Informed

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Welcome to Informed, a quarterly magazine for our clients. We hope you enjoy the articles in this edition.

If you are new to reading Informed, welcome.

If you are an avid reader of this publication you would be familiar with this forum, delivering relevant and interesting content from the financial planning industry, to help you better manage your financial life.

A core value of our business is that every Australian should have access to, and benefit from, good financial advice. In reading this publication, we hope that you find the articles interesting, and perhaps they will provide some talking points for your next review meeting with your financial adviser.

Enjoy reading this edition of Informed.

Understanding changes to granny flat arrangements

On 1 July 2021, a new capital gains tax (CGT) exemption was introduced for certain granny flat arrangements, making it easier for older Australians to enter formal granny flat arrangements with the added protection from possible financial abuse if circumstances within the family change.

A granny flat arrangement does not refer to a granny flat structure in someone's backyard, rather it refers to arrangements where a significant amount of money and/or assets is given in exchange for a right to occupy a dwelling for life.

The dwelling can be a room or self-contained dwelling located on someone else's property, however there are other types of accommodation which can meet the definition for tax or social security purposes. Your financial adviser can discuss the types of accommodation in more detail, in relation to your situation.

The benefit of a granny flat arrangement

Granny flat arrangement offers an alternative housing option to retirement villages, lifestyle parks or residential aged care by allowing older Australians to live on the same property as a family member who can assist them with day to day living and personal care needs.

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It may also be a financially more viable option as some aged care facilities and retirement villages have high entry or ongoing fees.

Many families like to be close to each other, and there can be a great many benefits to intergenerational living. A granny flat arrangement is ideal for this.

Understanding the new CGT exemption

The new CGT exemption (which provides that no CGT event happens) applies to the creation, variation, and termination of a granny flat interest if:

- an eligible individual (older person) is granted a granny flat interest by the grantor
- the grantor of the right owns the dwelling or agrees to acquire the dwelling in which the granny flat interest is or will be held
- the older person and the grantor of the right must both be parties to the arrangement
- the arrangement is in writing and indicates the intention of both parties to be legally bound by it
- the arrangement is not of a commercial nature.

For the CGT exemption to apply to a granny flat interest upon termination or surrender, the CGT exemption had needed to be applied when the granny flat interest was created or varied (on or after 1 July 2021).

Is the age pension affected?

Money or assets (or a combination of both) given for a granny flat interest may fall outside social security 'gifting' rules where certain conditions are met, which may mean the older Australian in the arrangement may retain or increase any age pension entitlements.

Tax implications

In the past, many families may have opted for informal granny flat arrangements to save time, expense and to avoid potentially significant tax consequences for the person granting the right ('grantor'), as the capital gain tax could be significant. The new CGT exemption removes some of the anxiety around the tax implications of having a formal arrangement in place.

Right to occupy

A granny flat interest requires that the older person be granted a lifetime right to occupy a dwelling. A dwelling could be accommodation in the grantor's family home, investment property or holiday home. A 'right to occupy' is distinguished from a life interest. A right to occupy provides the person with a right to live or reside in the property. A life interest may provide broader rights, for example, a right to 'use and occupy' a property, which may include rights to rents and profits from that property if the property was rented out. For social security purposes a granny flat interest may include a right to accommodation for life in the residence or a life interest in the residence.

The older person who holds the granny flat interest

The older person who holds the granny flat interest is eligible if they are, either:

- age pension age or older; or
- have an on-going disability and is likely to require help with their daily activities for at least the next 12 months.

The grantor of the granny flat interest owns the dwelling or agrees to acquire the dwelling

The grantor of the right must own the dwelling (or agree to acquire the dwelling) in which the older person has or will be granted a right to occupy for life. The grantor of the right may be any person, though it is often a family member.

Involve all family members in the process

The new CGT exemption for granny flat arrangements offers protection for older Australians because it details the obligations on each of the parties in the arrangement, and it ensures the arrangement is legally binding. For this reason it is important that an open discussion with all the parties and family members who are likely to be affected takes place, along with financial planning advice from your financial adviser, and legal advice from your lawyer or solicitor. This will get everyone on the same page and gives everyone the opportunity to ask questions and educate themselves on the situation, so the agreement is entered into with a complete understanding of the terms of the arrangement.

Formal, written arrangements must be in place, usually drafted by a lawyer or solicitor, and the arrangement must not be of a commercial nature. Your solicitor can further explain the specific terms and both parties' rights and obligations under the arrangement.

Speak to your financial adviser

If you, or someone you know, wants to consider a granny flat living arrangement, it's sensible to have these conversations with your financial adviser and put something in place whilst all parties are of sound mind and have the capacity to sign the legal agreement.

We are open for business and would welcome the opportunity to have this conversation with you, or someone you know. Call us today.

11 TAX FACTS ABOUT SUPERANNUATION

- Accumulation phase
- Retirement phase
- Accumulation or retirement phase

01 Investment earnings in your super have a lower tax rate.

02 Concessional (pre-tax) contributions to your super have a lower tax rate.

03 Non-concessional (after-tax) contributions to your super isn't reduced by a contributions tax.

04 Insurance premiums can be claimed as a tax deduction and rebated to your super acount.

05 Voluntary contributions may be used as a deposit via the First Home Super Saver Scheme.

For more information on the important considerations for each tax fact, talk to a financial adviser.

06 CGT concessions if selling a small business.

07 Pension payments (TRIS) from your super are generally tax-free (60 or over).

08 Investment income and capital gains are generally tax-exempt.

09 Pension payments (account-based pension or TRIS from your super are generally tax-free (60 or over).

10 Death benefit lump sum paid to a nominated beneficiary is tax-free.

11 Lump sum withdrawals are generally tax-free (60 or over).

11 tax facts about superannuation

Compared to other investment structures, super is widely considered to be one of the most tax-effective investment structures available from a wealth accumulation and cash flow generation perspective. Although not a comprehensive list, below are 11 of the top tax facts about super.

Super investment structure

Overview

When investing via super, it's important to understand that there is an accumulation phase and a retirement phase. From a life stage perspective:

- Accumulation phase generally coincides with the time in your life where contributions are being made to your super, and you are accumulating wealth via these contributions and investment earnings. Nearing retirement, some of us may commence a transition to retirement income stream (TRIS).
- Retirement phase generally coincides with the time in your life where you are using the wealth you have accumulated to help fund your retirement lifestyle via either a retirement income stream, lump sum withdrawals, or a combination of both.

With the above in mind, from a tax perspective, the tax facts listed below are grouped according to their relevance to each phase. For example, the tax facts regarding contributions are underneath the title 'Super (accumulation phase)', as contributions can't be made to a super account in retirement phase.

Super (accumulation phase)

01 Investment earnings in your super. Investment income is generally subject to a maximum of 15% tax. And, capital gains on assets held for longer than 12 months receive a 1/3 (33%) tax discount, which effectively reduces the tax rate to 10%.

02 Concessional (pre-tax) contributions to your super. The amount contributed is reduced by a tax of 15% (contributions tax). When considering salary sacrifice and personal deductible contributions (types of concessional contributions), this tax of 15% may be lower than your marginal tax rate. Please note:

a. If you have income and concessional contributions totalling more than $250,000, you can pay an additional 15% tax (called Division 293 tax) on some or all of your concessional contributions.

b. If you have adjusted taxable income of $37,000 or less, you may be eligible to receive the low-income super tax offset (up to $500).

c. Making concessional contributions to pay for premiums for certain insurance held through super can reduce contributions tax.

03 Non-concessional (after-tax) contributions to your super. The amount contributed isn't reduced by a contributions tax. Please note:

a. If you have total income less than $54,837, you may be eligible to receive the Government co-contribution (up to $500).

b. If you make a spouse contribution (i.e. non-concessional contribution to your spouse's super), you may be eligible to receive the spouse contribution tax offset (up to $540). The receiving spouse's income must be less than $40,000.

04 Insurance in your super. Your super fund trustee can generally claim the insurance premiums as a tax deduction, reducing the tax paid by your super fund trustee on your concessional contributions and super earnings. The tax saving is often rebated to your super account, effectively reducing the premium cost by 15%.

05 Saving for a home deposit via your super. If you make voluntary contributions, you may be eligible to withdraw all or part of these contributions plus associated earnings for use as a deposit via the First Home Super Saver Scheme.

Please note: The maximum amount that can be withdrawn is $15,000 of voluntary super contributions per financial year made since 1 July 2017 (up to a total of $30,000 across all years). The amount that can be withdrawn is 100% of eligible non-concessional contributions, 85% of eligible concessional contributions, plus 85% of associated earnings. Tax is payable on the associated earnings and concessional contributions portion of the withdrawal (taxed at marginal tax rates, including the Medicare Levy, less a 30% tax offset).

06 **Small business capital gains tax (CGT) concessions.** If you are considering selling a small business or the assets it uses, you may be eligible for CGT concessions that help reduce the taxable capital gain associated with the sale, and build your super retirement nest egg in the process.

Please note: You may be able to contribute amounts from the CGT 15-year asset exemption and retirement exemption to your super, without using your non-concessional contributions limits.

07 **Pension payments from your super.** Pension payments from an accumulation phase transition to retirement income stream (TRIS) are generally tax-free if you are aged 60 or over. If you are under age 60, the taxable portion of pension payments is taxed at your marginal tax rate, less a 15% tax offset.

Super (retirement phase)

08 **Investment earnings in your super.** Investment income and capital gains are generally tax-exempt. Please note: The transfer balance cap, which is currently set at $1.6 million (indexed) per person, limits the amount of super benefits that can be transferred to retirement phase.

09 **Pension payments from your super.** Pension payments received from a retirement income stream (e.g. account-based pension or retirement phase TRIS) will be tax-free to you if you are aged 60 or over at the time of receiving the pension payment.

Super (accumulation or retirement phase)

10 **Lump sum withdrawals from your super.** Any lump sum withdrawals made after 60 years of age are generally tax-free. If you make a lump sum withdrawal and you are aged between preservation age and 60, the taxable component of the lump sum is taxed as follows:

a. The amount up to the low rate cap amount (currently $215,000) is tax-free.

b. The amount above the low rate cap amount is taxed at 15% (plus the Medicare Levy).

11 **Passing away and your super:**

a. A death benefit lump sum paid to a nominated beneficiary who is a tax dependant is received entirely tax-free. If the beneficiary is a tax non-dependant, then any tax-free component is tax-free, but the taxable component is taxed at 15% (taxed element) or 30% (untaxed element), plus the Medicare Levy.

b. Income payments from a reversionary death benefit income stream paid to a nominated reversionary beneficiary who is an eligible pension recipient dependant are received entirely tax-free if you or the reversionary beneficiary are aged 60 years or over at the time of your passing.

If both you and the reversionary beneficiary are under 60 at the time of your passing, the pension payments from the reversionary death benefit income stream are taxed as follows:

a. the tax-free component is tax-free, and

b. the taxable (taxed element) component is taxed at marginal tax rate plus Medicare Levy, less 15% tax offset.

However, when the reversionary beneficiary turns 60, the pension payments from the reversionary death benefit income stream are tax-free.

Talk to us

Each tax fact outlined above isn't covered in detail (only a brief snapshot is provided) and other important considerations go with each.

For example, it's important to consider things such as contribution eligibility, and conditions of release.

To discuss how any of the 11 tax facts about superannuation may be relevant to your situation, give us a call. We would love to hear from you!

Important information:

Information is correct as at 20 May 2021.

For references to tax stats and facts you can see an outline via: https://www.ato.gov.au/rates/individual-income-tax-rates/

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