Fact sheet: Tax and the Pathway Education Fund

Supporting Children's Education | ASG

The Pathway Education Fund (PEF) has been established by ASG for the purpose of providing benefits for the education of nominated beneficiaries. It is designed to qualify as a 'scholarship plan' under the *Income Tax Assessment Act 1997*.

What are the tax benefits?

Earnings of the PEF are taxed at the company tax rate of 30 per cent. You can benefit from certain tax concessions made available for scholarship plans, including ASG's ability to get back any tax paid within the Fund (for your benefit) when you utilise your investment earnings to fund education related expenses (which we describe as an Education Benefit).

Under a scholarship plan, when your investment earnings are accessed as an Education Benefit, the amount you receive will be increased by this tax benefit. This is because ASG can claim a tax deduction on Education Benefits paid and pass on this benefit in the amount paid to your nominated beneficiary.

The main tax benefits of the PEF are as follows:

- ASG's PEF is a 'tax-paid' investment. This means that the Fund pays tax on the investment earnings of your contributions, at the current company tax rate of 30 per cent.

  As a result, periodic bonus allocations from Fund investment earnings to your Member Account are not required to be included in your assessable income and you therefore do not attract personal tax on those earnings. This particular tax concession means your taxable income stays down, and that may carry flow-on benefits, such as not attracting higher income-related levies and charges, and possibly attracting income-tested government benefits.
- If your marginal tax rate is above the corporate tax rate of 30 per cent, you may benefit from having ongoing investment earnings taxed within the Fund, rather than at your marginal tax rate. According to figures released by the Australian Bureau of Statistics most working Australians attract a marginal tax rate (including the Medicare levy) of 34.5 per cent or higher (Source: 6306.0 - Employee Earnings and Hours, Australia, May 2014).
- The amount of your Education Benefit will be increased by tax benefits. This is because ASG can claim a tax deduction on Education Benefits paid, and it will pass on the value of this deduction benefit in the amount paid to your nominated beneficiary.
- The amount of an Education Benefit paid is assessable to the nominated beneficiary instead of the member(s). Furthermore, as a student, your nominated beneficiary may not attract any personal tax on the amount received, especially if aged 18 years or over (by the end of the tax year) and if their taxable income is below the effective tax free threshold*.
- The Fund is entitled to utilise any imputation/franking credits it receives, which can reduce the tax it pays on earnings.
- If you happen to withdraw earnings for non-education purposes (this would arise if a particular withdrawal does not meet the criteria for paying an Education Benefit), and you have held the account for more than 10 years since the first contribution, generally there is no personal tax payable. The Insurance Bond Rules apply in this situation (please see page 2 of this fact sheet for more information).
- You can access your net contributions (your contributions less applicable fees and costs) at any time, without having to pay any tax.

See the Australian Taxation Office (ATO) website for more information on individual income tax rates: www.ato.gov.au. Currently, the standard effective tax-free threshold is $20,542.

PEF - tax treatment overview

A. Tax on your contributions

Contributions do not attract any tax. Also, withdrawals of contributions (net of fees) are treated as a tax-free return of capital to the member.

B. Tax on your investment earnings (while in the fund)

Ongoing investment earnings are taxed at the maximum rate of 30 per cent. Fund tax can be reduced by offsets such as dividend imputation credits and tax deductions available to the Fund.

C. Tax on benefit payments

Who will pay tax on withdrawals?

In summary, who is assessable for tax purposes and for how much, depends on a few factors. These include:

- whether your withdrawal comprises your contributions, your investment earnings or a combination of both
- whether the earnings portion of your withdrawal is for:
  - an education related expense (Education Benefit) or
  - a non-education related expense (Non-education Benefit).

Withdrawal type	Who is treated as receiving the amount for tax purposes?	Tax status of amount received	
Return of net contributions	Member	Not assessable	
Education Benefit	Nominated beneficiary	Under age 18: Taxed at rates applicable for minors (generally)[*]	Aged 18 or over within the financial year: Taxed at adult marginal rates
Non-education Benefit	Member	Assessable to the member at marginal tax rates, and subject to the Insurance Bond Rules[‡].	

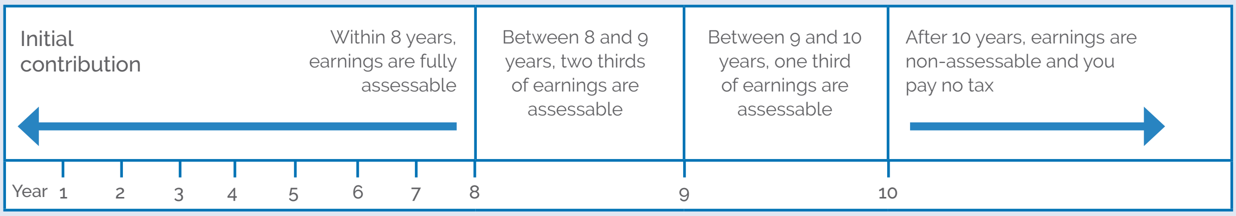
** Income received by an 'excepted minor' or if otherwise treated as 'excepted income' is taxed under the standard marginal tax rates applicable to adults (aged 18 or over).*
‡ See below for more detail on how Insurance Bond Rules work.

Insurance Bond Rules

Insurance Bond Rules are special tax rules that apply to a scholarship plan, when you withdraw your investment earnings as a Non-education Benefit.

If you receive any investment earnings as a Non-education Benefit after 10 years from the date of your initial contribution, and you also satisfy the 125 per cent rule (see 'What is the 125 per cent rule?' below), the amount you receive will be tax free. In other words, the tax on earnings has already been paid by the Fund.

If you receive any investment earnings as a Non-education Benefit within the 10 year period, the amount will count as part of your assessable income and be subject to tax at your marginal rate. The exact amount you will be required to declare, which will be assessed, will depend on when (in relation to the 10 year period) you make the withdrawal—please refer to the following table:



You will however be entitled to receive a 30 per cent tax rebate on the assessable amount, to compensate for tax already paid by ASG on fund earnings in the Fund. The Australian Taxation Office will automatically calculate this special tax rebate, if you declare the assessable amount within 'bonuses received from life insurance companies and friendly societies' in your individual tax return.

What is the 125 per cent rule?

The 125 per cent rule allows you to make additional contributions to your Member Account each year, provided they are not more than 125 per cent of the previous year's total contributions (i.e. they are limited to a 25 per cent increase on the prior year's total contributions).

If you exceed 125 per cent of the previous year's contributions, the start date of the 10 year period will be reset for tax purposes. Exceeding the 125 per cent rule will not alter the tax position of Education Benefits, it will only alter when the 10 year period commences.

Note: It is your responsibility to monitor your contributions with respect to the 125 per cent rule. ASG will provide you with information to help you manage your contributions via your Annual member statement and on our website. If you have any questions about the 125 per cent rule and your contributions please contact ASG or speak to your licensed financial adviser or tax agent.

Case study: Tax impact on education related costs (Education Benefits)

Jim and Mary want to withdraw $500 for an education related expense in the form of tuition fees for their 18 year old son, Alex, from their Member Account.

Even though Alex works part time his parents still want to support him. He earns less than the current effective tax-free threshold of $20,542.

The net contribution component of their account is $2000 and the earnings component is $200. So, in total, they have $2200 in their Member Account.

Because they want to use the money for an education related expense, they would be eligible to receive up to another $85.71 (the tax deduction benefit ASG passes on) in addition to their $200 earnings. It then means that Jim and Mary have a total of $2285.71 potentially available to withdraw.

When submitting the withdrawal, Jim and Mary decide to utilise the earnings component of their Member Account of $200. The tax deduction benefit ASG applies to this is $85.71 resulting in an increased Education Benefit of $285.71.

To complete the withdrawal they would need to take $214.29 from the 'net contributions' component of their Member Account (which is not taxable).

In this way, Jim and Mary are able to withdraw a total of $500 from ASG to fully fund Alex's tuition fees.

Note: Although $285.71 is assessable income to Alex, he is not required to pay any tax on this money because:

- he is 18 years old (satisfying the 18 year age rule), and
- his taxable income (including the Education Benefit) remains below the tax-free threshold at the time, of $20,542.

Case study: Tax impact on non-education related costs (Non-education Benefit)

Jim and Mary decide to withdraw $500 of their earnings from their Member Account. The amount withdrawn isn't an education related expense, but they need this money for personal reasons.

Scenario A (withdrawing after 10 years):

If they have had the Member Account for more than 10 years since the first contribution date and they satisfy the Insurance Bond Rules (subject to the 125 per cent rule, see page 2), they can withdraw the full $500 of earnings, tax paid. This means Jim and Mary receive the $500 and don't have to pay any further income tax on this amount received. ASG can't claim a tax deduction for this amount therefore there is no tax deduction benefit it can pass on to increase this payment amount.

Scenario B (withdrawing in the seventh year):

If they had held the Member Account for seven years, their earnings would be fully assessable and taxed according to their marginal tax rate.

However, the assessable amount here will attract an automatic 30 per cent tax rebate, to compensate for tax paid by ASG on Fund earnings prior to withdrawal.

Jim and Mary can also receive their $500 tax free (at any time) if they withdraw it from the net contributions component of their Member Account, providing they have sufficient balance in their 'net contributions' component.

D. Tax on death benefits

There is no tax payable on benefits received as a result of the death of the member or nominated student.

Additional information

Is there a need to quote a tax file number?

Under existing tax and privacy laws, members and nominated beneficiaries are not required to quote their tax file number (TFN) and no withholding tax will be deducted from earnings or withdrawals as a result of you not quoting your TFN to ASG.

Does withholding tax apply to non-residents?

If you are a non-resident member or student, your account's accrued earnings and any withdrawals from your Member Account are not subject to non-resident withholding tax.

This information has been examined by ASG's Independent Tax Consultant who has confirmed that it reflects the current tax rules as at 25/06/2015. This is general information only and does not substitute appropriate and independent professional advice, which should be obtained in seeking to ascertain how prevailing tax rules apply to your individual circumstances. This information may change over time and we recommend you refer to your tax agent or www.ato.gov.au to ensure this information is up to date.