SuperGuardian™

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YOUR GUARDIAN

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Shall I transfer my shares to a SMSF?

With the rapidly approaching 30 June deadline for the $1 million un-deducted contribution, many investors are considering whether or not they should transfer their shares to a self managed super fund (SMSF).

It is generally considered that unless at least $150,000 is invested within a self managed super fund, that it will be more expensive than public offer alternatives. Most public offer funds would have an annual management fee of 1 to 1.5% of the fund balance. Given that the average self managed fund might spend $2,000 per annum on accounting and administration costs, this equates in percentage terms if the fund balance was $150,000 (which would represent around 1.3% of the fund balance).

At balances above $200,000 to $300,000, it is possible that a self managed fund will be cheaper to run, as the costs tend to be relatively fixed, rather than based on the fund balance. For example, a fund with $1m invested might pay $10,000 in management fees in a public offer fund, but only $2,000 in accounting and administration fees with a self managed super fund.

The volume of trading activity is also relevant as brokerage costs on sales and purchases of shares need to be included.

The incentive for transferring shares to a SMSF is the low tax rates applicable to income and capital gains made within a super fund. A comparison of tax rates is shown in the table below.

Shares Held	Income Tax	Capital Gains Tax for assets held less than 12 months	Capital Gains Tax for assets held more than 12 months
Via Super Fund	15%	15%	10%
Personally – tax can be up to*:	46.5%	46.5%	23.25%
Via Super Fund in pension phase	Nil	Nil	Nil

** (Note: personal marginal tax rates vary from 0% to 46.5%. Only those with an annual income above $150,000 per annum are subject to tax at the 46.5% rate)*

You can clearly see from the above table the significant tax savings for investors on both income and capital gains that are available when shares are held in a super fund.

Also, from the time a fund starts paying pensions, there is no tax at all on the income from assets used to pay the pension. Even unrealised capital gains that may have accrued over several years within the super fund become tax free!

Once the fund moves into pension phase, a self managed super fund that holds Australian shares has the added bonus of being refunded tax imputation credits by the Australian Taxation Office (ATO). We are the accountants for many self managed superannuation funds that receive a cheque **from** the ATO as a refund of imputation credits. So effectively they are in a 'negative' tax situation!

Transferring Shares to a SMSF

When considering transferring your shareholding to a SMSF, there are certain rules that must be followed, and other important considerations as listed below.

1. **Investment Strategy**

   A self managed super fund must have an investment strategy, and the shares to be transferred into the fund must be consistent with that strategy.

2. **Market value**

   The transfer value must be fair market value. This is easy to determine for listed shares as it will simply be the share value per the market.

3. **Capital Gains Tax**

   The transfer from an individual to a SMSF is a disposal for capital gains tax purposes and hence will potentially give rise to capital gains tax to the individual.

   Whilst this could be a significant amount, it needs to be considered in the light of the future tax savings that will be achieved through holding the shares within the super fund.

4. **Liquidity**

   If the fund is going to be paying pensions, then it must maintain some liquidity. Transferring a 'lumpy' asset such as real estate may cause liquidity issues if the net income from the property is less than the amount of the required pension payment. This is much less of an issue for shares.

5. **Costs**

   Apart from capital gains tax, there are other costs to be considered.

   The cost to set up a SMSF is around $650. The cost to transfer shares will vary depending on your broker. An 'off market transfer' could be around $50 per security.

   You would need to compare the cost and benefits of doing an off market transfer compared to simply selling the shares, transferring the money to the fund, and buying them again in the fund. This would of course attract double brokerage.

   The ongoing cost of managing a SMSF is likely to be around $2,000 to $3,000 per annum (on average), which is likely to be higher than the costs of preparing a tax return for an individual with the same share holdings.

6. **Assets 'Locked In'**

   The super fund tax benefits rely upon the sole purpose of the fund being to fund retirement. Hence one must consider that the income from the portfolio will not be available to spend for living expenses until either retirement or another 'condition of release' is met.

   Full retirement is not necessary – from age 55 a person who is still working can commence to withdraw benefits from a super fund (this is known as a 'transition to retirement' pension).

   (Note – the retirement age of 55 applies to those born before 1/7/1960. For those born after this date, the retirement age will be between 50 & 60, depending on the date of birth).

Can I claim a tax deduction for the value of the shares transferred?

In certain circumstances, an individual can claim a tax deduction for the value of shares transferred into a SMSF. This can be very useful in offsetting any capital gains tax, and potentially can result in a tax deduction against other income. I have set out below an example of how this might operate.

Generally, to claim a tax deduction for the value of shares transferred into a super fund, the person must not have employment income of greater than 10% of total assessable income. The value of the tax deduction claimed cannot exceed maximum deductible contribution limits, which for a person over 50 in this financial year is $105,113.

The balance of the value of shares contributed to the fund over the deductible limit is considered an un-deducted contribution. This cannot exceed a value of $1million in the period 10 May 2006 to 30 June 2007.

Example

Bob has a share portfolio worth $300,000 in his own name, for which the cost base is $200,000. He has other income and his personal marginal tax rate is 41.5%.

Each year the fund generates income of around 4%, which is $12,000, plus imputation credits of a further $5,143.

If Bob held the shares in his own name, the tax payable would be $1,971 on the total income received, after allowing for imputation credits.

If the shares were held in a super fund and the franking credits were available to be refunded to the fund, the tax payable by the fund would be a **refund** of $2,571.

Hence net income after tax would be $4,542 higher if the shares are held via the super fund.

Assume that in five years time the shares have increased in value from $300,000 to $400,000, so that the total capital gain is $200,000 over Bob's original cost price.

If Bob holds the shares personally, and is still on a 41.5% marginal tax rate, the capital gains tax payable at the time of sale would be $41,500 (being 41.5% of half of the gain, allowing for the 50% general CGT discount).

If however they had been transferred to a super fund when they were worth $300,000, then the tax payable by the fund on sale would be no more than $10,000 (being 10% of the gain in the fund of $100,000). Bob would have had to pay $20,750 in capital gains tax to transfer them to the fund initially, but over 5 years he is much better off from a tax point of view having transferred them to the fund.

If Bob claimed a deduction for the super contribution on the initial transfer equal to the taxable portion of the capital gain of $50,000 (after allowing for the 50% discount), then the tax payable on the initial transfer would have only been $7,500 in contributions tax (of 15%), payable by the super fund.

There is even a greater tax saving if, in the period, Bob commences a pension in the super fund.

Of course, this example is based on current taxation law, so there is always the risk that these laws and tax rates will change, but in recent times most of the changes have been favourable.

As you can see, Shares, Tax and SMSFs is a complex area, so expert advice, relevant to your particular situation, is strongly advised.

Disclaimer

SuperGuardian Pty Ltd is not a licensed financial adviser and cannot provide advice in relation to investments or dealing with superannuation balances. SuperGuardian Pty Ltd is limited by legislation to only provide factual taxation and accounting advice. You should obtain independent financial advice that takes into account your personal financial situation.

SMSF Sector is Booming

Australia's DIY superannuation sector is booming, and we're expecting it to get even bigger in the coming months.

New figures from the tax office show that over 5000 SMSFs were established in the September 06 quarter. We've also seen the average assets per member increase as SMSF members make the most of the Government's radical changes to superannuation.

Almost one quarter of Australia's superannuation savings is held in SMSFs.

Further, we expect to see huge inflows of funds into the SMSF sector given the $1 million window for after-tax contributions that was announced in September 2006.

We have been presented with a variety of strategies being formulated by Advisers to maximise this $1 million window.

We recommend that Individuals contact their Advisers/Financial Planners to discuss their personal circumstances and ensure any important contribution strategies are not missed.

The changes to superannuation that take place on 1 July 2007 will have an effect on estate planning strategies – so Advisers and clients are encouraged to re-visit these strategies over the coming months.

Trust Deed Upgrades

We have received many queries from clients as to whether they need to update their trust deeds at this point in time.

As the superannuation legislation has now passed through the Senate, we recommend Trustees seek advice from their Financial Planner or Solicitor as to whether their trust deed requires amendment.

Further information will be forthcoming to SuperGuardian clients.

SuperGuardian Technical Support

We remind Advisers that SuperGuardian has a technical support service relating to compliance/taxation issues affecting self managed super funds.

If you have a strategy you would like to discuss with a SMSF expert, or to discuss a client specific issue, please phone us and we will be happy to provide you with ad-hoc advice free of charge.

For more information relating to this edition of Your Guardian, call **Phil Jaquillard** or **Ed Bernard** of our office on **1300 787 576**.

Adelaide
Level 8, Optus Centre
(cnr South Terrace)
435 King William Street
Adelaide SA 5000

Melbourne
Level 8
350 Collins Street
Melbourne VIC 3000

Sydney
Level 4
95 Pitt Street
Sydney NSW 2000

Postal
GPO Box 1215
Adelaide SA 5001

Tel 1300 787 576 (National)
08 8221 6540 (Adelaide)
Fax 08 8221 6552
Email info@superguardian.com.au

Internet www.superguardian.com.au