

Working it out



ROB LAVERY

is senior technical manager at KnowIT Group.

The federal government granted a significant concession in last year's budget with the introduction of the work test exemption for individuals who have recently retired. Rob Lavery explains how the new rule works and the pitfalls and opportunities associated with it for SMSF members.

The 2018/19 federal budget included a proposal to allow a work test exemption for those over the age of 65 wanting to make personal contributions to super. Treasury consulted on draft legislation and regulations that would implement this proposal in October. In December, the final regulations were registered. These regulations give rise to traps SMSF members will need to navigate to ensure they use the exemption correctly.

A quick background

Members aged 65 or older are required to meet a work test in order to have voluntary contributions to super made on their behalf. Such voluntary contributions include personal contributions, voluntary employer contributions, such as salary sacrifice, and spouse contributions.

Generally these voluntary contributions can be made any time from the age of 65 until the 28th day in the month following the member's 75th birthday.

The work test requires the member to have been gainfully employed for 40 hours in a period of no more than 30 consecutive work days in the financial year the voluntary contributions are made. What's more, this work test must be met before the voluntary contributions can be made.

It is important to note the work test does not apply to mandatory employer contributions, such as those stemming from superannuation guarantee requirements, or the downsizer provision.

The exemption

The exemption to the work test will commence in the 2020 financial year. Members aged 65 to 74 who meet all the following criteria will be able to have voluntary contributions made on their behalf. The criteria are that:

- they met the work test in the financial year immediately before the one in which the

- contributions are made,
- their total superannuation balance immediately before the year of contribution was less than \$300,000, and
- they have not used this work test exemption in any previous financial year.

Example

Chloe, 67, retires from full-time work in June 2020. Her total super balance is \$200,000 on 30 June 2020. She wants to make \$80,000 in personal contributions in July 2020. She is able to do so using the work test exemption as she:

- met the work test of 40 hours in 30 consecutive days in the previous financial year (2019/20),
- had a total superannuation balance of less than \$300,000 immediately before the financial year of contribution (that is, at 30 June 2020), and
- she has not used the work test exemption previously.

Accompanying legislation

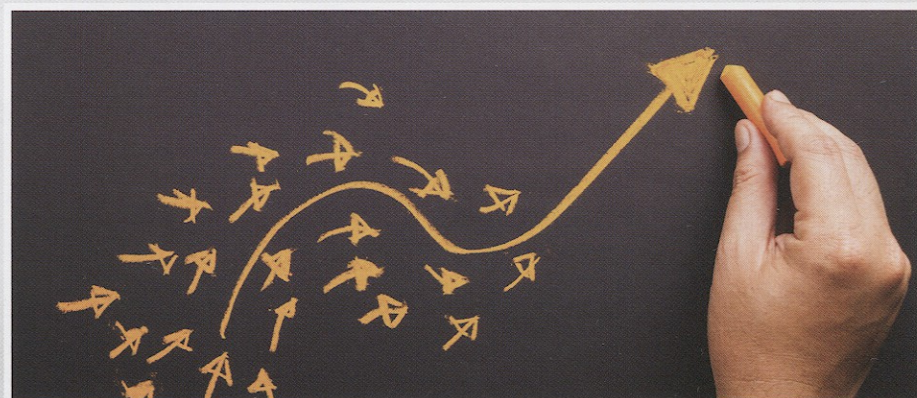
When Treasury initially consulted on the draft work test, the regulations were complemented by legislation. This legislation contained provisions to ensure non-concessional contributions made using the exemption could not trigger the bring-forward provisions.

It appears the government will not draft and attempt to pass this accompanying legislation. In a press release accompanying the regulations, Assistant Treasurer Stuart Robert stated: "Following feedback from stakeholders on the draft legislation, the government has decided to allow those who use the work test exemption in the year they turn 65 to access bring-forward arrangements for non-concessional contributions.

"These individuals will be able to make up to \$300,000 in contributions from after-tax income, providing extra flexibility to get their affairs in order as they prepare for retirement."

Example

On 30 June 2020, Suresh has a total superannuation balance of \$250,000. He turns 65 in August 2020 and in September



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2020 he retires from his full-time employment. In October 2020, he wants to make a personal contribution to his SMSF. He is able to do so using the work test exemption as he:

- met the work test of 40 hours in 30 consecutive days in the previous financial year (2019/20),
- had a total superannuation balance of less than \$300,000 immediately before the financial year of contribution (that is, at 30 June 2020), and
- he has not used the work test exemption previously.

What's more, Suresh can bring forward two future years' worth of non-concessional contributions using the bring-forward provisions as he was under age 65 at the start of the financial year of contribution. Assuming the non-concessional cap is the same in 2020/21 as it is now (that is, \$100,000), he can make up to \$300,000 in personal non-deductible contributions using the work test exemption in 2020/21.

A large contribution would take Suresh's total superannuation balance

over \$300,000. This, however, does not affect his ability to use the work test exemption in 2020/21. The only date at which his total superannuation balance is tested is the one immediately before the start of the financial year (that is, at 30 June 2020).

Practicalities

It would be difficult for any super fund to determine whether a member's total superannuation balance is under \$300,000 as it includes the member's account balances in all their super fund accounts.

It is common for super funds, including SMSFs, to use a member declaration to determine if the work test requirements have been met. The explanatory statement that accompanied the work test exemption regulations recommends taking a similar approach when confirming whether the total superannuation balance test is met.

"One way that a fund could be satisfied that this requirement has been met is to obtain a statement from a member attesting to the member having a total superannuation balance below \$300,000 on the 30 June of the previous financial year. A particular superannuation fund will not be in a position to independently calculate an individual's total superannuation balance as the fund will not have oversight of an individual's superannuation interests held in other funds," the explanatory statement says.

If the fund becomes aware it has accepted contributions incorrectly, it has 30 days to

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refund the contributions. As in most cases, members of an SMSF are the fund's trustees, or directors of the trustee company, so a false declaration may have more serious tax consequences, particularly if the refund period of 30 days has elapsed.

Dodge the snakes and climb the ladders

The wording of the exemption leads to a few traps members will need to avoid, as well as some new opportunities that can be used.

Members who have just turned 65

Where a member has turned 65 in the current financial year, they will need to have met the work test in the financial year they turned 64 if they want to use the work test exemption. Just having been under 65 in the previous financial year will not be enough to access the work test exemption.

This creates an unusual situation in that the member will need to have met the work test in a year where it was previously irrelevant to them contributing to super.

Example

Bronte is retired, turned 65 in August and is looking to make \$50,000 in non-concessional contributions to her SMSF in November. Bronte's total superannuation balance immediately before the start of the financial year was \$120,000.

Under the current rules, Bronte would need to meet the work test in the current financial year before she could make her voluntary contribution to super.

Under the work test exemption, she could potentially use the exemption from the work test in order to make her contribution to super. To do so, however, she would need to have worked 40 hours in a period of no more than 30 consecutive days in the previous financial year. This is the case even though she was under 65 in that previous financial year.

If Bronte had been employed for sufficient hours in the previous financial year, this could allow her to make the contributions.

If, however, she did not work enough in that previous financial year, she would be back to having to meet the work test in the current financial year.

Catching up and using the exemption

From 2018/19 onwards, the unused portion of a member's concessional contributions cap can be carried forward for up to five financial years. These catch-up concessional contributions, when combined with the work test exemption, present a new tax management opportunity for members.

Example

On 1 May 2020, Garry retires from full-time work at age 68. In the final two years of his employment (2018/19 and 2019/20), his only concessional contributions were his employer's compulsory superannuation guarantee contributions of \$10,000 and \$9000 respectively. His full concessional contributions cap in each of those years was \$25,000, meaning he had unused concessional contributions of \$15,000 in 2018/19 and \$16,000 in 2019/20.

Garry sells his investment property in August 2020, realising an assessable capital gain of \$150,000. Without the exemption, he would be prevented from making personal deductible contributions to super in 2020/21 to offset this gain unless he met the work test.

At 30 June 2020, his total superannuation balance is \$150,000. As such, the work test exemption is available to him in the 2021 financial year. He can use his unused cap in 2018/19 (\$10,000) and 2019/20 (\$9000), as well as his cap in 2020/21 (\$30,000), to make up to \$49,000 in personal deductible contributions to offset his capital gain.

If he so wished, he could also contribute up to \$100,000 in non-concessional contributions in 2020/21.

One and done

An important element of the work test exemption rules is that once a member has used the exemption in one financial year, they cannot use it again in any future financial years. It is important to note the multiple

contributions (up to the relevant caps) can be made in the same financial year using the work test exemption.

This limitation may need to be strategically managed where a member wishes to make personal contributions in as many years after turning 65 as possible while working as little as possible.

Example

Corinne plans to retire on her birthday in June 2020 when she turns 67. She has a significant investment portfolio, which will require careful tax management in her retirement. Contrastingly, she has less than \$200,000 in super.

One tax management strategy Corinne has been discussing with her financial adviser, Doreen, is making personal deductible contributions to super. Corinne's major problem is she does not wish to work any longer than is necessary.

If she retires on her birthday in June, under the work test exemption she could still make personal contributions to super in the following financial year. After that one exemption use, however, she would be unable to use the exemption in any subsequent years and would need to meet the work test in each financial year she wishes to make personal contributions.

If, however, she continued working full-time until the end of July 2020, she could use that employment to meet the work test in that year and make personal contributions. She could then use the work test exemption in the following financial year (2021/22) to make further personal deductible contributions and reduce her tax burden. Once used though, the exemption would be unavailable to her in future financial years.

Passing the test

For what seems a simple change, the work test exemption provides plenty for SMSF members to navigate.

Armed with a sound understanding of the rules, members can gain significant advantage from the exemption when building their savings for retirement. ▼