Norwest SMSF Discussion Group

Agenda for 26th April 2017

5.30 PM	Registration & Welcome Refreshments
6.00 PM	Pension Issues from 1st July 2017
6.45 PM:	Questions and Discussion on Pensions
7.00 PM	Changes to the requirements for obtaining an actuarial certificate
7.30 PM	Close of Meeting

Pensions

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Pensions
Effective from 1st July 2017

Covering the new super regime as it applies to pensions and TRISs, this session outlines the key steps, strategies and practical tips and traps that advisers need to be aware of including:

The most substantial changes to superannuation pensions since 1st July 2007

Pensions – Post 1st July 2017

1. New $1.6M transfer balance cap
2. Excess transfer balance penalties
3. CGT cost base relief (segregated and proportionate methods)
4. TRIS issues and removal of tax benefits
5. Lump sums and minimum pension requirements
6. Internal commutations
7. Key issues, actions and strategies pre 30 June 2017

3. CGT cost base relief (segregated and proportionate methods)

Who is it for:

Member has **more than $1.6 million** in superannuation pension phase

and/or

Member is on transition to retirement income stream (TRIS) they wish to **continue this TRIS from 1 July 2017**

If you have SMSF's who are NOT in Pension phase or TRIS – They are in Accumulation phase = then this CGT relief **does not apply to you**

Law Companion Guidelines LCG 2016/8 - Transfer balance cap and transition-to-retirement reforms: transitional CGT relief for superannuation funds

Balance Transfer Cap – From 1st July 2017

Accumulation Phase → Pension Phase (Tax Free Retirement) $1.6M BTC

Pension Balances above $1.6M on 1st July 2017

1) **Withdraw the excess** from the superannuation system

2) **Commute the excess back** to the accumulation phase (Internal Roll over)

From 1 July 2017, investment earnings and capital gains generated from transition to retirement income streams **(TRIS) will no longer be tax free**

Transitional CGT Relief

Fund is only exposed to CGT on future growth in the asset value from that point

Intent of the new rule is to **provide CGT relief** on the **gains accrued before that date**, so as not to disadvantage members who are required to commute a pension due to the new TBC, or are impacted by the TRIS tax changes - will lose the tax-exempt treatment of investment earnings.

Preserves the tax exemption **by resetting the cost base** of those investments to their market value

Assets owned by the fund on **9 November 2016** (being the date the legislation entered Parliament).

Relief is not automatic – the trustee of a super fund must **choose for the relief to apply** for a CGT asset in the approved form

Irrevocable election can be made on an asset by asset basis to reset the CGT cost **base to its market value (**deemed to have sold and re-purchased the asset at that market value)

One Member Fund with only one asset

30th June 2017

MV of
Pension
Assets
$2.6M

Accumulation

1st July 2017

TBC of
$1.6M

Asset Sold 2020
for $3.6M

Capital Gain $2.6M

Taxable Gain =
$1M X 1.6/2.6
(Approx – AC
Requirement)

Tax Free Gain
– Balance Amount

Asset Purchased
1997 $1M

30th June 2017
MV of House
$2.6M

1st July 2017
TBC is $1.6M
$1M in
Accumulation Phase

Transitional CGT Relief

Different rules apply depending on whether the fund currently uses the **segregated or proportionate (un-segregated)** method in determining its exempt current pension income (ECPI).

SMSF's will **no longer be able to use the segregated method in determining the ECPI**.

Segregated Assets: Where some assets (asset pool) of the fund are marked as pension assets and may belong to certain members of the fund – **income on these assets belong to pension members only**

Un-Segregated Assets – Proportionate : Where all assets of the fund belong to all members of the fund and **all members share the income of those assets**

Examples of Segregated Assets

100% Segregation

Mixed Segregated Accumulation Assets of all accumulating members of an SMSF

Segregated Pension Assets of a Particular member of an SMSF

Partial Segregation

Accumulation Assets

Mixed segregated Pension Assets of all Pension members of an SMSF

Segregated Pension Assets of a Particular member of a SMSF

100% Segregation

Mixed Segregated Accumulation Assets of all accumulating members of an SMSF

Mixed Segregated Pension Assets of all pension members of an SMSF

Examples of Un- Segregated Assets

All the Assets of a SMSF are Mixed for all members (Incl. Pension and Accumulation Members)

Transitional CGT Relief **-Segregated Assets**

- An asset or group of assets **is transferred from the pool of assets supporting the current income stream, to an accumulation pool** from 9th Nov 16 to 30th June 17
- "9 November 2016 to 30 June 2017" - meaning the **availability of market values** transfer and **deemed sale and re-acquisition can occur at any point** from during this time is key.
- The deemed sale to market value occurs as part of the exempt pension assets, so the **capital gain is ignored for tax purposes**
- Income and capital gains arising from those assets **after the move into the accumulation pool is subject to tax.**

Transitional CGT Relief **-Segregated Assets**

Mixed Segregated Accumulation Assets of all accumulating members of an SMSF

Segregated Pension Assets of a Particular member of an SMSF

Accumulation Pool

Pension Pool

Asset transferred from 9th November 2016 to 30th June 2017

Transitional CGT Relief **- Un- Segregated Assets**

- The deemed **sale occurs on 30 June 2017**, meaning this is the **important valuation date**
- The resulting notional capital gain **may be included as part of the 30 June 2017 assessable income of the fund**
- Capital Gain **actuarially determined exempt pension factor** applying to determine how much is taxable.
- Fund can **defer the notional capital gain until the asset is actually realised for CGT**
- **Date of acquisition** for the purpose of applying the one-third CGT discount will also be **reset**
- Documented in the approved form **before lodgement of the fund's 2016-17 annual return.**
- **Election is irrevocable** and trustee(s)/members cannot change things if they subsequently realise they got it wrong

Transitional CGT Relief -**Segregated Assets**

All the Assets of a SMSF are Mixed for all members (Incl. Pension and Accumulation Members

All the Assets of a SMSF are Mixed for all members (Incl. Pension and Accumulation Members

Asset transferred on 30th June 2017

1st July 2017

Transitional CGT Relief – Any action required

1. At least one member of an SMSF with **more than $1.6 million in pension phase** across all SMSF's you manage

   Options

   - **Commute some** or all of their pension to Accumulation phase in the SMSF to comply with the TBC

     Or

   - **Withdraw** amount above TBC

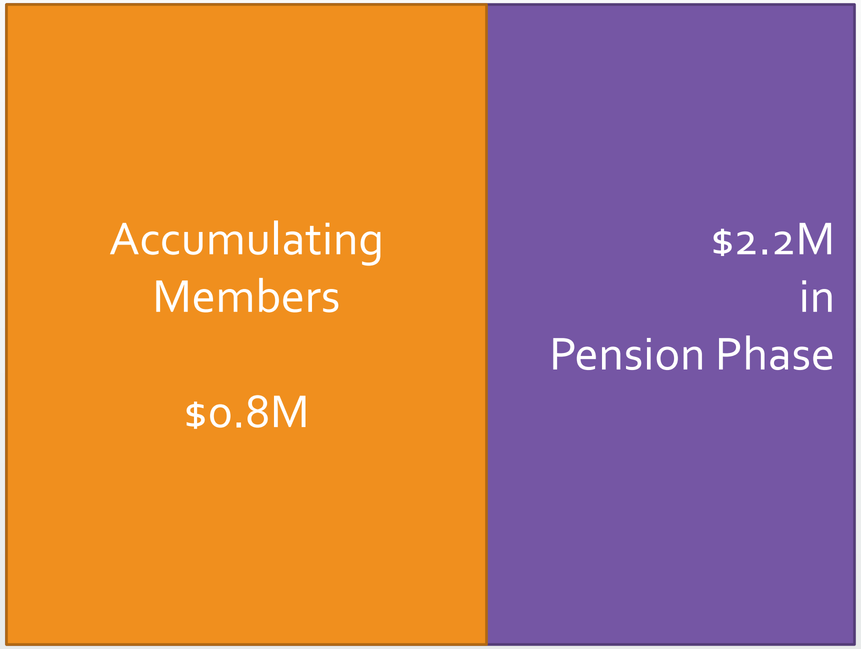
1. A defined benefit pension fund – **<u>is not part of our discussion</u>**

2. TRIS commenced before 9 November 2016 that **faces losing the tax-exempt treatment** of its investment earnings from July 1 2017 - **Since the member has not retired**

Transitional CGT Relief - Actions

- What method is the SMSF using to claim ECPI – **Segregated or Un-segregated**
- Which fund assets are eligible for CGT relief – **Only if MV is more than Cost Price**
- Will the asset be disposed of within 12 months of the date of the re-set
- Is the asset **likely to increase in value in future** or is it a defensive investment not subject to price variation
- What is the **ECPI percentage of the SMSF expected** to be in the year the affected assets are sold - This may include the impact of other **members entering pension phase** increasing this percentage – **next slide**
- Members with a TRIS; are they able to satisfy a condition of release so that **there is a potential to convert the TRIS to a standard account-based pension**

Actions – Un-segregated Assets
Accumulating members will go on pension



Current only one member is in Pension Phase

After 2 Years

When Accumulating members Move to Pension
– Asset can be sold tax free

Example

2 Member Fund Value $3M on 30th June 2017 – Henry (62 Years retired) is on Pension with $2.2M, Martha (58 Years – not retired) is in accumulation with $0.8M – Asset is one property purchased for $2.25M in 2004. Balances on 1st July 2017 - $1.6M Pension Phase and $1.4M in Accumulation Phase.

Options:

1) Sell the property in 2016 – 17 year and pay the CGT

2) Reset the cost base and notional CGT to be included in 2016 – 17 Income – Election Taken

3) Notional gain can be deferred until the property is sold – Election Taken

4) Martha will retire in next couple of years

Option 2 – Notional CGT included in 2016 -17 Income

Notional Capital Gain	$750,000
1/3 Discount	$250,000
Taxable Gain	$500,000
Exempt $2M/ $3M	$333,333
Assessable Income	$166,667
15% Tax Payable	$25,000

Option 3) Notional gain can be deferred until the property is sold

Assuming Property is sold for $4M in 2020	
Cost Base reset to	$3M
Selling Price	$4M
CGT	$1M
1/3 Discount	$333,333
Taxable CGT	$666,667
Exempt Proportion (Assumption $2M/$4M)	$333,333
Add Deferred CGT (Actual Gain is $1.75M)	$167,667
Total Taxable CGT	$500,000
Tax 15% $75,000	

Option 4) Martha retires in 2020 before property is sold

Selling Price of property	$4M
Assets in Pension Phase:	
Henry $1.6 + Growth $500K	$2.1M
Martha $1M + Growth $333K	$1.333M
Total	$3.43M
Henry Accumulation	
$400K + Growth $177K	$0.57M

1/3rd Discount and Exempt % 3.43M/$4M approx 86% or

$1.75M * 2/3 * 86% = CGT $166K and Tax 15% = $25,000

4) TRIS issues and removal of tax benefits

- Income from **Assets supporting a TRIS is no longer going to be exempt income** from 1st July 2017
- Three Options
  - **Commute TRIS** – pay 15% on income
  - **Continue TRIS – withdraw minimum** – pay 15% on income – reduce personal income tax
  - **Retire**

When can a TRIS become an Account Based Pension

SISR Schedule 1 Member is **no longer working (item 101) and is retired** or Age 65 (item 106)

SISR 6.01 (7) For the purposes of Schedule 1, the **retirement** of a person is taken to occur:

(a) in the case of a person who has reached a **preservation age that is less than 60**--if:

(i) an arrangement under which the **member was gainfully employed has come to an end**; and

(ii) the trustee is reasonably satisfied **that the person intends never to again become gainfully employed, either on a full-time or a part-time basis; or**

(b) in the case of a person **who has attained the age of 60**--an arrangement under which the **member was gainfully employed has come to an end**, **and either** of the following circumstances apply:

(i) the person **attained that age on or before the ending of the employment**; or

(ii) the trustee is reasonably satisfied **that the person intends never to again become gainfully employed, either on a full-time or a part-time basis.**

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When can a TRIS become an Account Based Pension

SISR 1.03

full-time " , in relation to being gainfully employed, means **gainfully employed for at least 30 hours each week.**

"gainfully employed " means employed or self-employed for gain or reward in any business, trade, profession, vocation, calling, occupation or employment.

part-time " , in relation to being gainfully employed, means **gainfully employed for at least 10 hours, and less than 30 hours, each week**

5) Lump sums and minimum pension requirements

- Minimum pension must be paid to ensure that there is no tax income supporting a pension
- A **Lump sum is a debit to BTC** amount
- **A Lump sum is not counted in minimum pension payment amounts**
- If future contributions are expected which will be converted to pension
  - **Lump Sum Vs Minimum Pension Amount**

Debit to Balance Transfer Cap

- usually arise when **person's superannuation interests are commuted** (ie changed from income stream to lump sum)
- **lump sum payment if income stream commuted**
- structured settlement contributions
- losses or payments resulting in lower superannuation balance (eg fraud, dishonesty or bankruptcy)
- payment splits (**divorce or relationship breakdowns**)

6) Internal Rollovers

- Converting a pension account to an accumulation account
- Does the trust deed allow it?
- How will internal rollovers happen
  - Minutes
  - Letter of commutation request from member
  - New Pension documents
  - Reversionary Pension Vs Non-Reversionary Pensions
  - An opportunity to change / adjust Tax Free and Taxable component prior to 30th June 2017

7) Key issues, actions and strategies pre 30 June 2017

Change Taxable / Tax Free Components

Example: Member Balance \$1.2M all taxable component – commute pension > move to accumulation – withdraw \$540K and commence Pension 1 with \$660K with taxable component and then contribute non-concessional \$540K (Tax free Component) and commence Pension 2

Set up 2nd SMSF

Example: Fund Balance \$5M – husband and wife – withdraw \$1.8M – two kids both are married – set up 2 new funds - contribute \$450K for each couple as non-concessional contribution before 30th June 2017 – Since you are also members – you can control the fund with kids