PPM
PRIVATE PORTFOLIO MANAGERS

Investment structure is a crucial consideration for SMSF trustees

Hugh MacNally, PPM Chairman and Portfolio Manager discusses the key benefits of matching investments to these different structures and through a simple working example demonstrates how effective structuring can enhance total after-tax returns.

Despite the increasing complexity of superannuation laws in Australia, SMSF Trustees and their investments still benefit significantly from the taxation concessions provided under the Australian superannuation system. However, when considering efficient after-tax returns, a SMSF fund is only part of the picture. SMSF Trustees in planning for their 'complete financial picture' and long term wealth management should consider both super and non-super investments and examine how different investment structures can enhance after-tax benefits. Indeed, how effective management of both non super and super investments can achieve a tax efficient outcomes for their 'total investment portfolio'.

It should be noted that PPM does not provide tax advice, but collaborates with our client's accountant and/ or financial advisers to ensure that our client's investments are managed in an efficient after-tax basis.

Matching investments to these different structures can produce significant after-tax benefits.

There are a broad variety of investment structures for Trustees to consider, from fully taxable entities to more tax efficient vehicles such as discretionary trusts, charitable trusts, companies, private ancillary funds, and superannuation funds. Each structure also offers different tax concessions depending on whether the fund is in accumulation or pension phase.

It is important to understand the differences and benefits between different structures and understand some of the common considerations that produce more benefits in some structures over others.

Common considerations:

- High income generating investments would be more appropriately placed in a lower tax structure, where regular tax liabilities from income generating investments do not occur.
- The question of whether or not to realise capital gains in a tax-free structure is not influenced by tax considerations, merely by the return prospects of the investment.
- All other factors being equal, high capital growth investments are best placed in a high tax environment as they produce few tax events until sold, and then often attract tax concessional rates.

- Companies that are likely to buy back their shares are best held in tax-free or low tax structure where the tax benefit of the buyback can be utilised.

Through proactive investment matching with holding structure strategy, tax positions can be managed more effectively.

Matching Investments to Holding Structure – A simple example

ASSUMPTIONS		Individual	SMSF
Fully franked dividend yield	(a)	6.00%	6.00%
Capital Gains	(b)	8.00%	8.00%
Turnover	(c)	30.00%	30.00%
Realised Capital Gains	(d) = (b) x (c)	2.40%	2.40%
Tax Rate	(e)	45.00%	15.00%
Discount CGT rate	(f)	50.00%	33.33%

As an example to demonstrate the benefits of effective structuring, let us consider two scenarios.

In **Scenario 1**, an investor has a personal portfolio and superannuation portfolio with exactly the same holdings, half in high yielding stocks and the other half in high growth stocks.

In **Scenario 2**, an investor also has a personal portfolio and a superannuation portfolio. However, all the high yielding stocks are held in the superannuation portfolio, while the high growth stocks are held in the personal portfolio.

		PORTFOLIO WITHOUT TAX MATCHING (SCENARIO 1)			PORTFOLIO WITH TAX MATCHING (SCENARIO 2)		
		Individual	SMSF	Combined	Individual	SMSF	Combined
High yield stocks	(g)	500,000	500,000		-	1,000,000	
High growth stocks	(h)	500,000	500,000		1,000,000	-	
Total Portfolio	(i)	1,000,000	1,000,000	2,000,000	1,000,000	1,000,000	2,000,000
Dividend before tax	(j) = (a) x (g)	30,000	30,000		-	60,000	
Franking credits	(k) = (j) x 30 / 70	12,857	12,857		-	25,714	
Tax on grossed up income	(l) = ((j) + (k)) x (e)	(19,286)	(6,429)		-	(12,857)	
Dividend after tax incl. franking	(m)	23,571	36,428		-	72,857	
Unrealised capital gains	(n) = (h) x ((b) - (d))	28,000	28,000		56,000	-	
Realised capital gains before tax	(o) = (d) x (h)	12,000	12,000		24,000	-	
Discounted tax on realised gains	(p) = (o) x (e) x (1 - (f))	(2,700)	(1,200)		(5,400)	-	
Realised capital gains after tax	(q)	9,300	10,800		18,600	-	
Total portfolio after-tax return	**(r) = (m) + (n) + (q)**	**60,871**	**75,228**	**136,099**	**74,600**	**72,857**	**147,457**

Although this example is simplified, it is from our experience a typical one, which illustrates that an additional $11,358 in after-tax returns is achieved through tax savings with effective matching of investments to the appropriate holding structure.

The additional after-tax return represents a risk-free return improvement without changing any underlying investment exposures.

A variety of other scenarios can produce similar benefits, but all tax matters are highly specific to the individual. Investment returns are enhanced through the tax advantaged superannuation structure; however certain types of returns may receive greater tax advantages than others.

PPM is a specialist provider of SMA & IMA solutions

PPM is a specialist IMA boutique investment manager with over 20 years' experience in successfully managing individual and Trustee client portfolios to meet the demands of these sophisticated investors who want a tailored investment solution to meet their investment requirements. PPM first developed IMA's in 1995 as a direct actively managed and administered investment solution for our sophisticated clients. In 2017, we launched the Australian Equities Growth SMA and the Global Equities Growth SMA, for both general and superannuation investment, to meet the growing demand for actively managed direct Australian and international portfolios of clients either do not require individual portfolio customisation or who do not satisfy the Corporations Law definition of a 'wholesale' investor.

SMSF Trustees are attracted to PPM's IMA and SMA solutions as they provide professional investment management, cost effective administrative ease and the transparency and control that astute SMSF Trustees demand. Super and non-super IMAs can be combined to assist our clients achieve tax efficient outcomes for their 'total investment portfolio'.

We would be happy to meet with you to discuss your requirements to determine in conjunction with your advisers whether a PPM IMA or SMA is suitable for you.

Please contact our team for further information of PPMs service offering.

Sally Humphris
Business Development Manager
sh@ppmfunds.com
M: 0418 968 785
P: (02) 8256 3777