SuperGuardian
Superannuation administration made simple!

SuperInfo>

Pensions and SMSFs

Pensions in SMSFs have been referred to as ‘Better than a tax haven!’ How do you better a tax haven? The ATO sends you a refund cheque each year! The tax environment within SMSFs is one of the reasons they are so attractive. This fact sheet will explain the benefits, types of pensions available and who is able to commence a pension.

Pension commencement

There are a number of reasons why you may decide to establish a pension from your SMSF. Common reasons for members to move into pension phase include:

- Retirement;
- Pre-retirement tax minimisation strategies;
- Incapacity (Temporary or Permanent); or
- You require cash to meet your living expenses.

The most common reason not to start a pension is that you do not yet need the cash to meet your living expenses and would like to retain the capital and earnings in superannuation.

What is a pension?

When a member is contributing to super, this is called ‘Accumulation’ phase. Essentially all contributions and earnings in the fund are allocated to the member’s account. This money then remains preserved until the member satisfies a condition of release.

Once the member has satisfied a condition of release, the money is reclassified to unrestricted non-preserved and the member can then begin to access their member balance.

If the member decides to establish a pension with their account, the balance is now referred to as in ‘pension phase’. This means that no further contributions can be made into this account.

Many SMSF members often have an accumulation account (to contribute to) and a pension account (to withdraw from) at the same time.

Benefits of setting up a pension

Tax free environment

While in accumulation phase, the fund will pay 15% tax on all contributions and taxable income within the fund. A fantastic benefit for a member moving into pension phase is that the portion of the fund supporting the pension also moves into a tax free environment. This means that there is nil tax to pay on any income or capital gains from these assets.

Refund of franking credits

Imputation credits also known as franking credits represent the tax paid by Australian companies and are attached to franked dividends. These credits are fully refundable to superannuation funds. Usually they are used to offset any tax liabilities the fund has, however for a fund in pension phase, the income is no longer taxable, so no tax liability and the franking credits will be refunded in cash to the fund.

Tax free income stream

For members receiving pension payments from the age of 60 onwards, there is no requirement to report the pension in your personal tax return. This means that all withdrawals from your self managed super fund are tax free!

Control

As long as the requirements of the pension are met, the member can control how much pension they will withdraw as well as the timing of those payments.

Condition of release & payment restrictions

A condition of release is a nominated event that the member must satisfy to be able to withdraw benefits from their superannuation. Once the member has satisfied a condition of release their benefits become unrestricted non-preserved and the member has the option of starting a pension.

Prior to the commencement of any pension the fund’s trust deed must be reviewed to ensure that it allows the commencement of that type of pension and does not restrict its operation within the fund. Some older deeds may not provide for recent changes to legislation and therefore newer pension types such as the Account Based Pension may not be allowed under the trust deed. If necessary, trustees can replace or vary the trust deed so that newer types of pensions can be paid to members.

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Condition Of Release	Cashing Restrictions
Retirement (preservation age—age 60)	Member who was gainfully employed (more than ten hours per week paid employment) has now stopped working and does not intend to return to work in the future.
Retirement (age 60 or older)	Member has ceased working under an existing employment arrangement (more than ten hours per week paid employment).
Attaining age 65	Regardless of work status, members aged 65 or older can access superannuation benefits without restriction.
Permanent incapacity	Member has stopped working and is unlikely to return to work because of ill health.
Temporary incapacity	In limited circumstances, member who has temporarily stopped working due to ill physical or mental health has restricted access to superannuation benefits.
Severe financial hardship	Member is unable to meet reasonable family expenses and has been receiving government income support can gain restricted access to superannuation benefits.
Compassionate grounds	Must be approved by APRA.
Terminal illness & injury	Illness must be certified by two medical professionals, that it will result in the member's death within the next 12 months.
Death	Upon death of a member, superannuation benefits can be released.

Types of pensions

There are several types of pensions that may be paid from an SMSF. The more common pensions include:

- Account Based Pension (ABP);
- Transition to Retirement Income Stream (TRIS or TTR)

Account based pension

Account Based Pensions (ABP) are very popular for SMSF members as they are simple to both calculate and understand. There is a requirement to withdraw a minimum amount that is calculated based on the age of the member and their account balance each year. However, there are no restrictions on the maximum that can be withdrawn or the timing of the payments. Members are able to dictate how much they receive from the fund and how often.

Transition to retirement pension

For members that have reached preservation age but are not yet able to satisfy a condition of release, there is hope! These members are able to commence a transition to retirement account based pension also commonly known as a transition to retirement income stream (TRIS). These pensions are also easy to understand, they are essentially an account based pension – with a minimum requirement and no restrictions on the timing of payments. However, there is a restriction that members can only withdraw up to 10% of their member balance each year.

Members receiving a TRIS are able to easily convert to an ABP as soon as a condition of release is satisfied, lifting the 10% maximum restriction.

Date of birth	Preservation age
Before 1 July 1960	55
1 July 1960–30 June 1961	56
1 July 1961–30 June 1962	57
1 July 1962–30 June 1963	58
1 July 1963–30 June 1964	59
After 30 June 1964	60

Annual minimum pension requirements: (ABP & TRIS)

The following table outlines the minimum annual drawdown requirement for both Account Based Pensions & Transition to Retirement Income Streams. The member's age at 1 July each year (or at pension commencement) will determine the minimum percentage of their member balance to be drawn.

Age of Member	Minimum
Under 65	4%
65 – 74	5%
75 – 79	6%
80 – 84	7%
85 – 89	9%
90 – 94	11%
95+	14%

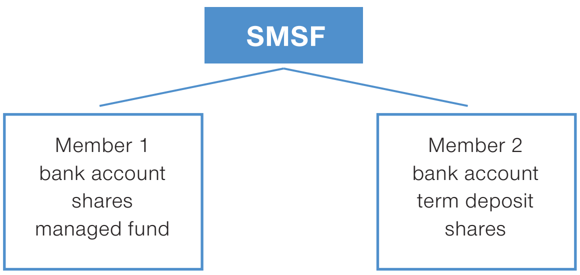
Can I continue to make contributions to super?

It is true that member balances in pension phase cannot be added to. However, this does not mean that members can no longer contribute to super. Contributions will simply be allocated to a new member account in accumulation phase. The normal rules and limits for superannuation contributions will continue to apply.

How is tax calculated if my fund is part pension & part accumulation?

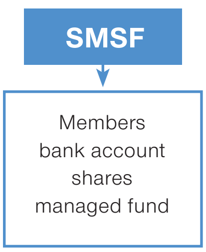
There are two options for SMSF's running both pension and accumulation accounts for members. The first option is to segregate assets of the fund which essentially means that assets are identified as being owned by separate member accounts. This means that it is simple to identify which income is tax free, however additional work is often required by the trustee and administrator to properly administer the fund.

Example: Segregated Accounts



The second option is to leave the assets of the fund unsegregated. The fund will then need to obtain an actuary certificate each financial year to determine the proportion of the fund's income that will not be subject to tax.

Example: Unsegregated Accounts



A fund in full pension phase will not require an actuary certificate.

What happens to my pension if I die?

It is important to consider your nominated beneficiaries when commencing a pension and to ensure that your nomination remains current and valid.

SMSFs have the ability to pay a reversionary pension if their trust deed allows. When commencing a pension, members can nominate an eligible reversionary beneficiary. With this nomination in place, upon death, the pension will continue to be paid to the reversionary beneficiary.

This can assist with preserving the components of the pension should the member have other interests also in the fund. It is best practice if a member wishes to have a reversionary beneficiary, that this is done at the commencement of the pension, rather than 'mid stream'.

Trustees should review the SMSF Trust Deed to ensure it allows for reversionary nominations prior to accepting them.

How many pensions can I start?

There are no restrictions on the number of pensions a member can start. A member can commence as many pensions as needed to suit their own personal situation.

Can I consolidate my member balance?

A member can at any time nominate to combine their separate balances. This can include consolidating accumulation and pension accounts or consolidating multiple pension accounts. This process is commonly known as a 'pension stop and restart' because it generally involves stopping the existing pension, then immediately transferring balances and commencing a new pension.

SMSF members should consider their situation carefully before consolidating accounts as tax free components are recalculated each time a new pension commences. Depending on beneficiary nominations, estate planning and personal circumstances, there may be instances where consolidation is not appropriate.

We strongly recommend that you seek advice from your financial adviser.

Centrelink issues

Some SMSF members qualify for additional Centrelink pension benefits. We recommend you contact Centrelink and your financial adviser to discuss.

What does SuperGuardian do to start my pension?

SuperGuardian is not licensed to provide financial advice and we cannot recommend a pension product to you.

It is a specialised area and we recommend you consult with your financial adviser, estate planning lawyer and SMSF deed specialist to document and fulfil your wishes.

The steps we then undertake include:

1. The preparation of compliance documentation and minutes of meetings,
2. A review of the investment strategy – Trustees need to consider risk/return, diversification, liquidity and the ability to meet pension liabilities,
3. If the account is to be segregated to provide separate assets to support the pension, the segregation must be done prior to commencement of the pension,
4. The fund needs to register for PAYG purposes, as tax must be deducted by the fund prior to payment of the pension to the member (members under 60),
5. The completion of a Pension Schedule for Centrelink/DVA purposes and
6. A review of the nominated beneficiaries and, where instructed, noting of a reversionary pension.

SuperGuardian's pension administration

By utilising the daily online information platform provided by SuperGuardian, you can check the minimum and maximum pension requirements for an applicable year, be advised of what you have taken year to date and how much more you must withdraw to ensure your maximum pension obligations are met.

At the beginning of each financial year, you can log onto SG's secure website to obtain indicative minimum and maximum pension calculations for the new financial year, to allow any adjustments to be made with respect to your pension payments. After completion of the SMSFs annual return, we provide finalised pension calculations for the new financial year.

Summary

You should consult your licensed financial adviser prior to undertaking any strategy. The information above should be considered general in nature and does not take into account your personal circumstances.

Postal
GPO Box 1215
Adelaide SA 5001

Telephone
1300 787 576 (National)
08 8221 6540 (Adelaide)

Facsimile
08 8221 6552 (Adelaide)

Email
info@superguardian.com.au

Adelaide
65 Gilbert Street
Adelaide SA 5000

Melbourne
Level 13
200 Queen Street
Melbourne VIC 3000

Sydney
Level 4
95 Pitt Street
Sydney NSW 2000

Perth
Level 24
77 St Georges Terrace
Perth WA 6000

Brisbane
Level 22
127 Creek Street
Brisbane QLD 4000

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Chartered Accountants
www.superguardian.com.au