Spouse equalisation strategies - is it worth it?

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Yvonne is Head of Technical Services with Australian Unity. Prior to this, Yvonne spent over 11 years in the technical team at Colonial First State, FirstTech as a senior technical manager. In her role Yvonne works closely with advisers by providing technical expertise and industry insights on legislative and regulatory related issues. She's also a regular presenter at professional development days and conferences.

Yvonne has over 13 years' experience in the financial services industry and has previously worked for Colonial First State, Financial Wisdom and RetireInvest prior to joining Australian Unity in 2018.

Yvonne holds a Masters of Taxation from Sydney University, an Advanced Diploma of Financial Services (Financial Planning) and degrees in both Actuarial Studies and Applied Finance.

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Agenda

- Why is it a good idea to equalise spouse's balances?
- How do you equalise super balances?
- Is it always a good idea to equalise?

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7 reasons why advisers should consider equalising superannuation balances for members of a couple.

1. Transfer Balance Cap

- $1.6M Transfer Balance Cap (TBC)
  - Maximising the amount that can be held in the tax-exempt retirement phase
    - Maximum $3.2 M between members of a couple

1. Transfer Balance Cap

Case study:

- Compare two couples with combined balances of $3M in their SMSF both retiring at age 60 and drawing down minimum pension payment.

Couple A – Uneven balances

SMSF A	Acct age 60	Acct at age 90
ABP (husband A)	$1,600,000	$2,017,422
Accumulation (husband A)	$900,000	$248,054
ABP (wife A)	$500,000	$630,444
Total	**$3,000,000**	**$2,895,920**

Couple 2 – Even balances

SMSF B	Acct at age 60	Acct at age 90
ABP (husband B)	$1,500,000	$1,891,333
ABP (wife B)	$1,500,000	$1,891,333
Total	**$3,000,000**	**$3,782,666**

After 30 years, a whopping difference of **$886,746**

Assumptions: minimum pension drawdown as per legislation; the drawdown amount is identical under both scenarios, lump sum commutation is taken from husband A's accumulation account to make up the difference in minimum pension payment. Annual return net of expenses is 7% pa. 15% tax is applied to earnings in accumulation phase.

2. Estate planning

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- Equalising balances allows the maximum amount to be retained in a SMSF if one partner dies.
- Death benefit income streams count towards recipient's transfer balance cap (TBC).
- Death benefits that exceed recipient's TBC must be paid as a lump sum.
- Surviving spouse can commute and roll back personal ABP to "free-up" TBC space.

2.Estate planning

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- Continuing with previous example of two couples each with combined balances of $3M, retiring at age 60 and drawing down minimum pension payments.
- What if the husbands die at age 75 and leave everything to their wives?

SMSF A	Balances
ABP (husband A)	$2,207,480
Accumulation (husband A)	$993,356
ABP (wife A)	$689,837
Total	**$3,890,674**

SMSF B	Balances
ABP (husband A)	$2,069,512
ABP (wife A)	$2,069,512
Total	**$4,139,025**

Assumptions: minimum pension drawdown as per legislation; the drawdown amount is identical under both scenarios, lump sum commutation is taken from husband's accumulation account to make up the difference. Annual return net of expenses is 7% pa. 15% tax is applied to earnings in accumulation phase.

2.Estate planning

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- Surviving spouse can commence DB income stream up to their personal TBC
- What is Wife A and Wife B's TBC?
  - Wife A used up $500k when TBC was $1.6M
  - Wife B used up $1.5M when TBC was $1.6M
  - Assume CPI of 3% pa general TBC is now $2.4M

Under proportional indexation available TBC are:

Immediate at death	Wife A	Wife B
Available TBC	$1,650,000[1]	$150,000[2]

1. Calculated as $2.4M x $1.1M/$1.6M
2. Calculated as $2.4M x $100k/$1.6M

The surviving spouses can further 'free up' her TBC by roll back her own ABP to the accumulation phase.

TBC	Wife A	Wife B
Personal TBC	$1,650,000[1]	$150,000[2]
Roll back of own ABP (DR)	$689,837	$2,069,512
Available for death benefit income stream	$2,339,837	$2,219,512

2.Estate planning

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- Case study continued…
- Even after rolling back her own ABP, Wife A still must cash out death benefit of $860,999. Wife B will be able to retain 100% of deceased's ABP in the SMSF.

SMSF's member account after death benefit payment

Post death benefit	Wife A	Wife B
Death Benefit ABP	$2,339,837	$2,069,512
ABP	-	$150,000
Accumulation	$689,837	$1,919,512
Lump sum DB	$860,999	

If wife A's MTR is 34.5% and she lives another 15 years.
Assuming pre-tax return of 7%pa
The difference in tax on earnings will result in a difference of **$362,160**

Assumptions: Annual return net of expenses but before tax is 7% pa. 15% tax is applied to earnings in accumulation phase and marginal tax rate of 34.5% applies to earnings outside of super. All income after tax are re-invested for the lump sum amount.

Total Superannuation Balance

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3. Allowing more contributions into super
- TSB < $1.4M for bring forward NCC cap
- TSB < $1.6M to make any NCC
- Benefit of tax concessions in super

4. Qualify for catch-up unused CC cap
- TSB < $500K to be eligible
- Potentially allowing additional CC up to $125K
- Tax savings up to $40k (32% of $125K)

5. Ability to use segregated method to determine ECPI
- TSB < $500K to be eligible
- Potentially allowing additional CC up to $125K
- Tax savings up to $40k (32% of $125K)

6. Government assistance
- TSB < $1,6M to qualify for Government co-contribution and spouse contribution tax offset

7. Minimise minimum pension drawdown

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If there's a significant age difference, having large balances in the older member's name would result in larger minimum drawdown over time and lower end balance.

Case study:
- Daniel age 67
- Mary age 57
- Both retired
- SMSF valued at $2M
- Drawing min pension
- 7% pa return

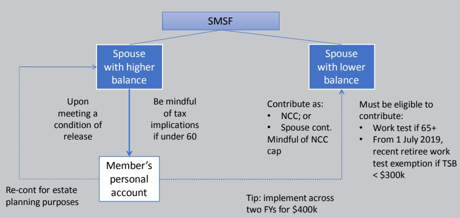
Scenario 1	Daniel	Mary
ABP	$1,600,000	$400,000
After 25 yrs	$1,544,925	$684,195
Total balance	$2,166,556	
Total pension	$3,779,888	

Scenario 2	Daniel	Mary
ABP	$1,000,000	$1,000,000
After 25 yrs	$965,578	$1,540,478
Total balance	$2,519,656	
Total pension	$3,645,296	

- Equal balance resulted in $353,100 end balance after 25 years
- $134,592 less pension payments being made

How do you equalise superannuation balances between members of a couple?

Cash out and re-contribute



Spouse contribution splitting

- Split concessional contribution from the spouse with higher balance to the lower balance spouse.
- Maximum splittable amount is the lesser of:
  - 85% of CC made in the previous financial year, and
  - The CC cap of that year (including increased CC cap under carried forward unused cap provision from 1 July 2019).
- The receiving spouse must be either:
  - Under preservation age; or
  - Not satisfied the "retirement" COR if aged between preservation age and 65.

Spouse contribution splitting case study

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- Lily (45) and Matt (42) are a married couple. Their respective superannuation balances as at 30 June 2018 are $350,000 (Lily) and $300,000 (Matt).
- They each receives employer SG of $10,000 a year.
- Lily has inherited an investment property from her parents which has substantial capital gains (over $200k) which she wants to sell a few years later but is concerned about capital gains tax.

Spouse contribution splitting strategy

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Case study: Spouse contribution splitting

- If Lily splits 85% of her employer SG to Matt for 5 years, her TSB will be less than $500,000 and will qualify for the carry forward of unused concessional contribution. Her unused CC cap is $74,409.

Super balance after 5 years	No splitting	Cont. Splitting
Lily	$519,702	$469,048
Matt	$452,948	$491,728

Benefits of the strategy:

- By making additional CC of $74,409, Lily will be able to reduce her CGT tax liability by **$23,811.**

Assumptions: CPI is 3% pa. Lily and Matt's salary hence SG is deemed to increase inline with CPI. Concessional contribution cap is indexed to CPI in increments of $2,500. All figures shown in future dollars.

Spouse contribution splitting strategy

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To be effective, contribution splitting strategy needs to be implemented over a number of years.

Total amount of super that can be split to a spouse assuming maximum CC cap

Number of years of splitting	5% pa	6% pa	7% pa	8% pa
5 years	$118,866	$121,103	$123,388	$125,723
10 years	$282,381	$293,550	$305,255	$317,523
15 years	$506,859	$538,221	$571,993	$608,370
20 years	$811,027	$880,211	$956,821	$1,041,702

Assumptions: CPI is 3% pa; CC cap is indexed to CPI in increments of $2,500; TBC is indexed to CPI in increments of $100,000.

Transition to retirement pension

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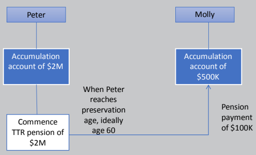
If the spouse with the higher balance attains preservation age first, commence a TTR pension and re-contribute pension payments to the spouse with lower balance.



If Peter starts a TTR at age 60, after 5 years he'll be able to transfer up to $596,654 to Molly.

Small business clients

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- Small business CGT retirement exemption where company or trust is claiming the exemption.
  - The exempt capital gains don't have to be distributed in accordance with the CGT stakeholder's participation percentage.
  - Distributed capital gains must add up to 100% of the exempt capital gains.
  - Can equalise super balances by distributing more to the spouse with lower balances.

Small business clients

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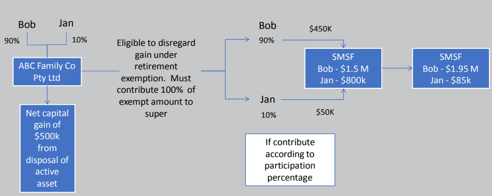
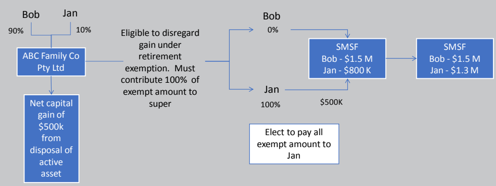
Case study: Streaming of CGT exempt payments



Small business clients

Case study: Streaming of CGT exempt payments



Is it always good to equalise spouse's balances?

- Depend on client's circumstances it may not be worth the hassle
- If there's significant difference in spouse's age
  - Commence a TTR strategy for the older members of the couple sooner to take advantage of tax savings
  - Gain a Centrelink advantage by hiding super in the younger spouse's name`

Let's have a look at Jack and Marilyn

- Jack (64) has super balance of $850,500 and Marilyn (48) has $450,500
- Have little other assets and are both big spenders.
- They've decided they'll spend the entire sale proceeds of Jack's business on a luxury 12 months around the world trip and a brand new European car.
- Is it worthwhile to equalise Jack and Marilyn's super?
  - Not really. Not at risk of exceeding TBC, death benefits also not a concern
  - However might be beneficial to funnel funds into Marilyn's super to maximize Jack's Centrelink age pension

Let's have a look at Jack and Marilyn

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Centrelink facts:

- Maximum asset for couple homeowner before age pension starts to reduce is $387,500
- Asset cut off threshold $848,000
- Amount of financial investment before age pension starts to reduce is $282,000
- Max partnered age pension is $690.70 pf / $17,958 pa
- Accumulation super for people under age pension age is exempt

Jack and Marilyn:

- Jack's age pension age is 66, their total Centrelink assessable assets are :
  - Home contents & car - $100,000
  - Jack's super - $850,500
  - Bank account -$20,000
- Marilyn's age pension age is 67.
- If Jack cash out and re-contribute $400,000 to Marilyn's super over two financial years, reducing asset to $570,500
- Jack will be entitled to age pension of $255 pf / $6,619 pa*.

Assumptions: current Centrelink rates and thresholds are indexed to CPI of 3% pa. No other changes to income and asset.

Conclusion

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- Couple clients with large super balances should equalise balances for transfer balance cap, estate planning purposes.
- Clients with lower balances i.e. combined balance less than $1.6M, benefits of equalising are limited with exception of qualifying for catch up unused CC.
- May be more beneficial to channel more super into the younger spouse's name for Centrelink purposes.

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QUESTIONS?

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