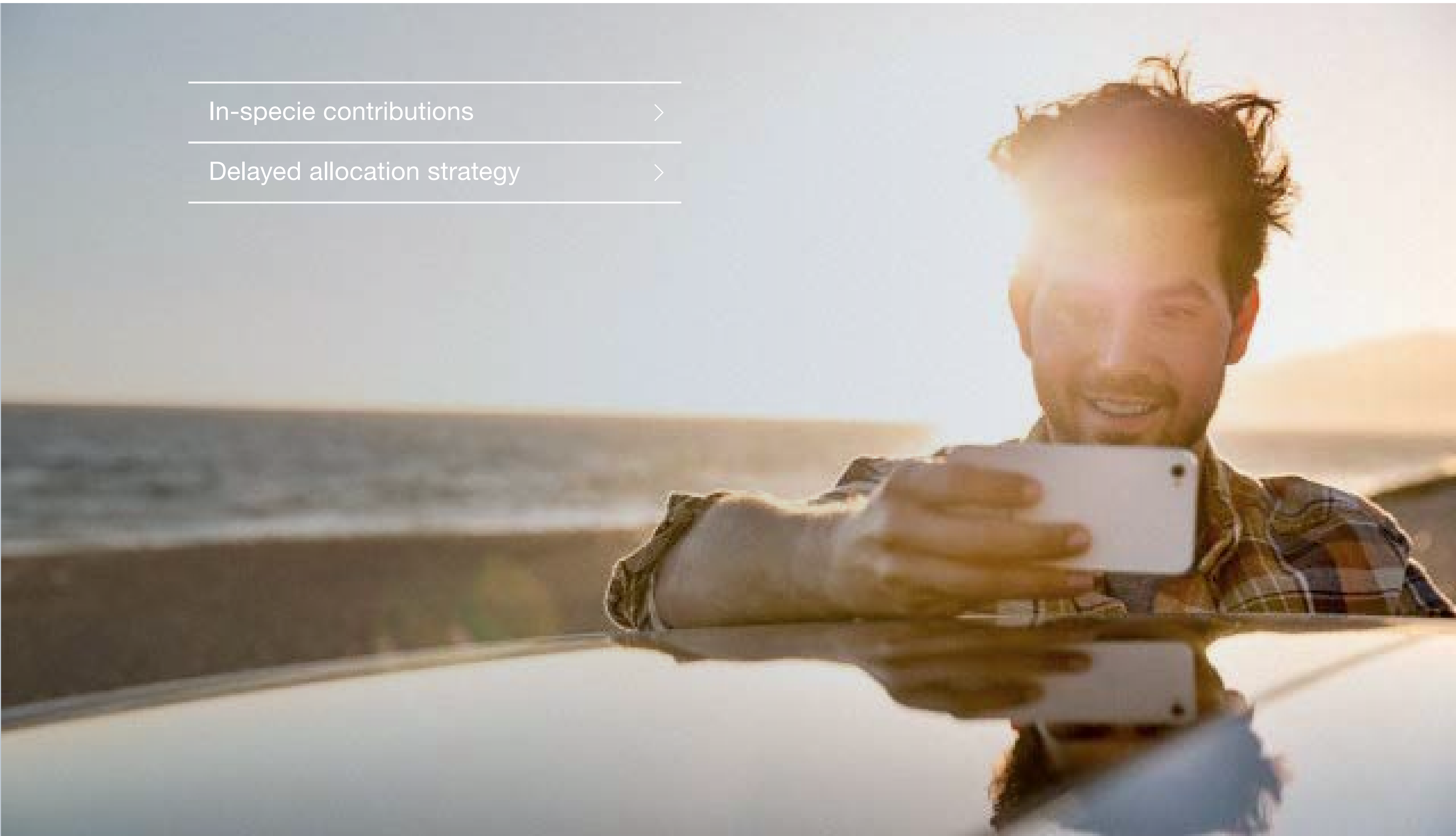
TechKnowledge Adviser

Contributions

SMSFs are generally subject to the same contribution rules as other superannuation funds. However, there are a couple of situations where SMSFs deal with contributions differently to other funds.



SMSF trustee must understand the tax implications of super contributions strategies

In-specie contributions

An in-specie contribution occurs when a member transfers ownership of an asset they own to the SMSF. In this case, the capital value of the fund has increased and the increase in value is considered a contribution for the member whose member balance has grown.

While all superannuation funds can accept in-specie contributions, it occurs far more commonly with SMSFs than with public offer funds. While an in-specie contribution is considered an acquisition from a related party and such acquisitions are generally prohibited, there are enough exceptions to the general prohibition for in-specie contributions to be a valid strategy.

Even though there are a number of such exceptions, the vast majority of in-specie contributions are made using listed shares or business real property. In any case, the transfer will be deemed to be a disposal for the member and any gain realised by the member may be subject to CGT, though there may be some concessions, particularly where the property was used in their own business or that of an associate. Further information on the small business CGT concessions can be found here.

In addition, it is not necessary that the entire value of an asset transferred to an SMSF be considered a contribution and this is particularly beneficial where the value of the asset is greater than the contribution caps available to the contributors.

For example, if a property valued at $700,000 was to be transferred to an SMSF and its entire value was considered a contribution, it could result in an excess non-concessional contribution of $160,000. To avoid this outcome, we could treat $540,000 of the transfer as a contribution using the higher cap available under the 'bring-forward' rules and the remainder as a sale. The SMSF would have to transfer $160,000 of cash or other assets to effect the sale on that portion of the property.

In addition, assets can also be transferred out of the fund as in-specie payments though importantly, only lump sum payments can be made in-specie. Pension payments have to be made in cash. The rules on acquisitions from related parties do not apply to these transactions as the SMSF is disposing of the asset, not acquiring it.

Delayed allocation strategy

The delayed allocation strategy allows an SMSF member to make a concessional contribution and claim a tax deduction this year yet not have the contribution count against this year's concessional cap. Instead, it counts towards next financial year's cap, effectively bringing forward the concessional cap for next year. The ATO's thoughts on the strategy are contained in their Tax Determination 2013/22.

Claim a tax deduction this year but have the contribution count towards next financial year's cap.

In essence, this strategy is allowed by the SIS regulation 7.08 which state that a trustee has until 28 days after the end of the month a contribution is received to allocate that contribution to a member's account unless it is not reasonably practicable to do so. The tax determination looks at the strategy whereby an SMSF Trustee receives a contribution in June and then relies on this regulation to delay allocating it to a member's account until July, the next financial year.

The salient point is that a contribution counts towards the cap in the year it is allocated and therefore, this strategy allows a member to make a contribution in one year and have it count towards the cap of the following year.

There are two categories of benefits to this strategy. Firstly, as the contributor is eligible for a tax deduction in the year the contribution is made, it is possible to have the deduction in an earlier year than the year the cap is used. For example, someone over 60 who was selling their business and didn't expect to have much taxable income in the following year could make two personal deductible contributions of $35,000 in the financial year the business is sold, one of which is made in June. Using the strategy, they could delay allocating the June contribution until July and as a consequence, they are able to get more into superannuation as they wouldn't have had sufficient taxable income in the following year to make a personal deductible contribution.

Further, they're able to claim a $70,000 deduction to offset their high assessable income from the sale of the business. And as they have spread the contributions over two years, they don't have any excess contributions. Importantly, in this situation, they would need to make two separate contributions of $35,000, not a single contribution of $70,000 as the ATO have stated that you can't allocate parts of a contribution separately.

The second category of benefits to the strategy is related to circumventing the age and work based restrictions on making contributions. Regulation 7.04 of the Superannuation Industry (Supervision) Regulations 1994 states 'A regulated superannuation fund may accept contributions only in accordance with the following table...' which means that the contributor must satisfy the contribution restrictions at the time the contribution is made, not when it is allocated.

This distinction would benefit three types of contributors who can make a contribution in June and allocate it in July, thereby using the cap from a year they would be unable to contribute.

Satisfy the contribution restrictions at the time the contribution is made.

1. Individuals no longer working who turn 65 in June where they make the contribution before their birthday.
2. Individuals aged between 65 and 75 who satisfy the work test this year but will not satisfy it next year.
3. Individuals who turn 75 after May. As a contribution can be accepted up the 28th day of the month after the individual turns 75, an individual turning 75 in May could make a contribution up to the 28th of June.

While the determination only covers concessional contributions, the strategy could also work for non-concessional contributions thereby allowing an individual to make non-concessional contributions in a year they otherwise wouldn't be able to. It could also assist with contributing lumpy assets. For example, take an individual with a $720,000 business real property they wish to contribute to their SMSF.

They have a couple of options:

1. Contribute $180,000 of the property this year, so that the individual and the SMSF are tenants in common and then transfer the remaining $540,000 next year.
2. Transfer the whole of the property to the SMSF this year and treat $540,000 as a contribution and $180,000 as a sale.
3. Transfer the whole of the property to the SMSF this year and treat $180,000 as a contribution and $540,000 as a sale, assuming the SMSF has sufficient other assets. The $540,000 received from the fund could then be contributed as a non-concessional in the following year.

However, each of these approaches has issues. Another approach would be to transfer the property to the SMSF in one go in June, with $540,000 as a non-concessional contribution and $180,000 as a sale. The $180,000 proceeds are contributed back to the SMSF and that contribution is allocated immediately.

The $540,000 contribution is then allocated in July resulting in the whole property being contributed in a single year without triggering an excess contribution. Importantly, the reason we need to do $180,000 of the transfer as a sale is due to the fact that we cannot allocate parts of a contribution separately and by doing the sale and re-contribution, we create 2 separate contributions.

The ATO has provided guidance on how this strategy is to be approached administratively. Their preferred method is to have contributions reported in the member contributions statement for the year the contribution is made, not the year it is allocated. They will then issue the member with an excess contributions tax notice and it is up to the member to object to the assessment with evidence that they used the regulations to delay allocating the contribution to the following financial year. For this reason, the strategy would need to be documented robustly.

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