

## Tech Time



### Perpetual's monthly technical guide

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#### Anti-detriment benefits

Anti-detriment payments compensate super fund members for the reduction in lump sum death benefits due to the 15% tax on contribution and investment income from 1 July 1988.

Super funds that accommodate for an anti-detriment payment on the death of a member can provide the member's eligible beneficiaries with a boost of up to 17.65% on the member's taxable component of their death benefit.

#### Background

When first introduced, the 15% tax on contributions and investment income was intended to bring forward tax on super benefits, not to increase existing taxes. But unfortunately, the new 15% tax meant that lump sum death benefits would inevitably be reduced.

As a result, the Government introduced the anti-detriment provision into the income tax law (s279D of the ITAA 1936). This effectively preserves the tax-free status of lump sum death benefits. It does this by allowing the fund trustee to increase the death benefit paid to dependants, and then recover the amount via a tax deduction paid to the fund.

As part of the better super simplification legislation, s279D of the ITAA 1936 has been rewritten and is now called the 'tax saving amount' in s295-485 of the ITAA 1997. However, while the name has changed in the legislation, the industry continues to refer to this payment as an 'anti-detriment benefit'.

#### Who is eligible to receive an anti-detriment benefit?

Eligible recipients include:

- a spouse or former spouse of the deceased
- a child (of any age) of the deceased
- a trustee of the deceased estate.

Where the payment is made to the estate, an anti-detriment benefit can only be paid to the extent that an eligible recipient could reasonably expect to benefit.

It is often uncertain how benefits received by an estate are eventually distributed. For this reason some public offer funds require a statutory declaration by the executor of the estate that the funds will be paid to eligible recipients. Many funds simply make the decision not to pay an anti-detriment payment to the estate.

You can apply the anti-detriment provisions and boost death benefits paid from either the accumulation phase or income phase, but the fund only gets the deduction where the benefit is paid as a lump sum. Consequently, no anti-detriment payment will be made where the beneficiary receives the super benefit as an income stream.

#### How is the anti-detriment benefit calculated?

Most super fund trustees will calculate the anti-detriment payment using the following formula:

$$\text{Anti-detriment payment} = C \times \frac{(0.15 \times P)}{R - (0.15 \times P)}$$

Where:

- C is the taxable component of the lump sum, excluding any of the insured amount of the benefit
- R is the total number of days in the service period after 30 June 1983
- P is the number of days in component R after 30 June 1988.

If the taxable amount (represented by 'C'), is reduced, then the amount of anti-detriment benefit will also be reduced.

### Example 1

John, aged 60, has just retired. He has \$450,000 in an account based pension consisting entirely of the taxable component. He joined the fund on 1 July 1988.

John dies on 1 January 2010 and his fund makes an anti-detriment payment to his spouse. The calculation is as follows:

$$\begin{aligned} \text{Anti-detriment payment} &= \$450,000 \times \frac{0.15 \times 7,855}{7,855 - (0.15 \times 7,855)} \\ &= \$79,412 \end{aligned}$$

Where:

- C = \$450,000 (taxable component)
- R = 7,855 (number of days in service period from 30 June 1983 to 1 January 2010)
- P = 7,855 (number of days in R that occurred after 30 June 1988 to 1 January 2010)

Where a member's service period commences after 30 June 1988, the maximum anti-detriment amount is 17.65% of the taxable component. Note that \$79,412 is approximately equal to 17.65% of the taxable component (of \$450,000).

Under the formula, the more pre-July 1988 service that a person has, the less anti-detriment benefit is payable. This trend continues until the member's service date reaches 30 June 1983 where the payment plateaus.

### Example 2

**Please note: This example replaces the example issued in the August 2009 Tech Time.**

Following on from Example 1, assume John joined his fund on 1 July 1983 and died on 1 January 2010. The calculation would be as follows:

$$\begin{aligned} \text{Anti-detriment payment} &= \$450,000 \times \frac{0.15 \times 7,855}{9,682 - (0.15 \times 7,855)} \\ &= \$62,350 \end{aligned}$$

Where:

- C = \$450,000 (taxable component)
- R = 9,682 (number of days in service period from 30 June 1983 to 1 January 2010)
- P = 7,855 (number of days in R that occurred after 30 June 1988 to 1 January 2010)

Therefore rolling over funds with an earlier eligible service period start date to amalgamate with other funds can reduce the potential anti-detriment payment.

The amount that the super fund can claim as a deduction is calculated as follows:

$$\begin{aligned} \text{Deduction} &= \frac{\text{tax saving amount}}{15\%} \\ &= \frac{\$62,350}{0.15} \\ &= \$415,667 \end{aligned}$$

If the tax deduction creates a tax loss, it may be carried forward providing significant tax advantages to the fund.

### Rethinking the re-contribution strategy

Before recommending a re-contribution strategy, it is important to determine whether a member's beneficiaries would otherwise be eligible to receive an anti-detriment payment.

Because the anti-detriment payment is only paid on the taxable component, using a re-contribution strategy to convert the taxable component into the tax-free component could reduce (or eliminate) the anti-detriment entitlement.

Since 1 July 2007, re-contribution strategies have been used to increase the tax-free component of a superannuation interest in order to minimise death benefits tax when paid to a non-tax dependant (eg independent adult child).

Another issue that members should be aware of when implementing a re-contribution strategy is that they could deny certain beneficiaries a potentially increased death benefit thanks to the anti-detriment provisions in the legislation.



### Example 3

Following on from the previous examples, what would the implications be if John implemented a re-contribution strategy, and the beneficiary is a spouse or financially dependent child?

Result if lump sum paid to spouse or financially dependant children:

	With re-contribution	Without re-contribution
Taxable component	Nil	\$450,000
Tax free component	\$450,000	Nil
<b>Total</b>	<b>\$450,000</b>	<b>\$450,000</b>
Anti-detriment payment	Nil	\$79,412
Tax payable	Nil	Nil
<b>Net benefit</b>	<b>\$450,000</b>	<b>\$529,412</b>

By **not** implementing the re-contribution strategy, his spouse or financially dependent children would be \$79,412 better off.

On the other hand, what if his only beneficiaries were adult independent children?

Result if lump sum paid to financially independent adult children:

	With	Without re-contribution
<b>Taxable component</b>	Nil	\$450,000
<b>Tax free component</b>	\$450,000	Nil
<b>Total</b>	\$450,000	\$450,000
<b>Anti-detriment payment</b>	Nil	\$79,412
<b>Tax payable</b>	Nil	(\$87,353)*
<b>Net benefit</b>	<b>\$450,000</b>	<b>\$442,059</b>

\* \$529,412 x 16.5%

By using the re-contribution strategy, his financially independent children will receive an additional \$7,941.

So, by not implementing a re-contribution, John's spouse and financially dependent children are going to be better off by 17.65%, but his adult independent children will be 1.8% worse off.

The question then becomes whether John should undertake a withdrawal and re-contribution strategy.

In John's case, if the benefit is paid to his adult independent children there is only a slight difference in the final benefit received by implementing the re-contribution, as opposed to simply receiving the taxable amount grossed up by the anti-detriment boost.

The difference would be \$7,941 or 1.5% of the pre-tax benefit (\$7,941/\$529,412). This is insignificant compared to the \$79,412 that John's spouse could potentially miss out on.



**Tech tip:** We have recently released an anti-detriment calculator to help you work out the calculations for your client's situation. For further information please contact your business development manager.

## Acquisition of shares or options from an employee share scheme by an SMSF

Taxpayer Alert TA 2010/3 has highlighted issues that may arise where a SMSF is nominated to receive shares or options under an employee share scheme (ESS).

The situation may arise where the ESS allows the individual or their associates (including the trustee of an SMSF) to acquire shares or rights to acquire shares (share options) in the company.

The shares or share options are provided in relation to employment, or services provided similar to employment, for no consideration, or less than market value consideration, and the individual nominates the trustee of their SMSF (the trustee) as the acquirer of the shares or the share options. The trustee also pays no consideration for the shares or share options, or the consideration given is less than market value.

A problem may arise where the trustee of the SMSF does not recognise and record the market value of the shares or the share options. As a result, the individual may not appropriately account for any income tax liability arising from the above transactions.

Specifically in this Alert the ATO has raised concerns around:

- assessment of a contribution and breaching the contribution caps
- acquisition of an asset from an employer sponsor (which can be a related party)
- the complying status of the fund.

It is important from the individual's perspective that the shares/ options acquired by the SMSF are to be treated as a contribution to the fund and that the appropriate discount amount is included in their personal tax return.

From the funds perspective it is important that:

- the amount is reported as a contribution
- the fund is able to acquire the shares
- the market value is correctly recorded for capital gains tax purposes
- the dividends are classified correctly for income tax purposes as in some cases it may represent non-arm's length income.

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