



T H E H E A L T H W E A L T H S P E C I A L I S T S

“MADA NEWS” MARCH 2007 EDITION

**Suite 13, 828 High Street
Kew Victoria 3101
Phone 03 9819 7308**

**45-47 Addison Street
Elwood Victoria 3184
Phone 03 9531 666**

INTRODUCTION

Welcome to our March of MADA News; the first for 2007!

Our Superannuation Roadshow has attracted great interest and great crowds so far this year (so much so that one of our recent seminars had a waiting list!). Thank you to all attendees and your positive comments regarding this seminar.

If you have any comments in relation to the contents of MADA News, please do not hesitate to contact either Caroline Poon at our Elwood office on (03) 9531 6666 or Michael Waycott at our Kew office on (03) 9819 7308 or email us at caroline@madabayside.com.au; or michael@mada.com.au.

If you feel that this newsletter may be of interest to your colleagues, please feel free to pass it on.

Topics covered

1. Contributions to superannuation – are you using the right entity?
2. Contribution caps – effective from 1 July 2007
3. How do I make a Binding Death Nomination in respect to my Superannuation?

Contributions to superannuation – are you using the right entity?

As the end of the financial year is fast approaching, we thought it would be useful to cover in some detail the technical aspects of tax deductibility for superannuation contributions made in respect of directors, especially directors of private companies and beneficiaries of family trusts where it is claimed that they are employees.

At general law, a director is not an employee. A director is the “mind” of the company rather than one of its “limbs”, that is, the employees. A director is responsible for the overall management of the company while the employees carry out the policy approved by the directors. Accordingly, both the income tax and superannuation guarantee legislation contain deeming provisions which deem directors to be employees in certain contexts.

For the purposes of tax deductibility of superannuation contributions; contributions to a complying fund in respect of “eligible employees” are deductible. “Employee” is defined to mean “a person who is employed by a taxpayer and:

- Is engaged in producing assessable income of the taxpayer; or
- Is a resident of Australia and engaged in the business of the taxpayer.”

Some practitioners mistakenly think that since a director is a deemed employee and the director must be engaged in the producing of assessable income of the company, there should be no problem with the company claiming a deduction for superannuation contributions in respect of the director.

However, there have been some recent private binding rulings (PBRs) which suggest circumstances in which the ATO would disallow deductions in respect of a director. There are others that deal with the situation of whether beneficiaries of family trusts are eligible employees.

It does not follow in all instances that every director of a company is engaged in producing the company’s assessable income, and whether the person is or not is a question to be determined in the light of the facts of each case.

Canberra Income Tax Circular Memorandum No 852 states “...if an investment company merely collects income from a fixed investment portfolio, the services rendered by directors to the company concerned would ordinarily amount to nothing more than the disposition of income after it had been derived. In these instances, superannuation contributions in respect of directors may be regarded as being made for the benefit of employees NOT engaged in producing the company's assessable income”.

Accordingly in this instance directors are not eligible employees and a deduction would be denied. The critical aspect here is the proposition that directors of a

company which is engaged in passive investment activities will not be engaged in producing the assessable income of the company but rather its disposition after derivation.

Apart from investment companies, the same applies for discretionary trusts where the income is merely a trust distribution from a (say) unit trust acting as a service trust. In essence if a trust is not in business and is merely deriving investment income, the beneficiaries cannot be engaged in producing assessable income and thus are not “eligible employees”.

So a blanket statement cannot be made that all company directors (who are deemed employees) are “eligible employees” for superannuation contribution purposes. Each case must be examined and turns on its facts.

Therefore in many instances with group practices; superannuation deductions must be made at unit trust level i.e. practice trust or service trust level if they are to be deductible provided the spouse or person for whom the contribution is made fits the definition of eligible employee i.e. engaged in the business of the entity or engaged in producing assessable income of the entity. They cannot be made at discretionary/family trust level i.e. at unit holder level.

Contribution caps – effective from 1 July 2007

New terminology has arrived! No more undeducted contributions and pre and post 1983.

Concessional contributions

‘Concessional contributions’ is the new term for contributions made by, or on behalf of, an individual that are included in superannuation fund’s assessable income (these are currently referred to as taxable/ deductible contributions).

Excess concessional contributions (i.e. contributions above the annual \$50,000 per person per annual limit) will be taxed at an additional rate of 31.5%, which will be levied on the individual, who must pay the tax to the ATO within 21 days. In this scenario, you can either pay this amount yourself or submit a release authority to your fund. This will subsequently release the required funds to the member or otherwise pay the funds to the ATO directly.

Non-concessional contributions

‘ Non-concessional contributions’ is the new term for contributions made by, or on behalf of, an individual that are not included in the superannuation fund’s assessable income (these are currently referred to as undeducted contributions). This includes concessional contributions in excess of the new concessional contributions cap of \$50,000, but does not include:

- The Government co-contribution
- Contributions relating to personal injury payments
- Contributions from the disposal of small business assets, or
- Roll over amounts from superannuation sources (including ETP annuities).

Non-concessional contributions made during the financial year exceeding \$150,000 will be taxed at the highest marginal tax rate plus Medicare levy. The tax payable will be levied on the individual who must nominate a superannuation fund to release benefits to pay the tax liability, with the balance of the excess contributions remaining in the fund.

Individuals who made non-concessional contributions in excess of the \$ 1 million transitional cap before 7 December 2006 will be able to withdraw these amounts without penalty by applying to the ATO to have the contributions returned prior to 1 July 2007. Individuals who made/make excess non-concessional contributions after 7 December 2006 may be subject to penalty tax.

Importantly, employer contributions made between 10 May 2006 and 30 June 2007 in excess of an employee's current age based limits will be included in your non-concessional cap.

Employment termination payments

Currently, payments made in consequence of termination of employment fall under the banner of eligible termination payments (ETPs). From 1 July 2007 ETPs will no longer exist and will be replaced by 'employment termination payments' and superannuation lump sums. Employment termination payments will cover payments in consequence of termination of employment and not from superannuation funds.

Employment termination payments will have to be paid within 12 months of termination of employment (genuine redundancy payments and approved early retirement schemes are excluded from this requirement). Employment termination payments, with the exception of certain transitional arrangements, will no longer be able to be rolled into superannuation.

Death benefit termination payments

New rules will also apply to death benefit termination payments from employers. A 'death benefit termination payment' is an employment termination payment made to a person following another person's death. Different rules to those applied to superannuation death benefits will be applicable to death benefit termination payments.

How do I make a Binding Death Nomination in respect to my Superannuation?

Binding Death Nominations are not always offered by the Trustees of the Superannuation Fund. However, if a Binding Death Nomination is made the Trustees are bound to pay a person's benefit to their nominated beneficiaries in the amounts and percentages specified in the Nomination.

Binding Death Nominations are important if you have a blended family i.e. have married again and have children from both marriages, etc. You can only make a Binding Death Nomination in favour of the following:

- A Spouse
- Children under 18 who are dependants
- Where an interdependent relationship exists e.g. same sex couples, living with and looking after an ill parent or child
- A financially dependant person
- As per will.

Primary criteria that must be satisfied for a valid Binding Death Nomination include:

- Nominated persons are dependants or a legal representative of the person making the Binding Death Nomination;
- The Binding Death Nomination was signed by the member in front of two witnesses who are over the age of eighteen (18) and independent of the nomination;
- No more than three (3) years have elapsed since the Binding Death Nomination was made (so remember to renew every 3 years); and
- All the members nominated are still eligible to receive the person's benefit (i.e. none of the beneficiaries have passed away etc).

There is no provision in legislation to allow for a Binding Death Nomination to be overturned by the Trustee Board.

The contents of these articles are general in nature and are not advice that applies to any particular client situation. Whilst every care has been taken in preparing the articles, specific advice should be obtained before proceeding with any suggestion or recommendation made

By Caroline Poon and Michael Waycott, Directors, Medical and Dental Accounting Pty Ltd. Note Caroline Poon is also an Authorised Representative of Hillross Financial Services Limited (AFS Licence No. 232705).