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# Strategies for a recovering investment market



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Despite all the traumatic events that have recently unfolded, market prospects look positive moving forward. Having suffered through the GFC, now is the time to talk to us to ensure that your portfolio is structured to best advantage.

## Using capital losses to best advantage.

There are a few fundamental rules with capital gains and losses that are crucial in planning for their efficient use. Capital losses for tax purposes are not available until the asset is disposed of. Capital losses when realised can only be used to offset capital gains and are available to be carried forward to future years if not fully utilised. There is no option not to use available capital losses (either realised in that year or brought forward) when there is realised capital gain in a financial year. There is a choice however to select which capital gain (if more than 1 asset is sold resulting in multiple gains) is to be offset with the available capital loss. Capital losses are best used against gains on assets that have been held for less than 12 months. This is because for assets held for more than 12 months, the losses are applied before the 50% discount is given.

## Starting a super pension

When a benefit is paid from a superannuation fund, it is split into tax free and taxable components. The split is based on the value of the tax free component (which is generally personal after tax contributions) at the time of payment with the balance being the taxable element. As the market improves and the value of the account grows, the tax free component, (personal after tax contributions), remains the fixed dollar amount and the taxable dollar amount increases.

An easy solution is to commence an income stream which locks in the tax free as a proportion. For example, a \$450,000 non concessional contributions (personal after tax) start up account will have a tax free proportion of 100%. If an income stream is immediately commenced, even if the account grows to \$600,000, the tax free proportion will remain at 100% and any payments, including lump sums commutations will be tax free. This is not the case if the account remains in accumulation. With an increased accumulated balance of \$600,000, any payment including an income stream commencement will bear a reduced proportion of 75% tax free and while it remains in accumulation phase, will continue to deteriorate as the balance grows.

## Contributing to your spouse's super account

The current \$50,000 superannuation concessional (from pre tax income such as salary sacrifice arrangements) contributions cap for individuals aged 50 or over will be phased out at the end of June 2012. Under the proposed new rules, from 1 July 2012 the \$50,000 cap will only be available for those aged 50 or over, but then only if their total superannuation balance is less than \$500,000. While the new rules are not yet law, it would be prudent for individuals with super balances heading toward the \$500,000 mark and with spouses with lower super balances to use spouse contributions to help equalise their superannuation balances as much as possible. Splitting contributions to your spouse with the lower balance can help keep your balance below the threshold for a longer period of time. Always seek advice first as the normal concessional contribution caps apply.

## Transferring assets

Transferring assets in-specie means that you transfer the asset itself rather than selling it and transferring cash. Such transfers are treated as a disposal of the asset and may crystallise a capital gain or loss. An in-specie transfer is usually undertaken to allow future income and capital gain to be dealt with in a more advantageous tax environment. Before the market improves further, now may be a good time to restructure and transfer assets to more tax efficient entities. By doing it sooner rather than later, the least amount of capital gain is realised and tax can be minimised.

A common application of this strategy is to transfer personally held assets into a superannuation fund as a contribution. However, if such a strategy is undertaken, it should be remembered that generally a super fund can only accept cash, listed investments, widely held unit trusts (managed investments) and business real property and that the contributions caps will apply.

## Centrelink Gifting

Gifting rules may allow you to reduce your assets and increase your Centrelink entitlements. The Centrelink gifting rules only allow an individual or a couple to dispose of \$10,000 of assets in a financial year or \$30,000 in any five consecutive financial years. Any excess assets disposed of above the thresholds will be considered as 'deprived assets'. Any deprived assets as a result of gifting will continue to be assessed and deemed for 5 years after the date of the gift which defeats the purpose of gifting. Gifting investments before the market fully recovers and asset values are lower will enable more assets to be disposed of at a much reduced market value. It may also be a useful consideration to gift away investments with a higher growth potential in preference to those with lower growth potential.

## Overseas pension transfers

There seems to have been a slowdown in the number of overseas pension transfers, most notably from the United Kingdom probably because of the appreciating Australian dollar. A tax liability can arise in Australia on transfer of funds from an overseas pension fund with the tax payable generally based on the growth of the fund since the client first became an Australian tax resident to the transfer date.

This is a complex area and you should always seek advice as there may be some exemptions and various ways of dealing with the tax issues. However, by transferring balances before the market has fully recovered, the assessable gain and tax exposure may be kept to a minimum. Where the concern is the high Australian dollar exchange rate, it is possible in some funds (particularly self managed superannuation fund) to maintain the transfer in a foreign currency bank account, pending the exchange to Australian dollars.

## Borrowing to make more investments in superannuation

Recent changes to the super laws mean that your super fund can borrow money (known as "gearing") to make certain investments. Gearing in superannuation can be an attractive option to build up substantial wealth in the tax concessional superannuation environment while, amongst other advantages, using investment income returns and contributions to pay the interest. With the usual risks of gearing, this strategy is obviously only appropriate for clients who meet the right profile to take on the risk. This strategy is another way to allow you to increase your exposure to an improving market.

Although the borrowing arrangements through self managed superannuation has predominantly been used to buy direct property, it is possible to borrow to buy a portfolio of shares as well, albeit with certain limitations. It should be appreciated that in the superannuation environment, borrowing costs are deductible at a much lower tax rate compared to outside superannuation but the benefit is any future income including capital gains will be taxed at a similar low rate. Having come through the GFC, having watched the market improve over the last 18 months and with the prospect of further improvement into the future, remaining "out of the market" may be very detrimental to the value of your portfolio and the achievement of your long term goals. As the old adage says – "it's time in the market, not, timing the market" that usually wins at the end of the day. Now more than ever it is very important to sit down with your adviser and review the structure of the portfolio and its investments to ensure that you can make the most of future opportunities.