

ATO and contribution reserving in ATO ID 2012/16

Introduction

ATO ID 2012/16 provides support for contribution reserving.

A contribution reserve holds any unallocated contribution to a fund. The contributions are then subsequently allocated to a member's account. The allocation generally must occur within 28 days after the end of the month in which the contribution is received.

ATO ID 2012/16 — the facts

An SMSF member made a personal contribution of \$25,000 on 28 June 2011. The trustees applied this amount to an 'unallocated contribution account'. On 4 July 2011, the trustees resolved to allocate this amount to a member.

The member was allowed a tax deduction for the \$25,000 in the 2011 financial year. The \$25,000 was counted towards the member's concessional contribution cap in the 2012 financial year (ie, the year of allocation).

ATO reasons in ATO ID 2012/16

The ATO confirmed:

... a contribution does not cease to be made to provide superannuation benefits for a particular person merely because the trustee does not immediately allocate it to the member.

Section 292-25(3) of the *Income Tax Assessment Act 1997* (Cth) includes in concessional contributions an amount allocated in accordance with the conditions specified in the regulations.

Interestingly, the ATO considered that there were two possible sub-regulations in the *Income Tax Assessment Regulations 1997* (Cth) that could have potential application, namely regs 292-25.01(2) and 292-25.01(4).

Broadly, sub-reg (2) covers allocations of concessional contributions that are allocated within 28 days. In contrast, sub-reg (4) broadly covers other amounts allocated from a reserve that count as concessional contributions unless the allocation is fair and reasonable and is less than 5% of each member's superannuation interest in the fund.

The ATO however confirmed that sub-reg (4) does not apply to an amount covered in sub-reg (2) as sub-reg (2) is the more specific regulation (and the specific has priority over the general).

The ATO then had to decide the outcome on the question of whether the same contribution was to be counted twice. As the 28 June 2011 contribution was received in the 2010–11 year it is covered by s 292-25(2) and when that amount was allocated to the member on 4 July 2011, that same amount appears to be also covered by s 292-25(3).

The ATO however adopted the interpretation that avoided double taxation and relied on comments in the explanatory statement to support this construction. The ATO therefore concluded that the \$25,000 amount constituted a concessional contribution in the year of allocation.

This lends tremendous support to the use of contribution reserving as a viable strategy. A contribution reserve can assist in minimising excess contributions tax. There were 45,330 excess concessional contribution assessments issued for 2009–10 (almost a 300% increase from the 15,315 for 2008–09).

How to implement contribution reserving

Trustees should consider whether their current deeds and related documents support reserving. Reserves can be maintained unless prohibited by the governing rules. Nevertheless, out of an abundance of caution, it's always best if the SMSF deed has express power.

Further, a reserving strategy (which is different to an investment strategy) should be in place. Also, trustee resolutions should be in place.

Finally, while ATO ID 2012/16 deals with personal contributions, reserving can also be deployed for employer and non-concessional contributions.

Due to this ATO clarification by the ATO, we now offer a Contribution Reserving Kit.

Contribution Reserving Kit

The kit contains a detailed memo outlining the practical 'how to', pros, cons and inherent risks of contribution reserving as well as template resolutions for those wishing to implement such a strategy. To order the kit, please visit: www.dbalawyers.com.au/strategy-compliance-kits

SMSF deeds and 'auto-reversionary' pensions

Since the release of TR 2011/D3 ('D3'), many query whether their pension will qualify as an 'auto-reversionary' pension. If they don't, then substantial tax concessions are lost. (Our August 2011 news, available from our website, outlines this in more detail.)

Broadly, the ATO considers an auto-reversionary pension exists where the nominated beneficiary will automatically receive the pension following the member's death without the trustee being able to exercise any discretion in this regard.

However, our experience has shown that most SMSF deeds and pension documents provide the trustee with a discretion to revert a pension or not, even if a reversionary beneficiary has been nominated. The SMSF deed is critical here. We have only detected one supplier of SMSF deeds over the past 20 years that expressly provides that the reversionary nomination has priority over the binding death benefit nomination ('BDBN') clause.

Note that we do not consider this to be appropriate as the BDBN should override pension documents. Moreover, a trustee's discretion cannot be limited (or 'fettered') unless there is express power in the deed to do so and Finkelstein J summarised the position succinctly in *Fitzwood Pty Ltd* [2001] FCA 1628 as:

Speaking generally, a trustee is not entitled to fetter the exercise of discretionary power ... in advance ... If the trustee makes a resolution to that effect, it will be unenforceable, and if the trustee enters into an agreement to that effect, the agreement will not be enforced ...

Nevertheless, it is possible to validly fetter a trustee's discretion where the deed or governing rules of the SMSF allow it. See, for example, *Muir* [1966] 1 WLR 1269, 1283.

Thus, for clients without a valid BDBN that requires a pension to be reversionary on the member's death to a specified individual (or, at least, refers to a 'spouse'), many reversionary nominations will not satisfy the ATO's views in D3. In this case, the pension ceases on death (and the pension exemption in the fund up to that time) and the tax free component of the pension may get mixed up with other taxable moneys in the deceased's accumulation account.

The reversionary beneficiary is then required to commence a new pension (should they want a pension), document same and calculate the proportioning rule, etc.

Having said that we eagerly await the ATO's final version of this important ruling and until this is finalised, many client's succession plans that rely on a 'discretionary reversionary nomination' (versus an 'auto-reversionary nomination') remain in doubt.

We offer several solutions including pension kits (revised following D3), SMSF deeds that have express powers to complete a BDBN that overrides a reversionary pension nomination and our 'reversionary nomination' service outlined below.

Ensuring pensions are reversionary

DBA Lawyers offers a 'Reversionary Nomination' service. For a fixed fee, DBA Lawyers will draft documentation to ensure that a pension is reversionary upon death and the tax exemption continues. Please visit www.dbalawyers.com.au/reversionary-pensions

SMSF Online Updates — 20 April 2012 — it's now easy to keep up to date!

DBA Network's webcasts have proved a great success based on client feedback. The second of four SMSF Online Updates for 2012 is on Friday 20 April 2012 from 12 noon to 1.30pm (AEST). The session will cover some hot topics including the latest cases, legislation, regulatory developments and other SMSF tips and traps.

May/June SMSF Strategy Seminars

Our May/June SMSF Strategy Seminars — to be held in seven locations around the country — are just around the corner. For more information or to register visit www.dbanetwork.com.au. Alternatively, contact Marie Zarifis on (03) 9092 9400 or dba@dbanetwork.com.au.

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