PERSONAL FINANCIAL
STRATEGIES
YOUR PERSONAL GUIDE TO WEALTH CREATION

When marriage fails

When a couple is the only member and trustee of an self managed super fund (SMSF) a marriage breakdown may result in the withdrawal of one party from this fund.

Many married couples in this situation, fail to consider the possible consequences for the funds if their marriage ends in divorce.

In reality, a marriage breakdown among members would be a significant issue for a large number of funds, given that the majority of SMSFs consist solely of a husband and wife or de facto couple as members.

Figures available from the Australia Bureau of Statistics suggest that over 40% of recent marriages will end in divorce. This does not take de facto relationships into account.

When a couple establishes a SMSF, they would typically be focusing on the potential opportunities that an SMSF presents and not considering what would occur if their personal relationship were to end.

The ATO warns that if the relationship of a couple who are the fund's only members fails and one spouse leaves the fund, the remaining member will need to restructure the SMSF. This is a measure to continue meeting the definition of an SMSF under superannuation law. The law also requires trustees to inform the ATO when there are any change in trustee or other details within 28 days of the event occurring.

Apart from whether a fund needs to be restructured, a key concern with the failure of married and de facto relationships is often how fund assets, including illiquid assets, are divided.

Decisions may also need to be made on how a super split will occur, how illiquid assets of the fund will be divided and what the taxation and insurance impacts on the fund and the members are.

Capital gains tax (CGT) rollover relief is available under the specific condition where a CGT asset, reflecting a personal interest of either spouse, is transferred to another complying super fund. This is something that needs to be discussed in detail with a professional adviser to confirm if rollover relief is available.

The consequences of marriage breakdown among SMSF members is a much overlooked issue members should be aware of.

IN THIS ISSUE - NUMBER 12

- When marriage fails
- Borrowing strategies for SMSFs
- Risk for SMSF's holding property
- ATO to expand data matching
- TFN withholding for closely held trusts
- New vs old properties: depreciation issues

BUSINESS WEALTH DEVELOPERS

Q1 Level 2, Suite 1201
4 Daydream Street
Warriewood NSW 2102

PO Box 1693
Warriewood NSW 2102

TEL 02 9997 7646

FAX 02 9997 2696

E-MAIL
vince@bwd.com.au

PARTNER
Vince Carmody

Small Business Tax & Compliance
Self Managed Super Funds

Liability limited by a scheme approved under Professional Standards Legislation.

Borrowing strategies for SMSFs

The Cooper superannuation review's warning that borrowing to invest should not become the "core focus" of self-managed super funds should act as a trigger for many fund trustees to review their practices.

Borrowing to invest through self-managed funds carries traps that could catch unwary trustees, placing a surprisingly high proportion of their retirement savings at risk.

1. Understanding the benefits.

   The main benefit of borrowing through a fund is that assets can be bought that could not have otherwise been afforded given the fund's prior assets and level of contribution. Capital gains are multiplied if the borrowed assets rise in value.

   Furthermore, earnings and capital gains are concessionally taxed within the fund, or are tax-free if they back the payment of a pension. This means that an asset can eventually be sold without ever being subjected to capital gains tax.

   In simple terms, borrowing is a means for funds to increase the size of their assets if limited by the contribution rules. Trustees need to be aware that borrowing may be detrimental to a fund unless the asset increases in value.

2. Understanding the borrowing laws.

   Amendments to the super law have allowed funds to borrow and to invest provided that the borrowing provisions in the legislation are precisely followed.

   The borrowed assets must be held in a trust until the funds pay the final instalment of the loan. In addition, a fund cannot give the lender recourse against the other assets of the fund in the event of a default on the loan.

   More recent amendments require that only a single asset or collection of identical assets may be acquired under a single borrowing arrangement. With property ownership for example, the new rules prohibit multiple titles under one borrowing arrangement even where the properties are effectively managed as a single property.

3. Understanding the risks.

   Lenders often insist on personal guarantees for super fund loans. Under the latest changes to SMSF borrowing rules, related parties of a fund, including its members, can give personal guarantees for loans to the fund. However, under these amendments, guarantors cannot pursue their funds in the event of a default or shortfall in repayments.

   The change in the law means that the personal assets of members of a SMSF can become placed at risk.

Risks for SMSFs' holding property

The ATO has issued a warning that a SMSF holding property could be sued if someone is injured or dies due to faults in that property.

The ATO has provided a recent example of a property owner being held liable for the death of an trades-person whilst he was replacing an old solar hot water system on the premises.

Trustees that hold property in an SMSF should ensure they are aware, to the best of their ability, of any hazards on their property. If any hazards do exist, they should have them dealt with appropriately.

In addition, trustees should also consider having an insurance policy in the SMSF to cover the property for any public liability that may exist.

In the case of the property being acquired with a limited recourse borrowing following new borrowing laws, the ATO has suggested that trustees should seek professional advice on the requirements of holding any insurance.

For more information, consult you accountant or financial advisor.

ATO to expand data matching

The ATO is taking its data matching processes to the next level with plans to match over 220 million records this year.

Motor Vehicles

Although the ATO has previously focused on luxury cars, it will now target a much larger group of taxpayers. The ATO is seeking data from Government authorities on every vehicle sale, transfer or registration between 1 July 2009 and 30 June 2010. The data search is limited to vehicles with a market value of greater than $10,000.

The ATO are looking to identify:

- businesses that sell vehicles and fail to report or under report those sales.
- Any use of business cash to conceal a transaction value. They will determine whether a taxpayer's income was sufficient to support the purchase of the vehicle.

Business property

The investigation of the property sector is even greater. The ATO will ask state authorities for details of every property title transfer between 1 July 1999 and 30 June 2010.

Data will be matched against taxpayer records to identify tax cheats by targeting those people who may have incorrectly reported or failed to include capital gains tax, income or GST in their income tax and business activity statements.

In addition to using government records, the ATO's data matching program will expand into areas as diverse as online selling, luxury goods, banking and share ownerships.

TFN withholding for closely held trusts

The Tax File Number (TFN) withholding rules now apply to closely held trusts, including family trusts, from 1 July 2010.

Under the new rules a TFN withholding obligation, at a rate of 46.5%, will occur where an affected beneficiary:

- receives a distribution from an affected trust.
- is presently entitled to a share of the income of the trust at the end of the income year.
- has not quoted their TFN to the trustee before the making of the distribution or becoming entitled to a share of the income of the trust.

Affected beneficiaries

The new measures generally apply in respect of distributions and present entitlements to income for all beneficiaries of closely held trusts and family trusts. Not all categories of beneficiaries are subject to the TFN withholding rules. These exclusions are:

- Distributions to beneficiaries who are non-residents or exempt from income tax.
- Distributions outside of the "family group". These distributions are instead subject to trust distribution tax.

Beneficiaries who have amounts withheld from distributions under the TFN withholding rules can claim a credit for these amounts in their tax return.

Where amounts have been withheld, the trustee must lodge a detailed annual report to the ATO no later than three months after the end of the income year. The amounts withheld must be remitted to the ATO by the 28th day following the month in which the annual report is due to the Commissioner.

Reporting requirements

The Bill also introduces a reporting regime which requires trustees to:

- report any TFNs quoted by affected beneficiaries to the ATO on a quarterly basis.
- lodge an annual report with the ATO detailing where amounts have been withheld.
- issue payment summaries to affected beneficiaries.
- report to the ATO the amounts distributed to beneficiaries and amounts payable.

New vs old properties: depreciation issues

Many property investors assume it is not worth looking at depreciation rates for older properties. While it is true that newer properties may have more deductions available than older properties, it is always worth considering the depreciation potential of an older property. This is typically done in conjunction with a quantity surveyor.

New Properties

Owners of new investment properties may be eligible to claim depreciation on the building structure and the fixtures and fittings in their property.

The effective life of a new building for ATO purposes is 40 years (some exceptions apply). This means a brand new property is able to claim the entire construction cost over the life of the property.

Properties that are not brand new can claim the residual of the 40 years. For example, if an investment property is 5 years old and its owner wants to claim depreciation on the structure they have 35 years left of deductions to claim.

Older Properties

Depreciation on the structure of a building is determined by the date that construction began. This may mean that a property might not be eligible to claim depreciation on the original structure. However, investors may be able to make a claim on the fixtures and fittings contained within the building. All eligible assets are valued at the time of settlement regardless of their age. Older properties that have had a renovation are also eligible to claim depreciation on the work completed, even if this work was carried out by a previous owner.

If you carried out the construction or contracted a builder to do so, you should make sure you keep detailed records of the construction costs.

Investors that previously purchased a property and do not have a record of the construction costs - if for example, the vendor did not provide them- can obtain this information from an appropriately qualified person. This could be a:

- quantity surveyor.
- clerk of works, such as a project organiser for major building projects.
- supervising architect who approves payments at project stages.
- builder experienced in estimating construction costs of similar building projects.

Investors can claim a deduction for the costs paid to obtain this information from an appropriately qualified person in the year it is paid.

Quantity surveyor reports can also include a schedule of depreciable assets (capital allowances). Investors claim a separate deduction for the decline in value of depreciable assets.

The Bookshelf

The Millionaire Next Door: The Surprising Secrets of America's Wealthy

Written by Thomas Stanley and William Danko

This book provides insight into how the wealthy have accumulated their riches and earned their titles as Millionaires.

Based upon the authors' research, the findings challenge societal conceptions of what it means to be wealthy. Instead of lavish spending, those people with a net worth of at least $1 million have shared qualities based all upon the premise of saving not spending.

Instead of an earn-and-consume attitude, their financial success is attributed to living below their means, efficient spending, allocating funds towards wealth building, proficiency in targeting market opportunities and choosing the 'right' occupation.

It may seem like common sense but Stanley and Danko's findings come to prominence in a context of a world whose major economies are struggling through a financial crisis; one such crisis that has been credited to the superfluous spending and lending of major businesses and unfortunately over zealous individuals.

The Millionaire Next Door squashes the common attitude of "spending tomorrow's cash today"; an attitude which has been deemed as the leading cause of debt and lack of net worth. Instead, the idea which is pushed forward is "save today's cash for tomorrow" with investments made only once an earning of more than 10% of annual income is achieved.

The Millionaire Next Door offers its readers tried and true methods of wealth accumulation. The follow up book The Millionaire Mind, concerns a deeper analysis of those successful wealth accumulators as more participants are interviewed further shedding light on their money handling characteristics.

We are sometimes asked if we are able to help additional clients. We are a growing firm and do appreciate your referrals. We consider it a compliment when you recommend us to your friends and business contacts.

Personal Financial Strategies is for guidance only, and professional advice should be obtained before acting on any information contained herein. Neither the publishers nor the distributors can accept any responsibility for loss occasioned to any person as a result of action taken or refrained from in consequence of the contents of this publication.