The new generation administration platform

By Helena Gibson

Traditionally one of the disadvantages of investing in platforms (or wrap accounts as they are sometimes called) has been the fact that when an investor wanted to move from one managed fund or security to another they incurred Capital Gains Tax on the disposal of each investment.

Keeping tabs on each acquisition and disposal for tax compliance purposes is time consuming and adds an additional layer of costs.

It is hardly surprising that in the last twelve to eighteen months, Separately Managed Accounts, Individually Managed Accounts and Managed Discretionary Accounts have grown in popularity. Some platform administrators are publicly announcing plans to launch one or more of these product types sometime in 2009.

It is probably true that many people do not seem to know the difference between these three terms. Nevertheless these structures are gaining a lot of attention because of the perceived tax efficiency.

Perpetual has developed a new product called WealthFocus Investment Advantage which provides three different types of CGT benefits to the platform space:

- CGT-free switching – that is, investments can be moved across asset classes and managers without triggering CGT
- CGT-free partial withdrawals unless the amount withdrawn exceeds the cost base of the unit
- Once the initial investment is held for more than 12 months the CGT discount applies to all investments; that is, additional investments in WealthFocus Investment Advantage will not alter the acquisition date

These CGT concessions are all backed by an ATO Ruling PR 2008/62.
HOW IT WORKS
An investor acquires one unit in the fund with their initial investment. The unit’s value is calculated based on the proportion of each investment option held in their portfolio and the value of the investment options in the investor’s portfolio.

Table 1 shows how this might apply to a Self Managed Super Fund.

Whilst this saving may not look particularly large it still represents a 22 per cent reduction in tax expense which is a significant reduction.

If we assume that the investor in Table 1 above is a 40 per cent taxpayer then the tax saving increases to over $9,000 and the percentage reduction in tax is a 36 per cent reduction.

As might be expected, the higher the tax rate the greater the longer term savings. Moreover because there is no CGT payable until final disposal (in most cases) there is an ability to have more money invested.

WHO CAN ACCESS THIS PRODUCT INNOVATION?
This product can be used by any investor. For example it could be used by individuals investing in their own name, trustees of non-super unit trusts, discretionary trusts or hybrid trusts.

It can also be purchased by super fund trustees investing trust assets. This means it can be used by Self Managed Super Funds.

It cannot not offered in a retail superannuation fund structure.

The remainder of this article deals with how adults might use this structure to invest for minors.

USE THIS NEW PLATFORM ON BEHALF OF CHILDREN
Investing on behalf of a child can be a complex area; this is in part due to the fact that most investments cannot be held in a child’s name (due to legal requirements) and in part due to the fact that children are subject to penalty tax rates.

The complexity can be further heightened when we also consider the impact on the adult’s Centrelink benefits and the protection of assets for the intended beneficiary in the event of the adult’s death.

Finding the right investment for your client’s child should be a consideration of the taxation, Centrelink, estate planning and investment considerations. Each of these considerations is explored in further detail below.

TAXATION CONSIDERATIONS
The taxation implications of an investment held on behalf of a child will depend on who the investment is deemed to belong to.

It is important to note that this is not a reflection of how the investment is held, for example could simply be in the adult’s name or the adult’s name as trustee for the child, but rather how the investment is maintained, that is taking into consideration the future purpose of the funds and how the earnings are applied.

If we consider the future purpose of the funds, if the source of funds were an unconditional gift to provide for their future needs upon reaching age 18 and the earnings were reinvested it would generally be accepted that the child would deemed to be the beneficial owner and will be liable to pay any tax that accrues on the investment.

Table 1. Applying WealthFocus Investment Advantage to SMSF clients

<table>
<thead>
<tr>
<th>What you do with your client’s portfolio?</th>
<th>Tax from standard managed fund</th>
<th>Tax from WealthFocus Investment Advantage</th>
</tr>
</thead>
<tbody>
<tr>
<td>In November 2008, invest $100,000 Perpetual’s Industrial Share Fund</td>
<td>• Realised gain $10,000</td>
<td>• Realised gain $0</td>
</tr>
<tr>
<td>• The value goes up to $110,000</td>
<td>• CGT payable $1,500</td>
<td>• CGT payable $0</td>
</tr>
<tr>
<td>After six months switch all $110,000 to cash</td>
<td></td>
<td></td>
</tr>
<tr>
<td>• Move $110,000 to the Platinum Asia Fund</td>
<td></td>
<td></td>
</tr>
<tr>
<td>• The value goes up to $120,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>• Redeem $60,000 from the portfolio</td>
<td>• Realised gain $5,000</td>
<td>• Realised gain $0</td>
</tr>
<tr>
<td>• CGT payable $750</td>
<td>• CGT payable $0</td>
<td></td>
</tr>
<tr>
<td>Nine months later invest $60,000 into the Platinum Asia Fund</td>
<td></td>
<td></td>
</tr>
<tr>
<td>• The value goes up to $180,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>• Eight months later fully redeem whole portfolio</td>
<td>• Realised gains $65,000</td>
<td>• Realised gains $80,000</td>
</tr>
<tr>
<td>• CGT payable $8,000</td>
<td>• CGT payable $8,000</td>
<td></td>
</tr>
<tr>
<td>• Total CGT payable</td>
<td>$10,250</td>
<td>$8,000</td>
</tr>
<tr>
<td></td>
<td>Tax saving $2,250</td>
<td></td>
</tr>
</tbody>
</table>
Alternatively if the gift is a conditional gift or the earnings are being used by the adult as their own, it is the adult that would be liable to pay the tax on the investment.

Where the investment is deemed to belong to the adult, if and when the ownership is changed to the child (for example upon attaining age 18), capital gains tax may be payable as there will be a deemed disposal by the adult.

However where the investment income has always been attributable to the child there will not be any capital gains tax triggered upon transfer of legal ownership as there will be no deemed disposal.

**TAX RATES FOR A MINOR**

The tax rates for a minor are outlined in the table below.

<table>
<thead>
<tr>
<th>Taxable Income</th>
<th>Tax Rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>$0–$416</td>
<td>Nil</td>
</tr>
<tr>
<td>$417–$1,307</td>
<td>66% (on the amount above $416)</td>
</tr>
<tr>
<td>$1,308 and over</td>
<td>45% (on the entire amount)</td>
</tr>
</tbody>
</table>

As minors are entitled to the low income tax offset, currently $1,200, this effectively provides them with the ability to earn $2,667 per annum tax-free.

With the low income tax offset increasing over the next two financial years to $1,350 and $1,500 respectively, this will take the amount they can earn tax-free up to $3,000 in the 2009/10 financial year and to $3,333 in the 2010/11 financial year.

These penalty rates do not apply to income earned by minors as a result of personal exertion, for example a part-time job while still at school.

**CENTRELINK CONSIDERATIONS**

Investing on behalf of a child will generally mean that the adult will still attributed with owning the asset for Centrelink purposes under the asset and income test. For example if a Grandparent invested $20,000 in a managed fund on behalf of their grandson, irrespective of who is paying tax on the income, the Grandparent will still be assessed as being the owner of the asset for Centrelink purposes. As a result the $20,000 will be included as their assessable asset and subject to the deeming rates.

Grandparents may wish to consider gifting the money to the child, provided it is a genuine and unconditional gift and is within the allowable gifting rules (that is $10,000 in a financial year and up to $30,000 over a 5 year period) the asset will be deemed to be that of the child’s for Centrelink purposes. This would be the case even where the asset is held on trust by the grandparent for the child and they make all the investment decisions until the child is legally able to do so.

**ESTATE PLANNING CONSIDERATIONS**

Another concern, particularly for Grandparents is that when they die that any investments held on trust for their grandchildren will end up with unintended beneficiaries. The reason that this may present a problem is that upon death generally these investments would form part of the adult’s estate (as they are still the legal owner of the investment) and then distributed according to the will, even though the will can direct the executor to pay the nominated benefits to the grandchild, other disgruntled family members are able to contest the will and ultimately end up with the benefits.

The grandparent may wish to consider the use of a trust with the grandchildren as the beneficiaries; however it is important to
weigh up the protection of benefits as against the potential loss of Centrelink benefits.

It should be noted however that where a child has received an inheritance that the investment is generally treated as an asset of the child’s for income tax purposes.

**INVESTMENT CONSIDERATIONS**

For most parents, investing for their children is part of a long-term plan. The two most common scenarios include funding for their higher school education or helping to set their children up for the future. Typically this would involve investing in growth assets. Further for many people using a platform can present the ideal investment vehicle as it allows for small investment amounts to be made and complemented by a regular savings plan.

Investing in WealthFocus Investment Advantage can allow parents to switch between investment options without triggering capital gains tax, further they can withdraw from the investment to fund education costs without triggering capital gains tax (provided they only withdraw up to the amount invested).