

pensions and your SMSF



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;
- Transition to retirement 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 earnings. 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 generated by 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 available to superannuation funds. Usually, they are used to offset any tax liabilities the fund has, however where a fund is in full pension phase, there is no tax payable, and any franking credits are refunded in full by the tax office.

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 within prescribed limits 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 within the prescribed limits 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 24 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)

annual 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

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, providing they draw at least the minimum amount per annum.

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

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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%

The importance of taking the annual minimum pension requirement

Legislation requires a minimum drawdown annually once a pension commences. Failure to do so results in the fund losing its tax exempt status, and therefore tax is payable on income and capital gains of the fund for the entire financial year.

It is therefore vital you ensure your minimum pension has been drawn prior to 30 June, each financial year. Our online reporting software assists in meeting your pension drawdown requirements by tracking pension withdrawals against your required minimum drawdown for the financial year.

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.

Concessional contributions will still attract 15% tax when entering the fund, regardless of the pension status of the fund.

For contributions made after a pension commences or establishes a new accumulation account for the member within the fund, earnings on these contributions will be taxed at 15% when a fund has both accumulation and pension accounts. Legislation requires that we obtain an actuarial certificate to ascertain what percentage of the fund's income is tax exempt.

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 can refer you to estate planning specialists or SuperGuardian for strategic tax advice, if you wish.

Summary

Simply download the pension commencement form on our website – email to us and commence your pension.