to the income ranges and marginal tax rates will occur in the 2009/10 and 2010/11 financial years.

### Medicare levy

A levy of 1.5% is payable on the whole of your taxable income on top of normal marginal tax rates. If you earn less than \$17,309 pa (\$29,207 pa combined for couples) you are exempt from the levy. If you earn slightly more than these limits, the levy is phased in. An additional 1% surcharge applies to singles with an income (including reportable fringe benefits) over \$50,000<sup>8</sup> (\$100,000<sup>8</sup> combined for couples plus \$1,500 per dependent child) who have no private health insurance.

## When can you access your super?

Your super can generally be accessed when you meet one of the following conditions of release:

- Retiring after reaching your preservation age (55 to 60; see page 26)
- Leaving your employer after age 60
- Attaining age 65
- Permanent incapacity (specific requirements apply)
- A terminal medical condition where two medical practitioners (one a specialist) certify that the person's condition is likely to result in death within 12 months
- Death
- Severe financial hardship (the amount is restricted and you must have received Commonwealth income support for six months consecutively or nine months cumulatively if aged 55 or over and not gainfully employed at the date of application)
- Compassionate grounds (must be approved by APRA/ATO)
- Upon permanent departure from Australia for certain temporary residents holding a specific class of visa
- Leaving the service of your employer who has also contributed into your super fund; restricted non-preserved benefits only.

A transition to retirement pension (see Glossary) may also be commenced with preserved and restricted non-preserved benefits if you have reached your preservation age (see page 26).

**Note:** You can access unrestricted non-preserved benefits at any time.

<sup>7</sup> These rates do not include the Medicare levy.

<sup>8</sup> The Government proposes to increase these thresholds.

# Frequently asked questions

## What are the preservation ages?

The age at which you can withdraw your super (ie the age at which it's no longer preserved) depends on when you were born. The table below shows the current preservation ages.

Date of birth	Preservation age
Before 1 July 1960	55
1 July 1960 – 30 June 1961	56
1 July 1961 – 30 June 1962	57
1 July 1962 – 30 June 1963	58
1 July 1963 – 30 June 1964	59
1 July 1964 or after	60

## How long can I keep my benefits in super?

You can keep your benefits in the accumulation phase of a super fund for as long as you like.

## What tax is payable when a super benefit is received as a lump sum?

The table below summarises the tax payable in 2008/09 on a lump sum benefit paid from a taxed super fund, including in the event of total and permanent disability but not death (see below).

Component	Tax payable
Tax free	Nil
Taxable:	
• If under age 55	• 21.5% <sup>9</sup>
• If aged 55 to 59	• First \$145,000 <sup>10</sup> is tax-free and rest is taxed at 16.5% <sup>9</sup>
• If aged 60+	• Nil <sup>11</sup>

**Note:** Where you have a tax free and taxable component, each lump sum withdrawal will include both components in the same proportion as these components make up the total interest immediately before the withdrawal.

If a super benefit (including insurance proceeds) is paid as a lump sum in the event of a fund member's death:

- unlimited tax-free amounts can be received by dependants for tax purposes<sup>12</sup>
- the table below summarises the tax payable on the various components by non-dependants for tax purposes.

Component	Tax payable by non-dependants
Tax free	Nil
Taxable:	
• Taxed element	• 16.5% <sup>9</sup>
• Untaxed element	• 31.5% <sup>9</sup>

## What is the Mature Age Worker tax offset?

This offset (with a maximum of \$500) is available if you are 55 years of age and over, and earn taxable income from personal exertion, including salary and wages, business income or personal services income. Taxable income from these sources also needs to be within the following limits in 2008/09:

Taxable income <sup>13</sup>	Offset available
\$0–\$10,000	5% of taxable income <sup>13</sup>
\$10,001–\$53,000	\$500
\$53,001–\$63,000	\$500 – [0.05 x (taxable income <sup>13</sup> – \$53,000)]
\$63,001 or more	Nil

### Example:

If you are 55 years old, with a taxable income from personal exertion of \$57,000 pa, you may be entitled to a tax offset of \$300 – ie \$500 less 5% of (\$57,000 – \$53,000) = \$300.

<sup>9</sup> Includes a Medicare levy of 1.5%.

<sup>10</sup> This low rate cap applies to the total of all taxable components (and post-June 1983 components prior to 1 July 2007) that are taken as cash at age 55 and over, and is indexed periodically.

<sup>11</sup> Lump sum payments received at age 60 or over do not need to be included in your tax return.

<sup>12</sup> Includes a spouse (legally married or de facto), a former spouse, minor children, a financial dependant and a person in an interdependency relationship with the deceased.

<sup>13</sup> From personal exertion.

## What are the benefits of purchasing an income stream with superannuation money?

Rolling over your super to purchase an income stream can provide benefits which aren't available if you take your superannuation as a lump sum. These include:

- Avoiding lump sum tax
- Investment earnings of the income stream accumulate tax-free
- A 15% pension offset on the taxable income payments received between age 55 and 59 (which means it's possible to receive up to \$44,211<sup>14</sup> pa tax-free in 2008/09 while you are in this age group)
- Unlimited tax-free<sup>15</sup> income stream payments at age 60 or over and you don't have to include these amounts in your annual tax return (which could reduce the tax payable on your non-super investments)
- A favourable social security treatment (which could make you eligible for, or increase your entitlement to, the Age Pension and associated benefits).

For further information on the benefits of investing in retirement income streams, see our brochure; Smart strategies for maximising retirement income.

## How are the income payments from a Transition to Retirement Pension (TRP) determined?

The minimum income that must be received each year from a TRP is calculated by multiplying the account balance at the start of the pension (and on 1 July each year) by a percentage that depends on your age; see table below. The maximum amount of income you can receive from a TRP each year is 10% of the account balance, regardless of your age.

Age at start of pension (and 1 July each year)	Minimum % of account balance that must be received
Under 65	4%
65-74	5%
75-79	6%
80-84	7%
85-89	9%
90-94	11%
95 or more	14%

**Note:** An income payment may be deferred until the following financial year where a TRP is commenced between 1 June and 30 June. A pro-rata minimum payment is required if it is commenced before 1 June. The maximum income payment of 10% does not need to be pro-rated.

### Example:

Peter turned 62 in June 2008 and on 1 July 2008 the account balance of his TRP was \$150,000. Based on his age, the minimum income he must receive in 2008/09 is 4% of his account balance, or \$6,000 (ie  $\$150,000 \times 4\% = \$6,000$ ). The maximum income payment he could receive in 2008/09 would be 10% of his account balance, or \$15,000 (ie  $\$150,000 \times 10\% = \$15,000$ ).

## When can you access money invested in a Transition to Retirement Pension (TRP)?

In addition to the income limits outlined above, you can only take a cash lump sum (or purchase a different type of income stream) once you; permanently retire, reach age 65, or meet another condition of release (see page 25). You can, however, transfer the money back to super at any time.

<sup>14</sup> Does not include the Medicare levy.

<sup>15</sup> Assumes the income stream is commenced from a taxed super fund (see Glossary).

# Glossary

## A

**Account based pension** – An account in which you can invest your super savings in exchange for a regular and flexible income.

**Assessable income** – Income (including capital gains) you receive before deductions.

## C

**Capital Gains Tax (CGT)** – A tax on the growth in the value of assets or investments, payable when the gain is realised. If the assets have been held by an individual, trust or super fund for more than one year, the capital gain generally receives concessional treatment.

**Complying super fund** – A super fund that qualifies for concessional tax rates. A complying super fund must meet the requirements that are set down by law.

**Condition of release** – Circumstance upon which you can withdraw your super benefits (see FAQs on page 25).

**Contributions tax** – A tax of 15% applied to personal deductible and employer contributions (including salary sacrifice) made to a super fund.

## D

**Dependant for tax purposes** – Those people eligible to receive unlimited tax-free lump sum payments from a super fund in the event of a fund member's death. Includes a spouse (legally married or de facto), a former spouse, minor children, a financial dependant and a person in an interdependency relationship with the deceased.

**Discretionary master trust** – A type of super fund that offers similar investment flexibility to a self-managed fund without the burden of having to be a Trustee.

**Disposal of asset** – When an asset changes ownership, which can include means other than through sale (eg by gift). Relates to Capital Gains Tax.

## E

**Eligible employment** – Broadly any work that classifies you as an employee for Superannuation Guarantee purposes.

**Employment termination payment (ETP)** – A payment made from an employer to an employee on termination of employment (previously known as an employer eligible termination payment). Only certain ETPs can be rolled over into super.

## F

**Fringe benefit** – A benefit provided to an employee by an employer in respect of the employee's employment. Super contributions made by an employer to a complying super fund are excluded from Fringe Benefits Tax.

**Fringe Benefits Tax (FBT)** – A tax payable by an employer on the taxable value of certain fringe benefits received as an employee. The current rate of tax is 46.5%.

## G

**Gainfully employed** – Employed or self-employed for gain or reward in any business, trade, profession, vocation, calling, occupation or employment.

## I

**Income stream** – An investment that provides a regular income, such as an account based pension or transition to retirement pension.

**In specie contribution** – The contribution of an asset into super rather than cash. It is achieved by transferring ownership of the asset to the super fund. Only certain types of assets can be transferred.

## M

**Mandatory employer contributions** – Super contributions an employer is required to make on your behalf by law. Includes Superannuation Guarantee (SG) contributions and employer contributions required under an industrial award or certified agreement.

**Marginal tax rate** – The stepped rate of tax you pay on your taxable income (see FAQs on page 25).

## P

**Pension offset** – A tax offset of 15% on the taxable income payments received from an income stream purchased with superannuation money between the ages of 55 and 59. The offset is also available before age 60 on death and disability benefits paid as an income stream.

**Personal after-tax super contribution** – A super contribution made by you from your after-tax pay or savings.

**Preservation age** – The age at which you can withdraw your preserved super benefits – between 55 and 60, depending on your date of birth (see FAQs on page 26).

**Preserved benefits** – Benefits that must be kept in the super system and cannot be withdrawn until you meet a condition of release (see FAQs on page 25).

## R

**Restricted non-preserved benefits** – Benefits that can only be withdrawn from the super system when you have met a condition of release (see FAQs on page 25).

**Rollover** – When you move your super benefits directly to a super or rollover fund.

## S

**Salary sacrifice** – An arrangement made with an employer where you forgo part of your pre-tax salary in exchange for receiving certain benefits (eg superannuation contributions).

**Self-employed** – To qualify as self-employed, you need to receive less than 10% of your assessable income, plus reportable fringe benefits, from eligible employment.

**Self-Managed Super Fund (SMSF)** – A super fund with fewer than five members, where generally all members are trustees of the fund and all trustees are members.

**Spouse contribution** – An after-tax super contribution made on behalf of an eligible spouse (see FAQs on page 24).

**Superannuation Guarantee (SG) contributions** – The minimum super contributions an employer is required to make on behalf of eligible employees (generally 9% of salary).

## T

**Tax deduction** – An amount that is deducted from your assessable income before tax is calculated.

**Tax free component** – That part of a superannuation benefit that is received tax-free.

**Tax offset** – An amount deducted off the actual tax you have to pay (eg franking credits).

**Taxable component** – The remainder of a superannuation benefit after allowing for the tax free component. The amount of tax payable on the taxable component may depend on the manner in which the benefit is received (ie lump sum or income stream), the age of the recipient, the dependency status of the beneficiary (death benefits only) and the size of the benefit.

**Taxable income** – Income (including capital gains) you receive after allowing for tax deductions.

**Taxed super fund** – A super fund that pays tax on contributions or earnings in accordance with the standard superannuation tax provisions.

**Transition to retirement pension** – An income stream that can be purchased with preserved or restricted non-preserved super benefits after reaching your preservation age (currently 55).

## U

**Unrestricted non-preserved benefits** – Benefits that have met a condition of release and therefore can be withdrawn from a super fund at any time.

## V

**Voluntary employer contributions** – Include salary sacrifice contributions and contributions made by an employer that are discretionary.



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**MLC also has guides on retirement income streams, wealth protection, debt management and wealth creation.**

**Ask your financial adviser for more details.**



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