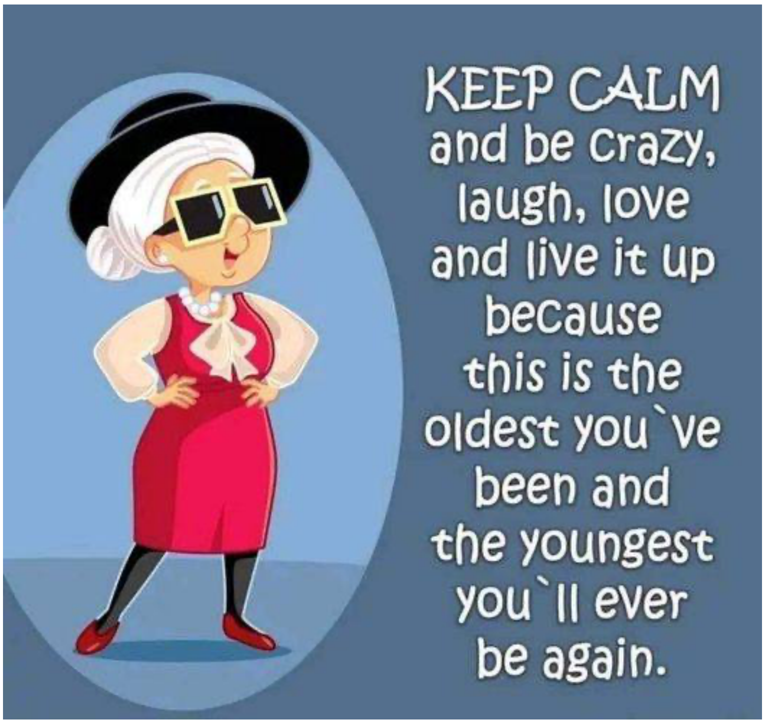
Retirement and Selling Your Residential Investment Property – A Lot is About Your Age



There is so much material around about buying and owning an investment property but not much about how it all works out in the end. The general idea is the investment property is negatively geared for much of your working life. The losses are then recovered by the capital gain you will realise when you retire and are in a lower tax bracket. Nevertheless, all that capital gain in one year is going to attract a lot of tax requiring very careful planning. A big part of that is putting the sale proceeds into superannuation, there is much to consider here regarding contribution caps and age restrictions. Bear with me, the example and table at the end of this blog should bring it all together.

Note if you are selling a commercial property that has been used in yours or an associate's small business there are a whole lot more CGT and Superannuation contribution concessions available. This blog is about residential rentals.

This spreadsheet will help you estimate the capital gain that you need to consider https://www.bantacs.com.au/shop-2/cgt-calculator/

Timing

If you are intending to make a superannuation contribution to offset the capital gain you need to make sure the funds are contributed in the same year you sign the contract with the buyer, not the date of settlement. Many superannuation funds won't accept contributions in the last weeks of the financial year, you need to make sure you get the cash into the fund in plenty of time. This creates a problem if settlement has not yet taken place. Firstly, you probably won't have the cash to make the contribution. Even if you do have the cash available there is a risk that the contract will fall over and you have locked your money into superannuation when you don't need the tax benefit. Fortunately, in retirement you should not have any problems getting the money back out, just make sure the 15% tax is not deducted, by not giving the superannuation fund a notice of intention to claim a tax deduction until you are sure the property has settled, assuming that happens before the following 30th June!

Another timing consideration is that once you reach 67 years of age you cannot make tax deductible contributions to superannuation without passing the work test and once you get to 75 years of age. there is no way you can make a tax deductible contribution to superannuation. The only contribution you can make to superannuation for yourself after reaching 75 is a downsizer contribution.

Concessional (tax deductible) Contributions

Caps

Each year a taxpayer is only entitled to make a maximum of $30,000 in tax deductible superannuation contributions and this includes any contributions made by your employer such as under the super guarantee or ones you have salary sacrificed before tax. High income earners may not have any room left after their employer's contribution.

If your superannuation balance at the end of the previous financial year was less than $500,000 and if, in the previous 5 years there have been years where you did not use up all of your concessional contribution cap, you will be entitled to contribute more than $30,000 to soak up the contributions you missed out on in the past 5 years. Your unused cap limit is available through mygov.

Tax on Contributions

Tax deducted (concessional) contributions are taxed at 15% in the hands of the superannuation fund. So, it is not completely tax free just a reduction from your marginal tax rate down to 15%.

There is another 15% tax payable for taxpayers earning more than $250,000. This is called Div 293 and is assessed after you lodge your tax return. The $250,000 is your:

- Taxable income except for any assessable first home super saver release amounts
- Plus reportable fringe benefits and any amount on which family trust distribution tax has been paid
- Net losses on financial investments and rental properties are added back so spending money on repairs on your rental property in excess of your rental income cannot bring your income under the $250,000
- Even the taxed element of a lump sum superannuation payment that has a zero tax rate is added in
- Any superannuation contributions that you or your employer have made that qualify as concessional contributions will also be added to your income for Div 293 purposes

It may look like the ATO has covered everything but there is a little trick, if you are close to the threshold. If you make a concessional contribution that is in excess of your available cap, you can still claim it as a tax deduction, reducing your taxable income but it is not added back for Div 293 purposes because, once it reaches the superannuation fund and the sums are done extra tax is taken out of the super fund to bring the tax on the excess contribution up to what you would have paid if you had not claimed the tax deduction. As this excess portion of the contribution is now not treated concessionally it is not added back. So, it can effectively reduce your taxable income in your tax return, without being added back. Be careful here to make sure the contribution will not receive concessional treatment. If you make a concessional contribution that is over the $30,000 cap you must either not qualify for (for example have a superannuation balance in excess of $500,000 at the end of the previous financial year) or have used up all your unused used cap. Otherwise, automatically your unused cap kicks in and the excess is still a concessional contribution so it is added back for Div 293 purposes.

Note you need to be under 67 years of age at the time you make the superannuation contribution or satisfy a work test and be under 75 years of age to claim a tax deduction for a superannuation contribution.

Non Concessional (non tax deductible) Contributions

These contributions are not going to give you a tax deduction to help reduce your capital gain. But they will give you tax benefits in the long run. Once you move to pension phase (note if you are first switching from accumulation to pension phase in the 2025-2026 financial year, the maximum you can transfer is $2mil) the earnings on your superannuation will no longer be taxed. The game is to manage the contribution caps over the years to get that $2mil into superannuation in the first place. If you have previously moved money into the pension phase your transfer balance cap will likely be less than $2mil. In that case, your pension cap can be obtained through mygov.

As you get closer to retirement age the opportunity cost of locking your money away in superannuation is reduced, in fact it can become just like having money in the bank. Once you have reached 60 years of age, if you have to retire or reduce your working hours you will be entitled to access your superannuation and once you reach 65 years of age you can access your superannuation regardless of employment status.

To qualify to make a non concessional (non tax deductible) contribution your superannuation balance in the previous year needs to be less than $1.9mil. The cap for non concessional (non tax deductible) contributions is $120,000 in a year but you can draw forward the next two years' caps and put $360,000 in this year. Of course, if you draw forward two years of concessional contribution caps you will not be able to make non concessional contributions in the following 2 years. So, if you need to put more than $360,000 into superannuation, it will get there quicker if you just put $120,000 in this year then once 1st July ticks over put $360,000 in. As long as you are under 75 years of age at any time in the financial year you choose to draw forward you will qualify (subject to your contribution limits – see below), even though technically you would not have been allowed to make a non concessional contribution in the following year because you will be too old.

If your superannuation balance at the end of the previous year was more than $1.78mil you are not entitled to utilise the draw forward concessions so the maximum non concessional contribution you can make is just $120,000 for the current year providing your balance is under $1.9mil. If the balance was between $1.66mil and $1.78mil you can only draw forward 2 years i.e. a total maximum amount of $240,000.

Work and Age Restrictions

If you're under 18 years old at the end of the income year in which you made the contribution, you can only claim a deduction for your personal super contributions if you also earned income as an employee or business operator during the year.

If you are 75 years of age or older the only superannuation contributions your fund can receive is downsizer contributions and employer superannuation guarantee contributions. The downsizer contributions are capped at $300,000 per individual or per member of a couple (even if the house is only in one spouse's name). To qualify the house must have been owned for at least 10 years and at some time qualified for the main residence exemption. Downsizer contributions are not tax deductible. Employer contributions under the superannuation guarantee are limited to the applicable rate for that year, which was 11.5% of salary for the 2024-2025 and 12% of salary for the 2025-2026 financial year. Employer contributions are only tax deductible to the employer. These restrictions and the obvious tax advantages of selling only one property per year, that will result in a taxable gain, after you retire, means that you need to have a plan and get on with it.

If you are between 67 and 74 years old* you need to meet a work test to be allowed to make a concessional (tax deductible) contribution to superannuation. To satisfy the work test, you must work at least 40 hours during a consecutive 30-day period each income year. There is a one off concession on the work test, that if your superannuation balance is below $300,000 and you satisfied the work test in that year you will qualify to make concessional (tax deductible) contributions in the following year.

*If you are 75 years old or older, you can only claim a tax deduction for contributions you made before the 28th day of the month following the month in which you turned 75 and of course you need to satisfy the work test.

Example:

Pete is 72 years of age selling an investment property that is going to give him a capital gain after the 50% CGT discount of $200,000. Pete has been retired for 6 years so has the following unused caps available.

2024	$27,500
2023	$27,500
2022	$27,500
2021	$25,000
2020	$25,000

	$132,500

Pete can pick up enough part time work to satisfy the work test but his problem is that he already has a bit over $500,000 in superannuation. So rather than selling the property in the 2025 financial year he delays and makes sure he takes enough out of his superannuation fund to bring his balance under the $500,000 mark, being careful to consider any possible capital growth, before 30th June 2025. As the $500,000 test applies to the closing balance at the end of the previous financial year he will now be able to sell the property in the 2026 financial and take advantage of his unused caps. With another year ticking over the 2020 $25,000 will drop off but be replaced at the top by $30,000 giving him $137,500 in unused cap plus the $30,000 for the 2025-2026 financial year, a total of $167,500.

Pete has very little in other taxable income because he is living off a tax free superannuation pension income stream. He makes a capital gain of $400,000, after the discount that is $200,000 taxable plus say $1,000 for wages and interest and maybe the property has earned some rent before it is sold, say $10,000, a total taxable income of $211,000. If he was to put $167,500 into superannuation as a concessional tax deductible contribution it would bring his taxable income down to $43,500 where at worst, his marginal tax rate will be 16% plus Medicare. As a senior there is SAPTO to consider which can be shared between spouses and a higher threshold before the Medicare levy kicks in, he may pay no tax at all.

This is where the careful planning comes in because any superannuation contribution that he claims a tax deduction for will be taxed at 15% in the hands of the fund. So he doesn't want to claim more than is needed. Near impossible to guess what his taxable income will be before the end of the financial year when he has to make the superannuation contribution. So the idea is to put in the maximum amount, worse case scenario, before 30th June 2026. He does not have to tell the superannuation fund what portion of that amount he will claim a tax deduction for until he prepares his tax return after the 30th June 2026 but this must happen before 30th June 2027. If he does not need it all then the over payment can just be treated as a non concessional contribution so no 15% tax is deducted.

If I haven't lost you yet, consider all of the above except the capital gain was $500,000, $250,000 after the discount, plus interst, wages and rent, total income of $261,000. The Div 293 threshold would add back the superannuation deduction for the $250,000 test so he would fail and the superannuation contribution of $167,500 would be taxed at 30% instead of 15%, an extra $25,125 in tax on the superannuation. He would have been better off reducing the sale price by $24,000! Or use our little tax trick of putting another $12,000 into superannuation that is over the threshold so that it will not be added back.

To bring the caps, restrictions and thresholds together in one spot, here is a table. But please do not rely on the table alone as there are many nuances.

Age	Maximum Deductible Contribution	Restriction
18-67	$30,000 Can Access unused cap from past 5 years	Nil Super Balance Under $500,000
68-74*	$30,000 Can Access unused cap from past 5 years	Must pass work test Super Balance Under $500,000 and work test
75 +	None	

Age	Maximum Non Deductible Contribution	Restrictions
18-74	$120,000 Can Draw Forward another $260,000 Or Can Draw Forward another $120,000	Superannuation balance under $1.9mil Superannuation balance under $1.66mil Superannuation balance between $1.78 And $1.66mil
55+	$300,000 Downsizer	Owned home for more than 10 years and at least some time covered with main residence exemption. Once in a lifetime. Must pay into superannuation Fund within 90 days of settlement.

This is general advice only and should not be relied on without professional advice tailored to your particular circumstantes. There is a lot to consider. Getting this right is how financial planners earn their keep. We have a financial planner who can help you. Adrian Ng, he can be contacted on adrian@dngfs.com.au