

News

April 2006

Our Partners Are Your Partners



Positive Changes For APs And TAPs

Recent improvements announced to retirement income facilities are now law. Allocated pensions (APs) and term allocated pensions (TAPs) are frameworks allowing flexible income streams and withdrawals from superannuation funds – including self managed superannuation funds. The new measures are aimed at helping retirees manage longevity risks – the chance of living longer and outliving the funds – while enabling them to tailor their retirement income needs.

Retaining retirement savings in the tax-free pension environment for longer can enhance the overall net income and estate planning results. The new laws alter some of the measurement criteria from 1 January 2006 and may affect various financial planning decisions including income levels, social security arrangements, tax, and estate planning.

TERM ALLOCATED PENSIONS

Retirees commencing a term allocated pension on or after 1 January 2006 can choose a wider range of terms (the length of the pension). The minimum term will be based on your life expectancy and the maximum term can be based on the number of years until you reach age 100 or your life expectancy as if you were five years younger. Where the pension is reversionary – such that it can be paid to your spouse on your death – a further range of terms may be available based on their life expectancy, someone five years younger than them, or the period until they reach age 100. Often couples will feel comfortable choosing a term based on the primary pensioner's age or life expectancy, knowing that they will retain full estate planning flexibility. Changes to the TAP terms will not apply to TAPs purchased prior to 1 January 2006.

Also from 1 January 2006, the level of annual income paid from a term allocated pension can be smoothed by up to 10% of the calculated annual payment. 10% up or down can significantly increase cash flow flexibility. This applies from the 2006 year onwards and includes TAPs purchased prior to the change.

ALLOCATED PENSIONS

A new set of drawdown factors are employed for allocated pensions commenced on or after 1 January 2006. The factors which are used to calculate the annual minimum and maximum withdrawals have been updated in line with current life expectancy factors reflecting Australians' improved longevity.

Transitional rules will apply from 1 January to 30 June 2006, enabling retirees who commence new APs during this period to choose from either the old or the new factors for the 2006 year. Thus pensions purchased prior to 1 January 2006 must use the old factors and pensions purchased on or after 1 January 2006 must use the new factors from 1 July 2006 onwards.

The new pension valuation factors will not dramatically change the annual level of income. The age at which the maximum drawdown is equal to 100% of the account balance has been pushed out from 80 to 83.

Some retirees may be considering ways to take advantage of the longer terms and the lower drawdown factors. To do this though they will need to commute their existing pension and commence a new one on or after 1 January 2006. For social security purposes, the point at which the age pension kicks in may be delayed due to the prolonged assessment of capital. Such a restructure requires careful consideration however as it will affect future income and cash flows as well as perhaps affecting measurements of Reasonable Benefit Limits, tax, and social security assessments.

These pensions are available within your self managed superannuation fund. It is worth noting that pensions are not just for retirees. In the right circumstances, it is possible to start a pension whilst you are still working. You may even continue contributing to a superannuation fund while at the same time withdrawing benefits. These considerations need to be tailored to your financial circumstances and proper financial advice is important... contact your Sothertons partner.

INSIDE

> More Good Health

> Family Law Issues

AUDIT-AND-INVESTIGATION

ADELAIDE

LITIGATION SUPPORT

CORPORATE-ADVISING

BRISBANE

STRATEGIC PLANNING

FRANCHISING

GLADSTONE

INSOLVENCY

INFORMATION-SYSTEMS

MELBOURNE

SUPERANNUATION-AND-PERSONAL-INVESTMENT

TAXATION

PERTH

Fabricating Deductions

The Administrative Appeals Tribunal has denied deductions for contributions to an employee benefit trust believing they were only paid to gain a tax benefit. The basic premise of tax deductibility is that a deductible amount should be incurred to gain or produce assessable income or carry on a business for that purpose. You can consider any amount paid (or a liability incurred) on this basis may be deductible if it is not ruled out by being purely private in nature or specifically denied elsewhere in legislation.

The Tribunal questioned the motive of the employer making contributions to an employee benefit trust and whether the contributions represented legitimate deductions for income tax purposes. The Tribunal found no evidence to support the proposition that the contributions made to the employee benefit trusts represented outgoings incurred in gaining or producing assessable income or that they were necessarily

incurred in carrying on the employer's business for the purpose of gaining or producing such income.

There have been numerous employee benefit schemes, including non-resident superannuation arrangements, attacked by the Tax Commissioner recently. In some cases it has appeared that the arrangements were designed to circumvent the tax law – in spirit and as it is written. The Tax Commissioner will also attack schemes seen to fabricate or create deductions particularly where there is not even an amount paid to support a deduction. In this case it was held that the contributions served no business purpose and that they were voluntary payments which did not affect the employer's capacity to derive income. It was disputed that the contributions were made to ensure the applicants' loyalty or productivity or as an incentive to continue in their employment – essentially the employer's story was not believed.



The Tribunal believed that the only motivation for making the contributions was the tax savings the employer sought to achieve.

Talk with your Sothertons partner before entering any scheme or arrangement that seems to produce a tax deduction or tax benefit without the necessary requirements to establish deductibility.

20% Medical Expenses Offset

A tax offset (aka 'rebate') is available when your net medical expenses in a financial year exceed the \$1,500 threshold. Once you pass this threshold, the offset available is 20% of the excess spent. The expenses can be summed for the whole family. Expenses paid by resident taxpayers qualify if paid for themselves and/or resident dependants. Medical expenses do not have to be paid in Australia though; expenses paid during an overseas trip may also qualify.

The offset is on your net medical expenses which is the total paid less any amount reimbursed, or eligible to be reimbursed, from Medicare or another government authority, your health insurance fund or another insurance company, or your employer.

The term 'medical expenses' is widely defined and covers payments to hospitals, doctors, nurses, dentists, opticians, and for prescription drugs. In most cases the bill is from a professional with a 'provider number' so it also covers payments for therapeutic treatment and medical or surgical appliances.

Some of the medical expenses that should qualify for the offset are:

- Dentists, orthodontists, registered dental treatments
- Opticians or optometrists, including prescription spectacles or contact lenses
- A carer looking after an invalid, a blind person, or someone who is permanently confined to a bed or a wheelchair
- Therapeutic treatment at the direction of a doctor including massage
- IVF (in vitro fertilization) procedures designed to overcome infertility
- Laser vision correction surgery
- Artificial limbs or eyes and hearing aids
- Keeping a trained working guide dog

The main exclusion is premiums or contributions paid to your health insurance funds. Expenses incidental to obtaining medical treatment, such as travel and hotel expenses are also excluded – even if someone lives in an outlying area and must pay for travel and then accommodation to get treatment. Payments for alternate medicines or cosmetic issues should be investigated – note that solely cosmetic operations, including some dental, where no Medicare benefit is payable under the Health Insurance Act are ineligible.

Tax planning... whilst it is generally better to avoid medical bills, if you have incurred some medical bills you might consider paying them before 30 June if your year to date total is approaching \$1,500 and you wish to include the bills in this year.

Not sure if your treatment qualifies for the offset? Ask your Sothertons partner.

DESK DIARY

"I miss having a luxury to... do you know?
Something to squander money on..."

Billy Connolly – on giving up smoking to please wife Pamela Stephenson

Good Health Important

Since reading the March issue have you spent time on your health? Many of us find ourselves busier than ever and good health is important to be able to deliver good productivity to get everything done. Ideally you need to spend 2 hours a day on your health. This might not be as time-consuming as it first sounds when you break it down into small portions – eating well, resting and relaxing, exercising, and making small efforts throughout the day.

You need to consider various aspects of your life – your diet, the environments you live and work in, and your total lifestyle. These all interrelate as does your attitude to each of the issues. Ultimately your attitude can play a big part as you sacrifice exercise time to work longer hours or sacrifice nutritiously good food to eat fast food on the run. Small improvements to your environment will also help such as correct posture at work, in the car, or at home.

If you want some helpful tips to have a healthy and productive lifestyle:

- Try eating unprocessed foods and certain foods raw – don't cook everything;
- Reduce your coffee and other caffeine intake and if you need an antioxidant increase your intake of tea;
- Eat red meat once a week and review your quantity of dairy products consumed;
- Eat sensible quantities regularly throughout the day – breakfast, morning tea, lunch, afternoon tea and dinner; and make sure they are real foods;
- Cut down on the chemicals you are buying and consuming in your home;
- Smile and breathe deeply – if you are stressed, relax the body to reduce stress; everyone will perform better if you smile;
- Integrate some exercise into your day – stretch, walk, or find something else active you enjoy – get out of the office for a brief stroll;

- Snack on fruit rather than chips or chocolate;
- Keep your fluids up and drink water;
- Learn to stop and slow down... the benefits of meditation and yoga are great.

If you watch all the ads, we were meant to eat red meat, put lamb on the Australia Day BBQ, there are vitamins and fish oil to help, rice is terrific, dairy is good, and so is a pint of Guinness. The message? Moderation and balance is the key – then you can enjoy almost everything.

Remember that only you can look after your health and the risks increase if you wait until tomorrow – you might not make it that far. Small increments in your productivity create room for even more improvements. If you gained half an hour each day you would have two hours spare one afternoon – just think of the extra work you could accomplish before the week is over, or the joy of finishing early to enjoy some more family or fun time. It only takes 5% to make a real difference.

Family Law Property Settlements



When a marriage breaks down, dealing with the emotional as well as the physical separation by both the husband and the wife is an exhausting process. Often the process of finalising orders for spousal maintenance, issues concerning children, and property settlements can take many months and sometimes a number of years. The interested parties and their legal advisers should also take note of another interested party – the Australian Taxation Office.

The focus of lawyers and accountants is initially set by the priorities often determined by the husband or the wife. The main issues at battle usually appear to pertain to custody of children, spousal maintenance, and the valuation of

business and property. These battles nearly always involve arguments about “who gets what? when do I get it? and how much do I get or do I have to pay?”

It is crucial to note the ATO can also have an interest in the outcome. Imagine the drama... thinking it is all over and then being back in the trenches fighting the ATO and their former spouse again. Careful consideration must be given to the transfer of family assets and particularly the transfer of business interests. The ATO has made some effort to exempt the parties to a marriage breakdown from capital gains tax.

Roll-over relief can be afforded to the parties in the property settlement when it comes to the transfer of specified assets subject to the Family Court orders.

However, the process of property settlement often involves complex solutions under very emotional circumstances. These solutions often result in Family Court orders that go well beyond existing tax relief under current legislation. The outcome may be an unexpected tax assessment. The financial expectations of both the husband and wife can be seriously jeopardised unless the tax consequences are properly assessed. Parties who enter into family property settlements where companies and trusts are involved may be assessed by the ATO under various legislation – such as ‘Div 7A’, commercial debt forgiveness provisions, and fringe benefits tax. Both parties need to instruct their legal advisors that property settlements must include the taxation consequences as part of the negotiations.

The separation and divorce of a married couple is a journey with unavoidable emotional impacts. If business and/or property is involved, it is important to know the taxation position before final orders are agreed to or risk an unsympathetic tax assessment. Your Sothertons partner can help.

Did You Know?

A hearse is not designed "mainly for carrying passengers". This means that it is not subject to the car depreciation cost limit. The ATO has announced this in Draft Taxation Determination TD 2006/D10.

Tax law defines a "car" as "a motor vehicle designed to carry a load of less than one tonne and fewer than nine passengers". A hearse would not be a car if designed to carry a load of one tonne or more. However, if a hearse is a "car" pursuant to its load bearing capacity, consideration must be given to whether it is "designed mainly for carrying passengers". Obviously, converting a car into a hearse involves extensive modifications which permanent alter the vehicle and change its inherent design into a vehicle that is not designed mainly for carrying passengers.

If the hearse were a car by definition, its cost for depreciation would be reduced by the amount of any GST input tax credit allowed on the purchase. It sounds obvious but it can be slightly confusing.

The depreciation cost limit of a passenger car purchased in this financial year is \$57,009. If a GST registered taxpayer purchases a car and is allowed the full amount of input tax credit (ie. no private use), the maximum GST credit and the reduction in the cost is \$5,182 being 1/11th of \$57,009. So if the car had a purchase price of \$77,000, the cost would be reduced by the input tax credit of \$5,182 and the acquisition cost of the car would be \$71,818. As this amount exceeds the car limit, the depreciable cost will be held at the car limit of \$57,009.

IMPORTANT: Professional advice should be considered before acting in any area. Clients and readers should not act solely on the material contained in this newsletter which is in the nature of general comments only. Material may or may not be applicable to your particular circumstances and changes in legislation sometimes occur quickly.

For details of each firm's financial planning arrangements and assistance with your financial affairs, please contact your Sothertons partner. Any decision to invest or not to invest should only be made after considering the specific advice of a licensed financial adviser.

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