

Defined benefit pensions

Despite the rumours, there was no clarification in last weeks Federal Budget on the status of defined benefit pensions ('DBP'). We understand that Treasury has finalised its review of DBPs and advised the Government accordingly. The Government now has to decide on what to do with DBPs. We eagerly await this news.

Superannuation surcharge to cease

The Government will abolish the superannuation surcharge from 1 July 2005. Funds that receive surchargeable contributions or individuals who receive employer termination payments after June 30 2005, will no longer pay surcharge (12.5% for the 2004/05 financial year). For 2004/05, the surcharge applies to individuals with adjusted taxable incomes exceeding \$99,710.

Thus, the tax on deductible superannuation contributions ('DSC') will be a maximum 15% payable by the fund. For someone on the top tax rate in 2005/06 of more than \$95,001 (or \$125,001 for 2006/07), they will obtain an immediate 33.5% tax saving from their DSCs. Naturally, any employer on costs (eg, workcover levy and payroll tax) also need to be considered.

Assuming the person has no pre-July 1983 service period, then that person will generally pay 16.5% tax on any eligible termination payment ('ETP') they receive from their fund. This equates to a total tax on entry and exit of 29% (15% + [85% x 16.5%]). Thus, DSCs now get a total of 29% in entry and exit tax if the ETP is within the person's reasonable benefits limit ('RBL') of \$619,223 for 2004/05.

Where the person's ETP exceeds their RBL (and they only have post-June 1983 service), then the overall tax rate on their super is 48.6% (being 15% + [85% x 39.5%]). While this appears to be close to the top personal tax rate, there is often the ability to accumulate superannuation in a concessional tax environment over a number of years. Note that persons with a pre-July 1983 service period pay tax on exit at 48.5% tax to the extent that their excess relates to their pre-July 1983 service period.

The surcharge status of allocations from reserves may be clarified once the legislation abolishing the surcharge is publicly available. Currently, such allocations are treated in a similar manner to DSCs, apart from certain exceptions. If reserves are no longer subject to the surcharge, then reserving is likely to become more popular.

Current remuneration packaging and salary sacrificing arrangements should be reviewed to determine whether any restructuring is required (eg, fringe benefits subject to FBT may now be less attractive). Taxpayers on the lower tax rates still need to consider whether superannuation is tax effective.

Splitting of contributions with spouse

From 1 July 2006 a person will be able to split both their employer and personal superannuation contributions with their spouse. Under the Government's original proposal in late 2004:

- surcharge was to apply to the spouse seeking to split their contributions. However, surcharge will no longer apply;
- splitting was to apply for the 2004/05 financial year but will now be delayed until mid 2006; and
- splitting by all funds was to be compulsory but will now be optional.

Splitting may enable a spouse to access the tax-free threshold on post-June 1983 ETPs (\$123,808 2004/05).

Choice of fund

Employers now have a three year transitional period (up to 30 June 2008) to comply with the minimum death insurance requirement in their default fund. This will generally apply where the employee has not chosen a fund and the employer continues to contribute to its fund. However, if the employee is covered by a federal award, the default fund under that award generally applies.

Employees should be mindful of the considerable risk that they may be exposed to if they change funds and fail to take out adequate insurance. Often people establishing SMSFs fail to obtain insurance and therefore, their families, may be exposed.

Employers should be mindful not to provide financial advice to employees unless they have an Australian Financial Services Licence.

Super Guarantee ('SG') Changes

The Government will provide an additional 30 days to employers to minimise the risk of SG penalties. The ATO will be empowered to remit the SG shortfall penalty within this additional 30 day period.

We understand that where an employer has overlooked making the relevant contribution within the 28 day deadline (of the end of a particular quarter), that it will be able to seek an offset to their SG shortfall penalty for the amount it contributed to the fund on behalf of the employee. To place the employer in a similar position to the current SG penalty regime, the employer's contribution will not be deductible to the extent it is permitted to offset the SG shortfall penalty.

Unfortunately, this concession is unlikely to be of much practical help as many employers do not realise they have overlooked their SG obligations for at least a number of quarters. It is also out of step with the choice of fund penalty regime where the ATO are empowered to fully remit penalties.

In addition, the definition of 'employee' for SG purposes will be amended to cover a former employee. Under the current definition, employers are only required to make contributions for a current employee. This means that salary paid after the quarter an employee ceases employment is not covered by the SG regime. This change will apply after the legislation is amended.

Superannuation Holding Accounts Special Account ('SHASA')

Employers will no longer be able to use SHASA to meet their SG obligations from 1 July 2006. Currently, employers can make deposits to SHASA for SG contributions. Furthermore, employers will be able to utilise SHASA to meet their choice of fund obligations for the 2005/06 financial year.

Thus, contributions made by an employer to reduce their SG obligations will, from mid 2006, have to be made to a complying superannuation fund or retirement savings account ('RSA'). This will preclude employers from relying on the SHASA system from mid 2006 for both the SG and choice of fund regimes.

SMSF deeds

As usual, DBA's lawyers have revised their documentation for these latest changes. Has your supplier?

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