KordaMentha

There is no Christmas cheer for this Grinch

Tax Brief

December 2018

As the year draws to a close, I thought that I would provide you with some issues to reflect on over the Christmas break.

Review of your personal financial strategies

I have been delighted with the results of reviews that I have undertaken recently with clients concerning their personal financial management strategies.

The discipline of revisiting taxation and asset succession strategies for clients has resulted in:

1. The simplification of their financial structure.
2. Clarity of taxation and asset succession strategies documented in a formal way that is available for other family members to review and can be revisited and updated annually.
3. Identification of key players providing clients with financial services and credentialising them with other family members.
4. Certainty with respect to the location of the originals of key financial and legal documents.
5. Peace of mind that the transition of the management of one's asset base can take place when a client loses interest in managing their asset base themselves, loses mental capacity to manage it themselves, or passes away.

For those who have not undertaken this exercise, I encourage you to embark on it in the New Year. It can be one of your New Year's resolutions!

Impact of a likely change in Federal Government

Whilst there are no certainties in life, 2019 will most likely see a change in our Federal Government. The Australian Labor Party ("ALP") have made a number of announcements as to proposed tax changes that will impact high net worth individuals.

As with proposed tax changes, the devil is always in the detail.

I thought it appropriate to outline these announcements made by the ALP and what actions (if any) you may consider taking prior to the May 2019 Federal Election. Accordingly, the comments below are predicated on the election of the ALP in next year's Federal Election and the policy announcements made to date being legislated.

Removal of Imputation Credit refunds

Clearly this is the policy that has obtained the most air time in the media.

Under a Labor Government, from 1 July 2019 imputation credits for individuals and superannuation funds would no longer be a refundable tax offset. This means that imputation credits can be used to reduce tax payments, but taxpayers will no longer obtain cash refunds for excess imputation credits.

Labor's policy proposal has so far outlined that it will only apply to individuals and superannuation funds. Income tax exempt charities and Not for Profit institutions with deductable gift recipient status will continue to receive refunds.

Labor's policy is silent on its application to companies who are able to convert unused imputation credits to tax losses.

Possible Actions

The action that you may consider is influenced by the value of your investments inside and outside your Self-Managed Superannuation Fund.

If you have less than $1.6 million per member in your Self-Managed Superannuation Fund and you are currently in Pension mode, then this change will result in an absolute increase in the overall tax rate on the income derived by your Fund.

If you have more than $1.6 million in superannuation, then part of your benefit will be in Accumulation mode.

The income generated on these assets is already suffering a 15% tax charge (or 10% capital gains tax rate).

Post 1 July 2019, if you are generating excess imputation credits in your Self-Managed Superannuation Fund for the year, you would simply trigger a taxable capital gain prior to yearend on your investment assets to soak up the excess. For those with excess imputation credits outside of the superannuation system, again you may consider accelerating a tax liability (e.g. triggering a taxable capital gain) prior to year end to soak up that excess imputation credit.

The real question will be whether the change in this tax policy will adversely impact the equity markets?

In light of this, do you consider reweighting your portfolio to more non-Australian equity investments (e.g. foreign equities, fixed interest, property etc.)?

This is of course an investment decision that you must consider in conjunction with your Investment Advisor.

Change in the tax payable on Trust distributions

This one is certainly quite contentious as many clients utilise discretionary trusts.

The ALP proposal is to apply a minimum tax rate of 30% on discretionary trust distributions to adult beneficiaries beginning 1 July 2019.

Currently, such distributions are subject to tax in the hands of beneficiaries at marginal tax rates. This gives clients the opportunity of apportioning investment income from Trusts and taking advantage of lower marginal rates with beneficiaries with respect to investment income.

The proposal is intended to only apply to Discretionary Trusts and is not proposed to apply to Fixed Trusts or Testamentary Trusts, meaning that asset succession plans for clients utilising Testamentary Trusts can remain on foot.

How this may work

If a trust were to make a distribution to an adult beneficiary, it may need to withhold 30% of the taxable distribution and pay this amount to the Tax Office on lodgement of the trust's annual tax return or upon receipt of an annual tax assessment. The beneficiary who receives the distribution would then get a credit for that tax. If their marginal rate was less than 30% its unlikely they would have this amount refunded.

Impact

If you are currently distributing from a discretionary trust to taxpayers at a rate of tax less than 30% (i.e. taxable incomes less than $87,000) then this change will have a financial impact. It will certainly increase the compliance costs of utilising discretionary trusts.

We may consider altering the ownership of assets for clients who use trusts to hold their investments and distribute income to family members. We may even consider looking at making Discretionary Trusts Fixed Trusts.

The current action for you is to review how you are currently using your discretionary trust so that you can prepare for this possible tax change.

Changes to negative gearing

The ALP proposes that negative gearing would be retained only for new housing and assets acquired prior to a pre-determined date. Investments made before this date would therefore be grandfathered and the new rules not apply. Losses from new investments (e.g. shares, existing properties etc.) will be carried forward to only be offset against any capital gain made on the disposal of that investment. It is proposed that all investments would be looked at in totality enabling gains and losses from investments to be consolidated annually.

Impact

The question of course is what impact this change will have on an already fragile property market?

If you were considering negatively gearing an investment asset, you should consider taking this action before the May 2019 election.

Changes to Capital Gains Tax rates

The ALP proposes halving the Capital Gains Tax discount, which is currently 50% for assets held for more than one year, to a discount of only 25%. It is proposed that the current 33.3% discount for superannuation funds would remain. The change would also only apply to assets acquired after a specific date (i.e. not a retrospective change).

Possible Action

Do you look at increasing your holdings in investment assets pre the May 2019 election to take advantage of this proposed grandfathering?

Superannuation changes

The ALP proposes to lower the annual non-concessional contribution cap from the current $100,000 p.a. to $75,000. It also proposes lowering the high-income Superannuation Surcharge payable on taxable contributions for people who earn over $300,000 p.a. to having this tax apply to taxpayers with an annual income over $200,000 p.a.

Possible Action

If you have less than $1.6 million currently in superannuation you should consider accelerating any non-concessional contributions.

As an asset succession strategy, many clients loan funds to their children to then make non-concessional contributions in their own name. The loan is then offset against distribution of assets on the death of the parent. This may be considered if you have adult children with minimal superannuation balances and can afford to provide them with these funds to make such a contribution.

Limit on tax deductibility of taxation fees

The ALP proposes to limit the tax deductibility of Tax Agent fees to $3000 p.a.

The date of the introduction of this change in the law is uncertain. If you are paying more than $3000 p.a. in taxation fees, you should consider a prepayment of this prior to 30 June 2019.

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Of course, there is a lot of water to go under the bridge between now and the next Federal Election.

Watch this space for election sweeteners by a Federal Government, with a better than expected 2019 budget outcome.

I will keep you abreast of changes as they are announced.

Other tax changes

Use of Private Companies

The current Federal Government has also announced changes to the anti-avoidance provisions applying to loans from, and unpaid present entitlements to, private companies.

No legislation has yet been released, so stay tuned if you are currently using a private company to hold your investments.

Changes to Financial Complaints Body

We now have a new Body dealing with financial complaints with respect to services provided by ASIC Financial Service Licence Holders.

This new Body is known as the Australian Financial Complaints Authority ("AFCA").

For me to provide advice on superannuation strategies I am required to hold an ASIC Licence.

If you have an issue with my advice of course you should contact me directly.

If an issue has not been resolved to your satisfaction, you can lodge a complaint with the Australian Financial Complaints Authority. AFCA provides fair and independent financial services complaint resolution that is free to consumers.

Its contact details are as follows:

Website: www.afca.org.au
Email: info@afca.org.au
Telephone: 1800 931 678
Australian Financial Complaints Authority, GPO Box 3, Melbourne VIC 3001

Strap in for a big 2019!!

Regards

Anthony Jackson