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DFP Module 3

Superannuation & Retirement Planning & SMSF

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Module 3

Superannuation and

Retirement Planning

(including SMSFs)

The units of competency covered in these course materials include:

FNSFPL502	Conduct financial planning analysis and research
FNSFPL503	Develop and prepare financial plan
FNSASICU503	Provide advice in Superannuation
FNSSMS501	Invest self-managed superannuation fund assets
FNSSMS505	Support trustee in the selection and performance monitoring of outsourced services
FNSSMS601	Provide advice in self-managed superannuation funds
FNSSMS602	Apply taxation requirements when advising in Self-Managed Superannuation Funds
FNSSMS603	Apply legislative and operational requirements to advising in self-managed superannuation funds

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1.0 INTRODUCTION

Australia's population is ageing. Between now and 2050, the number of older Australians (age 65 and over) is expected to more than double. At the same time, the proportion of working-age people in the total population is expected to fall. As a consequence there will be fewer people of working age to support an increasing number of older Australians. This will place greater demands on the Government's ability to provide services to the aged.

To address this problem, the Federal Government introduced compulsory superannuation for most Australian employees. At present, employers are required to pay 9.5% of an employee's salary into superannuation. The government wants people to fund their own retirement, because the alternative is that taxpayers will have to fund it for them. Australians want to control their own financial security, because it impacts their quality of life in retirement. And of course the sheer size of the financial services industry (which includes financial planners) is in large part due to the size and success of compulsory superannuation and the concessional tax treatment the government has bestowed on it.

For many Australians, superannuation may grow to be their largest asset. Because nearly all Australians have some superannuation, the advice needs that now flow from ordinary Australians with a superannuation asset as large, or larger than their car, contents or family home means the financial planning industry has a strong future.

The superannuation sector is a highly regulated space, and it is critical to understand the different elements that support the system. This module takes you through the key elements underpinning the superannuation system, and the factors that impact advice. It provides you with a framework to apply the knowledge and skills you have learned in this module, in the provision of superannuation advice.

Often people don't realise that superannuation has only been around since 1986. Since this time it has changed considerably and continues to do so.

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Key dates relevant to superannuation:

1986 - 3% superannuation payment introduced for those employed under certain awards

1992 - Superannuation Guarantee introduced.

1993 - Superannuation Industry (Supervision) Act introduced.

1999 - Superannuation preservation rules amended.

2002 - Superannuation Guarantee increased to 9%.

2003 - Superannuation Guarantee required to be paid quarterly.

2003 - Introduction of Government co-contributions.

2004 - Superannuation Safety Amendment Act introduced.

2004 - Government policy on superannuation co-contributions extended.

2004 - Compulsory portability of benefits introduced.

2004 - APRA superannuation licensing introduced from 1 July 2004 with a two year transition period.

2005 –Choice of fund legislation introduced.

2005 - Compulsory portability of benefits extended.

2005 - Contribution Surcharge Tax abolished from 1 July 2005.

2006 - Contribution splitting introduced from 1 January 2006.

2006 - Licensing transition period ended 30 June 2006.

2007 - Simplified Superannuation introduced from 1 July 2007.

2010 - Superannuation (Unclaimed and money and lost members) Act 1999 amended.

2013 - Stronger Super reform implemented

2013 - Introduction of government superannuation contribution rebate for low income workers.

2013 - Government co-contribution matching rate reduced from 100% to 50% and maximum entitlement capped at $500.

2013 - Superannuation (Unclaimed and money and lost members) Act 1999 amended.

2014 – Introduction of MySuper

2014 – Superannuation Guarantee increased to 9.5%

2017 - Super Reform Package effective 1 July 2017

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2.0 LEARNING OUTCOMES

When you have completed this module, you should be able to:

- Understand who regulates superannuation funds.
- Differentiate between an accumulation fund and defined benefit fund.
- Identify the different types of super funds.
- Understand who can contribute into superannuation, and under what circumstances.
- Identify the different kinds of contributions.
- Understand the different taxation applied to superannuation earnings, within all the different phases.
- Understand what the superannuation guarantee is, and who it applies to.
- Explain the government co-contribution.
- Understand super splitting and how it works.
- Understand what salary sacrifice is and how it is applied.
- Identify the role and responsibility of superannuation trustees.
- Know what preservation ages apply to accessing superannuation.
- Identify the tax applicable to superannuation benefits.
- Explain the benefits of a transition-to-retirement strategy.
- Explain the mechanics of a superannuation pension, and how it works.
- Understanding the transfer balance amount
- Understand how Self-Managed Superannuation Funds operate, including rules on borrowing.

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3.0 SUPERANNUATION IN AUSTRALIA

In the Investment Planning module, we looked at the four main asset classes - cash, fixed interest, property and shares and we examined their respective risk and return characteristics. One decision that anyone with funds to invest must make is how much of their investment they wish to place in each of these asset classes. The second decision that needs to be made is whether that investment should be made within superannuation or outside the superannuation environment. There are advantages and disadvantages to both.

Some people mistakenly think that superannuation is a 'fifth' asset class - they think they must decide how to allocate funds between cash, fixed interest, property, shares and super. What they fail to understand is that superannuation is ***not*** another asset class - it is merely an investment vehicle.

Example

Darcy and Luca each have $40,000 to invest. They both decide to invest in a fund that comprises 15% cash, 30% fixed interest, 20% property and 35% shares. Darcy chooses to invest his funds within the superannuation environment whereas Luca chooses to invest his funds outside of super. The advantage of investing in super is that there are significant tax benefits but the downside to superannuation is that the funds are generally not accessible until retirement.

WHY ARE THERE TAX BENEFITS FOR INVESTMENTS WITHIN SUPER?

If less Australians were dependent on the government for their retirement needs, this would take enormous pressure off the government leaving more flexibility to devote federal and state revenues to other sectors.

The Australian Government implemented both tax changes and savings policies through the 1980s and the 1990s as a means of encouraging Australians to become more financially independent in retirement. This need arose because of:

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- Australia's ageing population and subsequent rising dependency ratio (ratio of Social Security recipients relative to tax paying workers).
- The declining level of savings of the general population relative to the GDP (Gross Domestic Product).

The central mechanism by which increased financial independence can be achieved is superannuation, partly because funds invested in superannuation generally cannot be accessed until retirement. The attraction of investments in superannuation is that those investments can grow in a concessionally taxed environment compared with investments outside of superannuation.

WHAT IS MEANT BY A CONCESSIONALLY TAXED ENVIRONMENT?

To encourage Australians to save for their retirement, the Government provides tax incentives on superannuation at three different stages:

1) when you, or your employer add funds to superannuation from pre-tax dollars - such funds are called concessional (before-tax) contributions
2) when your super fund earns income
3) when you receive your superannuation benefit

WHAT ARE THE TAX INCENTIVES?

Tax incentive No.1

When concessional (before-tax) contributions are made to super, the super fund taxes those contributions at a base rate of 15%rather than a person's marginal tax rate. Exceptions apply for low income earners[1] and those earning combined superannuation contributions and taxable income above $250,000[2].

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[1]Low income earners can receive a super contributions tax rebate of $500 if their taxable income is less than $37,000.

[2] Individuals whose adjusted taxable income exceeds $250,000 from 1 July 2017 will have their concessional contributions taxed at the effective rate of 30% representing the base 15% contributions tax and a further 15% tax known as Division 293 tax for amounts of concessional superannuation contributions which bring the individual's combined relevant

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Case Study 1

Jamie is a 32 year old lawyer. She earns $95,000 per year. Her sister Sally, 29 years old, is a graphic designer with an annual salary of $65,000. Jamie's marginal tax rate is 37% and Sally's marginal tax rate is 32.5%. If Jamie contributes $10,000 of her salary to her super fund, she will only have to pay 15% tax instead of 37% tax meaning less tax is applied to her income and more is left over to invest. If Sally contributes $10,000 of her salary to her super fund, she too will only pay 15% tax even though her marginal tax rate is 32.5%. These marginal tax rates do not include the Medicare levy- if we included the Medicare levy the tax savings from superannuation contributions are even more stark.

Tax Incentive No.2

When funds invested within superannuation earn income, the earnings on those funds are only taxed at up to 15% instead of being taxed at the investor's marginal tax rate. (For retirees, income on earnings in superannuation may be tax free).

Case Study 2

Jamie is a 32 year old lawyer. She earns $95,000 per year. Her sister Sally, 29 years old, is a graphic designer with an annual salary of $65,000. Jamie's marginal tax rate is 37% and Sally's marginal tax rate is 32.5%. Jamie and Sally both receive an inheritance of $50,000. Jamie adds the money to her super fund. Sally invests her inheritance in a managed fund outside of super. Both investments earn income of $3,000 this year. Jamie's super fund will pay tax on the $3,000 of earnings at the rate of 15% whereas Sally's investment income will be taxed at her marginal tax rate of 32.5% plus the Medicare levy.

superannuation contributions and other relevant "income" above $250,000. The "income" amount for this calculation represents taxable income plus net financial investment loss plus net rental property loss plus net amount on which family trust distribution tax has been paid less super lump sum taxed elements with a zero tax rate. The Division 293 tax may apply on a lower sum if the member has excess concessional contributions as extra tax will instead be reflected in excess contributions tax.

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Tax Incentive no.3

When you receive your superannuation benefit either as an income stream (called a pension) or as a lump sum, if you are age 60 or over, those benefits might be tax free. This is a complex area and will be discussed in depth later in this module.

THE PHASES OF SUPER

Superannuation can be divided into three phases:

- Accumulation phase
- Transition to retirement income stream phase
- Retirement income stream phase

Accumulation Phase

The accumulation phase is the period of time during which an investor (super fund member) accumulates a superannuation portfolio to help fund their retirement at some point in the future.

These funds can be accumulated by contributing new funds into the super portfolio investment or they can be funds that are added from income earned on the funds already invested, or they can arise from the change in value (growth) of the investments already within the super fund.

Case Study

Cameron age 54 has a super fund which at the start of the year was worth $180,000. Throughout the year, Cameron's employer contributed $9,000 into his super fund and the investments themselves generated income of $10,200. At year end, the value of Cameron's super fund was $199,200. Cameron cannot access his super funds until he retires but both he and his employer can contribute to the fund as it is still in the accumulation phase. It will remain in the accumulation phase until Cameron elects to take an income stream when he reaches a condition of release.

Transition to retirement phase Income stream

This phase is where a super fund member continues to work, and at the same time, they are able to withdraw some of their super money in the form of an income stream via a

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separate account. In this phase no further contributions may be added to the income stream account. The super fund pays an income stream or pension to the super fund member from the monies that have been transferred from the accumulation account plus any new earnings (income) that the income stream account continues to generate.

Case Study

Cameron age 61 is still working but he decides to reduce his work days from 5 days to 3 days to help him adjust to the idea of retirement. As there has been a reduction in his employment income Cameron decides to transfer some of his superannuation from the accumulation phase into a pension phase and draw a regular income stream (pension) from the pension account comprising an initial $400,000 superannuation balance to make up for the shortfall in his income. Contributions can still be made into his accumulation account.

Retirement phase Income stream

The retirement phase Income stream is the period during which an investor chooses to access their superannuation via an income stream (pension). In this phase, no further contributions can be added to the income stream account. Rather, the super fund will be in an income stream account and it pays an income stream or pension to the super fund member from the monies that have previously accumulated in the accumulation phase plus any new earnings (income) that the super fund (income stream account) continues to generate. Retirement phase income streams include all superannuation pensions and annuities, except for transition to retirement income streams and non-commutable allocated pensions and annuities.

Case Study

Cameron retires when he turns 64 years of age. His super fund has accumulated quite a bit of money over the years and is now worth $512,000. Cameron decides to transfer his account from the accumulation account into the pension account and draw a regular income stream (pension) to meet part of his living costs during his retirement years. He has an investment property that provides good rental income for him as well.

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3.1 WHO REGULATES SUPER FUNDS

The legislation which provides the rules for superannuation is the *Superannuation Industry (Supervision) Act 1993 (Cwlth) (SIS Act*). The regulators who ensure compliance with the legislation are the Australian Securities and Investments Commission (ASIC), the Australian Prudential Regulation Authority (APRA) and the Australian Taxation Office (ATO).

ASIC regulates financial services to protect consumers.

ASIC's primary role in relation to SMSFs is to regulate the accountants, financial planners, SMSF auditors and providers of products and services to SMSFs. ASIC also regulates many of the financial products that SMSFs commonly invest in.

ATO regulates Self-Managed Superannuation Funds (SMSFs) in accordance with the super laws and also administers the tax system.

APRA regulates large super funds (other than SMSFs) and assesses applications for the release of retirement benefits on compassionate grounds from SMSFs.

Any particular superannuation fund is governed by the specific rules outlined in the fund's trust deed, a legal document which sets out the rules of the fund and the rights and obligations of the trustee and members of the fund.

The trustee of the fund holds the assets in the fund for the benefit of the fund's members and their dependants. It is the trustee who is responsible for the operations of the fund.

One of the key sections of the *SIS Act* is Section 62. This section specifies that a superannuation fund must be maintained *solely* for the provision of benefits for its members in retirement or that member's legal personal representative or dependants upon the death of the member. This is known as the 'sole purpose test'. Any breach of the sole purpose test by the trustee of the fund can result in monetary penalties or imprisonment. See Appendix 1 "Failing the sole purpose test – it's a crime."

THE SOLE PURPOSE TEST

When a super fund invests in assets with the sole purpose of providing benefits for its members in retirement, this purpose will normally be able to be shown by the fund's

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investment strategy. An example of where a trustee fails to maintain a fund for the required "sole purpose" was illustrated by the "Swiss Chalet" case (Administrative Appeals Tribunal, 19 July 1995). That case involved a fund, the assets of which included shares in a private company whose only assets were shares in a golf club, units in a unit trust whose only asset was a chalet in Switzerland, and a property in Sorrento (a Victorian beachside resort) which had been used for the personal use of a member of the fund. The Tribunal held that the ownership of those assets caused the fund to fail the sole purpose test.

The acquisition by a fund of "life style assets" such as a holiday home, artwork, or vintage cars, normally has sole purpose test implications. Purchases of these types of assets by a fund could possibly be justified by the expectation that the assets' values will be subject to capital growth and therefore provide benefits to members in retirement. However the problem is that members normally want to use the holiday home, or hang the artwork at home, or drive the vintage car. Such applications of an asset will cause there to be breaches of the sole purpose test – the fund members are not permitted to derive "benefits" from these assets prior to retirement. The sole purpose test for such assets cannot normally be overcome by leasing the asset at an arm's length rent to the member because it will likely breach the in house asset test restrictions (discussed later in this module).

Funds which do comply with the Act are said to be 'complying superannuation funds', and such funds pay only 15% tax on investment earnings – whilst the fund is in accumulation phase. If a fund is not a complying superannuation fund, any taxable income derived from the fund may be taxed at the highest marginal tax rate, and the capital amount can be taxed as well! A breach of the sole purpose test might render the fund a non-complying fund.

Case Study

Belmont Super Fund is a small superannuation fund with assets of $1,220,000 and earnings income of $74,000. The super fund members have marginal tax rates that vary between 32.5% and 37% plus Medicare Levy. The fund is found to be a non-complying super fund. Consequently, the earnings of the fund are taxed at the highest marginal tax rate and a tax penalty at the highest marginal tax rate is also applied to the $1,220,000 capital amount of the fund.

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MARKET LINKED VS DEFINED BENEFIT FUNDS

There are two main types of superannuation funds to which individuals can belong.

They are:

- market linked funds
- defined benefit funds

MARKET LINKED FUNDS

Market linked funds are currently the most common type of superannuation fund operating in Australia. For these funds, both the employer and employee can make contributions. These funds can be invested in the same way as any managed funds are invested, and when the employee retires, he/she receives all that has been contributed plus any earnings of the fund less any fees.

With market linked funds, the member of the fund has a strong interest in the performance of the fund in which their money is invested because this determines what they will ultimately receive.

DEFINED BENEFIT FUNDS

These are old style funds that were common in the public sector and local government workplaces until the 1990's. Defined benefit funds are mostly closed to new members.

A defined benefit fund provides an employee with a set amount on retirement. The amount is calculated based upon a formula taking into account the employees final average salary and a benefit multiple (derived from period of service and a contribution rate multiple). Unlike a market linked fund, the employee is not concerned about the performance of the fund since they will receive the same payout regardless of the fund's performance. The employer agrees to make up any shortfall if there are not sufficient monies in the superannuation fund to cover the defined benefit on payout. Naturally, the employer will therefore be very interested in the performance of the fund.

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Example

Aaron has been a member of corporate super fund for 25 years and his fund provides defined benefits. Aaron's benefit might be something like:

5 X his final average salary as a lump sum, or

75% of his final average salary as a monthly income stream until he dies

Pro Tip

Defined benefit funds are by far the most complex superannuation accounts to provide end clients with advice on. This is because they are inevitably all different, and you need to undertake appropriate research for each specific defined benefit fund at all times.

3.2 SUPERANNUATION OPERATION

Superannuation investment options are offered by fund managers, life insurance companies, banks and other financial institutions. Of course you can do-it-yourself via a Self-Managed Super Fund (SMSF) which we will discuss later in this module.

Superannuation funds can be invested in cash, fixed interest, property and equities (international and domestic) or any combination of these in the same way as non-superannuation managed funds can be invested across the four asset classes. In fact super funds can also invest in other 'exotic' types of investments including race horses, gold, art and other collectibles – but with extreme caution!

Superannuation funds are made up of:

- members' contributions
- employers' contributions
- earnings (income) from investments
- government co-contributions
- spouse contributions

From these funds are withdrawn:

- fund benefits paid to members when they leave a fund
- insurance premiums

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- insurance benefits
- management fees
- taxation
- administration fees

TYPES OF FUNDS

Superannuation funds include:

1) **Industry superannuation funds**: in general, the members of these funds belong to the one industry, e.g. Legal Super represents legal practitioners and staff, however many industry funds are available to anyone and actively marketed via the media.
2) **Public sector superannuation funds:** membership of these funds is restricted to government employees.
3) **Company or employer sponsored superannuation funds:** these funds are established by private sector employers or groups of employers to benefit their employees, e.g. Telstra Superannuation Fund.
4) **Public offer superannuation funds:** these funds are available to members of the public and are also an attractive option for small businesses that do not want to establish and manage their own employer sponsored fund for their employees. Public offer superannuation funds are generally managed by life offices or fund managers. These funds are sometimes referred to as retail superannuation funds or wholesale superannuation funds. The difference between retail and wholesale is essentially the size of the member's contributions that can be accepted by the fund. Many retail funds accept ongoing contributions from as little as $100, whereas most wholesale funds accept contributions starting from $500,000. The distinction is a little academic because most financial planners access wholesale funds (for their clients) via 'platforms' such as Master Trusts or Wrap accounts. This allows them to invest much smaller amounts across different managers whilst receiving preferential pricing and consolidated reporting on their behalf. This is discussed in detail in module 2.
5) **Self-managed superannuation funds (SMSFs):** these funds are established by people wishing to manage their own superannuation investment. Such funds have one to

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four members. Although these funds are not subject to all the restrictive requirements outlined in the SIS regulations, the trustees must adhere to the sole purpose test. Note the Australian Taxation Office as opposed to APRA is in charge of compliance for SMSF's. It is easier to be found non-complying if you are operating an SMSF – so be warned. For example, if you own a property in the SMSF and you receive any personal benefit from the property (such as using it as a holiday house), it represents a breach of the sole purpose test and the SMSF may be found to be non-complying by the ATO (in an audit) with strict penalties such as 47% taxation applied to both the income and capital!

6) **Small APRA funds:** A small APRA fund can be an alternative to an SMSF. These funds have the flexibility of an SMSF without the responsibility of being a trustee. The trustee duties are undertaken by a specialist trustee company regulated by APRA. They may be suitable for SMSF members who no longer wish to perform trustee duties; members who go overseas for an indefinite period; or if they become a disqualified person and are no longer permitted to be a trustee. The trustees of small APRA funds are not members of the fund.

RESPONSIBILITY OF TRUSTEES

Regardless of the type of superannuation fund, trustees of superannuation funds must adhere to some basic rules. One such rule which we have already mentioned in this module is the *sole purpose test*. Briefly, the sole purpose test is designed to ensure that trustees have as their main objective the investment of funds for the purpose of providing benefits in retirement.

As long as the trustees have this as their main objective, they are free to make decisions as to what is the most appropriate form of investment. Trustees must however, follow rules relating to both *investment* and *borrowing*.

Super fund trustees can generally use borrowed monies to acquire any asset they would be permitted to invest in directly. Examples include managed funds, shares and direct property.

When deciding whether the fund should borrow to invest in these or other eligible assets, the trustees should consider a range of factors, including the expected

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investment returns, the risks associated with the investment and relevant borrowing costs, such as loan interest.

HOW MUCH IS INVESTED IN SUPER?

As at 31 December 2016, there were 587,544 super funds in Australia, 585,260 of these were self-managed super funds (SMSFs).

Type and Number of Super Funds				
Type of Fund	Number of Super Funds			
	March 2016	June 2016	Sept 2016	Dec 2016
Industry	42	41	41	41
Public Sector	20	19	19	19
Company or employer sponsored	32	31	31	30
Public offer - retail	141	139	139	139
Subtotal	**235**	**230**	**230**	**229**
SMSFs	569,769	574,988	581,736	585,260
Small APRA funds	2,197	2,184	2,188	2,055
Total*	**572,201**	**577,402**	**584,154**	**587,544**

*This excludes pooled superannuation trusts and single-member Approved Deposit Funds (ADFs). An ADF is generally a bank account offered by a banking institution that satisfies the SIS Superannuation requirements.

Source: Extracted from Statistics, Quarterly Superannuation Performance, December 2016 (released 21 February 2017), Australian Prudential Regulation Authority.

SUPERANNUATION FUND CHOICE

Superannuation choice should not be confused with investment choice across the asset classes which may be offered by a superannuation fund. Since 1 July 2005, most Australian employees have been able to choose the fund their contributions are paid into. This makes sense given it is ultimately your own money within super, and not anyone else’s, so you should have control as to who looks after your super, and how the

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money is invested. (Please note we will discuss superannuation guarantee contributions later in this module). Choice of superannuation funds allows employees to:

- change funds when their current fund is not available with a new employer;
- consolidate superannuation accounts to cut costs and paperwork;
- change to a lower-fee and/or better service superannuation fund;
- change to a better performing superannuation fund.

If an employee does not make a choice as to which super fund they wish their employer's superannuation guarantee contributions to be paid to, contributions will be made to a default fund (also known as an employer fund).

A default fund (employer fund) is the superannuation fund nominated by an employer to receive their employees' superannuation guarantee contributions if the employee does not make a choice. A default superannuation fund must be a complying fund and also offer a minimum level of life insurance as is generally required in the super choice regulations.

WHAT IS MYSUPER?

MySuper was introduced as part of the stronger super reforms to ensure that the default fund selected by employers offers a low cost and simple fund for those employees who do not make a choice.

Since 1 January 2014 all employer default funds must satisfy the MySuper legislation.

Members of existing default funds must have their balance transferred into a MySuper account by 1 July 2017.

MySuper accounts offer lower fees and have restrictions on the type of fees they can charge; simple features so you don't pay for services you don't need and a single diversified investment option or a lifecycle approach.

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4.0 SUPERANNUATION CONTRIBUTIONS

There is a lot of regulation as to who can actually contribute to a member's superannuation investment fund. There are also rules around how much can be contributed. In this section, we will look at both of these issues.

4.1 WHO CAN CONTRIBUTE?

Almost everyone can contribute to superannuation funds. This includes:

- Employees
- Employers
- Self-employed
- Unemployed
- Spouses
- Pensioners

There are however some restrictions that apply to those who are contributing to super. Before we look at those restrictions, it is necessary to understand that all contributions into a super fund fall into one of two categories. We will discuss the categories in more detail later in this module but for now at least know that all contributions to super are either:

Concessional contributions (contributions for which a tax deduction can be claimed - these contributions are from before tax money); or

Non-concessional contributions (contributions for which no tax deduction can be claimed because these contributions come from after tax money).

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Contribution type	Employee's Age < 65	65 – 69	70 – 74	75+
Concessional Contributions				
• Mandated Superannuation Guarantee or award contributions	Accepted without restriction	Accepted without restriction	Accepted without restriction	Accepted without restriction
• Additional employer contributions, including salary sacrifice. • Personal deductible contributions from members	Accepted without restriction	Accepted providing member meets **work test**	Accepted providing member meets **work test**	Cannot be accepted
• Contributions made by someone other than the member or employer e.g.: spouse contribution	Accepted without restriction	Accepted providing the receiving spouse meets **work test**	Cannot be accepted	Cannot be accepted
Non-concessional contributions				
• Voluntary after-tax contributions	Accepted without restriction	Accepted providing member meets **work test**	Accepted providing member meets **work test**	Cannot be accepted

THE 40 HOUR WORK TEST - WHAT DOES GAINFULLY EMPLOYED MEAN?

Anyone age 65 and over that wishes to contribute to super must satisfy a work test. The work test requires the individual member whose super fund it is, to have worked at least 40 hours over a consecutive period of no more than 30 days during the financial year. That is, they need to be gainfully employed for this period of time.

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Gainfully employed means employed or self-employed for gain or reward in any business, trade, profession, vocation, calling, occupation or employment. Gain or reward includes salary or wages, business income, bonuses, commissions, fees or gratuities, in return for personal exertion.

To satisfy the work test, "employment" includes receiving payment for your efforts, including farming, babysitting, cleaning, lawn mowing, gardening, consulting and paid employment. Note, the paid employment technically doesn't have to involve payments in the form of 'cash', it could for example, involve food or other gratuities. Nevertheless, volunteer work does not count towards the 40-hour work test.

Worked Example

Excluding super guarantee contributions (for which there are no restrictions), which of the following can contribute to super?

1) Anthony is 45 years old and unemployed.

Yes, Anthony can contribute as there are no restrictions placed on anyone contributing to super if they are under age 65.

2) Brenda is 59 years old and works part time helping out at the local school for 5 hours per week.

Yes, Brenda can contribute as there are no restrictions placed on anyone contributing to super if they are under age 65.

3) Charles is 67 years old and works as a volunteer for 20 hours each week for Oxfam.

No, Charles cannot contribute as he does not satisfy the 'work test'. Volunteer work does not count towards the 40-hour work test.

4) Diana is 68 years old and is a part owner of a restaurant. She works in the restaurant 3 days per week.

Yes, Diana can contribute as she does satisfy the 'work test'.

5) Edward is 71 and is retired.

No, Edward cannot contribute as he does not satisfy the 'work test'.

6) Fiona is 73. She runs a small dressmaking and alteration business and works in that business full time

Yes, Fiona can contribute as she does satisfy the 'work test'.

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4.2 HOW MUCH CAN BE CONTRIBUTED TO SUPER?

Superannuation contributions can be divided into two types — concessional (before-tax) and non-concessional (after-tax). Concessional contributions are subject to 15% tax upon entry into a super fund. Non-concessional contributions are not subject to tax upon entry into a super fund, because they are sourced from an individual's after-tax money (i.e. tax has already been paid on that money).

CONCESSIONAL CONTRIBUTIONS

Concessional contributions are contributions for which the person contributing the funds can claim a tax deduction. This of course assumes that the person making the super contribution has assessable income against which to claim the tax deduction.

This is not an exhaustive list of the types of concessional contributions; however, these are the main ones.

1. Superannuation guarantee.

In the 2017/18financial year, if you are an employee who earns $450 or more a month from an employer, your employer is required to contribute 9.5% of your salary to your super fund. The compulsory rate is called Superannuation Guarantee contributions (SG). Your employer receives a tax deduction for these contributions and your super fund must deduct 15% tax on each contribution.

For employees under 18, the employer only needs to make Superannuation Guarantee contributions on their behalf if the employee works 30 or more hours a week.

Case Study

Andrew earns $60,000 plus 9.5% super. Each year his employer must make superannuation contributions, at least quarterly, worth an annual total of $5,700 (or $1,425 per quarter).

Individuals can also make voluntary superannuation contributions in addition to their employer's contributions, although if you are age 65 or over, you must satisfy a work test.

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2. Salary sacrificing by employees.

If you can arrange for your employer to direct some of your before-tax salary to superannuation as contributions, your super fund deducts 15 cents in the dollar in tax[3], **rather than your marginal tax rate** which may be much higher (up to 47% including the 2% Medicare Levy in 2017/18). This type of arrangement is known as salary sacrificing. The employer will receive a tax deduction for this contribution. It makes no difference whether your employer pays you a salary or directs the same amount into your superannuation account. In both situations, the employer would receive the same full tax deduction on either 'salary' or 'salary sacrifice' monies. The advantage to you is that more of your salary can be invested instead of paying it to the tax office.

Case Study

Gemma aged 32 earns $75,000 (before tax) per year. Her marginal tax rate is 32.5%plus Medicare Levy. Gemma wishes to salary sacrifice $10,000 of her salary. Instead of paying tax at the marginal tax rate of 32.5% (plus Medicare Levy) on these funds, she can contribute the $10,000 to her super fund and pay a contributions tax on those funds of only 15%.

3. Personal deductible contributions

As part of the Super Reform Package, effective from 1 July 2017, if you are eligible to make voluntary super contributions you may also make personal concessional contributions.

The superannuation fund will deduct 15% contributions tax and the individual making the contribution can claim a tax deduction for the contribution. This will only apply if the individual has assessable income (e.g. employment income, business income, capital gains or net rental income) to justify the tax deduction.

The ability to make personal deductible super contributions provides an outcome which is similar to salary sacrificing, while offering more flexibility.

Prior to the Super Reform Package this option was restricted to the self-employed and unemployed who satisfied the 10% rule which will be defunct from 1sth July 2017.

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[3]Low income earners can receive a low income superannuation tax offset of up to $500 if their taxable income is less than $37,000.

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Case Study

Anthony aged 48 earns $100,000 (before tax) per year. His marginal tax rate is 37% plus Medicare levy. His employer will contribute $9,500 in Superannuation Guarantee contributions for the financial year ended 30 June 2018. Anthony plans to sell some shares in December 2017 which are held in his personal name. A capital gain (after discount) of $50,000 will be added to Anthony's assessable income.

Anthony intends to contribute a personal deductible contribution of $15,500 to his super fund in June 2018. The outcome will be a reduction in his assessable income and the $15,500 will incur 15% contributions tax in the fund rather than 37% plus Medicare levy if he had not made a personal deductible contribution.

This will result in a tax saving of $3,720.

$15,500 x 15% = $2,325. (instead of $15,500 X 39% = $6,045)

Note: If a tax deduction is to be claimed, you must also lodge a notice of intention with your super fund. There are strict timeframes around providing the super fund with a 'notice of intent to claim a tax deduction' and having it acknowledged by the fund in writing.

4. Insurance in super paid by employer.

If an employer pays insurance premiums for an employee, and the insurance is held inside superannuation, the premium is counted as a concessional contribution and included in the concessional contributions cap.

Case Study

Phillipa age 45 has a small company from which she draws a wage of $100,000 per year. The company will pay Superannuation Guarantee for Phillipa in the amount of $9,500 for the 2017-18 financial year. The company also pays an annual insurance premium of $4,500 for life and TPD cover held within Phillipa's superannuation fund. No other concessional contributions have been made, so Phillipa has used up $14,000 of her concessional contributions cap for the 2017-18 financial year.

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CARRY-FORWARD CONCESSIONAL CONTRIBUTIONS

The ability to carry forward concessional contributions will commence from 1 July 2018. As you can only carry forward from this date, the first time it can be used will be the 2019-20 financial year. This will allow members to carry forward any unused concessional cap amounts from the previous five years. This may be useful to those who have had a break in employment to allow them to catch up on missed contribution opportunities.

To be eligible to make catch up contributions the member's 'total super balance'[4] must be less than $500,000 as at 30 June in the financial year preceding the year that catch up contributions are made.

Example

Max has a total superannuation balance of $350,000 as at 30 June 2020. If Max has any previously unused concessional caps from the 2018-19 year and the 2019-20 year he can add them to his cap for the 2020-21 financial year.

Max only used $10,000 of his concessional cap in 2018-19 and $15,000 of his concessional cap in 2019-20, so he can add $25,000 to his 2020-21 cap of $25,000[5]. This will allow him to contribute up to $50,000 in the 2019-20 financial year.

Pro Tip

The ability to carry-forward unused concessional contributions from the past provides a great opportunity to reduce taxable income and could be used to reduce future capital gains tax liabilities.

NON-CONCESSIONAL CONTRIBUTIONS

Non-concessional contributions are superannuation contributions made from after-tax dollars. You cannot claim a tax deduction for these contributions.

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[4] Total superannuation balance is the sum of all superannuation interests held by an individual and includes interests in defined benefit funds

[5] Assuming that this is still the concessional cap amount.

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You can make non-concessional contributions up to the age of 74. You don't have to be working to make a non-concessional contribution, unless you're aged 65 or over. Non-concessional contributions can be from any source including employment, self-employment, savings, gifts or an inheritance.

A non-concessional contribution is a superannuation contribution made from money which you (or someone else in the case of gifts or inheritance) have already paid income tax at some point in the past. This means that the 15% contributions tax does not apply, and isn't deducted from such contributions.

If you make a non-concessional contribution, and your assessable income is below $51,813 for the 2017/18financial year, you may also be eligible for a tax-free bonus from the government called the co-contribution. Full details of the government's co-contribution scheme are discussed in section 4.5.

ARE THERE LIMITS ON HOW MUCH CAN BE CONTRIBUTED TO SUPER?

Because the tax on earnings in a super fund is only 15%, many people who have high marginal tax rates would choose to contribute large sums of money into their super fund instead of paying large amounts of tax. This would mean the Australian Government would miss out on a significant amount of income tax revenue. To ensure sufficient tax revenue is raised, the government has placed limits on the amount that can be contributed to super without penalty.

Both concessional and non-concessional contributions are subject to a limit called a "contributions cap". A contributions cap sets a limit on the amount of contributions you can make to super in any one year. If you exceed the cap, your excess contributions are likely to be subject to a penalty tax.

CONTRIBUTIONS CAPS

Concessional contributions cap

From the 2017/18financial year, individuals can make concessional contributions up to $25,000 p.a. The concessional contributions cap has continued to reduce over a number of years as the government targets this area to raise more taxes. (Remember these

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contributions are taxed at 15% inside super compared with marginal tax rates outside of super).

To summarise, all of the following types of contributions added together have a concessional contributions cap limit of $25,000:

- Superannuation Guarantee,
- Salary sacrifice,
- Personal deductible contributions,
- Employer paid premiums for insurance inside super.

Case Study

Stephanie age 54 earns $70,000 per year plus Superannuation Guarantee. At the end of the 2017-18 financial year she contributes an extra $10,000 to her super fund as a concessional contribution so she can claim a tax deduction and reduce her taxable income for that year. No other concessional contributions apply.

Stephanie has used $16,650 of her allowable $25,000 annual cap.

($70,000 x 9.5%) + $10,000 = $16,650.

Non-Concessional contributions cap

Individuals can also make non-concessional (after-tax) contributions up to $100,000 a year (for the 2017-2018financial year), while individuals under the age of 65 can use the 'bring forward' rule to make non-concessional contributions of up to $300,000. The 'bring forward rule permits an individual (under the age of 65) to make non-concessional contributions for the total of the current year's cap, plus the next two years' caps, in a single year representing his or her limit for the next three years.

If a member already has a total super balance of at least $1.6million, then no further non-concessional contributions can be made to super.

There is also a modified bring forward rule for members with a total super balance between $1.4million and $1.6million which is detailed in the next section.

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THE BRING FORWARD RULE EXPLAINED

Don’t confuse the ‘bring forward rule’ with the ability to make $300,000 non-concessional contributions each and every year – you can’t! A $300,000 contribution is for a 3 year period. If you utilise the ‘bring-forward’ allowance, your non-concessional contributions for that year and the following 2 years will be restricted to a combined total of $300,000 and any additional amount will result in excess contributions tax.

Transitional bring forward caps

For the years prior to the 2017-2018 year, the non-concessional contributions cap was $180,000 with the ability to bring forward 2 years to give a combined total of $540,000. So for clients who have already triggered the bring forward rule in the 2015-16 or 2016-17 years there are transitional bring forward cap limits.

- If the bring forward rule was triggered in the 2015-16 financial year and not fully used up, the total bring forward cap is $460,000 (that is, $180,000 for 2015-16; $180,000 for 2016-17 and $100,000for 2017-18).
- If the bring forward rule was triggered in the 2016-17 financial year and not fully used up, the total bring forward cap is $380,000 (that is, $180,000 for 2016-17; $100,000 for 2017-18 and $100,000for 2018-19).

Case Study

Josephine is 52 years old and she has already triggered the bring forward rule in 2015-16 by making a non-concessional contribution of $250,000. She has not made any non-concessional contributions in the 2016-17 year.

On 1 July 2017Josephine’s bring forward cap is recalculated to account for the reduction in the caps. Josephine's bring forward cap is now $460,000.

As she has already contributed $250,000, Josephine can only contribute up to $210,000 for the 2017-18 financial year.

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Case Study

Jack is age 55 and he has already triggered the bring forward rule in 2016-17 by making a non-concessional contribution of $250,000.

On 1 July 2017 his bring forward cap is recalculated to account for the reduction in the caps which is relevant for the 2017-18 and 2018-19 financial years. Jack's bring forward cap is now $380,000.

As he has already contributed $250,000, Jack can only contribute a combined total of up to $130,000 across the 2017-18 and 2018-19 financial years.

Pro Tip

If a client has triggered the bring forward rule under the old limits and utilised the full $540,000 (the old cap) prior to 1 July 2017 they will not be penalised.

Total superannuation balance

The concept of a 'total superannuation balance' is new from 1 July 2017. There are some contribution restrictions (such as the non-concessional contributions cap and the carry-forward concessional contributions cap) which are determined by a member's total superannuation balance. **The 'total superannuation balance' is the sum of:**

- *all accumulation account balances*
- *all account based income stream balances (including Transition to Retirement accounts)*
- *all non-account based income stream balances included in the transfer balance account*[6]
- *rollovers in transit*
- *the value of an accruing interest in a defined benefit fund*

Modified bring forward rule

If a super fund member already has a total super balance of at least $1.6million, they are no longer able to make any further non-concessional contributions.

[6] Broadly, the transfer balance account is a ledger which contains credits of retirement phase income streams and debits of lump sum pension commutations. Refer to section 8.1 for full details of the transfer balance account.

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There is also a modified bring forward rule for members who have balances between $1.4million and $1.6million.

This modified bring forward rule is summarised in the table below:

Total superannuation balance at prior 30 June	**Non-concessional contribution and bring forward allowed from 1 July**
Less than $1.4million	3 years ($300,000)
>/= $1.4million, but less than $1.5million	2 years ($200,000)
>/= $1.5million, but less than $1.6million	1 year ($100,000)
>/= $1.6 million	Nil

Note: Remember that you can still only access the bring forward provisions if you are under the age of 65.

Case Study

Dan is age 58 and his total super balance as at 30 June 2017 is greater than $1.4 million and less than $1.5 million so he is able to contribute up to $200,000 in non-concessional contributions for the 2017-18 financial year.

Pro tip

The member's total super balance at the end of the previous financial year is re-tested each year to determine their eligibility to contribute further non-concessional contributions in a bring forward period.

Case Study

Nancy is age 60 and has a total super balance of $1.35million on 30 June 2017 so she is able to utilise the bring forward rule and contribute up to $300,000 in non-concessional contributions. Nancy decides to contribute $150,000 in the 2017-18 year. At 30 June 2018 her total super balance is $1.55 million after contributions and earnings.

Therefore, Nancy can now only contribute a further $100,000 (previously $150,000) in non-concessional contributions for the 2018-19 financial year.

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Review Questions

1) Kristin is 45 years of age and has a superannuation balance of $220,000. She made a non-concessional contribution of $270,000 on October 2016 and will be making no further non-concessional contributions for the 2016-17 year.

What are the maximum non-concessional contributions she can make for the combined period of 2017-18 and 2018-19?

2) Melanie is 45 years of age and has a superannuation balance of $220,000. She made a non-concessional contribution of $270,000 on September 2015 and will be making no further non-concessional contributions for the 2015-16 or 2016-17 years.

What are the maximum non-concessional contributions she can make for the period of 2017-18?

3) Albert is 60years old and has a superannuation balance of $1.43million as at 30 June 2017. Assuming that Albert has not previously triggered the bring forward rule, what is the maximum non-concessional contribution he can make in the 2017-18 year?

Review Answers

1) $110,000

This is because Kristin triggered the bring forward rule in the 2016-17 year when the annual Non Concessional Contributions cap was $180,000. Her total cap is$380,000 (2016-17 $180,000; plus 2017-18 $100,000 plus 2018-19 $100,000)

2) $190,000

This is because Melanie triggered the bring forward rule in the 2015-16 year when the annual Non Concessional Contributions cap was $180,000. Her total cap is $460,000 (2015-16 $180,000; plus 2016-17 $180,000 plus 2017-18 $100,000)

3) $200,000

Firstly Albert is less than age 65, so he can utilise the bring forward rule.

Secondly, he is restricted by his existing super balance which is greater than $1.4million but still less than $1.5million.

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INDEXATION

The annual concessional contributions cap is indexed in line with AWOTE in increments of $2,500.

The non-concessional contributions cap is indexed in line with the concessional cap in increments of $10,000 (4X $2,500).

WHAT IS THE PENALTY IF THE CONCESSIONAL CONTRIBUTIONS CAP ISEXCEEDED?

Concessional contributions are subject to 15% tax within a super fund. For excess concessional contributions made from 1 July 2013, 100% of the excess will be included in the member's assessable income and taxed at their marginal tax rate plus an interest charge due to the Australian Taxation Office collecting the tax on a later date than the member's normal income tax. A 15% non-refundable tax offset will be applied. The government allows individuals to withdraw up to 85% of the excess contribution to pay their tax liability. The amount withdrawn will not count towards the member's concessional contributions cap.

Any excess concessional contributions retained in your super fund (as opposed to withdrawing them) will not only be taxed at the member's marginal tax rate plus an interest charge, but these excess contribution amounts will be added to the member's existing non-concessional contributions.

Beware: Make sure that the consequences of leaving excess contributions in super do not result in a breach of the non-concessional contributions cap.

Case Study

Thomas (age 46) earns $84,000 plus his employer's Superannuation Guarantee contributions (total package of $91,980).Thomas was intending to salary sacrifice $25,000 and make the most of his contributions cap. But Thomas runs the risk of making a common mistake. He has forgotten to take into account his employer sponsored Superannuation Guarantee. If Thomas proceeds with his strategy he will exceed his cap by $7,980 (i.e. 9.5% of his $84,000 salary). Any excess contributions above his cap of

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$25,000 will be subject to 32.5% contributions tax (his marginal tax rate) plus Medicare Levy PLUS an interest charge.

WHAT IS THE PENALTY IF THE NON-CONCESSIONAL CONTRIBUTIONS CAP IS EXCEEDED?

Non-concessional contributions within the annual or bring-forward limits are not subject to any tax within a super fund. From 1 July 2013, the Government allows individuals to withdraw 100% of any excess non-concessional contributions and 85% of any associated earnings after a release authority is received from the Australian Taxation Office. The release authority will specify the associated earnings amount based on a general interest charge rate. The withdrawn excess non-concessional contributions will not form part of assessable income. Regardless of whether the excess amount and 85% of the associated earnings are withdrawn from superannuation or not, the full 100% of associated earnings will be added to the individual's assessable income and taxed at the individual's marginal tax rate subject to a 15% tax offset for the investment earnings tax already paid by the superannuation fund.

Case Study

Cassandra (age 46) exceeded the non-concessional contributions cap by $50,000. The Australian Taxation Office later sends her an excess non-concessional contributions notice for $56,111 (i.e. $50,000 excess amount plus $6,111 associated earnings). Cassandra has the option to withdraw the $50,000 excess amount as well as 85% of the $6,111 associated earnings, i.e. $55,194.35 in total, but she may choose not to withdraw this. Regardless of whether she elects to withdraw this amount from superannuation, the full $6,111 associated earnings will be added to Cassandra's assessable income for the year in which the excess non-concessional contribution was made and she will receive a 15% ($916.65) tax rebate on the $6,111 amount.

Pro Tip

A tax offset or rebate can be worth almost twice as much (for tax payers at the top marginal rate) as a tax deduction. This is because a tax offset (or rebate) comes straight off tax payable, as opposed to a tax deduction which reduces assessable income.

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4.3 WHAT IS THE SUPERANNUATION GUARANTEE?

The introduction of the Superannuation Guarantee (SG) legislation in 1992 required employers to contribute a minimum of 3% of the employee's salary to superannuation fund (4% for employers with an annual payroll exceeding $1 million). For the 2017/18financial year, the superannuation guarantee rateis9.5% p.a. and this will be increased incrementally until it reaches the rate of 12%in July 2025. This further increase in the SG will result in a significant increase in funds invested in superannuation.

The maximum earnings base on which SG applies to each employer from 1 July 2017 is $52,760 per quarter, or $211,040 per year. SG does not have to be paid on income which exceeds these amounts. This will prevent an excess concessional cap situation when there is only one employer, however, if a member has more than one employer, SG contributions may result in a breach of the caps.

Generally speaking, most employees are entitled to compulsory superannuation contributions paid by the employer. You must however be an 'eligible employee' to receive SG contributions. Different rules apply to workers under the age of 18. If you're under the age of 18, you must work at least 30 hours each week and be paid at least $450 (before tax) in a calendar month to be eligible for SG. A calendar month is, for example, the month of March or April rather than a 30-day period.

Any employee aged 18 years or over must earn at least $450 a month (before tax) to be entitled to the 9.5% superannuation guarantee contributions. For employees aged 18 or over there is no requirement to work a minimum number of hours, unless the employment relates to work of a private or domestic nature, such as babysitting or house cleaning. In these specific private or domestic circumstances, such an individual is entitled to SG if they work at least 30 hours each week and earn at least$450 a month.

Pro Tip

When salary information is collected from a client, SG may be expressed as an addition to their salary, or it may be part of a salary package.

A client with a salary of $100,000 plus super, will receive SG contributions of $9,500 per year.

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A client with a salary package of $100,000 including super, would receive a salary of $91,325 plus SG contributions of $8,675 per year.

4.4 SALARY SACRIFICE

Salary sacrifice involves the foregoing of salary entitlements to receive a different form of remuneration such as employer superannuation contributions. The benefits are derived as long as the amount sacrificed is not taxable to the individual or is taxed at a lower effective tax rate than would be the case for gross salary payments.

Employees who salary sacrifice with superannuation contributions are in essence foregoing salary so that their employer contributes additional amounts to their superannuation. These amounts are not part of the employee's salary. If they were, they would be assessable for tax. They are in fact considered to be employer contributions to superannuation.

If an employee salary sacrifices, the employer contributes additional amounts to the super fund beyond the superannuation guarantee that must be paid on behalf of the employee. These additional amounts are 'employer contributions'.

WHY SALARY SACRIFICE?

Reasons for choosing to salary sacrifice include:

- The earnings on investments are taxed within the super fund at a maximum of 15% instead of the individual's marginal tax rate.
- Generally there will be more to invest as the tax rate on entering a super fund may be lower than the employee's marginal tax rate.
- At retirement there are tax advantaged income streams available from superannuation investments.

Note: a reduction in salary may affect other entitlements such as long service leave, annual leave and superannuation guarantee contributions.

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Case Study

Max has a taxable income of $100,000 which puts him the marginal tax bracket of 37% plus Medicare levy of 2%. If he sacrifices$10,000 of his income to super he will lower his taxable income to $90,000.The $10,000 will incur 15% contributions tax rather than 39% personal income tax (a tax saving of 24% of $10,000 = $2,400).

Pro Tip

As part of the Super Reform Package, effective from 1 July 2017, if you are eligible to make voluntary super contributions you will now also be able to make personal concessional contributions and receive a tax deduction.

This is effectively the same as a salary sacrifice contribution although it may require extra discipline and you must remember to submit the relevant form to your super fund.

Also, as you are not reducing your salary with your employer, your other entitlements will not be affected.

4.5 WHAT IS THE GOVERNMENT'S CO-CONTRIBUTION?

A superannuation co-contribution is a tax-free super contribution paid by the Federal Government into your super fund when you make a non-concessional (after-tax) contribution in a financial year.

If you earn $36,813or less (for the 2017/2018 year), the Federal Government pays $0.50 for every dollar you contribute to your super fund in after-tax dollars, up to a maximum of $500 a year. If you earn more than $36,813 (in 2017/2018), your co-contribution entitlement reduces by 3.33¢ for every dollar you earn over $36,813, until it cuts out at $51,813 (for the 2017/2018 year).

For example, if you earn $37,000 and you make an after-tax contribution of $1,000in the 2017/18 financial year, the Government's maximum contribution of $500 is reduced by $6.23, which gives you a co-contribution of $493.77.

Although the co-contribution is treated as a non-concessional contribution, the co-contribution is not counted towards an individual's non-concessional cap.

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THE PROCESS TO RECEIVE THE GOVERNMENT CO-CONTRIBUTION

To make a non-concessional (after-tax) contribution, an individual must provide their tax file number to their super fund. The Government will pay a co-contribution, once a tax return is lodged for the financial year in which the non-concessional contribution is made and the Government has received information about the amount of non-concessional contributions that have been made for the year, from the super fund.[7]

The tax free co-contribution is subject to four tests:

- Co-contribution work test
- Co-contribution income test
- Co-contribution age test
- Co-contribution total superannuation balance test

CO-CONTRIBUTION WORK TEST

To be eligible for the co-contribution scheme, you must earn 10% or more of your income from eligible employment, or 10% or more of your income from carrying on a business, or a combination of both.

If you're aged 65, you must satisfy a second work test to be eligible for the co-contribution. In effect, if an individual is aged 65 or over (but under 71), they must meet two work tests to be eligible for the co-contribution. One work test enables an individual to make personal contributions to a super fund, and a second work test enables an individual to be eligible for the co-contribution scheme.

Work test one:

If you are aged 65 or over and plan to make super contributions, then you must satisfy a work test. You must be gainfully employed for at least 40 hours in a period of not more than 30 consecutive days in the financial year in which the contribution is made.

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[7] You can only receive a Government Co-contribution on eligible voluntary contributions if you are under age 71.

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Work test two:

You must earn 10% or more of your income from eligible employment, or 10% or more of your income from carrying on a business, or a combination of both.

CO-CONTRIBUTION INCOME TEST

You must also satisfy an income test. The Government's tax-free co-contribution is available for any person who receives total income from employment or self-employment and earns less than $51,813 in the 2017/2018 financial year, and makes a non-concessional (after-tax) contribution to their super fund. This income threshold is indexed each year in line with increases in average weekly earnings.

It is worth noting that the co-contribution 'total income' threshold is "assessable income", plus the value of any fringe benefits that you have as part of your salary package, such as a car PLUS any salary sacrificed contributions. Assessable income also includes bank interest and net capital gains from selling shares or property.

Because the co-contribution income threshold includes salary sacrificed contributions, this means that individuals on higher incomes, seeking to access the co-contribution scheme, cannot salary sacrifice (that is, make before-tax super contributions to their super fund), to lower their income to a level that allows them to receive the tax-free Government co-contribution.

If you run a business, your income, for the purposes of satisfying the income threshold of $51,813 (in 2017/2018), is reduced by any business deductions incurred in carrying on the business, i.e. net business income is a component of this total income threshold. For satisfying the 10%-plus work test, however, you are measured against your gross business income which is not reduced by business deductions.

CO-CONTRIBUTION AGE TEST

To satisfy the age test, you must be under 71 at the end of the financial year in which you make your after-tax contribution to be eligible for a co-contribution.

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CO-CONTRIBUTION TOTAL SUPERANNUATION BALANCE TEST

From 1 July 2017 an additional condition has been added to the eligibility criteria to receive the government co-contribution. You will not be eligible to receive the government co-contribution if:

- your total superannuation balance is greater than or equal to $1.6million on 30 June in the year prior to the contribution being made or
- you have exceeded your non-concessional contributions cap for that year

THE CO-CONTRIBUTION PAYMENT PROCESS

1) Assuming you earn less than $51,813 for the 2017/2018 year, you then make a non-concessional (after-tax) contribution to your super fund.
2) You lodge your 2017/2018 tax return.
3) Within 60 days, the Government pays the co-contribution into your super fund.

You can work out your co-contribution entitlement by using the ATO co-contribution calculator. Go to www.ato.gov.au.

4.6 SPOUSE CONTRIBUTIONS PROVIDING A TAX OFFSET

Prior to the super reform package the spouse contribution was restricted to spouses on a very low income. Effective from 1 July 2017 the lower threshold was increased to $37,000. If an individual has assessable income of less than $37,000, then his or her spouse can make contributions on their behalf and claim a tax offset. The contributing spouse can access the maximum tax offset of $540, provided that an after-tax (non-concessional) contribution of at least $3,000 is made to the receiving spouse's super account. The tax offset is progressively reduced until the tax offset reaches zero when the receiving spouse earns$40,000or more in assessable income in a year.

The contributing spouse can be any age, but the receiving spouse must be under 65 years unless they satisfy the work test. Once the receiving spouse turns 70, spouse superannuation contributions cannot be made on their behalf.

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The contribution counts towards the non-concessional cap of the receiving spouse.

Case Study

Richard earns income of $95,000 per year and his wife Jo-anne earns $35,000 per year. If Richard contributes $3,000 to Jo-anne's superannuation account in a financial year he will receive a tax offset of $540.

However, if Richard contributes $5,000 to Jo-anne's superannuation account he will still only receive a tax offset of $540.

The offset is calculated as 18% of the contribution, subject to a maximum offset of $540.

So if Richard only contributes $2,000 to Jo-anne's superannuation account in a financial year he will only receive a tax offset of $360.

4.7 SPLITTING CONTRIBUTIONS WITH YOUR SPOUSE

Splitting super contributions can be a valid strategy where a higher-income earning spouse salary sacrifices contributions (i.e. makes concessional contributions), and then splits the contributions with the lower-income earning spouse. The higher-income spouse gets to reduce their salary (to the extent of the amount of their concessional contribution). This may have the impact of reducing their marginal tax rate, or least ensuring part of their salary is being taxed concessionally at a maximum of 15%. At the same time, the receiving spouse gets the boost to their super benefits.

Non-concessional contributions cannot be split between spouses, but concessional (before-tax) contributions can be split with a spouse provided that the super fund the individual belongs to permits contribution splitting. If an individual plans to split super contributions with a spouse, then the receiving spouse must be under the age of 65.

The amount which can be split is up to 85% of concessional contributions or the concessional contributions limit, whichever is lower. This is because 15% contributions tax is deducted before splitting.

A special form is required to be completed if an individual intends to split super contributions. A sample of this form is contained in the appendix. Only contributions made in the previous year can be split. For example, contributions made during the 2016/2017 year, can only be split during the 2017/2018 year.

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Case Study

Jackson is 42 years old and his wife is 40. Jackson's employer contributed $10,000 to his super fund in the 2016–17 financial year. Jackson also made $5,000 in non-concessional contributions during the same year. Jackson's wife, Laura, does not have very much super, as she has only been working on a part-time basis since the birth of their daughter.

Jackson advises his super fund that he wishes to split his 2016–17 contributions jointly with Laura, and the fund responds that he is eligible to apply after 30 June 2017.

Jackson completes the Superannuation contributions splitting application and lodges it with his fund in August 2017. He requests that $8,000 be transferred to Laura's super fund. (Jackson is unable to split his non-concessional contributions.)

His super fund accepts his application and determines that it is valid since the $8,000 is:

1) less than 85% of the $10,000 contributed by his employer
2) Jackson is still under the concessional contributions cap which applied in the 2016/17financial year.

His super fund transfers $8,000 to Laura's super fund in September 2017.

The total contributions tax applicable to Jackson's $10,000 contribution is $1,500 leaving $8,500. Jackson splits this so his wife receives $8,000 and he retains the remaining $500 in his own super fund.

WHEN WOULD SUPER SPLITTING BE A USEFUL STRATEGY?

1) If you're planning to retire before reaching the age of 60 and plan to take all or part of your super benefit as a lump sum (assuming you have reached preservation age), then both spouses can access their own tax-free threshold for lump sums. This will be discussed later in this module but for the 2017/18 tax year, it would mean that each of the spouses can access a tax-free amount (from what is known as the taxable component) of up to $200,000.

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2) If your spouse is older than you, then by splitting super contributions the older spouse is able to access super benefits at an earlier stage. The older spouse reaches age 60 first, which means tax-free super benefits are available earlier.

3) With the introduction of the super reforms package effective from 1 July 2017,

super splitting may become an effective strategy for couples aiming to equalise their superannuation balances to take advantage of tax free earnings in the retirement income stream phase. The balance of these accounts is restricted to $1.6 million for individuals from 1 July 2017.

4) The effectiveness of this strategy may increase when the ability to carry forward concessional contributions comes into effect from 1 July 2018.

Case Study #1

Vivienne age 51 and Zamir age 59 want to retire and travel around Australia when Zamir reaches age 60. Vivienne has made concessional contributions of $25,000 to her super fund this financial year. She decides to split her concessional contribution and transfer $20,000 to Zamir's super account. When Zamir reaches age 60 and retires, he will be able to access his super benefits tax free and fund their trip around Australia.

Case Study #2

Cheryl is age 58 and has $1 million in her accumulation account. She intends to continue contributing up to her concessional contributions cap each year until she retires. Her balance is projected to exceed the cap[8] which is applied to income streams in retirement.

Cheryl's husband Andrew is age 60 and has a small balance of $200,000 in his accumulation account. To maximise the combined amount that Cheryl and Andrew can use to purchase their retirement phase income streams, Cheryl is planning to split her future concessional contributions each year and transfer them (net of the 15% contributions tax) to Andrew's account.

[8] Section 8.1 provides full details of the transfer balance cap which applies to retirement phase income streams

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This strategy will have the effect of increasing Andrew's account and keeping Cheryl's account lower, although continued earnings may still bring Cheryl's balance above the transfer balance cap in the future.

Case Study #3 (based on example from AMP tech speak, figures and names altered by Monarch)

Michael is able to make concessional contributions of $70,000 in the 2020-21 financial year using the carry forward provisions and unused concessional contributions cap from 2018-19 and 2019-20. After 30 June 2021, Michael can request his super fund to split up to $59,500 ($70,000 X 85%) of his concessional contributions from the prior year and transfer them to his wife's account. His wife, Elizabeth, will retire earlier than Michael so the funds can be accessed sooner.

4.8 LOW INCOME SUPERANNUATION TAX OFFSET (LISTO)

The standard tax rate on concessional contributions is 15%. However, this is not the case for individuals earning less than $37,000. Individuals earning up to $37,000 will have any tax deducted from superannuation guarantee (SG) contributions returned to their super accounts in the form of a Low Income Superannuation Tax Offset (LISTO). The LISTO is effective from 1 July 2017 and it replaces the low income superannuation contribution (LISC). This refund of contributions tax payments is made up to a maximum of $500.This in effect means that any superannuation guarantee contributions for low income earners are not taxed.

TFN alert: If your super fund doesn't have your tax file number, your concessional (before-tax) contributions, including SG contributions, are subject to an additional tax of 32 per cent, which means you end up paying 47% tax on your concessional contributions.

Case Study

Manuel aged 47 earns $32,000 (before tax) per year. His employer makes 9.5% superannuation guarantee (SG) contributions of $3,040 into Manuel's superannuation fund. When those funds are contributed, there is a 15% contributions tax deducted

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($456). Because Manuel earns less than $37,000 he is entitled to the maximum Low Income Superannuation Tax Offset (LISTO) refund of $456.

4.9 TOTAL SUPERANNUATION BALANCE (TSB)

The concept of a 'total superannuation balance' is effective from 1 July 2017 and has been addressed throughout the contributions section as it can affect a members' eligibility to make contributions.

To summarise, the total superannuation balance measures the total value of a client's superannuation interest which includes both the accumulation phase and the retirement phase. It is measured as at 30 June each year so it is affected by investment returns and withdrawals.

The following table summarises the contributions that may be restricted by the total superannuation balance.

Type of contribution	Added restriction in addition to other eligibility criteria
Non-concessional contributions	If TSB is $1.6 million or more, no NCC allowed If TSB is more than $1.4 million and less than $1.6 million, bring-forward NCC's are restricted[9]
Government co-contribution	Not eligible if TSB is $1.6 million or more
Spouse contribution tax offset	If TSB of the receiving spouse is $1.6 million or more, tax offset cannot be claimed
Concessional contribution carry-forward (effective from 1 July 2018)	If TSB is $500,000 or more, ineligible to carry forward unused concessional contributions

[9] Refer to the table in the bring-forward contributions section

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4.10 SUPER CONTRIBUTIONS OTHER THAN CASH

To transfer personally held shares into a super fund, the fund's trust deed must permit 'in-specie' contributions. An individual can choose to make concessional (before-tax) or non-concessional (after-tax) contributions as in specie (non-cash) contributions.

Whether it is cash or other assets that are contributed to superannuation, the contributions are still subject to the applicable contributions caps.

Case Study

Mark personally owns a parcel of BHP shares with a market value of $15,500. The cost base of these shares was $20,000. He will not be subject to a capital gain at this stage so now may be a good time to transfer the ownership of these shares to his SMSF. (He can use the capital loss to offset future capital gains in his personal name.) Mark earns $100,000 and his Superannuation Guarantee contributions for the 2017-18 financial year will be $9,500.

With the new rules for personal deductible contributions Mark will be able to 'contribute' his BHP shares 'in specie' as a concessional contribution and claim a tax deduction of $15,500.

Pro Tip

It is a common occurrence that a financial adviser will see a client who wants ongoing advice on their investment portfolio (including their super). Often, recommendations entail transferring shares between tax entities. For example, it may include transferring a husband's shares into a wife's name because she is on a lower marginal tax rate (or vice versa). Recommendations also often include transferring shares into superannuation to benefit from the concessional tax rates on investment earnings. Whilst transferring shares between entities may trigger capital gains tax, there are many benefits to transferring the shares in-specie. For example, the shares may not be very liquid, and/or there may be many small parcels making brokerage for buying and selling expensive.

Even if you (as the adviser) didn't initially recommend the shares that your client owns, transferring the shares 'in-specie' so that you can track and report on the shares as part of the client's total position is also beneficial. Most platforms such as Wrap accounts and Master Trusts (discussed in module 2) allow in-specie transfer of shares.

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Nevertheless be warned, it can take up to 90 days (… and often longer) to actually be able to transfer the shares – so ensure your client don't have misguided expectations about how quickly it will be done.

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5.0 TAX AND SUPERANNUATION

Superannuation tax is the one area that creates the most confusion for new students.

There are three levels at which tax may be levied in the super environment:

- LEVEL 1: CONTRIBUTIONS TAX
- LEVEL 2: EARNINGS TAX
- LEVEL 3: WITHDRAWAL TAX

Each level of tax has different trigger points which turn the tax on or off.

CONTRIBUTIONS TAX

'Contributions tax' is the first level of tax that applies in the super environment, when money is first contributed to a member's super account. The trigger for contributions tax is the **type** of contribution. Provided that the contributions are within the cap limits:

- *Concessional contributions are subject to tax and*
- *Non-concessional contributions are not subject to tax.*

The 'general' tax rate for concessional contributions is 15% and this is deducted inside the fund.

Exceptions apply for low income earners[10] and those earning combined superannuation contributions and taxable income above $250,000[11].

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[10]Low income earners can receive a return of the contributions tax paid up to an amount of $500if their taxable income is less than $37,000.This will be paid back into their super fund account.

[11] Individuals whose adjusted taxable income exceeds $250,000 from 1 July 2017 will have their concessional contributions taxed at the effective rate of 30% representing the base 15% contributions tax and a further 15% tax known as Division 293 tax for amounts of concessional superannuation contributions which bring the individual's combined relevant superannuation contributions and other relevant "income" above $250,000. The "income" amount for this calculation represents taxable income plus net financial investment loss plus net rental property loss plus net amount on which family trust distribution tax has been paid less super lump sum taxed elements with a zero tax rate. The Division 293 tax may apply on a lower sum if the member has excess concessional contributions as extra tax will instead be reflected in excess contributions tax.

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Case Study #1

Megan has total income of $240,000 for the 2017-18 financial year. In addition she has concessional contributions totalling $25,000. The additional 15% contributions tax will apply to $15,000, which is the amount above the allowable combined total of $250,000.

This YouTube video link from the ATO explains the Division 293 tax applicable to high income earners.

https://www.youtube.com/watch?v=Woy5kSPwxro

EARNINGS TAX

Superannuation contributions from all sources are invested across a variety of asset classes for the benefit of the fund members. These assets may produce income earnings such as rent, interest and dividends and/or capital gains (or losses) which result from the sale of an asset of the fund.

The tax treatment of superannuation fund earnings depends upon two things:

1. Which 'phase' is the fund (or member) in?
2. Are the earnings 'income' or 'capital' related?

Firstly, the 'phase' will determine whether earnings tax applies or not.

ACCUMULATION PHASE

YES, earnings tax does apply in the accumulation phase

TRANSITION TO RETIREMENT INCOME STREAM PHASE

YES, earnings tax will apply in the transition to retirement income stream phase, although this will only be the case with the introduction of the super reform package effective from 1 July 2017.

RETIREMENT INCOME STREAM PHASE

NO, earnings tax does not apply when investments are used to fund a retirement phase income stream in this phase.

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Pro Tip

It is possible that you will come across fund members who remain in the accumulation phase even though they have actually retired from the workforce. In this case, the investments will continue to incur earnings tax as an income stream has not commenced.

When earnings tax **does apply** (accumulation phase and transition to retirement income stream phase), the rate of earnings tax depends upon the classification of the earnings.

- **Income Earnings.**

  Super fund income earnings such as interest, rent and dividends are subject to a standard maximum of 15% tax.

  If your super fund owns Australian shares that pay franked dividends, your fund will pay less than 15% tax on its earnings. A fully franked dividend is a dividend that has company tax already paid (at 30% – the company tax rate). To avoid double taxation, investors (including superannuation funds themselves) receive a credit (known as an imputation credit) for this pre-paid company tax.

- **Capital gains.**

  Any capital gains that your superannuation fund realises from the sale of an asset are subject to capital gains tax. If the asset has been held for less than 12months the super fund pays tax of 15%. If the asset sold has been held for more than 12 months, then the super fund only pays tax on two-thirds of the capital gain - in effect, a tax rate of 10% (i.e. 2/3rds of 15%).

Case Study #1 Accumulation phase

The XYZ Superannuation fund has a range of investments across different asset classes.

The fund has produced the following earnings:

Income earnings from rent and interest which total $100,000 plus the sale of an asset which was owned by the fund for only 10 months produced a capital gain of $20,000 plus the sale of an asset which was owned by the fund for 5years produced a capital gain of $80,000.

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The earnings tax which applies to the accumulation phase is calculated as follows:-

$100,000 X 15% = $15,000; + $20,000 X 15% = $3,000; + $80,000 X 10% = $8,000.

Total earnings = $200,000. Total earnings tax = $26,000.

Case Study #2 Transition to retirement (TTR) income stream phase

The ABC Superannuation fund has a range of investments across different asset classes.

The fund has produced the following earnings:

Income earnings from rent and interest which total $100,000 plus the sale of an asset which was owned by the fund for only 10 months produced a capital gain of $20,000 plus the sale of an asset which was owned by the fund for 5years produced a capital gain of $80,000.

The earnings tax which applies to the TTR income stream phase is calculated as follows:-

$100,000 X 15% = $15,000; + $20,000 X 15% = $3,000; + $80,000 X 10% = $8,000.

Total earnings = $200,000. Total earnings tax = $26,000.

Note that the earnings tax treatment which applies here is the same as that in the accumulation phase.

Case Study #3 Retirement income stream phase

The ZZZ Superannuation fund has a range of investments across different asset classes.

The fund has produced the following earnings:

Income earnings from rent and interest which total $100,000 plus the sale of an asset which was owned by the fund for only 10 months produced a capital gain of $20,000 plus the sale of an asset which was owned by the fund for 5years produced a capital gain of $80,000.

Earnings tax does not apply in the retirement income stream phase.

Total earnings = $200,000. Total earnings tax = zero.

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Case Study #4 Franking credits

The XYZ super fund is in the accumulation phase and the ZZZ fund is in the retirement income stream phase. Each fund holds investments in fully franked Australian shares. Each fund received fully franked dividends of $70,000 with a franking credit of $30,000. These earnings are classified as income earnings.

In each case the company has already paid $30,000 tax.

The XYZ fund is in accumulation phase and will therefore receive a tax refund of $15,000 as a result of this investment because the company has paid tax at the rate of 30% and the fund is only subject to 15%.

The ZZZ fund is in the retirement income stream phase and will receive a tax refund of $30,000 as a result of this investment because the company has paid tax at the rate of 30% and the fund is not subject to earnings tax.

WITHDRAWAL TAX

Withdrawal tax is more complex than contributions tax and earnings tax and to understand it fully you need to understand the different components of a superannuation benefit which is covered in the withdrawals section.

To summarise it here, the triggers which determine whether withdrawal tax applies are:

1. How old is the member?
2. Is it a lump sum benefit?
3. Is it an income stream benefit?
4. Is it a death benefit?

'Generally', withdrawal tax is switched off at the age of 60.[12]

[12] From age 60, the taxed element of the taxable component is tax free when paid to the member. The same does not apply to the untaxed element of the taxable component. Different rates may apply to death benefit payments.

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Pro Tip

Withdrawal tax is a more complex level of tax and is subject to its own distinct rules. Withdrawal tax is not solely determined by the phase that the fund or the member is in.

To summarise, you need to be aware of the triggers for the 3 levels of tax when you are presented with a superannuation tax question.

WHICH TAX?	TRIGGER
CONTRIBUTIONS TAX	**TYPE OF CONTRIBUTION** Concessional contributions are taxable Non-concessional contributions are not taxable
EARNINGS TAX	**WHICH PHASE?** Accumulation phase is taxed Transition to Retirement phase is taxed Retirement income stream phase is not taxed **TYPE OF EARNINGS (if tax applies)** Income earnings = 15% tax Capital gains = 15% tax or 10%tax (if held 12months or more)
WITHDRAWAL TAX* *refer to section 8.3 for full explanation of withdrawal taxes	**AGE** *Generally* no tax from age 60 (benefit from a 'taxed' source **LUMP SUM PAYMENT** Low rate cap under age 60 **PENSION PAYMENT** **PAYEE (member or beneficiary)** Death benefit may be taxed

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IMPORTANT

You must now complete Part A of your Multiple Choice assessments for Module 3.

A few tips:

- You can access the Multiple Choice Questions at training.monarch.edu.au
- Press "Ctrl F" if you want to search the pdf course materials for any key words or terms.
- You have 2 attempts. Please note, if you require a second attempt, the answers are shuffled so read them carefully. The highest score counts.
- If you are unsuccessful after 2 attempts, please contact our office on 1300 738 955.

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6.0 WHEN CAN I ACCESS MY SUPER?

So far in this module, the focus has been on the rules and regulations around contributions to superannuation. In this next section, we will look at the rules that relate to accessing superannuation funds.

There are various laws governing when you can access your super and specific ages when super becomes accessible. Because super is specifically intended for your retirement, the Government has restrictions on when you can access it, known as your 'preservation age'. The preservation age for accessing super has increased over the years, so your preservation age will vary depending on when you were born.

You don’t have to withdraw your superannuation benefits by a certain age. You can choose to leave your super account untouched indefinitely. If this is what you decide, i.e. you do not withdraw a lump sum or commence an income stream (pension) then your super account will remain in accumulation phase.

The special rules that apply to superannuation mean that you cannot access your super benefits until you meet one of the following criteria:

1) reach age 65 or
2) reach your preservation age and retire, or
3) satisfy another condition of release.

WHAT IS PRESERVATION AGE?

Your preservation age is based on the year that you were born. For anyone born before 1 July 1960, their preservation age was 55. The preservation age steadily increases until it reaches 60 years of age for those born on or after 1 July 1964.

Although you must have reached your preservation age to access your super benefits, merely reaching that specified age, or even reaching the age of 60, is not sufficient to access your super benefits. Your super benefits remain ‘preserved’ until you satisfy a condition of release. ‘Preserved’ for the purposes of superannuation simply means not accessible.

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Minimum age for accessing super benefits	
Date of birth	**Your preservation age**
Before 1 July 1960	55
From 1 July 1960 until 30 June 1961	56
From 1 July 1961 until 30 June 1962	57
From 1 July 1962 until 30 June 1963	58
From 1 July 1963 until 30 June 1964	59
On or after 1 July 1964	60

Source: (www.ato.gov.au/super)

CONDITIONS OF RELEASE

Satisfying a condition of release means your preserved benefits can become unrestricted or accessible — that means you can access your super now, provided the rules of your fund also let you cash out your super.

The most common conditions of release are:

- **Deciding to retire on or after preservation age**. You have unlimited access to your super benefits when you retire on or after your preservation age.
- **Cessation of employment on or after the age of 60**. Special 'retirement' rules apply for an individual who terminates an employment arrangement on or after the age of 60. Where a person is aged 60 or over but under the age of 65, and ceases an employment arrangement, then the person can be considered 'retired' for the purposes of accessing preserved super benefits. There is no restriction on the person ceasing employment and then changing their mind and recommencing their original job or taking on a new employment position. To satisfy the condition of release they simply have to cease employment after age 60 even if they are only temporarily unemployed. If an employment arrangement continues uninterrupted however, then turning 60 on its own is not considered a condition of release.

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- **Reaching the age of 65**. By turning 65 you can have unlimited access to your super benefits as a lump sum or income stream, and you don't have to retire if you don't want to.
- **Starting a transition-to-retirement pension (TTR)**.TTRs are special superannuation income streams (superannuation pensions) that enable individuals from preservation age to age64 to continue working while drawing down on super benefits. The maximum amount that can be withdrawn each year is 10 per cent of the account balance, and a minimum amount must be withdrawn each year. Once you retire or reach 65 then you have unlimited access to your super benefits. TTRs will be discussed in more depth later in this module.

Most super benefits are 'preserved' until you reach preservation age and satisfy a condition of release, but some Australians who have had superannuation accounts prior to 1999 may also have some 'unrestricted non-preserved' benefits which they can access at any time.

OTHER CONDITIONS OF RELEASE – ACCESS TO YOUR SUPER BEFORE RETIREMENT

There are some conditions of release where you can access your super before retirement or turning age 65. These include:

- **The preserved amount is less than $200** - If you leave a job where your employer was contributing to your fund on your behalf, and the preserved superannuation benefit is less than $200.
- **Severe financial hardship** - The trustee of your fund may give you access to a portion of your benefit, subject to certain conditions including:
  - you have been in receipt of Commonwealth Government income support, for example, unemployment benefits, for at least 26 weeks continuously, and the trustee of your super fund is satisfied that you can't meet immediate family expenses. Any payment is for the purposes of meeting everyday living expenses and can be one payment of no more than $10,000 (including tax) in any 12-month period

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  – you have reached your preservation age, and may be able to receive your entire superannuation benefit provided that you've been in receipt of government income support for at least 39 weeks

- **Compassionate grounds** (to be approved by the Department of Human Services) - Your fund can release part of your preserved benefits to prevent the bank selling your home because of overdue loan repayments. You can also apply for early release on compassionate grounds to fund funeral or medical expenses, or palliative care. If you or one of your dependants is severely disabled, you can apply to access your super if this disability requires your home or car to be modified due to the disability.
- **Terminal medical condition** - If a person suffers from an illness or injury which is likely to result in their death within 24 months, and two medical practitioners (one must be a specialist in an area related to the condition) provide a certificate, the fund can release the benefit.
- **Non-resident leaving Australia permanently**- If you're a non-resident of Australia, you can access your Australian superannuation benefit when you permanently leave Australia.
- **Permanent disability -** You can access your preserved super if you become permanently incapacitated, that is, the trustee is satisfied that, due to ill health, you're unlikely ever to be able to work in a job for which you're qualified by education, training or experience.
- **Temporary incapacity -** Your fund may automatically provide income protection insurance, or you may be able to apply for such insurance via your superannuation fund. If you suffer prolonged illness or disability you can access this insurance cover and receive a regular income, usually for up to two years.
- **Death -** If you die, your superannuation fund pays your death benefit to your estate, or to your spouse or other dependants.
- **Taking your benefit as lifetime pension or annuity -** Provided you take your super as a non-commutable lifetime pension or annuity, you can access your super at any age. A non-commutable lifetime pension or annuity is one that you receive for your lifetime and which you can't convert to a lump sum amount. Typically, this lifetime pension option is available in older public sector super funds.

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7.0 PLANNING FOR RETIREMENT

Whether you are planning to leave your job and never return to work for a living again or, planning to gradually leave the workforce by taking up a part-time role or even beginning a new career, you need to work out what sources of income you plan to have in retirement.

Life expectancy tables are very useful for financial planners in helping to determine how long retirement income will be needed. These tables are usually issued by actuaries and life companies. A female retiring at the age of 65, has a life expectancy of nearly 22 years. For a male, life expectancy is closer to 19 years at age 65. Retiring at the age of 60 will mean that you need to finance on average 24 years (male) to 27 years (female) of your life in retirement.

A rule of thumb is that you are likely to require between 60 and 80 per cent of your pre-retirement income to lead the active life that you're probably expecting in retirement.

RETIREMENT ISSUES TO CONSIDER

It's important to remember that no two clients are alike. In determining client needs for retirement you should consider asking some of the following questions:

- What type of lifestyle do you want in retirement? For example, do you want to travel?
- Do you have any lump sum capital needs in retirement such as changing over the car?
- Are you going to live in your house, down-size at some stage or move to rental accommodation at some point?
- Are you planning regular local holidays or overseas holidays?
- What other lifestyle choices that have financial implications are important to you?
- Do you think you will spend more money in the early years of retirement, or the later years of retirement? Note, medical bills may be higher later in retirement but travel expenses, and so forth might also be less compared to earlier in retirement.
- How much will such a lifestyle cost per week, or annually?

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- How much money in savings will be needed for the lifestyle you are planning in your retirement?
- How much superannuation and savings do you have now?
- How much super and savings will you have when you retire?
- If a gap exists between how much you want, and what your super and non-super savings are going to deliver, what steps are needed to fill that gap?

RISKS TO KEEP IN MIND

Pre-retirees and retirees may well have decades of life expectancy and consequently need to consider the asset allocation of their superannuation funds to ensure they are appropriately invested. As with any investor, investment markets are affected by the broader national and international economies and the political landscape. Consequently whether investments are inside superannuation or outside superannuation, there are investment risks that need to be recognised.

In Module 2, we looked at three commonly used measures of risk:

a) loss of capital value (market risk)

b) loss of purchasing power (inflation risk)

c) actual returns are different to expected returns (variability or volatility of returns)

There are a number of other important definitions of risk that investors should be aware of before they undertake an investment strategy. These types of risk include:

Risk of not diversifying: the possibility that if the client puts all of their investment capital into one basket, e.g. the share market, a fall in that market will adversely affect all of their capital. Diversification is a deliberate strategy aimed at reducing the impact that volatility in one asset class, sector or single product will have on the overall portfolio of assets.

Re-investment risk: the possibility that if a client invests in a fixed rate investment, e.g. bonds, the client may have to re-invest maturing money at a lower rate of interest if rates generally decline during the life of that investment.

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Liquidity risk: the possibility that the client may not be able to readily access their funds when they want or need them most, because they are invested in illiquid assets, e.g. real estate.

Credit risk: the possibility that an institution holding the capital, e.g. a debenture issuer, may fail to pay interest or return that capital.

Regulatory risk: the possibility of government policy changes, negatively affecting the financial strategy, e.g. changes to the treatment of Capital Gains Tax.

Timing risk: the possibility that a strategy of trying to time entry and exit of markets will expose the client to greater short term volatility.

Value risk: the possibility that the client will pay too much for a particular product or that it will be sold too cheaply.

Manager risk: the possibility that the client will invest in a fund manager based primarily on their recent past performance, without regard to their fundamental ability to cater to the particular needs of the client or performance expectations over the time frame in mind.

Currency risk: the possibility that investments held in other countries may rise or fall in value compared to the value of the currency held relative to the domestic currency.

This risk can be minimised by 'hedging' foreign currency exposure by the use of derivatives which can reduce the impact of exchange rate movements on the underlying portfolio return. For example, an 'unhedged' international share fund's returns would comprise the underlying investments' performances plus or minus any exchange rate movements of the underlying investments compared to the portfolio's currency. However, a portfolio which is 'hedged' will negate much of the exchange rate risk (in either positive or negative directions) so that the returns will approximate the underlying investments' performances less any fees associated with hedging. The actual methods which fund managers use to hedge this risk are beyond the scope of this course.

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8.0 SUPERANNUATION PAYMENTS

How much you withdraw from your super depends on several factors including your age, the type of payment you wish to access and whether or not you are retired. Superannuation withdrawals may be taken as either a lump sum, an income stream or a combination of both.

An income stream is simply a 'regular payment'. An income stream coming out of a superannuation fund is referred to as a pension[13].

The new style pension (and the most common) taken from a superannuation fund is the account based pension, which will be our main focus.

An income stream may also be purchased from an insurance company with either a lump sum of money withdrawn from a superannuation fund or with non-superannuation funds; this type of income stream is referred to as an annuity.

ACCOUNT-BASED PENSION

You can start a regular income stream or account-based pension, subject to reaching your preservation age and retiring or satisfying another condition of release. The main restriction on an account-based pension is that you must withdraw a minimum amount, and you can withdraw as much as you like. An account-based pension has no upper limit on withdrawals.

[13] The pensions we refer to in this course are pensions which come from the superannuation environment. They are totally different from the age pension which is provided by the Government. The age pension is covered in the Centrelink module of the Advanced Diploma of Financial Planning. The interaction between super pensions and Government pensions is an important area which is also covered in the Advanced Diploma.

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Minimum annual pension payments (for account-based pensions) for 2017/2018	
Age	**Minimum payment**
55-64	4%
65-74	5%
75-79	6%
80-84	7%
85-89	9%
90-94	11%
95 or older	14%

Note: The minimum payment is calculated on 1 July each year, unless it is the first year of the account-based income stream, in which case the amount is pro-rated from commencement day. The minimum amount is rounded to nearest $10.

ALLOCATED PENSION

If you retired before 20 September 2007, you may be receiving an allocated pension from a superannuation fund. However this is unlikely unless it is an SMSF pension because all large super funds and financial organisations offering allocated pensions, converted such pensions into the more flexible account-based pensions.

If you're running an SMSF and still receiving an allocated pension from your SMSF, then such income streams are subject to minimum and maximum annual pension payments. You can elect to have the more flexible account-based pension rules apply to this type of income stream too so it is worth considering.

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LIFETIME PENSION OR ANNUITY

If you belong to a public sector fund, or a defined benefit corporate fund, or you have purchased an annuity from a financial organisation then you may be receiving a guaranteed income stream from your super fund. The annual income payments are generally fixed, and you may lose your capital if you die. However, many annuities do allow you to provide a reversionary beneficiary (e.g. a spouse), in which case a portion, or the total annuity reverts to the spouse in the event of death. Depending on the product, some annuities provide a guaranteed payment period of up to 20 years or your life expectancy, whichever is the shorter period (but they do all vary).

TRANSITION-TO-RETIREMENT PENSION

A transition-to-retirement pension (TTR) enables individuals who have reached preservation age or over (refer to the previous table for preservation ages), to access their superannuation benefits in the form of a pension (income stream) without retiring or satisfying another condition of release. You can work part-time or full-time or even casually. TTRs are subject to three main conditions:

- You must have reached your preservation age.
- You cannot convert your TTR into a lump sum unless you retire, or turn 65, or satisfy some other condition of release.
- You can withdraw no more than 10% of the value of your pension account balance each financial year (and must withdraw a minimum of 4% of the value of your pension account balance).

A TTR may boost super savings for individuals over preservation age while cutting their tax bill.[14]

An individual can salary-sacrifice up to their annual concessional contributions cap and then withdraw pension income from a TTR to supplement their reduction in income.

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[14] Prior to the super reform package effective 1 July 2017 the earnings on the capital supporting the TTR were entirely tax-free. From 1 July 2017, the earnings on the capital supporting TTR pensions are treated the same as those in accumulation phase.

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This strategy can offer the following advantages:

- salary sacrificing reduces a person's taxable income while the sacrificed contributions reside in a concessionally taxed environment.
- salary sacrificing can be a good way to grow your super

Case Study

Adrian, age 61, is still working full time, earning $100,000 plus 9.5% super, and plans to retire when he is 65. With 4 years until he retires, Adrian wants to boost his retirement savings. While he will be limited by his concessional contributions cap of $25,000 a year (in 2017/18), he considers starting a transition-to-retirement pension so he can salary sacrifice more into his super. He salary sacrifices as much as possible of his salary into his current super account and draws down an amount from his Pension Account (subject to a maximum of 10% of his Pension Account) so that he still has the same amount of money on which to live.

In one year, Adrian can save $3,607in tax and can contribute this to his superannuation account. The full calculation is illustrated on the next page.

This strategy is tax effective because income payments from a Pension Account are tax free for people over 60.If Adrian was aged between preservation age and under 60, he could still benefit from this strategy while maintaining the same take home pay. The level of salary sacrifice contributions would be the same, but the income he would receive from the pension account would be assessable for taxation with a 15% tax offset rather than being tax free.

Prior to 1 July 2017 there was an added bonus to the TTR strategy because the earnings on the assets supporting the transition to retirement income stream were tax free.

Pro Tip

A TTR pension can be converted to an account-based pension upon satisfying a condition of release. The benefits of a TTR for a member under age 60 will depend on their tax-free and taxable components[15]as the pension income is assessed for tax purposes.

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[15]For further details refer to the section on benefit payment tax.

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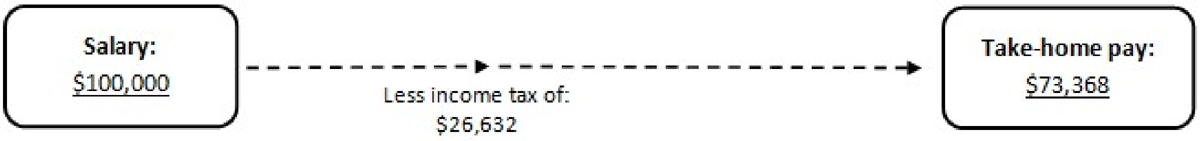
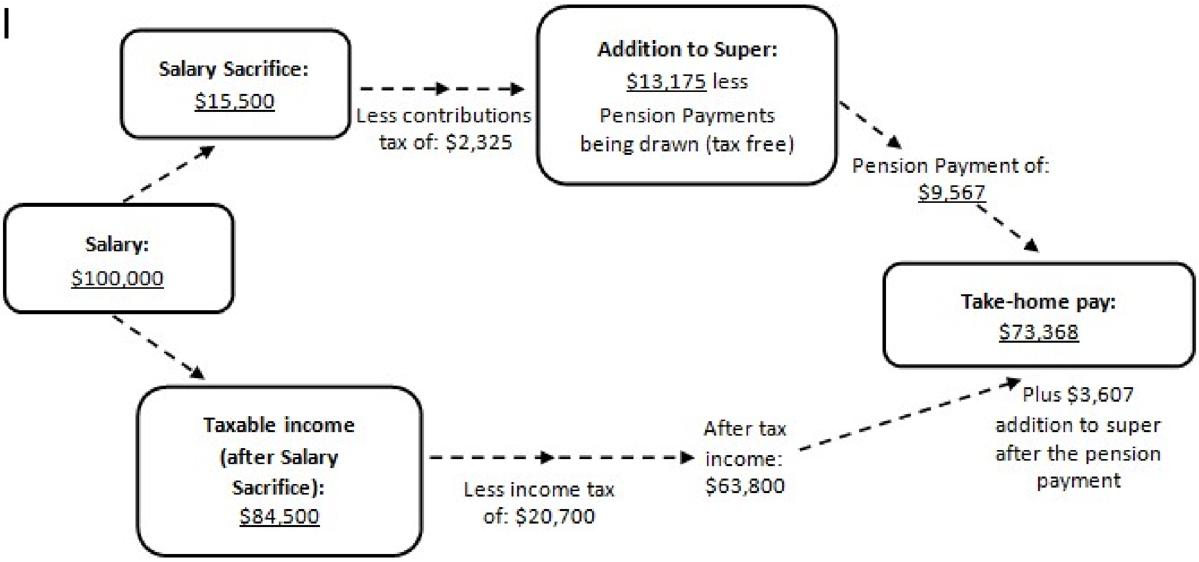
Without a Transition to Retirement strategy:



With a Transition to Retirement strategy:



Without a transition-to-retirement strategy	Total tax:	$26,632
With a transition-to-retirement strategy ($2,325 contributions tax +$20,700 income tax)	Total tax:	$23,025
Savings with a TTR strategy		$ 3,607

The illustration above is based on the tax rates applying for the year 2017/18. It assumes other concessional contributions e.g. Superannuation Guarantee contributions are not included.

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8.1 PENSION BENEFIT CAPS

Prior to 1 July 2017; when a pension or annuity was commenced using money from the superannuation environment, the total amount used to fund the pension received the benefit of zero tax on all future earnings; both income earnings and capital gains. There were no restrictions on the size of the pension balance or the reason for commencing the pension account. It could have been an account-based pension on retirement or a transition to retirement pension while you were still working.

The super reform package, effective from 1 July 2017, places restrictions on the amount of superannuation money that can be used to fund a retirement phase income stream. The current pension benefit cap is $1.6 million and is subject to future indexation. The amount which is in excess of the pension benefit cap must remain in an accumulation account where it will now be subject to future earnings tax, or it must be withdrawn from the superannuation system.

Furthermore, a transition to retirement pension account does not satisfy the criteria of a retirement phase income stream so these accounts will now be subject to earnings tax in the same way as an accumulation account.

The reforms were designed to limit the amount that can be transferred to the tax-free retirement phase.

Case Study #1

Jake has reached preservation age and permanently retired from the workforce. He has a balance of $800,000 in his account-based pension account as at 1 July 2017. During the 2017-2018 year, his fund returns income earnings equal to $40,000 plus a capital gain of $10,000. The total earnings of $50,000 will not incur any earnings tax as Jake has permanently retired and his balance is below the $1.6million cap.

Case Study #2

Susan has a balance of $300,000 in her transition to retirement pension account as at 1 July 2017, which is used to supplement her income whilst she transitions to part-time employment. During the 2017-2018 year, her fund returns income earnings equal to

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$15,000 plus a capital gain of $2,000. The total earnings of $17,000 *will be* subject to earnings tax.

HOW DOPENSION BENEFIT CAPS OPERATE?

The pension benefit caps apply to 'retirement phase' income streams.

An income stream that is paid out of the superannuation environment is referred to as a 'pension'. These income streams will be our main focus and the terms pension and income-stream are interchangeable.

The most common form of pension, the account-based pension, is classified as a retirement phase income stream[16].

In addition, there are special pension benefit cap rules which apply to non-account based income streams, non-commutable defined benefit income streams and market linked income streams. These are outside the scope of this course.

To be entitled to tax-free earnings you must be in 'retirement phase' AND be the recipient of a superannuation income stream.

If you are in transition to retirement, this is not considered to be retirement phase.

The ATO will keep records of retirement phase income streams from information that they receive from superannuation funds and life insurance companies.

The first time you are in the retirement phase AND receive a superannuation income stream, a 'transfer balance account' (TBA) will be created for you. The earliest date that a TBA will commence is 1 July 2017. Once a TBA has commenced for you it will not cease until you die[17].

Pro Tip

If the recipient of a transition to retirement pension meets another condition of release, such as retirement or reaching age 65, which makes the pension unrestricted non-preserved, then the value of the TTR pension will be included in the transfer balance account.

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[16] The transition to retirement income stream is not classified as a 'retirement phase' income stream.

[17] Special rules apply for children who are beneficiaries of a death benefit income stream.

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THE TRANSFER BALANCE ACCOUNT EXPLAINED

The transfer balance account works like a general ledger, with amounts credited that increase your account, and amounts debited which decrease your account.

CREDIT ITEMS

- *Purchase price of new income streams from 1 July 2017, including death benefit income streams*

- Existing income stream balances as at 30 June 2017

- Reversionary pensions after 12months, valued at date of death

- Notional earnings on excess transfer balance accounts

DEBIT ITEMS

-*Transfers back to accumulation*

- Lump sum withdrawals from income stream

-Transfer to a new pension

-Personal injury contributions

- Family law pension payment splits

-Pension losses due to fraud or dishonesty

-Out of character super contributions intended to defeat creditors (bankruptcy provisions)

IMPORTANT:

- investment earnings and investment losses do not affect the transfer balance account
- pension payment withdrawals from an income stream do not affect the transfer balance account
- transition to retirement accounts do not affect the transfer balance account as the recipient is not in retirement phase.

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Case Study

Martin has been retired for several years. Prior to 1 July 2017 he was receiving superannuation pension payments from two different superannuation funds.

MLC account based pension valued at $250,000 as at 30 June 2017.

HESTA account based pension valued at $400,000 as at 30 June 2017.

Following the new legislation, Martin will now have a 'transfer balance account' commencing on 1 July 2017 with a balance of $650,000

Case Study

On 1 September 2017, Darcy commences an account-based pension with an amount of $1.2million.

Investment returns and pension payments change the value of his account-based pension to $1.1million as at 1 July 2018 however these amounts do not cause a debit or a credit to arise in his transfer balance account.

Darcy's account-based pension has a balance of $1million as at 1 July 2019 at which time Darcy decides to fully commute the pension.

These are the debits and credits which will be seen in his transfer balance account.

Transfer balance account: Darcy			
Date	Debit	Credit	Balance
01-Sep-17		$1.2 million	$1.2 million
01-Jul-19	$1 million		$200,000

It is also possible for a transfer balance account to show a negative balance.

This enables retirement phase income stream recipients to transfer to a different provider without exceeding their transfer balance account cap.

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Gypsy commences an account-based pension on 1 October 2017 with $1.6million. The account-based pension balance in December 2019 is $1.7million (taking into account earnings and pension payment withdrawals).

Gypsy decides to fully commute the pension in December 2019 and rollover the lump sum to commence a new pension with a different provider.

Gypsy's transfer balance account will look like this:-

Transfer balance account: Gypsy			
Date	Debit	Credit	Balance
01-Oct-17		$1.6 million	$1.6 million
01-Dec-19	$1.7 million		-$100,000
02-Dec-19		$1.7 million	$1.6 million

Pro Tip

Recipients of an account based pension are required to withdraw a minimum amount annually.

Should they require more than the minimum amount it may be useful to withdraw any extra amounts from the pension account in the form of a lump sum as this will effectively result in a reduction to the members transfer balance account.

Alternatively, if they also had an accumulation account they could withdraw their extra income requirements from the accumulation account and keep a higher amount of capital in the tax-free earnings pension phase.

The following terminology applies to the transfer balance account:

General transfer balance cap

The general transfer balance cap is the amount that is permitted to be transferred into the retirement phase for the purpose of providing a superannuation income stream.

The general transfer balance cap is $1.6 million for the 2017-2018 financial year and is subject to future indexation.

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Personal transfer balance cap

An individual's personal transfer balance cap is initially equal to the general transfer balance cap for the financial year that they begin to have a transfer balance account. Over time, the personal transfer balance cap may differ from the general transfer balance cap due to the indexation rules (see below).

Case Study

Sally becomes the recipient of a retirement phase superannuation income stream (for the first time) in August 2017. The general transfer balance cap for the 2017-2018 financial year is $1.6 million.

Sally's personal transfer balance cap will initially be equal to $1.6 million.

Personal transfer balance cap space

If you have not used the whole of your personal transfer balance cap your cap space is the available cap space between the balance of the transfer balance account and the personal transfer balance cap.

From the above example, Sally commences a retirement phase income stream with $700,000 so her cap space is $900,000 ($1.6million less $700,000).

INDEXATION OF PENSION BENEFIT CAPS

The *general transfer balance cap* will be indexed annually in line with the CPI, but increases will only occur in increments of $100,000.

The *personal transfer balance cap* is subject to proportional indexation based on the amount of cap space available to the individual.

Case Study

Magnus retires on 1 August 2017 and commences a retirement phase income stream with $800,000. The general transfer balance cap is $1.6million for the 2017-2018 year so Magnus's personal transfer balance cap is also $1.6million, so he has used up 50% of his cap.

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Let's assume that the general transfer balance cap increases by $100,000 to $1.7million on 1 July 2019 due to indexation.

Magnus has not commenced any other retirement phase income streams so his personal transfer balance cap will be indexed by $50,000 ($100,000 X 50%). He now has a remaining personal cap of $850,000 (his initial cap space of $800,000 plus the $50,000 indexation).

Note: The proportional indexation is based on the highest ever balance in the transfer balance account, so there would be no benefit to commuting a pension in an attempt to benefit from full indexation.

Pro Tip

For a client with a high accumulated super balance which is getting close to the general transfer balance cap, it may be beneficial to commence a retirement phase income stream as soon as possible as future increases in a pension account that arise from earnings, will not be credited to the transfer balance account.

Case Study

Genevieve is age 63 and she has an accumulation account balance of $1.5 million and is considering retiring permanently from the workforce.

The market is on an upward trend and even modest earnings on this sum could push her balance above the $1.6 million cap. This would mean that any amount above the $1.6million cap would have to remain in the accumulation phase and would not benefit from tax exempt future earnings.

If Genevieve retires now and commences a retirement phase income stream with a transfer balance of $1.5 million, future earnings will not be credited to her transfer balance account. Therefore $1.5 million plus the future earnings will all be tax exempt, even when they exceed $1.6 million.

Pro Tip

Indexation will only apply to the personal transfer balance cap IF the transfer balance has NEVER equalled or exceeded your transfer balance cap.

If you ever exceed your transfer balance cap (even if you correct it) you will permanently lose your entitlement to future indexation increases. This diagram from the Macquarie webinar on super reforms, illustrates how a transfer balance account may change over

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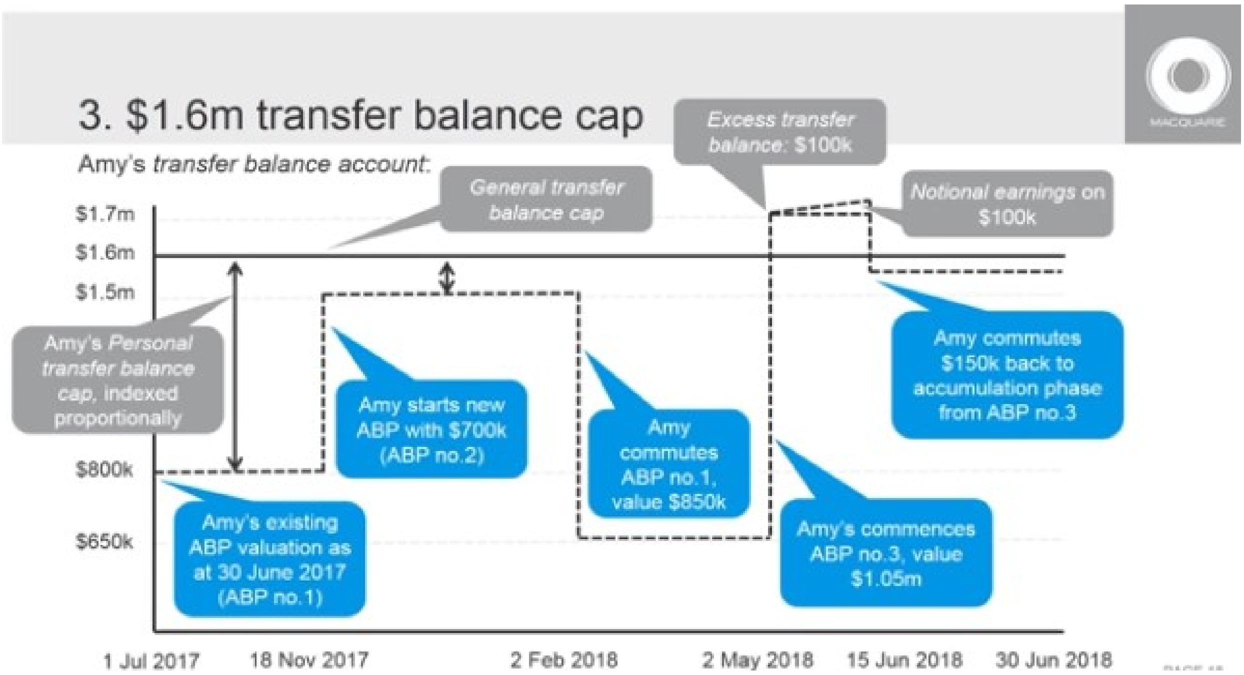
time. Please note that the concept of notional earnings is covered later, in the section on excess transfer balance earnings.



Note:

Special transfer balance cap rules apply to non-account based income streams.

For non-commutable defined benefit income streams and market linked income streams, the value of the income stream in respect of the transfer balance account is the member's annual income amount times a pension valuation factor.

Review Questions

1) Harry retired at age 66 and commenced an account-based pension with $900,000 on 30 December 2017. He withdraws $50,000 in pension payments for the period ending 30 June 2017.

What is Harry's a) transfer balance account?

b) personal transfer balance cap?

c) personal transfer balance cap space?

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2) Rosemary commences a Transition to Retirement pension with $350,000 at 1 September 2017. She also has an accumulation balance of $50,000.

What is Rosemary's personal transfer balance cap?

3) Glenda has a transfer balance account with a balance of $1.2million which is 75% of the general balance cap of $1.6million. This is the only entry in her account. Assume that the general balance cap is increased by $100,000 to $1.7million due to indexation in the year 2020.

a) What is Glenda's new personal transfer balance cap?

b) What additional amount could Glenda transfer to a retirement phase pension account without exceeding her cap?

Review Answers

1a) Harry's transfer balance account is $900,000.

1b) Harry's personal transfer balance cap is $1.6million.

1c) Harry's personal transfer balance cap space is $700,000.

2) A transfer balance account does not commence until the start of a retirement phase income stream. TTR is not a retirement phase income stream.

3 a) cap space of 25% ($400,000/$1.6million), SO 25% of the $100,000 indexation = $25,000 additional cap. So, original personal transfer balance cap of $1.6million + indexation = $1,625,000.

3 b) $425,000 (initial cap space + proportional indexation)

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STRATEGY IMPLICATIONS

- The introduction of the transfer balance cap may create new interest in strategies such as contribution splitting and cashing out and re-contributing to a spouse account in order to equalise accounts. That is, a couple can have a combined transfer balance account of $3.2 million ($1.6 million each).

- Historically, due to the Centrelink implications, when an additional pension payment is withdrawn, an important decision is whether to classify the payment as an additional pension payment or a lump sum commutation.
  Centrelink aside, this decision is now important in light of the new caps as commutations create a debit in the transfer balance account whereas pension payments do not.

- For clients with balances which are in excess of the transfer balance caps it is important to compare other investment vehicles outside the super environment.
- The changes are also likely to affect estate planning in light of the treatment of death benefit dependants.

MODIFIED TRANSFER BALANCE CAP FOR CHILD BENEFICIARIES

It is possible that a child may receive a death benefit income stream from a parent. To ensure that the child's retirement transfer balance cap in the future is not affected, there is a modified transfer balance cap for children.

A child's transfer balance account will cease when the death benefits pension ceases (usually at age 25) or when the pension assets are used up, in the case of, say, a disabled child beyond age 25.

If a child is already receiving a death benefit income stream at 1 July 2017 when the cap commences, the child's transfer balance cap will be $1.6million.

If the child's death benefit income stream commences on or after 1 July 2017, and the parent did not already have a transfer balance account, the child’s transfer balance pension cap will be proportionate to their share of the death benefit.

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Case Study

If 2 children each receive 50% of their parent's death benefit as an income stream; then each child will have a pension benefits cap of $800,000.

If the parent already had a transfer balance account at the time of death, the child's cap will be their proportionate share of the parent's existing retirement phase income stream.

Case Study

If the parent had $400,000 in an account based pension and each child receives 50%, the transfer balance cap for each child is $200,000.

WHAT IF MY TRANSFER BALANCE ACCOUNT EXCEEDS THE CAP?

If on any day, *your* transfer balance account exceeds *your* transfer balance cap you will have an excess transfer balance.

There are transitional provisions[18] for the period 1 July 2017 - 31 December 2017 whereby if the value of your income streams as at 30 June 2017 exceeded the transfer balance cap by less than $100,000 and it was rectified in this period you are deemed not to have an excess transfer balance.

Pro Tip

Even though your excess has been disregarded for the transitional period, you have still exceeded your transfer balance cap, so future indexation of your transfer balance cap is not available to you.

Excess transfer balance earnings

For the amounts that exceed the transfer balance cap, the ATO will calculate notional earnings and the excess amount plus the notional earnings must be moved out of the retirement phase income stream.

[18] Excess transfer balance tax does not apply under the transitional provisions.

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Excess transfer balance earnings are calculated on a daily basis using the General Interest Charge and added to your transfer balance account until the member takes action to remove the excess amount or the Commissioner issues a determination.

Case Study

On 1 August 2017, William starts a pension worth $2 million. William has an excess transfer balance of $400,000 as his personal transfer balance cap is $1.6 million. Assuming a General Interest Charge rate of 8.76%, after 45 days, excess transfer balance tax earnings of $4,320 will have accrued.

An individual can remove the excess amount themselves by converting it back to the accumulation phase or withdrawing it as a lump sum commutation.

If this does not occur the ATO will issue a determination to the member to elect which income stream will be commuted. A default commutation notice is included in the event that no election is made.

Excess transfer balance tax

The member will be required to personally pay excess transfer balance tax based on the notional earnings.

The ATO will issue an assessment notice in respect of the excess transfer balance tax.

The excess transfer balance tax applies to the notional earnings at the rate of:

15% for the year 2017-2018.

from 1 July 2018; 15% for the first breach; 30% for subsequent breaches

So, in the previous example, William will be subject to excess transfer balance tax calculated as:-

$4,320 X 15% = $648

The 15% tax represents the earnings tax that is applied to income earnings in the accumulation phase.

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8.2 BENEFIT STATEMENT COMPONENTS

A superannuation member benefits statement is issued by the super fund and provided to the member when benefits are withdrawn from the fund or rolled-over to a different fund. Member benefit statements are also issued at least on an annual basis. A benefit quote can also be requested at any time.

The member benefits statement breaks the total benefit down into preservation components and taxation components.

Each of these sections will add up to the total benefit but they are derived differently so don't try and link the two together.

PRESERVATION COMPONENTS

The preservation components section is all about accessibility. Since 1 July 1999 all contributions to super, along with any earnings from that date are required to be preserved for retirement purposes. Historically, members could access their super when they resigned and then spend it rather than keep it for retirement purposes.

Preservation amounts:

Preserved amount	$
Restricted non-preserved amount	$
Unrestricted non-preserved amount	$

Preserved amount

All superannuation contributions made since 1 July 1999, as well as all earnings since 1 July 1999 will appear in the preserved amount. This amount cannot be taken until a condition of release with 'nil' cashing restrictions is met, such as, retirement on or after preservation age, attaining age 65, death or total and permanent disablement.

Restricted non-preserved amount

A member who did not receive any employer super contributions prior to 30 June 1999 will not have an amount in this section. For those that do have an amount in this field,

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the value is crystallized as at 30 June 1999 and any future earnings will appear in the preserved amount.

This amount may be able to be accessed when the member has left the employer who made these contributions.

Unrestricted non-preserved amount

This amount is crystallized as at 30 June 1999 and any future earnings will appear in the preserved amount. This amount is not subject to the preservation rules and can be withdrawn at any time[19].

TAXATION COMPONENTS

Assuming that the benefit can be accessed, the way that the money is treated for taxation purposes is dependent upon the taxation components.

Taxation components

Tax-free component	$
Taxable component:	
Element taxed in the fund	$
Element untaxed in the fund	$

What is included in the tax-free component?

- Government co-contributions
- Spouse contributions
- Non-concessional contributions

What is included in the taxable component?

- Employer contributions
- Salary sacrifice contributions
- Earnings on superannuation investments

[19] Withdrawal tax may apply.

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– Superannuation insurance proceeds (taxed element and untaxed element)

A super benefit from an untaxed source is a super benefit paid from a fund that doesn't pay 'contributions' tax on concessional (before tax) contributions, and is not liable for earnings tax on fund earnings. These types of super funds are generally older public sector super funds whose benefits are sourced from consolidated revenue and are subject to higher tax rates than benefits paid from a 'taxed source'. They make up less than 10% of large super funds.

Important:

Going forward with our future examples we will focus on benefits with just a tax-free component and a taxable component (taxed element).

Pro Tip

When a pension account has commenced, the proportion of tax-free and taxable components are set at commencement and remain that way for the life of the pension.

All future earnings on a pension account are credited in the same proportions.

Case Study **Pension account**

	Benefit	Future earnings	New benefit
Tax-free component	$100,000	$25,000	$125,000
Taxable component[20]	$300,000	$75,000	$375,000
Total benefit	$400,000	$100,000	$500,000

As you can see, the pension account is 25% tax-free and 75% taxable and all future earnings will be allocated in the same way. So the total benefit will continue to be split25% tax-free and 75% taxable.

[20] Element taxed in the fund.

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Pro Tip

The proportions of the tax-free and taxable components for an accumulation account will change continuously as contributions are received from different sources and earnings, positive or negative, are applied to the account.

Important: Don't forget that the earnings from superannuation form part of the taxable component, regardless of whether those earnings came from concessional or non-concessional contributions, or previous earnings (i.e. compounded earnings).

Case Study Accumulation account

	Benefit	Future earnings	New benefit
Tax-free component	$100,000	$nil	$100,000
Taxable component	$300,000	$100,000	$400,000
Total benefit	$400,000	$100,000	$500,000

All accumulation earnings form part of the taxable component. No further contributions were made in this example. The split prior to further earnings was 25% tax-free and 75% taxable component, but over time it continues to change. It is now 20% tax-free and 80% taxable.

8.3 WHAT TAX IS PAYABLE ON SUPER WITHDRAWAL BENEFITS?

Now that we understand the taxation components of a member's benefit, we are in a position to understand the tax treatment of each component.

Superannuation withdrawal tax is influenced by:

- the components of the benefit

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- whether the benefit is taken as a lump sum or a pension payment
- the age of the fund member
- the recipient of the benefit

The tax-free component is always tax-free, including when you retire before the age of 60. The tax-free component is also tax free when it is paid out as a death benefit.

AGE 60 IS A TRIGGER FOR WITHDRAWAL TAX

Generally, withdrawal benefits become tax free from the age of 60 (unless there is an untaxed element, in which case withdrawal tax is payable).

If the taxable component of your benefit is from an untaxed source[21], tax is still payable on the benefit even after the age of 60.

Pro Tip

Even though benefit payments may become tax free from age 60, the tax-free and taxable components must be recorded indefinitely as they may have an effect on future death benefit payments.

TAX ON LUMP SUM WITHDRAWALS

AGE 60 AND ABOVE

If a superannuation fund member has reached the age of 60 and withdraws a benefit as a lump sum, it will be taxed as:

Tax-free component is tax-free

Taxable component (taxed element) is tax-free

[21] Generally an untaxed amount will be from a fund that is from a statutory or government superannuation fund or from the proceeds of an insurance benefit.

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The payment does not form part of the member's assessable income.

PRESRVATION AGE TO AGE 59

If a superannuation fund member withdraws a benefit as a lump sum between preservation age and age 60, it will be taxed as:

Tax-free component is tax-free

Taxable component (taxed element) is taxed as follows:

The first $200,000[22]of the taxable component is not taxed

Any amount above $200,000is taxed at 15% plus the Medicare levy (i.e. 17%)

BELOW PRESERVATION AGE

If a superannuation fund member withdraws a benefit as a lump sum before their preservation age, it will be taxed as:

Tax-free component is tax-free

Taxable component is taxed at 20% plus the Medicare levy (i.e. 22%)

Example 1: Lump sum benefit received from a taxed source at age 63

	Benefit	Withdrawal tax	Net Benefit
Tax-free component	$100,000	Nil	$100,000
Taxable component	$300,000	Nil	$300,000
Total benefit	$400,000		$400,000

[22]This is referred to as the low rate cap, an indexed lifetime limit that applies to an individual's taxable component. An individual can receive up to $200,000 (for the 2017/18 year) of their taxable component tax-free, provided the component is from a taxed source. The low-rate cap is in addition to any tax-free component.

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Example 2: Lump sum benefit received from a taxed source at age 58

	Benefit	Wdrl tax rate	Tax amount	Net Benefit
Tax-free component	$100,000	Nil	Nil	$100,000
Taxable component	$300,000	$200,000 X 0% $100,000 X 17%	$17,000	$283,000
Total benefit	$400,000			$383,000

Pro Tip

Lump sums may be withdrawn across a number of years. It would be prudent to only take as much as you can tax-free until you reach age 60. The low rate cap is relevant to lump sum withdrawals made from preservation age to age 60.

Example 3: Regular lump sums within the low rate cap

	TOTAL	**AGE 58 withdrawal**	**AGE 59 withdrawal**	**AGE 60 withdrawal**
Tax-free component 25%	$100,000	$ 25,000	$ 37,500	$ 37,500
Taxable component 75%	$300,000	$ 75,000	$112,500	$112,500
Total benefit	$400,000	$100,000	$150,000	$150,000

No tax would be payable on any of the above withdrawals.

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This is because the taxable components withdrawn prior to age 60 equal $187,500 which is less than the $200,000 low rate cap, and withdrawals from the age of 60 become tax-free.

Each withdrawal is taken proportionately from the tax-free and taxable components.

Remember, if the taxable component of your benefit is from an untaxed source[23], tax is still payable on the benefit even after the age of 60.

TAX ON INCOME STREAM WITHDRAWALS

AGE 60 AND ABOVE

If a superannuation fund member has reached the age of 60 and withdraws a benefit as an income stream, it will be taxed as:

Tax-free component is tax-free

Taxable component (taxed element) is tax-free

The payment does not form part of the member's assessable income.

PRESRVATION AGE TO AGE 59

If a superannuation fund member withdraws a benefit as an income stream between preservation age and age 60, it will be taxed as:

Tax-free component is tax-free

Taxable component (taxed element) is taxed at the member's Marginal Tax Rate with a 15% tax offset

BELOW PRESERVATION AGE

If a superannuation fund member withdraws a benefit as an income stream before their preservation age, it will be taxed as:

Tax-free component is tax-free

Taxable component is taxed at marginal tax rates

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[23] Generally an untaxed amount will be from a fund that is from a statutory or government superannuation fund.

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If you are below your preservation age and accessing your super via an income stream for reasons such as hardship, the rules are slightly different. The tax-free component of your income payment will be tax free. The taxable component of your income payment will be added to your taxable income and taxed at your marginal tax rate. No tax offset of 15% is applicable.

Remember, if the taxable component of your benefit is from an untaxed source[24], tax is still payable on the benefit even after the age of 60.

Example 1: Income stream benefit received from a taxed source at age 63

	Total Benefit	Pension withdrawal	Withdrawal tax
Tax-free component 25%	$100,000	$ 4,000	Nil
Taxable component 75%	$300,000	$ 12,000	Nil
Total	$400,000	$16,000	Nil

Example 2: Income stream benefit received from a taxed source at age 58

	Total Benefit	Pension withdrawal	Withdrawal tax
Tax-free component 25%	$100,000	$ 4,000	Nil
Taxable component 75%	$300,000	$ 12,000	Marginal Tax Rate less 15%*
Total	$400,000	$16,000	As above

[24] Generally an untaxed amount will be from a fund that is from a statutory or government superannuation fund.

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*Let's assume a marginal tax rate (MTR) of 37% (including Medicare levy); withdrawal tax will be calculated as $12,000 x 22% (37% less 15% tax offset) = $2,640

Another way of showing this is:

$12,000 x 37% MTR = $4,440

less tax offset of $1,800 ($12,000 X 15%) = $2,640

Note: If you are aged 60 or over and receiving a super benefit from a taxed source, the size of your tax-free component is irrelevant — you receive 100 per cent of your lump sum or income stream payment free of tax. The tax-free component only becomes important if:

- You receive a lump sum benefit under the age of 60, OR
- You receive a lump sum benefit from an untaxed source, OR
- You leave your super to non-dependants when you die.

Pro tip

The withdrawal tax on income streams is the same whether it is a retirement phase income stream or a transition to retirement phase income stream.

This differs from earnings tax which was discussed earlier in this module.

Case Study #1

Bill is 58 years old, retired and has commenced an account based pension. Bill's contributions come from a taxed source. The taxable component is $180,000 and the tax-free component is $30,000, representing a total of $210,000 pension starting balance.

a) What is the minimum percentage he must withdraw each year?

b) Is there a maximum amount Bill must withdraw each year?

c) How is the tax on his pension determined?

d) Does Bill need to include his pension income on his tax return?

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Answers:

a) The minimum pension for people aged under 65 is 4% p.a. Bill's minimum pension is therefore 4% X $210,000 = $8,400.

b) As Bill is retired, there will be no maximum pension amount required and he could potentially withdraw 100% of his balance in a year. However, if he commenced the pension via a Transition to Retirement Pension whilst working, his maximum pension would be 10%.

c) As Bill is aged between preservation age and 60, the tax-free component of his pension funds will be tax-free and the taxable component will be assessed at his marginal tax rate and he will also receive a 15% tax rebate in relation to the taxable component. His tax-free component will be based on the pension starting balance and this will be $30,000 / $210,000 = 14.3%, while his taxable component will be $180,000 / $210,000 = 85.7%. Let's assume that he withdraws the minimum pension of $8,400 in the first year. Out of this amount, 14.3% ($1,200) will be tax-free, whilst the remaining 85.7% ($7,200) will be taxable and added to his assessable income and taxed at his marginal tax rate. He will then receive a 15% tax offset for the taxable component (i.e. 15% X $7,200 = $1,080 tax offset).

d) Yes, the taxable component will need to be included in his tax return.

Case Study #2

Simone is 66 years old, retired and has commenced an account based pension. Simone's contributions come from a taxed source. The taxable component is $250,000 and the tax-free component is $30,000, representing a total of $280,000 pension starting balance.

a) What is the minimum percentage she must withdraw each year?

b) Is there a maximum amount Simone must withdraw each year?

c) How is the tax on her pension determined?

d) Does Simone need to include her pension income on her tax return?

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Answers:

a) The minimum pension for people aged under between 65 and 74 is 5% p.a. Simone's minimum pension is therefore 5% X $280,000 = $14,000.

b) As Simone is over 65, there will be no maximum pension amount required and she could potentially withdraw 100% of her balance in a year.

c) As Simone is over 60, her entire pension payments will be tax-free.

d) No, it is not relevant to include non-assessable income in Simone's tax return.

CAN YOU CHOOSE WHICH COMPONENT TO ACCESS?

No! When a super benefit is withdrawn, it must be withdrawn proportionally from both the tax-free component and the taxable component. For example a client has $450,000 in superannuation:

Tax-free component = $150,000

Taxable component = $300,000

The client wishes to withdraw $180,000. This must be taken proportionately from tax-free and taxable components relative to the total benefit.

$150,000/$450,000 = 1/3 of $180,000 = $60,000 is from the tax-free component

$300,000/$450,000 = 2/3 of $180,000 = $120,000 is from the taxable component

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Case Study

Miranda retires on her 59th birthday and wishes to withdraw a lump sum of $120,000 to purchase a share in a beach house with friends. Miranda's superannuation balance of $400,000 is made up of a tax-free component of $50,000 and a taxable component of $350,000. Both components are from taxed sources. Miranda can withdraw the $120,000 tax-free because:

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- $50,000/$400,000 = 12.5% of $120,000 = $15,000 is from the tax-free component
- $350,000/$400,000 = 87.5% of $120,000 = $105,000 is from the taxable component

and Miranda has not yet accessed any of her low rate cap of $200,000 (2017/18) which she can access during her lifetime.

After withdrawing the $120,000 lump sum, Miranda's new superannuation balance is $280,000. The tax-free component left will be $35,000 (12.5% of $280,000) and the taxable component left will be $245,000 (87.5% of $280,000).

Based on 2017/18 rates, Miranda can still withdraw up to $95,000 tax-free from her taxable component ($200,000 lifetime limit less $105,000 for the beach house = $95,000), but she will pay 17% tax on the excess.

Two months after withdrawing the lump sum of $120,000 from her super, Miranda decides to renovate her home. She requires an additional lump sum of $150,000 for the renovation.

This lump sum would be taken as follows:

- 12.5% of $150,000 = $18,750 is from the tax-free component

  87.5% of $150,000 = $131,250 is from the taxable component

Miranda's withdrawals are detailed in table below.

	Total Benefit	1st lump sum wdrl	Balance	2nd lump sum wdrl	Balance
Tax-free component 12.5%	$ 50,000	$ 15,000	$ 35,000	$18,750	$16,250
Taxable component 87.5%	$350,000	$ 105,000	$ 245,000	$131,250	$113,750
Total benefit	$400,000	$120,000	$280,000	$150,000	$130,000

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Miranda still has not used up her tax-free component (initial tax free component of her super balance was $50,000 less $15,000 from the first withdrawal less $18,750 now = $16,250). Miranda however has exceeded the lifetime limit of $200,000 tax-free that applies to her taxable component (in the 2017/18 financial year). (Miranda withdrew $105,000 for the beach house purchase and another $131,250 for the renovation, a total of $236,250). She has exceeded the lifetime limit of $200,000 by $36,250.

Tax implications for Miranda in 2017/18:

First withdrawal of $120,000

$15,000 from the tax-free component	Tax- free
$105,000 from taxable component	Tax-free (as this is less than the lifetime low rate cap)

Second withdrawal of $150,000

$18,750 from the tax-free component	Tax- free
$95,000 from taxable component	Tax-free (still available from low rate cap)
$36,250 from taxable component	Tax 17% (in excess of lifetime low rate cap)

If Miranda waited until she reached age 60 before withdrawing the amount in excess of her lifetime limit ($36,250), she would receive this tax-free, as all superannuation benefits are tax-free if a person is able to access their super at age 60 or over (i.e. satisfies a condition of release). Note this assumes the funds are from a taxed source. Most super funds are from a taxed source unless they are government funds which are sometimes 'untaxed' as discussed earlier.

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9.0 SUPERANNUATION DEATH BENEFITS

TAKING A LUMP SUM OR A PENSION

A question often raised is whether it is better to take a lump sum or a pension if given the opportunity (as a consequence of the death of a superannuation member). The rule of thumb that you should work on is that superannuation is always the most tax effective environment to build and maintain wealth. Hence, for recipients of pensions (particularly elderly spouses) that cannot contribute to superannuation because they are over age 65, it is generally always within their best interest (if given the opportunity) to continue to draw a pension from the deceased member's benefit and receive all the tax benefits that superannuation provides. The alternative would be that a lump sum would be paid to them (tax free if they were a dependant), but they would be forced to invest the proceeds outside of superannuation where often the tax treatment is less favourable.

DEATH BENEFIT NOMINATIONS

Superannuation does not automatically become an estate asset upon the death of a member so consideration must be given to estate planning arrangements. With the increase in the number of blended families and the rise in the popularity of SMSFs it is important that your superannuation death benefit instructions are made clear to the super fund trustees.

When a member has not left any instructions on how to deal with their superannuation benefits upon death then the trustees of the fund have ultimate control over who receives the benefit.

Whilst this may not be such a serious concern with public offer funds that follow a process to identify and locate potential beneficiaries, it can have serious consequences in an SMSF when the remaining trustee has only their interests at heart.

As the fund is often left under the control of one person after a partner has died, the remaining partner may end up with the ultimate discretion when paying out the benefit of the deceased, as illustrated in the case of Katz vs Grossman.

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Even if the member has a 'Nomination of Beneficiary' in place, this is just an expression of the member's wishes and the trustee is not legally bound by that request.

Most funds provide a Binding Death Benefit Nomination (BDBN) form which, if completed correctly, allows for more certainty.

If a BDBN is completed correctly the member's request must be followed by the Trustees, although, if completed incorrectly it can be declared invalid and then the decision goes back to the Trustee.

There have been many recent legal challenges where the remaining SMSF trustee/s have challenged the validity of BDBNs. Some have been successful and some have not. Some BDBNs are very poorly drafted or completed incorrectly. This is an emerging area of increased risk for advisers.

A sample BDBN form can be found in the appendix.

WHO IS A DEPENDANT FOR SUPERANNUATION SIS PURPOSES?

Upon death, a superannuation benefit can only be paid to a superannuation (SIS[25]) dependant.

A dependant for superannuation (SIS) purposes includes a spouse (including de facto), a child of any age, a financial dependant or someone who was in an 'interdependent' relationship with the deceased.

The term 'interdependent relationship' defines a relationship as a close personal relationship between two people who live together, where one or both provides for the financial and domestic support and personal care of the other. Individuals maintaining a close personal relationship but not living together due to physical, intellectual or psychiatric disability are also considered to have an 'interdependent relationship'. This definition can include same-sex couples.

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[25] SIS refers to the Superannuation Industry (Supervision) Act 1993

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A superannuation death benefit can only be paid to a SIS dependant or to the member's Legal Personal Representative (their estate). Therefore it is important that a person's Will and their superannuation death benefit nomination are aligned.

WHO IS A DEPENDANT FOR TAXATION PURPOSES?

How a superannuation death benefit is taxed will depend on how the benefit is paid and who the recipient of the payment is. To reiterate, a lump sum benefit paid to a dependant is tax free, whereas a benefit paid to a non-dependant is taxable. The definition of a dependant is different for tax purposes. A tax dependant is defined as a spouse, former spouse, deceased's child aged less than 18, a person who was in an interdependency relationship with the deceased just before they died or a dependant of the deceased.

The following table summarises the similarities and differences between the definition of "dependant" for superannuation purposes and tax purposes. In addition to this list, a trustee may also pay the death benefit to the member's legal personal representative.

Beneficiary[26]	**"Dependant" for the purposes of being eligible to receive superannuation death benefits**	**"Dependant" for tax purposes**
Current spouse (married or de facto)	Yes	Yes
Former spouse	No	Yes
Child under age 18	Yes	Yes
Child over age 18	Yes	No (unless financially dependent or interdependent)
Financially dependent	Yes	Yes
Interdependent	Yes	Yes

[26] A trustee may also pay the death benefit to the member's legal personal representative.

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TAX ON SUPERANNUATION DEATH BENEFITS

The two things to be considered from a tax perspective in respect of a super death benefit are:

- Is the beneficiary a dependant or non-dependant for tax purposes?
- Will the benefit be paid as a lump sum or an income stream?

LUMP SUM DEATH BENEFITS

If a death benefit beneficiary is a dependant for tax purposes, no tax is payable on any part of the death benefit.

If a death benefit beneficiary is not dependant for tax purposes, the benefit is taxed as follows:

Tax-free component will always be tax-free

Taxed element will be taxed at 15% + Medicare levy

Untaxed element will be taxed at 30% + Medicare levy

Pro Tip

If the accumulated benefit comes from a taxed source there will not be any amounts in the untaxed element of the death benefit. However, if the benefit includes proceeds from an insurance policy, the proceeds will be split across the taxed element and untaxed element (which is outside the scope of this course).

Case Study

Johannus is a super fund member with $160,000 in his account. On his death, in line with his binding death benefit nomination, the fund pays $160,000 to his children - $80,000 to his non-dependent son James (age 26) and$80,000 to his dependent daughter Julie (age 15). Each benefit has a taxable and tax-free component of $40,000. The payment is from a taxed source.

The tax payable on the benefit would be:

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Julie, as a dependant, will receive the full amount of $80,000 tax free.

James, as a non-dependant, will be taxed at 15% plus Medicare Levy on the taxable component ($40,000) of his $80,000 death benefit.

BENEFICIARIES		James(26)	TAX(James)	Julie(15)	TAX(Julie)
Tax-free component	$80,000	$40,000	nil	$40,000	nil
Taxable component	$80,000	$40,000	$6,800	$40,000	nil
TOTAL	$160,000	$80,000	$6,800	$80,000	nil

PENSION (INCOME STREAM) DEATH BENEFITS

In the event of your death where you have nominated a reversionary beneficiary, your spouse may continue to receive the balance of your superannuation benefit as an income stream and may be entitled to tax concessions[27]. Generally, if at the time of your death you are:

- age 60 or above, the income stream is tax free for your spouse.
- under age 60, the income stream is tax free for your spouse if he/she is age 60 or above.
- under age 60, and your spouse is under age 60, no tax will be payable on the tax-free component and the taxable component will be taxed at your spouse's marginal tax rate (15% tax offset may apply). Once your spouse turns age 60 the income stream will be tax free.

The trust deed may also allow the *trustee* to choose to pay a death benefit as an income stream.

Otherwise, your income stream account on your death will be paid out as a lump sum and generally taxed as follows:

- If paid to a dependant for tax purposes, the lump sum will be tax free.

[27] This section assumes that superannuation funds are from a taxed source.

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- If paid to a person who is not a dependant for tax purposes, the tax-free component of the lump sum amount will be tax free. Tax at a maximum rate of 15% plus Medicare Levy will be payable in respect of the taxable component of the lump sum.

Case Study

Tim and his wife, Rebecca, are both 63. Their superannuation balances are in the accumulation phase. Tim dies and his benefits comprise $100,000 current balance (fully taxable component) and $150,000 insurance proceeds, for a total of $250,000. Rebecca is the nominated beneficiary and the fund allows Rebecca to receive the $250,000 death benefits as a lump sum or a pension.

If Rebecca receives the $250,000 benefits as a lump sum (i.e. withdrawing the funds from superannuation), she would potentially invest the funds in a Term Deposit which could earn 5% p.a. and the interest would be assessable at her marginal tax rate which is assumed to be 47% including Medicare Levy. The total annual tax would therefore be $250,000 X 5% X 47% = $5,875 p.a.

However, if Rebecca chooses to take the $250,000 as a pension, no tax would apply on the earnings (assumed to be 5% p.a.). She would withdraw the minimum pension of 4% p.a. ($10,000). The $10,000 would be not be assessed as she is over age 60 so withdrawal tax does not apply. This is $5,875 p.a. lower than the tax that would apply if the funds were taken as a lump sum.

DEATH BENEFITS AND THE TRANSFER BALANCE ACCOUNT

If you become a recipient of a death benefit income stream, *your* transfer balance account will be affected.

Remember, the transfer balance account keeps a record of retirement phase income streams.

The amount and timing of the credit into your transfer balance account will depend upon whether the death benefit pension is reversionary or not.

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NON-REVERSIONARY DEATH BENEFIT

Depending on the trust deed, a superannuation fund may choose to pay the recipient of a death benefit as either a lump sum or an income stream.

If an income stream is paid to a death benefit beneficiary, the amount of the benefit which is credited to the transfer balance account of the recipient will be the benefit at the date of death plus the earnings between date of death and payment date.

Case Study#1

On 7 September 2017, Fred commences a $500,000 superannuation income stream. Fred has a transfer balance of $500,000.

Fred's wife, Wilma, dies on 29 December 2018, leaving superannuation interests of $288,000. On 14 August 2019, Wilma's superannuation fund advises Fred that he is the sole beneficiary.

The superannuation fund cashes the death benefits (now worth $290,000) as a death benefit income stream to Fred from 1 September 2019. This increases Fred's transfer balance account to $790,000 on that date, which is still below his transfer balance cap. Fred does not need to take any further action.

Transfer balance account: Fred			
Date	Debit	Credit	Balance
07-Sep-17		$500,000	$500,000
01-Sep-19		$290,000[28]	$790,000

REVERSIONARY DEATH BENEFIT

When you commence a retirement phase income stream you can nominate a reversionary beneficiary. What this means is that if you die, your income stream will continue be paid to your beneficiary (usually your spouse and/or minor children).

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[28] The superannuation value at death was $288,000. The amount credited is the value at the transfer date.

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In order to give the reversionary pensioner time to organise their finances, the value of the account supporting the income stream will be credited to their transfer balance account 12 months after the date of death.

NOTE:

The government intends to amend the legislation so that member's taking a transition to retirement pensions are no longer permitted to nominate a reversionary beneficiary.

Case Study #2

David has a retirement phase income stream worth $1.0 million at the time of his death on 1 August 2017. He has nominated his wife Shirley as the beneficiary of his pension. The pension reverts to David's wife, Shirley, and payments from the pension continue to be made to their joint bank account. Shirley already has her own pension and a transfer balance account with a balance of $800,000.

In September 2017, Shirley is advised that she became the recipient of John's pension in August. Shirley is advised that, unless she acts, the combined value of the two pensions will cause her to exceed her transfer balance cap. Shirley has a number of options to respond to the situation. She can fully commute either pension, she can undertake a partial commutation of her pension for the potential excess of $200,000or she can transfer at least $200,000 from her pension back into the accumulation phase.

On 1 December 2017, Shirley makes the decision to transfer $200,000 of her own pension back into an accumulation account in order to allow enough cap space for her to receive the reversionary pension. On that date a debit arises in her transfer balance, bringing her transfer balance down to $600,000.

The $1 million credit in respect of the reversionary pension is credited to Shirley's transfer balance account on 1 August 2018. Shirley has not exceeded her transfer balance cap.

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Transfer balance account: Shirley			
Date	Debit	Credit	Balance
01-Aug-17			$800,000
01-Dec-17	$200,000		$600,000
01-Aug-18		$1 million	$1.6 million

If Shirley did not already have a transfer balance account then her transfer balance account would start on 1 August 2017, the date of David's death.

Pro Tip

By choosing to rollover part of her own pension back into the accumulation phase, Shirley has made space in her transfer balance account to receive the full reversionary pension without exceeding her transfer balance cap.

Alternatively, Shirley could have chosen to commute part or all of the death benefit to a lump sum payment. However, choosing this method would result in the money leaving the superannuation environment where it was receiving concessional tax treatment.

Note the different treatment of the above pensions.

The reversionary death benefit pension uses the balance of the account at the date of death whereas the non-reversionary pension uses the balance at date of death plus earnings up to payment date.

Pro Tip

Death benefit income streams must be kept separate from other income streams, they cannot be combined. If a death benefit income stream exceeds the transfer balance cap, then the excess must be withdrawn as a lump sum death benefit and cannot be rolled back to accumulation.

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Pro Tip

If a life insurance policy is held inside superannuation and the premiums are paid from the accumulation phase, the proceeds of the policy are not included in the retirement phase income stream of the deceased; they are included in the accumulation phase.

CASH OUT AND RE-CONTRIBUTION STRATEGY (FOR ESTATE PLANNING)

Prior to age 65 and assuming the member is age 60 or above, there is an opportunity to cash out and re-contribute monies already in a superannuation account to minimise the effect of this quasi 'death tax'. Hence it is a merry go round of money where ultimately for all intents and purposes it ends up in the same place as it started. So how does it work? Firstly, you could withdraw monies from superannuation without incurring tax penalties if the member is age 60 and satisfies a condition of release but is less than 65 (which really is the only time you would realistically recommend this strategy). The member would not have to satisfy the work test to re-contribute into their super fund (up to their maximum contribution limits of $300,000[29] for non-concessional contributions based on 2017/18 rates), based on the bring-forward rule. This means members have the opportunity to 'recycle' some of their 'taxable' superannuation component to a 'tax free' status. It doesn't have any impact if a member dies and the lump sum is paid to a dependant, but it could save 17% (based on 2017/18 rates) if it was paid to a non-dependant such as an adult child.

A similar strategy could be employed for someone over 65 who meets the work test although they will be restricted to $100,000[30] non-concessional contributions each year based on 2017/18 rates).

Case Study

Estelle is 62 years old and has just retired with an accumulated balance of $400,000 which is 25% tax-free and 75% taxable (from a taxed source). She does not have a

[29] Provided that the member's total superannuation balance is less than $1.4 million.

[30] Provided that the member's total superannuation balance is less than $1.6 million.

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spouse and upon death she will leave her total super benefit to her 40 year old independent son Peter who is not a dependant for tax purposes.

Let's look at how the re-contribution strategy will affect the payout that Peter will receive in the event of Estelle's death.

Scenario #1

If Estelle died today without a re-contribution strategy the super fund will deduct $51,000 (17% of the $300,000 taxable component) in tax and pay a net benefit of $349,000 to Peter.

		Death	Tax	Net death benefit
Tax-free	25%	$100,000	$0.00	$100,000
Taxable	75%	$300,000	$51,000	$249,000
TOTAL	100%	$400,000	$51,000	$349,000

Scenario #2

If Estelle had implemented a re-contribution strategy before she died the fund would only deduct $12,750 (17% of the $75,000 taxable component) in tax and pay a net benefit of $387,250 to Peter.

		Total benefit	Part withdrawal*	Balance	Re-contribution	New balance	New proportion
Tax-free	25%	$100,000	$75,000	$25,000	$300,000	$325,000	81.25%
Taxable	75%	$300,000	$225,000	$75,000	$0	$75,000	18.75%
TOTAL	100%	$400,000	$300,000	$100,000	$300,000	$400,000	100%

*Estelle has only withdrawn $300,000 as this is the maximum amount that she is able to re-contribute as a non-concessional component using the bring-forward rule.

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Pro Tip

This is only one example of a re-contribution strategy. Depending upon the individual client's situation it could be possible to withdraw and re-contribute across a number of years to further increase the tax-free proportion.

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10.0 INSURANCE WITHIN SUPER

Superannuation is often used as a structure to own insurance cover on behalf the fund members. The benefit of this arrangement is that Superannuation Guarantee contributions can be used to pay insurance premiums; however, this can result in an overall lower balance of a member's super account.

The other downside is the tax treatment of the member's insurance benefit when it is paid to a beneficiary who is not a tax-dependant.

Insurance is covered in detail in Module 4 of this course.

The types of personal insurance that can be structured inside the super environment are term life, total and permanent disability and income protection. Trauma is not available in super as a trauma event alone does not satisfy a condition of release under the SIS Act.

TERM LIFE INSURANCE INSIDE SUPER

Whereas life insurance premiums are not tax-deductible for personal tax purposes, they are generally tax deductible within a super fund. Most new life insurance policies are 'term life' covers which expire at a certain age, and premiums for such policies are fully deductible by the fund.

If the fund claims a tax deduction for life insurance premiums, and the member dies and leaves their benefits to a non-dependant, then some or all of the insurance payout will be treated as an ***untaxed element*** of the death benefit and may be subject to tax of 30%plus Medicare Levy (or 30% if paid to the estate for the benefit of a non-tax dependant). This is higher than the tax rate of 15%plus Medicare Levy (or 15% rate if paid to the estate for the benefit of a non-tax dependant) which would apply on the taxable component of the death benefit. If the life insurance payouts were left to tax dependants they would be tax-free.

Case Study

Trevor is a member of the XYZ Super Fund and he dies. In accordance with Trevor's binding death benefit nomination, his death benefit will be paid to his 19 year old son, Michael. The death benefit amount comprises $50,000 tax-free component, $120,000

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taxable (taxed) component from prior employer contributions and earnings as well as a further $100,000 life insurance payout (taxable component – 30% taxed element and 70% untaxed element[31]), for a total of $270,000. Michael is considered to be a non-dependant of Trevor for tax purposes.

The tax consequences of Michael receiving the death benefit in the 2017/18 financial year are as follows:

- No tax will apply on the $50,000 tax-free component.
- 17% tax (i.e. 15% plus 2% Medicare Levy) will apply on the $150,000 taxable (taxed) component = $25,500.
- 32%tax (i.e. 30% plus 2% Medicare Levy) will apply on the $70,000 taxable (untaxed) component = $22,400.
- Total tax will be $25,500 + $22,400 = $47,900.
- Net after-tax proceeds will be $270,000 - $47,900 = $222,100.

If Trevor nominated his wife, Emma, as the beneficiary instead of Michael, Emma would not pay any tax on the $270,000 death benefit and this would improve the after-tax position by $47,900.

TOTAL AND PERMANENT DISABILITY (TPD) INSURANCE INSIDE SUPER

Holding TPD insurance policies inside super is a little more complex. The premiums for TPD insurance policies inside super may be tax deductible depending on the type of TPD policy. It is really important that the type of insurance cover and the terms of the cover are consistent with superannuation rules.

For example, if the TPD policy definition is for "any occupation" i.e. the insured is covered for TPD in the event that due to ill health they are unlikely to be employed in ANY occupation for which they are reasonably qualified by education, training, or experience, then the premiums are likely to be fully tax deductible.

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[31] The *actual* calculation of the taxed and untaxed element of a benefit which includes an insurance component is complicated and outside the scope of this module.

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A TPD policy for an "own occupation" definition, where cover applies if a member is totally and permanently unable to work due to ill health where they are unlikely to ever be employed in their OWN occupation again, cannot be purchased inside super after 1 July 2014. This type of policy must be purchased outside of super.

If an insurance policy covers bundled term life and “any occupation” TPD, the premiums will generally be fully deductible.

Case Study

Francine has an ‘any occupation’ definition TPD Insurance policy which will pay the super fund $200,000 in the event of her suffering TPD. She currently works as a lawyer. Two years after taking out the insurance policy, Francine is in a bad car accident which dramatically hampers her work skills such that she is no longer able to perform her duties as a lawyer. However, she still possesses other skills and abilities which can allow her to do other paid work such as cleaning or selling books.

She is unable to make a successful claim under the ‘any occupation’ definition of TPD as she could still potentially work as a cleaner or book seller.

Pro Tip

It is important to consider the limitations on access to superannuation benefits imposed by the superannuation law. Death and terminal illness benefits can generally be accessed from superannuation funds, but the circumstances when a disability benefit can be paid are sometimes more restrictive than if the insurance is held outside of super.

Because of the more narrow definition of “own occupation[32]”, a situation can arise where an event has happened (say the loss of one limb) where you qualify for a payout of the insurance (the SMSF receives the money) but because the disability is not sufficient to qualify under the more onerous definition of "permanent incapacity" under the superannuation 'condition of release' rules, the money may be stuck in the fund and the member might not be able to access those funds until another condition of release is met. This is one reason why it is common to hold an "own occupation" TPD insurance policy outside of super.

[32] Some members may still have TPD for ‘own occupation’ inside super which was put in place prior to 1 July 2014. However, it can no longer be purchased inside super after 1 July 2014.

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INCOME PROTECTION INSURANCE INSIDE SUPER

Premiums for income protection insurance purchased either inside or outside super are tax deductible. However, the tax deduction is likely to be higher outside super.

The maximum tax deduction inside super is 15%, whereas outside super it may be up to 47% including the Medicare levy.

A Trustee is prohibited from acquiring an income protection policy which provides ancillary lump sum benefits such as rehabilitation and home care benefits.

The terms and conditions of the income protection policy must also satisfy the definition of temporary incapacity contained in the SIS Regulations which requires the member to have:

- ceased to be gainfully employed due to ill-health, or
- have temporarily ceased to receive any gain or reward under a continuing employment arrangement due to ill-health.

Further, the Trustee cannot hold a policy which pays a partial benefit when a member reduces their work hours as a result of accident, illness or injury, rather than ceasing work completely.

The following table summarises the general tax treatment of payouts (benefits) and premiums from pre-tax income (inside super) and post-tax income (outside super).

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Insura nce		Inside super	Outside super
Term Life	**Premium**	Premiums are tax-deductible	Premiums not tax-deductible
	Benefit	Tax free to dependants* Non-dependants taxed up to 30% + Medicare Levy (i.e.32% in 2017/18)	Tax free to any beneficiary
TPD	**Premium**	Premiums may be 67%-100% tax-deductible	Premiums not tax-deductible
	Benefit	Taxed as part of super	Tax free
Income Protection	**Premium**	Premiums are tax- deductible	Premiums are tax-deductible
	Benefit	Subject to income tax rates	Subject to income tax rates

*The term dependant has a different definition for superannuation purposes vs tax purposes.

Superannuation dependants for tax purposes include:

- the deceased's spouse (including same or opposite sex and de-facto).
- the deceased's child under age 18.
- any other person who was financially dependent on the deceased just before they died.
- any other person with whom the deceased person had an interdependency relationship just before he or she died.

Calculating the tax on TPD super benefits, and death super benefits for non-dependants, is a complex formula involving the number of days in work, days to retirement and whether the insurance was paid from pre or post-tax income.

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IMPORTANT

You must now complete Part B of your Multiple Choice assessments for Module 3.

A few tips:

- You can access the Multiple Choice Questions at training.monarch.edu.au
- Press "Ctrl F" if you want to search the pdf course materials for any key words or terms.
- You have 2 attempts. Please note, if you require a second attempt, the answers are shuffled so read them carefully. The highest score counts.
- If you are unsuccessful after 2 attempts, please contact our office on 1300 738 955.

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11.0 SELF MANAGED SUPER FUNDS

OVERVIEW

A Self-Managed Super Fund (SMSF) is a small superannuation fund established for 1-4 people with the fund being controlled by trustees/directors who are also the members. Control is kept in the hands of the members, and the members decide how the fund will operate and what investments the fund will invest in.

There are over 550,000 SMSFs in Australia and this number is increasing every year. When discussing SMSFs with clients, it's important to keep in mind, clients have vastly different levels of financial literacy. When speaking with clients be aware of their knowledge level and communicate appropriately. If a financial adviser uses acronyms during a conversation such as “SMSFs”, “ETFs”, “CGT”, “IPOs”, “TPD”, “IP” etc., make sure you clarify where necessary so that everyone is on the same page.

All of the superannuation rules in respect of contributions, withdrawals etc. which have been discussed so far in this module apply equally to SMSFs. The Trustees must ensure that all these rules are adhered to.

RECOMMENDING AN SMSF

Although having an SMSF appears to be 'in fashion' at the moment, this product is not suitable for everyone and an adviser must consider their client's goals, needs and objectives carefully and ensure that it is in the client's best interests to be a member of an SMSF.

ASIC provides information about super switching advice and the following is an extract from 'Super switching advice - complying with your obligations INFO 182.'

Super switching advice will generally be inappropriate if the adviser knew (or should have known) that:

- the overall benefits likely to result from the 'to' fund would be lower than under the 'from' fund, unless outweighed by overall cost savings.
- the cost of the 'to' fund is higher than the 'from' fund, unless the 'to' fund better satisfies your client's needs.

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ASIC also offers the following compliance tips in respect of the types of things they will be looking for when auditing financial advice providers who have recommended switching superannuation funds:

1. They will look closely at files of advisers who seem to have a number of clients who only want advice about the 'to' fund, although they are still eligible to remain in their 'from' fund.

2. If super switching is recommended with no obvious overall advantage to the client, ASIC will look closely at the disclosure given to the client about conflicts, fees and the basis for the advice.

3. It might be misleading to describe a feature of the 'to' fund as a benefit unless that feature satisfies a client's needs or objectives and is not already available in the 'from' fund.

4. ASIC will look for cases where an adviser has:

Advised a client to establish an SMSF when their current super savings are insufficient and their circumstances do not otherwise support the advice; or

Failed to advise a client properly about ongoing costs (at least in very broad terms based on average costs) and the time and skill needed to administer an SMSF.

ADVANTAGES OF MANAGING AN SMSF

Having your own super fund provides a number of benefits:

- **Control** - An SMSF provides maximum control over your superannuation assets.

  SMSFs allow you the flexibility to decide how your funds are invested and how the fund is to operate.

  SMSFs also allow for greater control over how members’ superannuation benefits will be distributed in the event of their death as the trustees can amend the benefit clauses in the trust deed to pay a death benefit to a particular person and in a particular way.

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- **Investment Choice** - An SMSF can be structured to meet the specific investment needs of members who can exert greater control over investment strategies. The fund can invest in a wide range of investments including property, shares, cash or any other assets that suits the investment objectives of the fund (provided it meets the sole purpose test). Access to investment gearing opportunities also exists.
- **Tax Effectiveness** – An SMSF allows a member to transfer funds from an accumulation phase of superannuation to the pension phase without having to sell any underlying investments. The transfer would simply be via the recording of investments being moved into the pension (income stream) phase upon commencement of the SMSF pension. When investments are sold, if the members are in the retirement phase and they are drawing an income stream from the fund if there is a gain on the sale it will be exempt from Capital Gains Tax. Whilst in the accumulation phase, or the transition to retirement income stream phase trustees can also manage Capital Gains Tax by selling certain investment parcels which will realise capital growth losses to offset tax which would otherwise apply on other parcels being sold with growth being realised.

Case Study

Rhonda's superannuation comprises $600,000 direct shares and $200,000 cash. The shares were initially purchased for $300,000 over 12 months ago and there is currently a $300,000 unrealised capital gain. If the shares are sold while Rhonda is in the accumulation phase of superannuation, she will realise $300,000 capital gains, which would attract capital gains tax within superannuation of 10%, i.e. $30,000.

However, as Rhonda is 60 and has retired, the trustees of the SMSF decide to transfer her accumulation account into a retirement phase income stream. When she eventually sells the shares via her SMSF pension, no capital gains tax will apply.

- **Cost Savings** – SMSFs can result in lower fees than retail or industry funds. If a person or couple have significant superannuation balances, they could establish an SMSF and consolidate their funds into the SMSF which could result in a low ongoing administration and investment fee as a percentage of the SMSF assets. For example, the ongoing administration and investment fees for an SMSF with a balance of $1,000,000 may be 1% p.a. of the fund's assets compared to retail superannuation funds which may have ongoing administration and investment fees of 1.5-2% p.a.

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DISADVANTAGES OF MANAGING AN SMSF

- **Accounting and Audit Fees –** The cost of running an SMSF can be high if the total SMSF assets are low. SMSFs will usually incur ongoing fixed-dollar based accounting and audit fees as well as additional investment management fees. For example, if someone wants to commence an SMSF with a balance of only $50,000, the annual SMSF accounting and audit fees may be $2,500 p.a. which represents 5% of the SMSF balance, where no such fees would apply for retail or industry funds.
- **Trustees' Obligations** – Trustees are responsible for managing SMSFs for the members and significant administration and compliance effort may be required. There can be severe penalties if the trustee does not comply with their obligations.
- **Lack of Investment Expertise** – Someone with limited financial investment knowledge or experience may be unable to choose appropriate investments given their limited access to research on fund performance compared to that of a professional fund manager who can easily access research.
- **Regulation**– SMSF members do not receive the same government protection as they would if they were in an APRA regulated fund, such as statutory compensation in the event of theft or fraud, or access to the Superannuation Complaints Tribunal.

Case Study

The running costs of an SMSF may be an advantage or disadvantage

Using the example of a fund with an average annual cost of $3,600 which includes a full administration service; accounting and audit fees.

If the total SMSF balance is $1,000,000

The annual cost will be $3,600/$1,000,000 which equates to 0.36%

____

If the total SMSF balance is $200,000

The annual cost will be $3,600/$200,000 which equates to 1.8%

____

If the total SMSF balance is $50,000

The annual cost will be $3,600/$50,000 which equates to 7.2%%

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So, the running cost in this example is 1.8% for a $200,000 balance which is comparable to public offer funds; but an expensive 7.2% for a fund with a small balance of just $50,000.

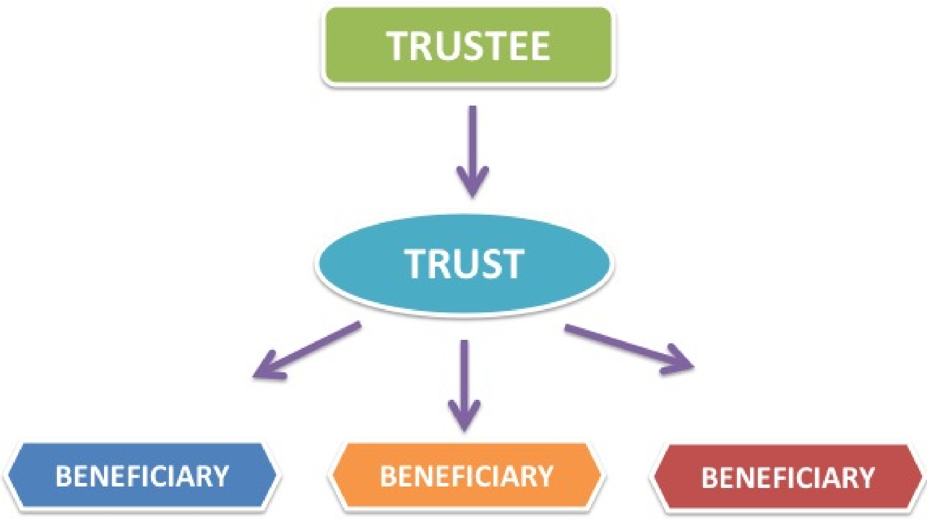
Research exercise - SMSF Regulation

Research 'Trio Capital' to see how a fraudulent investment affected SMSF investors. Note the different outcome for SMSF investors compared to members of APRA regulated superannuation funds.

An SMSF is best suited to those people looking for maximum control over their superannuation assets, but who are also willing to accept certain regulatory responsibilities placed on trustees of SMSFs and willing to work at managing their investments. Self-managed superannuation funds are usually most cost effective when assets exceed $200,000.

SMSFs are regulated by the Australian Taxation Office (ATO) whereas non-SMSFs are regulated by the Australian Prudential Regulation Authority (APRA).

An SMSF is a trust structure. As a trust, superannuation funds can hold assets (e.g. cash, property, shares etc.) which are referred to as ‘trust property’. This means the assets are managed and held by the trustee on behalf of the trust’s beneficiaries. The beneficiaries are the superannuation fund’s members (and their dependants in the event of the death of the member). An SMSF (like all superannuation funds) must have trustees in place who are ultimately responsible for all the affairs of the fund.



http://www.mybe.net.au/blog

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TRUSTEE STRUCTURE

An SMSF will have one of two types of trustees:

- individual members as trustees or
- a corporate trustee.

Generally, all members of an SMSF are required to be either a trustee of the SMSF or in the case where the trustee is a company (corporate trustee); all members are required to be a director of the trustee company.

For single member funds, there are a number of options, as a fund cannot have a sole individual as a trustee. As a consequence of this restriction, the member can:

1. be the sole director of the trustee company; or
2. appoint a second person to be a trustee (provided there is no employer/employee relationship between the two unless they are a relative.)

   What does the term 'relative' mean?

   The SIS Act defines relatives to include a parent, child, grandparent, lineal descendent (e.g. grandchild), sibling, aunt, uncle, niece, nephew, of self or spouse. The definitions include individuals with these relationships through spouses, adoption, and re-marriage. Spouses include de facto and former spouses.

   What does the term 'employee' mean?

   A member is an employee of another person if the other person or one of that person's related parties employs the member directly, via a company of which the other person or their relative is a director or via a trust if the other person or relative is a trustee.

   Note:

   An employee is unable to become a member of their employer's SMSF unless the employer and employee are relatives.

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Case Study

Nick runs a small company and he has his own SMSF. Sharon is employed by Nick and receives SG contributions. Sharon is unable to become a member of Nick's SMSF as they have an employer/ employee relationship.

However, if Sharon was Nick's sister (a relative) she would be able to be a member of Nick's SMSF and her SG contributions could be paid into that fund.

While SMSF members will usually be trustees or directors in the case of a corporate trustee, the following exceptions apply:

The member is a minor–However, once a minor turns 18, the parent, guardian, or legal personal representative acting as trustee on the minor's behalf must resign as trustee and the minor will generally need to be appointed as trustee to remain a member of the fund.

The member is too ill or old to meet the responsibilities of being a trustee or

The member has a mental incapacity (legal disability) – the member's enduring power of attorney can be appointed to act as trustee on their behalf. If the person does not have an enduring power of attorney, a family member or eligible person(s) will need to be court appointed to act on that person's behalf (i.e. become that person's legal personal representative).

The member travels overseas for an extended period - If a fund member plans to go overseas permanently or, in some cases, temporarily, the Australian Tax Office may deem that the 'central management and control' of the fund has not remained in Australia. In order to ensure that the fund continues to meet the definition of a 'resident Australian superannuation fund' and retain the associated tax concessions, the member can appoint an Australian resident as the member's enduring power of attorney. If the member is not comfortable to appoint such a person to act in their place as the trustee, they may prefer to roll over their benefits to a public offer fund or convert the SMSF to a Small Australian Prudential Regulation Authority Fund.

If a fund member dies, they will no longer be a trustee of the SMSF and the deceased member's legal personal representative will generally act as trustee until a death benefit can be paid. However, some trust deeds may allow the remaining trustees to appoint someone else to act as trustee until a decision has been made to make a death benefit payable. Once the death benefit decision has been reached (which can include a partial death benefit payment), the person generally must step down as trustee unless they are also a member of the SMSF. The remaining trustees of the fund are then responsible for

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the ongoing management of the fund. Where a part death benefit payment is made, the subsequent payments will be determined by the remaining trustees.

Trustees are legally responsible for all affairs of the fund even if some decisions are delegated to professionals such as accountants or financial advisers. Trustees must be competent and willing to take on this level of responsibility if an SMSF is established.

Trustees and directors of a corporate trustee are not allowed to receive remuneration from the SMSF for any duties or services performed in relation to the fund. However, they may be remunerated if they perform duties or services in another capacity other than as fund trustee. This would only apply if they are qualified and hold necessary licenses to perform the other services in the ordinary course of their business or provide similar services to the public and the remuneration is at arm's length.

To be eligible to be a trustee or director of a trustee company, the following rules apply:

Generally, anyone 18 years or over can be a trustee of a super fund, as long as they are not under a legal disability (e.g. bankrupt or mentally impaired) or a 'disqualified person'.

A person is disqualified from being an SMSF trustee if they:

- have ever been convicted of an offence involving dishonesty;
- have ever been subject to a civil penalty order imposed by superannuation law;
- are considered an insolvent under administration (i.e. are an undischarged bankrupt); or
- have been disqualified by a regulator (i.e. ATO or APRA).

A company will be disqualified from being an SMSF trustee if:

- a responsible officer of the company (director, secretary or executive officer) is a disqualified person;
- a receiver, official manager or provisional liquidator has been appointed; or
- the company is being wound up.

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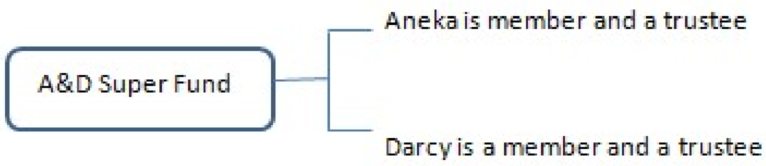
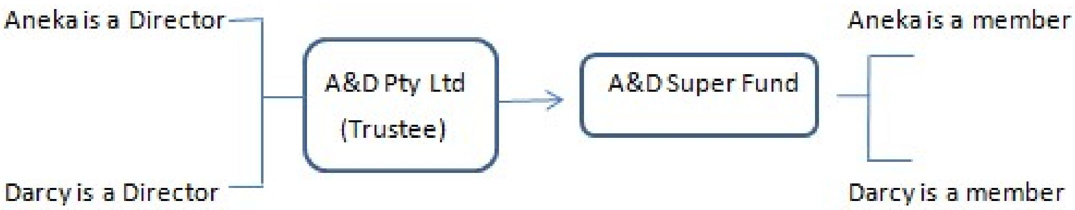
Case Study

Aneka and Darcy wish to establish a SMSF. They are unsure about how the SMSF should be structured. You prepare a chart outlining 4 options they should consider.

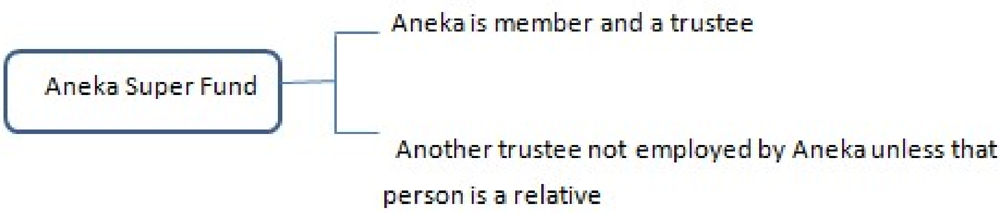
1. Individual trustees (2-4 members in SMSF)



2. Corporate trustees (2-4 members in SMSF)



3. Individual trustees (single member SMSF)



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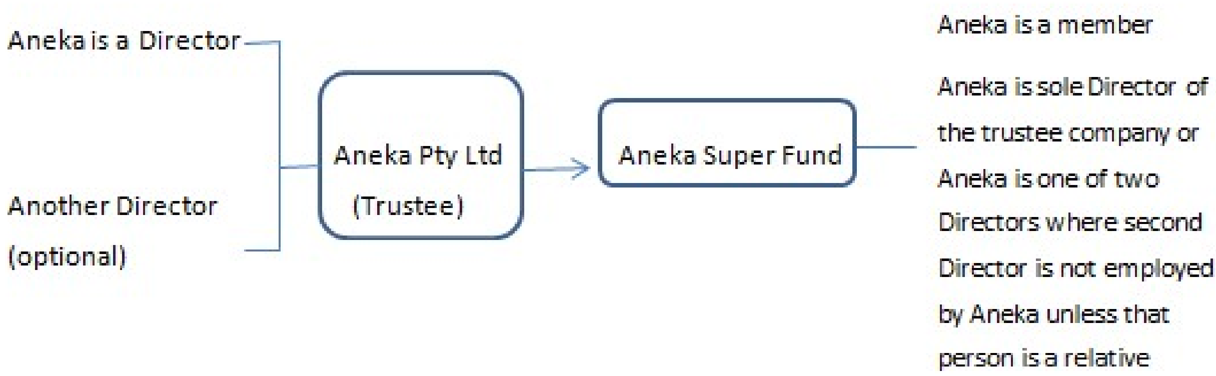
4. Corporate trustee (single member SMSF)



Case Study

Aneka and Darcy decide to have a corporate trustee for the A&D Superannuation Fund. Three years after the establishment of the A&D SMSF, Aneka and Darcy's daughter Abigail, now 17 years of age, wishes to join the fund. Because Abigail is under age 18, she is unable to be a director of the trustee company. Abigail can still become a member of the fund with her parents acting as her legal representative on the board of the trustee company. When Abigail turns 18, she would need to be appointed as a director of the trustee company.

CHOOSING BETWEEN INDIVIDUAL TRUSTEES AND A CORPORATE TRUSTEE

A corporate trustee should not engage in other business activities. Its primary purpose should be to act as trustee for the SMSF.

The benefits of individual trustees compared to a corporate trustee are as follows:

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1. The SMSF can be less costly to establish with individual trustees as a separate company will not need to be set up to act as trustee. An SMSF with a corporate trustee is more expensive as the cost of incorporation needs to be included.
2. A corporate trustee will have additional ongoing compliance and reporting requirements to ASIC. Note that if the trustee company is set up correctly as a sole purpose SMSF trustee company, the annual review fee with ASIC is around 20% of the usual company fee.

Notwithstanding the above, there are some very real benefits in using a corporate trustee, as summarised below:

1. If a member or a trustee joins or leaves an SMSF (or dies), and the SMSF has individual trustees, this is considered to be a change in the trustee of the fund. There is a significant amount of administration relating to the assets of the SMSF that needs to be undertaken in this instance as the trustees may be required to change the ownership details of all the fund's assets. However, with a corporate trustee, the assets of the fund will remain in the company name which will only require a change in the directors of the company – a much simpler scenario administratively.
2. As all SMSFs are required to keep the member's fund assets separate from their personal assets, a corporate trustee structure can help avoid confusion regarding which assets belong to the SMSF.
3. The decision to have a corporate trustee means it is easier to administer if an SMSF becomes a single-member fund. For example, if one member of a two member fund dies, if the fund's trustee is a corporate trustee where both members are directors, the corporate trustee can continue to function with the remaining member as the director without replacing the director who dies. However, with individual trustees, if one trustee dies, another trustee must be appointed in their place.
4. A limited liability company provides greater asset protection.

Using a company as trustee is generally recommended for an SMSF. Although there is a cost to establish the company and also a small ongoing ASIC cost, it could save a considerable amount of time and money in the long run. Here are 2 case studies that highlight why having a corporate trustee can be a very real advantage.

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Case Study- Going overseas

Nancy and Chris, two individual trustees and members of an SMSF, are going overseas indefinitely. In order to keep the central management and control of the fund in Australia and keep it a complying resident fund, 2 new individuals (that have enduring powers of attorney in favour of each member) are appointed as replacement trustees. As well as having to organise a deed to appoint the new trustees and retire the two members (Nancy and Chris) as trustees, all of the investments (e.g. cash, shares, property, managed funds etc.) that the super fund holds also need to be changed into the new trustee's name. This can be a time consuming and costly exercise.

Furthermore, if Nancy and Chris returned to Australia after a few years, and resume as the trustees again, the names of the investments would all need to be updated again.

If in the above scenario there was a corporate trustee in place, the only action that would have been required would be to change the appropriate directors of that company when Nancy and Chris left Australia and when they came back.

Other situations such as death, divorce, marriage or simply a change of family dynamics may cause a change of trustee and each time a trustee is changed where the individuals are trustees there will be considerable time and cost involved.

Case Study- Administrative and director penalties

Under the new SMSF penalty regime which came into effect 1 July 2014, having individual trustees can prove to be very costly as seen in the following scenario.

The XYZ Super Fund has Adam Smith and his wife Julia as members of the SMSF. The fund was found to have breached section 65 of the SIS Act, having provided financial assistance to a member (for example, they loaned money to a member or relative).

As a result of this breach, the ATO imposes a penalty on each trustee of $10,200 (60 penalty units at $170 per penalty unit). Each individual trustee in this case is required to pay $10,200 each ($20,400 in total). They are required to pay this liability personally and it cannot be paid or reimbursed from the fund. If there was a third and/or fourth individual trustee, they would also be charged a $10,200 penalty.

In the above scenario, if there was a company trustee in place, there would only be <u>one</u> fee of $10,200 imposed to which each director is joint and severally liable.

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Pro Tip

Even though a greater percentage of SMSF's are currently structured with individual trustees, the trustees may suffer damages by not having a limited liability company.

For example, in the event of an insurer denying liability, the occupants of a property may make a claim against the property owner, that is, the individual trustees. This could result in a very poor outcome for the trustees and potentially for the adviser for recommending this trustee structure.

Have a look at this short video on SMSF trustees from the ATO.

https://www.ato.gov.au/super/self-managed-super-funds/in-detail/smsf-resources/smsf-videos/?anchor=smsftrusteesindividualorcorporate#smsftrusteesindividualorcorporate

11.1 RESPONSIBILITIES OF SMSF TRUSTEES

SMSF trustees are responsible for all aspects of the fund, including the administration, investment decisions and meeting of legal requirements. Trustees may engage an accountant or other financial professionals to assist them in these responsibilities. In administering the fund, trustees will be responsible for the acquisition and disposal of assets, the payment of taxation and other liabilities, and all of the decisions relating to the fund, on behalf of all of the fund's members.

Corporate trustees will need to adhere to a number of rules:

- SMSF trust deed rules (set out in the SMSF trust deed)
- Superannuation laws
- Company rules (set out in the company's constitution)
- Corporations Act

For individual trustees, all the rights and obligations will be contained within the SMSF trust deed. Note though, if the trust deed is more flexible than superannuation law requires, the more restrictive superannuation law will apply.

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What is included in a trust deed?

Some common areas that a trust deed covers include:

- compliance with superannuation law
- rules prescribing how trustee decisions about the fund are made (including the voting)
- rights of particular trustees, if the trustees are individuals
- how trustees are appointed or removed
- preparation of accounts
- record-keeping
- who can join the fund as a member
- what and how investments and insurances can be affected
- whether the fund is able to borrow
- circumstances in which benefit entitlements arise
- who can make contributions and the types of contributions that can be received
- whether members can split concessional contributions with their spouse
- whether the fund can make internal rollovers
- how to transfer benefits to the fund
- how to transfer benefits from the fund such as lump sum and/or income stream
- acceptance of binding death benefit nominations
- who can receive death benefits
- rules to establish and administer fund reserve accounts
- how to vary the rules by amending the trust deed
- how to wind up the fund.

The SMSF's trust deed can be amended as long as the trustee follows the guidelines set out in the original trust deed in terms of how to amend the trust deed. This may be appropriate when legislation changes and the SMSF wants to take advantage of those changes to benefit members.

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Amendments to the trust deed cannot reduce a member's entitlements unless it is approved with the member's written consent or the regulator.

An SMSF will breach superannuation law if the fund breaches its own trust deed.

Have a look at this short video on 'What's involved with an SMSF', from the ATO.

https://www.ato.gov.au/super/self-managed-super-funds/in-detail/smsf-resources/smsf-videos/#WhatsinvolvedwithanSMSF

SUMMARY OF SMSF INVESTMENT RULES

These course notes outline the various SMSF investment rules which SMSF trustees will need to follow to ensure that their SMSF remains compliant. In summary, the main SMSF rules which must be followed when purchasing and managing investments are as follows:

- Satisfy the 'Sole Purpose' test (as explained earlier in this module)
- Ensure all transactions are at arm's length
- Not borrow (unless one of the limited exceptions to this rule apply such as via a Limited Recourse Borrowing Arrangement)
- Not provide financial assistance to members or relatives
- Not acquire assets from related parties (unless one of the limited exceptions to this rule apply such as buying Business Real Property or ensuring that the amount purchased is within the 'in-house assets test' limit)
- Satisfy the 'in-house assets test'
- Ensure investments are consistent with the fund's investment strategy
- Not use fund assets as security for borrowing

A sample of the Australian Taxation Office's "Trustee Declaration" instructions and form which must be completed by new SMSF trustees is contained in the appendix. This declaration form includes detailed sections on the Sole Purpose test and investment restrictions which are outlined above, as well as further sections on trustee duties, accepting contributions and paying a benefit and administration of the SMSF.

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The appendix also contains the compliance section of the self-managed superannuation fund independent auditor's report from the ATO, which lists all the rules that must be adhered to.

Have a look at this short video on the sole purpose test, from the ATO.

https://www.ato.gov.au/super/self-managed-super-funds/in-detail/smsf-resources/smsf-videos/?anchor=Solepurposetest#Solepurposetest

11.2 STEPS INVOLVED IN SETTING UP AN SMSF

When setting up an SMSF, there may be a need for specialist advice. Clients may need to be referred to their accountant, lawyer, bank manager or a more experienced or specialist financial adviser to best serve their interests. The ideal outcome for the client is when different professionals are all working together to help the client. As advisers build referral relationships with other professionals, over time, the value of these referrals may become a two way street.

There are a number of steps that trustees must undertake to establish an SMSF.

1. Create a Trust Deed

The Trust Deed sets out the rules under which the SMSF will operate and must be signed and dated by the trustees.

2. Appoint a trustee or trustees and sign the declaration of consent

Trustees or directors of corporate trustees need to consent in writing to their appointment, indicating awareness of their responsibilities. The declaration must be signed within 21 days of the trustee's appointment.

3. Record TFN of each member

It is important that the SMSF records the TFN of each member so the SMSF can receive member contributions.

If a member hasn't quoted their TFN:

The fund can't accept certain contributions made on their behalf, including personal and eligible spouse contributions

The fund may need to pay extra tax on some contributions made to that member's account

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The member may not be able to receive super co-contributions

4. Open a bank account

To establish the SMSF as a trust, a small contribution needs to be made into the fund's bank account when the trust deed is executed. This bank account can then be used to receive cash rollovers from other super funds, interest from savings, dividends from shares and sales proceeds from the disposal of any investment assets. Distributions such as payment of benefits, payments of tax and fees incurred for other services can be withdrawn from the fund's bank account.

5. **Register the SMSF with the ATO**, obtain a Tax File Number (TFN) and an Australian Business Number (ABN) for the SMSF and possibly register for Goods and Services Tax (GST)

Within 60 days of the execution of the trust deed, both a TFN and ABN need to be obtained. (These can be applied for online at www.ato.gov.au). Once an ABN has been obtained, the fund can register for GST.

Note: The fund must also be registered for GST if its annual turnover exceeds $75,000. Annual turnover does not include contributions, gross income from financial supplies (including interest and dividends), most residential rent or income generated outside Australia. It does include gross income from the lease of equipment or commercial property and any fee the fund charges a member for salary continuance insurance.

If a fund is not required to register for GST, the trustees may still choose to register in order to claim Reduced Input Tax Credits (RITCs) which can be claimed on expenses such as legal, financial advice and accounting fees when setting up the fund and some ongoing administration fees. However, funds that register for GST will need to lodge quarterly Business Activity Statements (BAS) which can lead to additional costs.

6. Prepare an investment strategy and consider insurance needs of members

An investment strategy provides the trustees with a framework for making investment decisions to increase members' benefits for their retirement. It should be in writing so any investment decisions can be consistent with the written strategy and therefore comply with the super laws.

When preparing an investment strategy, you need to consider:

- diversification (choosing to invest in a range of assets and asset classes to limit downside risk

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- the risk and likely return from investments, to maximise member returns based on the level of risk the members are willing to accept (for example, each member may have different risk profiles or timeframes and require a different mix of investment assets)
- the liquidity of fund's assets (how easily they can be converted to cash to meet fund expenses and pension payments)
- the fund's ability to pay benefits when members retire and other costs the fund incurs
- the members' needs and circumstances (for example, their age and retirement needs)

Whilst there is no requirement for the fund to obtain insurance cover on behalf of members, trustees will need to consider the types and amounts of life insurance member's should seek (if any) and whether the fund should own the life insurance policies such as term life insurance, TPD insurance and income protection insurance on behalf of the member inside the SMSF or if the member should instead seek insurance outside of the SMSF. Documentation of the trustee's decisions in this area could be recorded in the investment strategy or alternatively via separate trustee minutes.

Once an investment strategy has been set, it must be implemented and reviewed regularly such as annually; whenever membership of the fund changes or a member's personal circumstances change.

The appendix contains a sample investment strategy.

Click on the following link to view an investment strategy video from the ATO.

https://www.youtube.com/watch?v=PLxbGqnYJ30

Case Study

Aneka and Darcy commence an investment strategy for their SMSF. Six months later, Aneka decides to retire and draw down a pension via her SMSF balance. It would be appropriate to review the investment strategy of the SMSF to ensure that the investment mix would still be appropriate for the members and update it if, for example, Aneka wants to reduce her exposure to growth assets in order to increase the exposure to cash-based investments which could be used to provide her with regular pension income.

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IMPORTANT ISSUES TRUSTEES MUST CONSIDER

The following areas are important for trustees to consider when commencing and reviewing their SMSF:

1. Arrange and review death benefit nominations for members

A death benefit nomination states who the member wishes to receive their superannuation benefit in the event of their death. Depending on who the benefit is paid to, a member may also be able to stipulate whether the benefit should be paid as a lump sum or pension. There are limitations on who can receive a death benefit and different tax treatments apply to different types of beneficiaries.

When a member dies, the remaining trustees must pay out the member's death benefit. Where a member has made a non-binding death benefit nomination (or invalid binding death benefit nomination), the trustees will need to consider the member's nominations before paying out any death benefits. Having said this, the trustees still have total discretion provided that their decisions are allowed by law and the trust deed. This can result in some trustees choosing to pay a deceased member's death benefit to themselves or a beneficiary whom they prefer rather than the beneficiary to whom the deceased member planned to provide the death benefit. This can cause disputes.

Example

In the case *Katz v Grossman [2005] NSWSC 934*, upon the death of his wife, Mr Katz appointed his daughter to act as the second trustee of his SMSF and he put in place a non-binding nomination in favour of his daughter and son. Upon his subsequent death, his daughter appointed her husband to act as the new second trustee and they refused to pay the death benefit to Mr Katz' son, effectively using their discretion as trustees to over-ride Mr Katz' non-binding nomination.

A valid *binding* death benefit nomination provides greater certainty and will help ensure the remaining trustees implement the member's wishes.

An alternative to a binding death benefit nomination is a trustee side agreement which can specify how a member's death benefits will be paid, provided that it is consistent with the trust deed and legislation. Trustee side agreements are contracts between the

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trustees and a member which should be stamped by the Office of State Revenue in the relevant state to be legally binding.

It would be appropriate for SMSF trustees and members to review the death benefit nominations over time as members' personal situations change.

Case Study

Bob and Judy are members of an SMSF along with their son, Jack. Judy has a binding nomination in place for her superannuation to be paid to Bob in the event of her death. Three months later, Bob dies. At that time, Judy's nomination would no longer be relevant and it would be appropriate for her to nominate another person as her beneficiary.

2. Ensure all SMSF assets are kept separate from members' assets

As an SMSF is a separate legal entity, all records must be maintained in the name of the SMSF. Trustees of an SMSF must ensure their personal assets are held separately from those belonging to the SMSF.

SMSF assets should never be held in the trustee's own name without also being identified as an asset of the SMSF. Shares and bank accounts should be in the name of the fund, not the individual.

Where property is purchased by the trustees for an SMSF, the contract on purchase of the property should show the name of the trustee as trustee for the superannuation fund. This is a clear statement of the capacity in which the trustee is acting.

Case Study

Aneka and Darcy decide to purchase a commercial property for the SMSF. They have a corporate trustee structure. The title ownership of the property will read "A & D Pty Ltd as trustee for A& D Super Fund".

3. Maintaining records and lodgement of returns

Trustees are responsible for reviewing the fund's investment strategy regularly to take into account the changing circumstances of the fund and its members.

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Trustees are also responsible for valuing the fund's assets at their market value for the purpose of preparing the financial accounts and statements of the fund.

Market value is defined in the SIS Act as the amount that a willing buyer of the asset could reasonably be expected to pay to acquire the asset from a willing seller under the following assumptions:

- The buyer and the seller dealt with each other at arm's length in relation to the sale;
- The sale occurred after proper marketing of the asset; and
- The buyer and the seller acted knowledgeably and prudentially in relation to the sale.

Trustees must arrange for the completion of the SMSF's annual return and lodgement of the annual return with the ATO each year by the due date. The annual return comprises the following:

- Tax return – This incorporates the fund's assessable income and deductions
- Member contributions statements – This reports the types and amounts of contributions received for each member each year.
- Financial and compliance audit - This involves an approved auditor auditing the fund's financial statements and accounts (assets, liabilities, entitlements, and transactions) to ensure they correctly reflect the fund's financial position, as well as verifying that a fund has complied with specific sections of the SIS Act at all times during the year as outlined in the approved audit report form. The approved audit report form can change from year to year and will generally include compliance areas such as meeting the definition of an SMSF and meeting the sole purpose test.

There is a legal obligation to have an SMSF independently audited each year by an approved auditor. An auditor's report is required before the SMSF can lodge its annual return. The law requires that an independent auditor be appointed at least 30 days before the annual return is due to be lodged. Any breaches of the super rules will result in the auditor reporting such breaches to the ATO.

An approved auditor must be a current member of a registered professional body. The auditor must be a member of one of the following professional bodies or organisations:

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- a member of CPA Australia Ltd
- a member of the Institute of Chartered Accountants in Australia
- a member of the National Institute of Accountants
- a member or fellow of the Association of Taxation and Management Accountants
- a fellow of the National Tax and Accountants' Association Ltd
- an SMSF specialist auditor of the SMSF Professionals' Association of Australia Ltd
- a registered company auditor
- an auditor-general of the Commonwealth, a state or a territory.

SMSF documentation must be keep up to date and accessible at all times.

The following documentation must be kept and retained for at least 10 years:

- Minutes of all trustee meetings at which matters affecting the fund were considered (this includes investment decisions , decisions to appoint members and trustees and decisions to pay benefits);
- Records of all changes of trustees, including directors of the corporate trustee;
- Each trustee’s consent to be appointed as a trustee of the fund or a director of the corporate trustee;
- All trustee declarations; and
- Copies of any reports provided to members.

The following documentation must be kept and retained for at least 5 years:

- Accounting records of the fund;
- Copies of the fund’s annual operating statement and statement of financial position;
- Copy of the annual return lodged with the ATO;
- Copies of any rollover benefit statements provided to other funds.

It is also the responsibility of the trustees to notify the ATO within 28 days if the SMSF has any changes in the following information:

- trustees, directors of the corporate trustee or members of the fund

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- fund name
- members of the fund
- details of the contact person, contact phone and facsimile numbers, and
- the postal address, registered address, or address for service of notices for the fund

STEPS INVOLVED IN SETTING UP A PENSION VIA AN SMSF

Once an SMSF member satisfies a condition of release and chooses to commence an SMSF pension or reaches preservation age and wishes to commence a Transition to Retirement pension, there are a number of steps the trustees should follow:

1. The member must provide a written request to commence the pension – this includes the date of commencement, type of pension and capital used to commence the pension, as well as the amount of pension income in the event of an account-based pension.
2. Review the trust deed to ensure that it allows for the payment of the pension.
3. Prepare minutes of a meeting of trustees to resolve to pay the pension.
4. Obtain the member's Tax File Number Declaration and bank account details.
5. Prepare minutes of a meeting of trustees to resolve to pay the specified level of pension payments to the member.
6. Generally, upon commencing an account-based pension, trustees will be required to value the assets at market value.
7. If the member is under 60, the fund needs to register for Pay As You Go (PAYG) in order to deduct tax prior to paying the pension.
8. If required, the trustees must prepare a 'Details of Income Stream' report for social security purposes.
9. Decide whether to undertake a segregated or un-segregated approach to fund the pension. **

If a member has retired and reached their preservation age and is less than 65, the member should write a Retirement Declaration to their SMSF to confirm that they have

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met the required condition of release to be able to withdraw funds as a lump sum or alternatively as a pension.

Example 1

Jill is aged between preservation age and less than 60. She is 58 and has retired and she wants to access her superannuation funds.

She may write a letter to the trustees of the SMSF with the following text:

"I hereby declare that I have ceased employment and at the time I ceased employment I was over preservation age and less than 60. I further declare that I never intend to work again either on a full-time or part-time basis (defined as more than 10 hours per week). I understand that whilst I never intend to work again, I may ultimately do so and that this will not alter my status for superannuation purposes of being retired."

Example 2

Fred is 62 and has been made redundant. He plans to obtain a new job although he wants to access a large part of his superannuation to travel.

He may write a letter to the trustees of the SMSF with the following text:

"I hereby declare that I have ceased employment and at the time I ceased employment I was over 60. I understand that my intention to return to the workforce is irrelevant and that for the purposes of the superannuation regulations I am considered "retired".

** The income which is produced by the assets supporting a retirement phase income stream is exempt from 'earnings' tax. This is referred to as 'exempt current pension income'. There are two ways to determine the amount of exempt current pension income.

You can choose to have the assets 'segregated' or 'un-segregated' (pooled) for pension purposes.

If the assets are pooled (un-segregated) and the entire fund does not support pension payments, that is, there are also accumulation account/s, an actuarial certificate is required to determine the amount of exempt current pension income.

An actuarial certificate is available online from a number of providers for an average cost of $200 each year.

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Alternatively the segregated approach requires you to identify specific assets in the fund which are set aside to provide for pension payments.

Section 11.10 further discusses segregated and un-segregated assets.

MID-YEAR BALANCES

Trustees will be required to ensure that each account of each member is accurately valued at the end of each financial year after apportioning any earnings and considering any contributions or withdrawals.

In some situations, trustees will also need to ensure that account balances are accurately valued mid-way throughout the year when the following situations arise:

- Commencing a pension
- Commuting a pension (i.e. a lump sum withdrawal from the pension which is treated separate to an additional pension payment)
- Rolling benefits out of the fund (e.g. transferring a member's SMSF holding into a retail superannuation fund if the member no longer wants to be a trustee of the SMSF)
- Withdrawing from a fund
- Winding up a fund

11.3 ENSURING THE SMSF REMAINS COMPLIANT

When an SMSF is set up and registered with the ATO and has lodged its first annual return, it is granted complying superannuation fund status. By following the rules, it will retain its complying status and continue to enjoy benefits such as concessional taxation treatment.

The ATO has the power to revoke an SMSF's complying status or impose penalties if the trustees are in breach of their duties and responsibilities. The regulators can and have penalised trustees for breaking the rules and have in more severe circumstances of deliberate breaches, withdrawn the fund's complying status.

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Generally, penalties imposed on trustees and/or the fund depend on the type and extremity of the breach but may include one or more of the following:

Administrative penalty – The ATO may levy an administration penalty (e.g. a fine) on the fund. For example where the trustee has failed to lodge returns on time or where a change of trustees has not been reported.

Rectifying agreements – written agreements or enforceable undertakings may be required to ensure that the trustee will rectify a breach and how they intend to do so.

Disqualification – being disqualified as a trustee of your own SMSF which will also mean an inability to be a member of the fund.

Tax penalties – For very serious breaches, the tax office has the power to strip an SMSF of its complying status. This will result in the fund's assets – less non-concessional contributions – being taxed at 47%. The Cooper review referred to this as the "nuclear option" because it is so devastating for a fund with up to almost half of a fund's assets being eroded by tax. A fund that has its complying status revoked by the ATO will also have earnings taxed at 47% instead of the concessional rate of 15%.

Prosecution – if a trustee is prosecuted and found guilty of either a civil and/or criminal offence, the maximum penalties which may apply under Part 21 of the SIS Act are $220,000 (civil proceedings) and/or five years imprisonment (criminal proceedings).

The penalties outlined above may be imposed on an individual or on the fund. The penalties for non-compliance are severe. Both trustees and their advisers must use care, skill and diligence in running an SMSF.

Generally, the potential impost of penalties can most easily be overcome by trustees performing their duties with the same degree of care, skill and diligence that would be expected of a normal prudent person.

Where the trustee acts in good faith, exercises the appropriate degree of care, skill and diligence, and acts with the best interests of all the members of the fund in mind, the compliance status of the fund can be expected to be maintained.

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IS THE SMSF A RESIDENT FUND?

To be a complying super fund and receive tax concessions, an SMSF must satisfy the residency test. As a trustee, you must make sure your fund meets all conditions of the residency test to ensure it qualifies as an Australian superannuation fund.

The residency test has three elements:

a. the fund was established in Australia, or at least one of the fund's assets is located in Australia;

b. the central management and control of the fund is ordinarily in Australia (as explained below); and

c. the fund satisfies the *active members* test (also explained below).

What does central management and control ordinarily in Australia mean?

Central management and control of the fund is ordinarily in Australia if the fund's strategic decisions are regularly made, and high level duties and activities are performed, in Australia. This allows trustees to be non-residents without causing their fund to fall outside the definition of an Australian Superannuation Fund as long as their period of non-residence is only temporary and the central management and control is ordinarily in Australia. Whether the trustee meets the definition of 'temporary' will be determined on a case by case basis taking into account the intention of the trustee prior to departing Australia.

What is the active members test?

An 'active member' of an SMSF includes someone who has contributed to the fund or who has had contributions made on their behalf, except if a foreign resident has had contributions made on their behalf relating to the time when they were an Australian resident.

A fund will satisfy the active members' element of the residency test at a particular time, and for the income year in which that time occurs, if either the fund has no active members or has active members who are Australian residents holding at least 50% of:

The total market value of the fund's assets attributable to super interests held by active members; or

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The sum of the amounts that would be payable to or in respect of active members if they voluntarily ceased to be members.

However, a member will not be an active member at a particular time if contributions have been made on their behalf and:

- they are a foreign resident;
- they are not a contributor at that time; and
- the contributions made on their behalf after they became a foreign resident were made in respect of a time when they were an Australian resident.

What happens if the SMSF doesn't satisfy the residency rules?

The SMSF must satisfy the residency rules at all times to be eligible for the tax concessions available to complying super funds. There are tax consequences if the fund becomes non-complying.

If the fund stops being a complying fund because it does not satisfy the residency rules and therefore cannot meet the definition of an Australian superannuation fund, an amount equal to the market value of the fund's total assets (less any contributions the fund has received that are not part of the taxable income of the fund) will be included in the fund's assessable income. This amount is taxed at the highest marginal tax rate.

For every year that the fund remains non-complying, its assessable income is taxed at the highest marginal tax rate.

Case Study (based on example from ATO SMSFR 2010/2)

Andrew works for a large international group of companies. He and his wife, Jane, are trustees and members of their SMSF. From 1 February 2015 Andrew is transferred to an overseas company for an indefinite period of time. Andrew and his wife each execute an enduring power of attorney in favour of their friend and retired accountant, Trevor. They both resign as trustees of their SMSF and appoint Trevor as the Trustee.

Trevor is a legal personal representative of both of the members as he holds an enduring power of attorney for each of them. Trevor is now the trustee of the SMSF in place of both Andrew and Jane.

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ACCEPTING CONTRIBUTIONS AND ROLLOVERS

Trustees are expected to know the rules for accepting contributions and rollovers. It is their responsibility to ensure contributions and rollovers are:

- properly documented, including the amount, type and breakdown of components; and
- allocated to the correct member's account.

Contributions can be made to the fund in the form of money or an asset other than money (called an 'in specie' contribution). All contributions must be allocated to each member's account within 28 days after the end of the month in which those contributions are received.

Contribution reserving strategy

As the fund has 28 days to allocate contributions to a member's account, it is possible to implement what is known as a 'contribution reserving strategy'.

This is where a concessional contribution is remitted to the fund in the current financial year, but is not allocated to the member account until the following financial year.

Previously this has resulted in the automatic generation of 'excess contribution' notices from the ATO as the system could not match concessional contributions remitted with concessional contributions allocated. This created much angst among those who favour this strategy.

The ATO issued a Taxation Determination TD 2013/22 around this strategy providing the following example.

Example

Harry's concessional contributions cap for the 2015-16 financial year is $30,000. Harry is a member of a complying superannuation fund which is not a constitutionally protected fund. Harry makes a personal contribution of $30,000 which is received by his fund on 30 June 2016. The Trustees apply this amount to an unallocated contributions account established in accordance with the governing rules of the fund. On 2 July 2016, the trustees allocate the amount of $30,000 to Harry's member account in the fund with effect from 2 July 2016.

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Harry's contribution is covered by a valid and acknowledged notice given to his fund under section 290-170 of the ITAA 1997 of his intention to deduct the amount of the contribution.

The $30,000 contribution is included in the amount of Harry's concessional contributions for the 2015-16 financial year as an amount covered under subsection 291-25(3) of the ITAA 1997.

The ATO has subsequently produced a form- NAT74851 'request to adjust concessional contributions' which helps to alleviate the problem of excess contribution notices.

There is a sample of this form in the appendix.

Rollovers and transfers

Once the SMSF is established, a member can rollover or transfer some or all of their existing super benefits to it. Before they can do this, they need to provide proof to their former super fund that the SMSF is a regulated fund and is eligible to receive rollovers. They can do this by visitingwww.superfundlookup.gov.au

Members can use a 'Request to transfer whole balance of superannuation benefits between funds (NAT 71223)'form to roll over the whole balance of their super benefits to the fund. They must also meet the requirements of the fund they are leaving.

Please refer to the appendix for the 'Request to transfer whole balance of superannuation benefits between funds (NAT 71223)' form.

Generally, when the ABN of the SMSF first appears on Super Fund Lookup, a message will show that the application is still being processed and provide an estimated date for completion. When the fund's application has been processed and approved, the status of the fund will be updated to appear on Super Fund Lookup as 'Registered – Status not determined'. The fund will keep this status until it has lodged its first tax return and has been issued with a notice of compliance.

Super funds cannot roll over super benefits to the SMSF while an application is being processed.

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If a member only wants to roll over part of their super benefits from another fund, they must contact the fund directly to organise the paperwork. The fund will complete a '*Rollover benefits statement* (NAT 70944)'. The completed statement will be sent to the SMSF within seven days of paying the rollover payment and a copy to the member within 30 days.

Note: Rollovers and transfers are not treated as contributions in the fund and therefore do not count towards the contributions caps.

Reserves

Reserves can be established in an SMSF if these are allowed by the trust deed. There are various types of reserves which include an investment reserve where earnings of the fund assets accumulate. These reserves are an asset of the fund where the members are not presently entitled. Reserves funds can be distributed to members as determined by trustees or the trust deed.

SMALL BUSINESS CAPITAL GAINS TAX (CGT) CONCESSIONS

All assets subject to CGT are subject to standard CGT discounts for assets held over 12 months, depending on the entity which owns the asset. For example, individuals are entitled to a 50% CGT discount and superannuation funds are entitled to a 1/3 discount.

As a business owner of active assets, if you are aged 55 years or over and are retiring, or if you are permanently incapacitated, there is no assessable capital gain if your business has owned active assets for 15 years and makes a gain when those assets are sold.

As well as this CGT exemption, further concessions are made available to business owners. Business owners are not generally required to pay Superannuation Guarantee contributions towards their own superannuation. As such, many business owners elect to treat their business as their retirement funding mechanism instead of contributing to their superannuation.

In recognition of the above, the Government allows up to $1,445,000 (2017/18 year) of a members' entitlement from the sale of business active assets to be contributed as a tax-free component of superannuation. This limit is known as the CGT Cap and it is a lifetime limit which is separate from a member's annual concessional contributions and

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non-concessional contributions limits. A member could potentially contribute maximum funds to superannuation under all three limits if the CGT Cap has not previously been utilised.

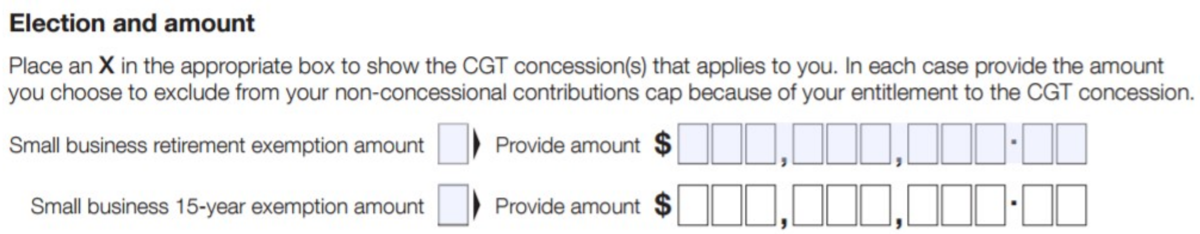
To ensure that your super fund does not count this contribution as a non-concessional contribution the 'capital gains tax cap election' form must be provided prior to, or at the time that the contribution is made. If this does not occur then the contribution will be counted towards the non-concessional cap.

A sample of this form can be viewed in the appendix; the screenshot below is an extract from the form.

Case Study

If a small business owner, with no current super balance has a capital gain of $800,000 from the sale of a business and they have not satisfied the 15-year exemption, an amount of $500,000[33] can be contributed to super under the small business retirement exemption and the balance of $300,000 could be contributed as a non-concessional contribution using the bring forward rule provided that the individual is under the age of 65.

Alternatively, if the small business 15-year rule was satisfied, the full $800,000 could be contributed under the 15-year exemption. This would leave the ability to contribute $500,000 under the retirement exemption at a later date from a future small business venture that does not satisfy the 15-year rule.



Election and amount

Place an **X** in the appropriate box to show the CGT concession(s) that applies to you. In each case provide the amount you choose to exclude from your non-concessional contributions cap because of your entitlement to the CGT concession.

Small business retirement exemption amount ▶ Provide amount $, , .

Small business 15-year exemption amount ▶ Provide amount $, , .

The amount in the first box must not exceed $500,000 and both amounts combined must not exceed $1,445,000 (2017/18 year). This assumes that no previous elections have been made.

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[33] Lifetime limit for small business retirement exemption

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Case Study

Jason, aged 62, recently sold a small business he had founded and run for the last 19 years. The business sold for $1.5 million. Jason owned the active business assets personally and made a capital gain of $1 million upon the sale.

Jason is eligible to claim the 15-year CGT exemption, which will enable him to disregard the entire capital gain.

He does not currently have any money in a superannuation account and he has not claimed any of his lifetime CGT cap. Jason is able to invest the full sale proceeds of $1.5 million in super without exceeding the contribution caps. (To do this Jason will claim the full CGT cap of $1,445,000 (2017/18 year) and he will be able to contribute the remaining $55,000[34] as a non-concessional contribution as his total superannuation balance is less than $1.6 million.

11.4 CAN AN SMSF LEND MONEY TO FUND MEMBERS?

An SMSF must NOT lend money or provide financial assistance to a member of the fund or a member's relative. This includes a prohibition on lending money to a relative even if the money is to be paid back or taking money temporarily to meet a personal cash flow shortage.

This is covered in Section 65 of the SIS Act.

'The trustees must not loan monies or provide financial assistance to any member or relative at any time during the financial year'.

[34] The $55,000 will count towards the non-concessional cap for the financial year that the contribution is made.

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11.5 CAN AN SMSFPURCHASE ASSETSFROM FUND MEMBERS?

In general an SMSF is prohibited from acquiring assets for the fund from members or other “related parties” of the fund (where “related parties” are defined later).

This is covered in Section 66 of the SIS Act.

'The trustees must not acquire assets (not listed as an exemption) from any member or related party of the fund'.

There are exceptions where an SMSF is permitted to acquire assets from members or related parties. A super fund can acquire:

- Listed securities on an approved stock exchange
- Term deposits
- Units in widely-held unit trusts (managed funds)
- Business real property (real estate used 100% for business or commercial purposes)
- In-house assets valued at no more than 5% of a fund assets
- Units in a 13.22C unit trust **

If an SMSF purchases an allowable asset from a fund member, then any capital gains on the sale of that asset is the liability of the fund member, not the super fund.

If an individual makes an in-specie (non-cash) contribution in the form of listed shares or other assets, any capital gains on the transfer is again the liability of the fund member.

Where a member transfers listed shares to the fund at market value, the fund would treat the shares as both a member contribution and as an asset purchase by the fund.

(www.moneymanagement.com.au)

** In order to meet the requirements of SIS regulation 13.22C, the trust must:

- Be a unit trust,
- Have no debt and not allow any security to be taken over its assets;
- Have no lease arrangement with a related party other than one relating to business real property;

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- Not acquire an asset (other than business real property) from a related party;
- Not lend money to any entity other than an authorised deposit taking institution (e.g. a bank);
- Not conduct a business; and
- Not own an interest in another entity – which means it cannot own shares or invest in another trust.

Broadly, this means the trust will only own residential or business real property and cash on deposit.

Pro Tip

The value of an in-specie contribution will be the market value of that asset at the time of transferring the asset into the SMSF. If the asset transfer triggers a profit on the sale of the asset, the individual may have to pay tax on the capital gain.

Depending on the person's tax bill, if that person is self-employed, it may be possible to offset all or part of the CGT liability by making concessional (before-tax) superannuation contributions in the year that the CGT is incurred.

In order to make an in-specie transfer of investments from a member to an SMSF, the SMSF's trust deed must allow for such a transaction and the investments being transferred must meet the SMSF's investment strategy.

In-specie transfers can allow for a member to effectively retain an exposure to a specific investment held outside of superannuation whilst being able to fund a contribution:

Case Study

Marianne owns $10,000 worth of BHP shares which she would like to retain. Marianne would like to make a $10,000 non-concessional contribution to her SMSF but she doesn't have enough cash in her personal name to make the contributions. Her SMSF trust deed and investment strategy allow for in-specie transfers of listed shares.

Marianne can therefore arrange to make an in-specie transfer of her $10,000 BHP shares to her SMSF as a non-concessional contribution. She will be assessed for capital gains or a capital loss based on the market price on the date of transfer and the market value will represent the cost base of the shares for the SMSF. No brokerage fees would

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apply for the transfer as the BHP shares would not actually be bought and sold on the market. (off market transfer fees apply)

If Marianne was unable to make an in-specie transfer and she wanted to make the non-concessional contribution and retain her exposure to BHP, the alternative would be for her to sell the $10,000 BHP in her personal name, wait for the sales proceeds to settle into her bank account, then contribute the $10,000 cash amount to her SMSF, wait for the funds to clear in the SMSF bank account and then arrange to buy $10,000 worth of BHP. This process may take 1-2 weeks and brokerage would be incurred upon the initial sale (Marianne to pay brokerage) and the subsequent purchase of BHP shares (SMSF to pay the brokerage). Additionally, the price of BHP may have increased between the time of sale and the time of purchase, in which case the total number of BHP shares able to be bought by the SMSF would be less than the amount Marianne initially planned to transfer.

An SMSF cannot acquire an asset that has an existing charge or loan against it. This means that business real property would have to be unencumbered before it can be transferred to an SMSF. Business real property could therefore only be acquired by the SMSF if the property is currently owned outright, or the business owners have other financial resources to extinguish the debt before transferring ownership.

If a permissible asset is acquired from a related party the transaction must be at market value.

Case Study

Richard is a 59 year old business owner who wants to sell (transfer) his $400,000 business real property to his SMSF in exchange for cash. However, there is a $100,000 mortgage against the property. In order for Richard to transfer the property to his SMSF, the property must be unencumbered at the time of transfer. He therefore decides to do the following:

Repay the $100,000 property mortgage by sourcing $100,000 funds from a redraw facility (loan) linked to his personal home;

Obtain an independent valuation of the business real property from an appropriately qualified valuer;

He then makes an in-specie transfer of the business real property to his SMSF and the SMSF pays Richard $400,000 cash in exchange for the property.

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Richard uses $100,000 of his cash proceeds to repay his personal loan and pockets the residual $300,000.

Case Study

What if the SMSF doesn't have enough cash to buy the Business Real Property from the member?

Mario is a 58 year old business owner who wants to sell (transfer) his $500,000 business real property to his SMSF in exchange for cash. The Business Real Property is unencumbered. However, the SMSF only has $370,000 available cash to provide towards the property purchase from Mario. He therefore decides to do the following:

The SMSF commences a Bare Trust which receives the in-specie transfer of the $500,000 business real property from Mario.

The SMSF borrows $130,000 from a lender and secures the loan against the property in the Bare Trust.

The SMSF then uses this $130,000 and a further $370,000 available cash to pay Mario the required $500,000 funds in consideration of the property transfer.

Option 2

Borrowing costs can be expensive especially when they are relative to a small loan amount.

If Mario doesn't need the whole $500,000 in cash he could do a combination of part acquisition and part contribution. This is how it would work:

Mario makes an in-specie transfer of the business real property with a market value of $500,000 to his SMSF.

The SMSF pays Mario $370,000 which is the amount of cash available in exchange for the property.

The remaining $130,000 is recorded as a contribution against Mario's member account (provided that it does not exceed his allowable contribution caps).

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WHAT IS BUSINESS REAL PROPERTY?

The ATO issued ruling SMSFR 2009/1 in respect of business real property for the purposes of SISA.

To satisfy the definition of Business Real Property; the property must be used wholly and exclusively for business purposes.

The following examples of what does, and does not meet the definition of Business Real Property have been extracted from SMSFR 2009/1.The complete ruling with further examples can be accessed from the ATO website

Example 1: Primary production business with private residence

Lesley-Anne owns and operates a cattle farm of 40 hectares. She breeds cattle in a primary production business. Lesley-Anne lives on the property and has built a large home. She is also a keen gardener and maintains a large hedge maze and ornamental lake and garden. The total area of the property that she uses for private or domestic purposes is about 3 hectares.

Lesley -Anne is a member of the Jasper SMSF. She wants to sell the property to the trustee of the Jasper SMSF at market value.

Because Lesley-Anne uses more than 2 hectares for private and domestic purposes, the subsection 66(6) exception will not apply.

In this case, the non-business use of the property is not entirely incidental and relevant to the underlying primary production business, nor is it minor or trifling. Therefore, as the property is not used wholly and exclusively in a business, it is not business real property of Lesley-Anne. Any acquisition of the freehold interest in the land by the Jasper SMSF will contravene the related party asset acquisition rule in section 66.

Example 2: Mr Peters' poultry farm - unused paddocks

Mr Peters operates a poultry farm. His business is run from a property on which 4 large poultry sheds are constructed. The property also consists of 2 paddocks that are unused. Mr Peters sometimes considers building more poultry sheds on the unused land but is yet to pursue any definitive plans to this end.

Mr Peters is a member of the Nest Egg SMSF. Mr Peters wants to sell and lease back the property on which his poultry farm is located at market value to the Nest Egg SMSF.

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The property is business real property of Mr Peters. In this case, the property is used to an appreciable degree in the primary production business of Mr Peters. The property therefore satisfies the 'wholly and exclusively' threshold under the business use test. Accordingly, the farm can be sold at market value to Nest Egg SMSF without contravening the related party asset acquisition rule in section 66. The farm will not be an in-house asset of the Nest Egg SMSF when it is leased back to Mr Peters.

Example 3: Vacant land

Brendan and Millie own three blocks of land adjacent to each other. Their factory and retail outlet is located on one block, another block contains the car park for the business, and the third block is vacant.

Brendan and Millie want their SMSF to acquire the three blocks. They then want their business to lease back blocks one and two with the third block as an investment in the fund.

The first and second blocks are business real property as they are used wholly and exclusively in the business. The third block has no business use and is not business real property. Acquisition of the third block by the fund would contravene the related party asset acquisition rule in section 66.

Example 4: Motel with manager's residence

The Bruce family company owns and operates the Highway Motel. The company is a related party of the Bruce SMSF.

The trustee for the Bruce SMSF wants to purchase the motel.

The Bruce family company employs Nadia as the manager of the motel. Nadia lives on site and is expected to make all decisions in relation to the day to day management of the motel.

The real property on which the motel is located is used in a business. The fact that the manager's residence is part of the motel is incidental and relevant to that business. Additionally, the use of the property by the guests for non-business purposes does not cause the business use test to be failed as this use is clearly an inherent part of the business.

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The real property is therefore used wholly and exclusively in the motel business, making the company's interest in the land business real property. The proposed acquisition of the motel by the Bruce SMSF will not contravene the related party asset acquisition rule in section 66.

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Example 5: Bed and breakfast

Dean Lamont owns a house with 5 bedrooms and 2 living areas. He uses one of the bedrooms himself. The other four bedrooms are let year-round as part of a bed and breakfast business. One living area is set aside for the exclusive use of guests. Breakfast is included in the room cost and other meals are available by arrangement.

Dean advertises his rooms with Worldwide B&B Internet bookings agency. Dean has a business plan, pays tax, and has three permanent part time employees. The business has operated since Dean acquired the house 17 years ago.

I*n this case, a business is being carried on. Dean's non-business use of the property is incidental and relevant to that business. Accordingly, the property is used wholly and exclusively in the business and is business real property.*

Example 6: Doctor's surgery in residential premises

Dr Mary owns a house used exclusively by her medical practice.

Dr Mary is a member of the Yianni SMSF. Dr Mary, in her capacity as trustee of the SMSF, wants to acquire the house for market value and then lease it back so the medical practice can continue to operate from the house.

Although the house was built to be residential premises, it is not used as such. The real property is used wholly and exclusively in Dr Mary's medical practice business. For the purposes of the related party asset acquisition rule in section 66, the property is business real property of Dr Mary. Once acquired by the Yianni SMSF, it is also business real property of the fund and is therefore not an in-house asset of the SMSF.

WHAT ARE IN-HOUSE ASSETS?

The in-house asset rules are covered in Sections 69-71E of the SIS Act.

Generally speaking, an SMSF can invest no more than 5% of a fund’s assets in investments involving related parties, such as purchasing shares in a company owned by a fund member. Such investments are officially known as ‘in-house assets’. An in-house

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asset is a loan to, or an investment in, a related party or trust of the fund. An asset of the fund that is leased to a related party is also an in-house asset.

You are restricted from lending to, investing in or leasing to a related party of the fund more than 5% of the fund's total assets.

There are some exceptions, including business real property that is subject to a lease between the fund and a related party of the fund. Business real property relates to land and buildings used wholly and exclusively in a business, and can include offices, shops, factories and even farms. Often business owners buy their premises, and put the property into their SMSF. As it represents business real property, it circumvents the 5% in-house asset rule.

Follow the link to view the in-house asset video produced by the ATO.

https://www.ato.gov.au/Super/Self-managed-super-funds/Investing/Restrictions-on-investments/In-house-assets/

An in depth analysis of in-house assets is provided in the next section.

WHAT DOES THE TERM 'RELATED PARTY' MEAN?

A related party of an SMSF includes a member of the fund, a standard employer sponsor of the fund and an 'associate' of either a member or a standard employer sponsor of the fund (as defined below).

What does the term 'associate' mean?

An associate of an individual includes a 'relative' of the individual (as defined earlier in this module), other members, trustees and directors of a corporate trustee of the SMSF if the individual is a member of an SMSF, a partner of the individual in a partnership, the spouse and children of an individual who is a partner of a trustee, a trustee of a trust where the person controls the trust and companies that are sufficiently influenced by, or in which a majority voting interest is held by, the individual and/or the individual's associate(s).

An associate of a company includes partners of the company , partnerships in which the company is a partner, spouses and children of an individual who is a partner of the trustee, a trustee of a trust controlled by the company, a controlling entity which sufficiently influences the company or holds a majority voting interest in the company,

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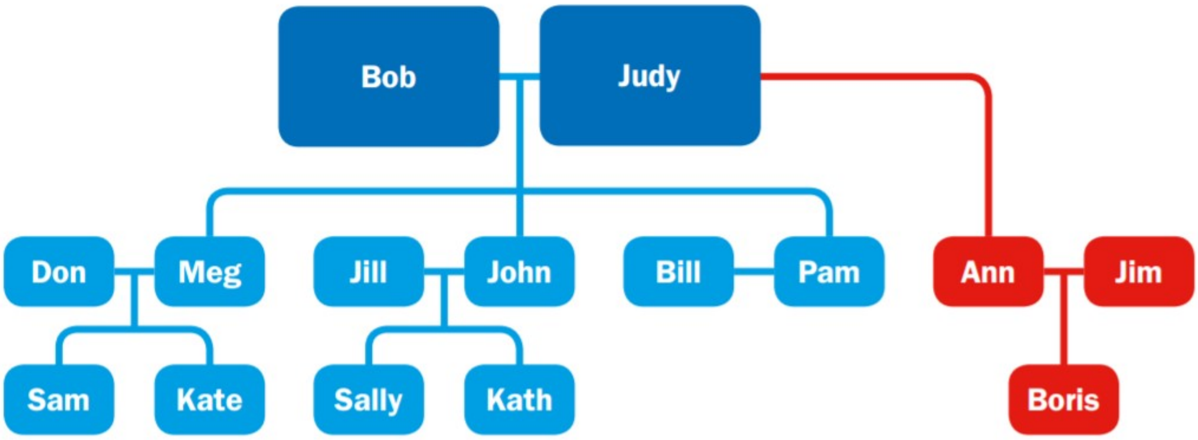
associates of a controlling entity and another controlled company which the other company or an associate sufficiently influences or holds a majority interest.

Related Party Analysis

A detailed analysis may be required to determine if the SMSF is dealing with a 'related party'. Here are some case studies from Colonial First State which show how detailed this process can be.

Case Study- Related party relatives

Bob and Judy are married and have three children, Meg, John and Pam. Judy also has a daughter, Ann, from a previous relationship. All of Bob and Judy's children, including Ann, are in relationships and Meg, John and Ann also have children of their own. Bob and Judy's family tree is outlined as follows:



If Bob had his own single member SMSF (without Judy), the following people would be defined as a relative of Bob and therefore a related party of his fund:

- Judy – as she is Bob's spouse
- Meg, John and Pam – as they are lineal descendants of Bob
- Don, Jill and Bill – as they are the spouses of Bob's lineal descendants
- Ann – because she is a lineal descendant of Bob's spouse
- Jim – because he is the spouse of the lineal descendant of Bob's spouse
- Sam, Kate, Sally and Kath – because they are lineal descendants of Bob
- Boris – because he is the lineal descendant of Bob's spouse.

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Case Study- Related party companies

A company will be a related party of an SMSF where:

• the company is sufficiently influenced by a member or an associate of a member, or

• a member or their associate holds a majority voting interest in the company

Referring back to our family tree – Assume Bob has part ownership of a private company through which a business is operated.

The distribution of the voting shares of the company is as follows:

• Bob – 1 share

• Don (Bob's son-in-law) – 1 share

• Company X (as trustees of the J&J Unit Trust) – 3 shares.

Bob's son and daughter-in-law, John and Jill, are the sole directors of Company X, that acts as the trustee of the unit trust. John and Jill hold 100% of the units (50% each) in the unit trust.

So, the private company would be a related party of Bob's SMSF, as Bob and his associates (Don as well as Company X) between them hold 100% of the voting shares – which exceeds the 50% control test.

Follow the link to view the related party video produced by the ATO.

https://www.ato.gov.au/super/self-managed-super-funds/in-detail/smsf-resources/smsf-videos/?page=11#SMSF___related_party_transactions

ANALYSIS OF IN-HOUSE ASSETS

In respect of an SMSF, the in-house asset rule is one of the more difficult concepts to understand.

We need to look at in-house assets from 3 perspectives:

- Acquiring an in-house asset from a related party of the fund;
- Investing into an in-house asset; and
- Existing fund assets which may give rise to an in-house asset

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In order to analyse the in-house asset rule in detail we first need to understand the rules around collectables and personal use assets.

Collectibles and personal use assets (source: www.ato.gov.au)

Collectables and personal use assets are things like artworks, jewellery, vehicles, boats and wine. Investments in such items must be made for genuine retirement purposes, not to provide any present-day benefit. So collectables and personal use assets can't be:

- leased to, or part of a lease arrangement with, a related party
- used by a related party
- stored or displayed in a private residence of a related party.

In addition:

Your investment must comply with all other relevant investment restrictions, including the sole purpose test. The decision on where the item is stored must be documented (for example, in the minutes of a meeting of trustees) and the written record kept.

The item must be insured in the fund's name within seven days of the fund acquiring it.

If the item is transferred to a related party, this must be at market price as determined by a qualified, independent valuer.

For collectables and personal use assets that you held before 1 July 2011 you have until 30 June 2016 to comply with these rules.

Definition of collectables and personal use assets

Collectables and personal use assets are:

- artwork – including paintings, sculptures, drawings, engravings and photographs
- jewellery
- antiques
- artefacts
- coins, medallions or bank notes
- coins and banknotes are collectables if their value exceeds their face value

  Bullion coins are collectables if their value exceeds their face value and they are traded at a price above the spot price of their metal content

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- postage stamps or first-day covers
- rare folios, manuscripts or books
- memorabilia
- wine or spirits
- motor vehicles and motorcycles
- recreational boats
- memberships of sporting or social clubs.

Now that we understand the definition of a collectable and personal use asset, we are better able to explore each part of the in-house asset rules.

Definition of an In-House Asset (IHA)

Extract from: SUPERANNUATION INDUSTRY (SUPERVISION) ACT 1993 - SECT 71

………. an in-house asset of a superannuation fund is an asset of the fund that is a loan to, or an investment in, a related party of the fund, an investment in a related trust of the fund, or an asset of the fund subject to a lease or lease arrangement between a trustee of the fund and a related party of the fund……………………

The total amount of in-house assets must not exceed 5% of the total asset value of the fund.

The value of in-house assets must be reviewed each financial year, using current market values.

For example, if the total fund value decreases there is a risk that the value of the IHA investments may increase above the allowable 5%, relative to the new fund value.

Case Study

Jenny and Carl are members and trustees of the J & C Super Fund which is an SMSF. The market value of the fund's total assets in Year 1 was $1,000,000.

Jenny and Carl have a small haberdashery business called – Bows and Buttons Pty Ltd. The shares in Bows and Buttons Pty Ltd are owned by Jenny and Carl (50% each). So Bows and Buttons Pty Ltd is a related party of both members of the J & C Super Fund.

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The J & C Super Fund holds the following investments:

FUND ASSETS	Market Value Year 1	Market Value Year 2
ASX listed share portfolio	$200,000	$150,000
Business Real Property	$500,000	$500,000
Investment in Bows and Buttons Pty Ltd	$50,000	$55,000
ANZ Bank term Deposit	$150,000	$150,000
ABC Managed Fund	$100,000	$90,000
TOTAL FUND VALUE	$1,000,000	$945,000

In Year 1 the percentage of in-house assets was 5% ($50,000/$1,000,000).

In Year 2, the share market has fallen, resulting in a decrease in the investments in the managed funds and the share portfolio.

Conversely, the haberdashery business is booming and the value of the investment has increased. Hence, the in-house assets now make up 5.82% of the fund. ($55,000/$945,000).

The value of the IHA now exceeds the allowable 5% so to restore the correct balance the SMSF may:

Option 1:

Sell $7,750 of the investment in Bows and Buttons Pty Ltd. This will reduce the in-house asset value to $47,250 which will equal 5% of the total fund value. ($47,250/$945,000).

Option 2:

Make an additional contribution to the fund in the amount of $155,000. This will increase the capital of the fund and restore the IHA value to 5% ($55,000/$1,100,000). Even though the percentage has only moved from 5% to 5.82%, this amount may be prohibitive for the members of the fund which makes this the least viable option in this scenario.

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So what constitutes an in-house asset?

In order to fully understand how the IHA rules operate in respect of the investment choices for an SMSF, we need to break it down and look at each section.

"A loan to a related party of the fund"

It must first be noted that under s.65 of SISA, the general prohibition states that an SMSF must not loan money to a member of the Fund or to a relative of the member of the Fund.

Therefore, this follows that an SMSF can loan money to a related party of the fund as long as the related party is neither a member of the SMSF or a relative of the member.

So, loans to a related party company or a related party trust are allowed.

"An investment in, a related party of the fund, or an investment in a related trust of the fund"

An SMSF is permitted to invest into a related party company or a related party trust as illustrated in the following case study:-

Case Study: Ben and Jasmine

Ben and Jasmine are members and trustees of the B & J Super Fund which is an SMSF. The current market value of the fund's total assets is $500,000, which includes $80,000 in cash.

Ben and Jasmine have a small bakery business called Jasmine's Fine Foods Pty Ltd. Ben and Jasmine would like to buy shares in Jasmine's Fine Foods Pty Ltd using the cash held by the SMSF.

The shares in Jasmine's Fine Foods Pty Ltd are owned by Ben and Jasmine (50% each). So Jasmine's Fine Foods Pty Ltd would be a related party of both members of the B & J Super Fund.

Therefore, an investment by the B & J Super Fund in Jasmine's Fine Foods Pty Ltd would be an in-house asset. As long as the fund does not have any other in-house assets, the maximum amount that the B & J Super Fund can use to purchase shares in Jasmine's Fine Foods Pty Ltd is 5% of $500 000, i.e. $25,000.

"An asset of the fund subject to a lease or lease arrangement between a trustee of the fund and a related party of the fund"

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Firstly we must note that "Business Real Property" is not considered to be an in-house asset.

The general prohibition under Section 66 of SISA restricts an SMSF from intentionally acquiring an asset from a related party of the fund, unless it is one of the exceptions. Business Real Property can not only be "acquired" from a related party, but it can also be leased to a related party regardless of the value, without breaching the in-house asset rule.

Subject to the 5% restriction (across all in-house assets) an asset of the SMSF may be leased to a related party of the fund (if it satisfies all the criteria). The arrangement must be at market rates, in consideration of s.109 of SISA which refers to the arm's length rule. This rule states that the investment must be entered into and maintained on commercial terms. So the lease agreement must reflect true market rates.

Secondly, we must consider the rules around collectables and personal use assets.

As collectibles and personal use assets cannot be leased to, or part of a lease arrangement with a related party; assets such as artworks, antiques and motor vehicles are not investments that would be acquired from; invested in; or leased to a related party of the SMSF.

That is, they are not on the list of exceptions which can be acquired from a related party, nor do they satisfy the definition of an IHA (even if the value is less than 5% of the fund value).

What about an existing asset which may give rise to an in-house asset?

Consider the following scenario which is often raised when discussing the IHA rules:-

Scenario:

An SMSF has invested into a beachside property. The property was purchased in the open market from a "non-related" party. The market value of the property is $350,000.

The total value of the fund assets is $2,000,000.

If a related party of the fund wishes to rent the property over the Christmas break, and they agree to pay market rates (thus satisfying the arm's length rule), is it OK for them to stay in the beach house?

The short answer is **"NO"**, but let's break it down.

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OK, so you have satisfied the arm's length rule by paying rent at the market rate, but you must also consider the in-house asset test.

By renting the property, this action has effectively resulted in a lease arrangement between the SMSF and a related party of the fund, involving an asset of the fund.

This gives rise to the property becoming an in-house asset, so the value of that asset must be considered.

The $350,000 house represents 17.5% of the total fund assets ($350,000/$2,000,000) which is in breach of the allowable 5%.

So it is possible, but in practice it would be very difficult to achieve. In the above scenario, in order to avoid breaching the in-house asset rule, the SMSF would need to have a total $7,000,000 in assets.

Every asset must also satisfy the sole purpose test which is to provide retirement benefits.

The attached case from dbalawyers.com.au is worth a read. It refers to a court case and involves the sole purpose test and the arm's length test.

http://www.dbalawyers.com.au/ato/smsf-penalties-sole-purpose-test-illuminated-federal-court/

Follow the link to view the in-house assets video produced by the ATO.

https://www.ato.gov.au/super/self-managed-super-funds/in-detail/smsf-resources/smsf-videos/?anchor=Inhouseassets#Inhouseassets

SMSF INVESTMENTS

According to the super rules, investments by SMSFs must be made and maintained on a strict commercial basis. A fund trustee must obtain an independent valuation report to determine market value before purchasing the asset for the super fund. There must be a written contract in place and the purchase or sale price of SMSF assets must reflect true market value. A good example is when an SMSF purchases residential property. While an SMSF cannot purchase a residential property for investment purposes from members (if it comprises more than 5% of the portfolio – i.e. the in-house asset rule), the

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residential property can comprise more than 5% if it is purchased at public auction or in a private sale from a non-related party.

Of course members could never live in the property, or rent it out to themselves because this would breach the sole purpose test. AN SMSF can purchase many assets outside the 'traditional' assets of cash, fixed interest, property and shares – this includes investments in gold, antiques, art, vintage cars, and wine. Note, however the ATO has a strong focus on ensuring that any asset purchased by an SMSF doesn't breach the sole purpose test. Art for example must be properly stored and cannot be hung up in a member's house as this would constitute a breach of the sole purpose test.

11.6 CAN MEMBERS PURCHASE FUND ASSETS FROM AN SMSF?

Fund members/trustees can purchase assets owned by the SMSF. This means an SMSF can pay out cash benefits or transfer assets to members that are non-cash such as shares (in-specie) and any property (not just business real property).

If the SMSF makes a profit on the sale of an asset and the SMSF is in the accumulation phase, or transition to retirement phase, then the fund will have to pay CGT on that gain. If the SMSF is in the retirement income stream phase, tax is not payable on fund earnings, including capital gains.

ARM'S LENGTH AND NON-ARM'S LENGTH TRANSACTIONS

To comply with regulations, all transactions between an SMSF and a non-arm's length party (e.g. relative) must be at arm's length (i.e. market value) to maintain compliance and to receive the standard superannuation tax concessions.

If a transaction such as a lease or asset sale between the SMSF and non-arm's length party is not at commercial market rates, the transaction or agreement would be treated as being non-arm's length and the SMSF may become non-complying. If the arrangement is at a rate which effectively provides higher than market rate of funds to the SMSF, the additional amount may be treated as a contribution and subject to

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contributions limits (for example, selling assets from the member to the SMSF at a higher than market rate).

If the SMSF derives income which is above the market rate (e.g. from private company dividends), the non-arm's length income will be taxed at the rate of 47% and franking credits cannot be used to reduce any tax on the non-arm's length income. Other income of the fund will continue to be taxed at standard rates of 15%.

The following example from Tax Ruling 2006/7 illustrates a case where dividends are treated as special income (that is, non arms-length income).

Example

This example considers the relevance of paying full market value in the acquisition of shares in a company when determining whether dividends are special income.

The facts

On 1 June 2001 a self-managed superannuation fund, the Toby Superannuation Fund, acquires 100,000 shares for 50 cents each in a private company, Extension Products Pty Ltd. The Toby Superannuation Fund pays a total of $50,000. At the time of the acquisition of the shares, the market value of one share in Extension Products Pty Ltd is $1.00. Also on 1 June 2001 nine other entities acquire 100,000 shares each in Extension Products Pty Ltd. The nine other entities pay $1.00 for each share, paying a total of $100,000 each. The members of the Toby Superannuation Fund are related to the directors and the other shareholders.

On 1 June 2003 Extension Products Pty Ltd pays dividends on all of its shares at the rate of 5 cents per share. All ten shareholders are paid a dividend of $5,000. In the following year no dividends are paid on the shares. On 1 June 2005 Extension Products Pty Ltd pays dividends on all of its shares at the rate of 5 cents per share. All shareholders are paid a dividend of $5,000.

Consideration of the matters under subsection 273(2)

The rate of dividend paid on 1 June 2003 and on 1 June 2005 is the same rate for all of the shareholders.

The cost to the Toby Superannuation Fund of the shares in Extension Products Pty Ltd is 50 cents for each share. The market value of the shares at the time of acquisition is $1.00 per share. The cost of the shares is less than the market value of the shares.

The relationship between the Toby Superannuation Fund and Extension Products Pty Ltd appears not to be at arm's length and the result of their dealing is not consistent with an arm's length outcome.

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The decision

On the whole, having regard to the matters listed in paragraphs 273(2) (a) to (f), including the fact that the parties are related, the Commissioner is not of the opinion that it would be reasonable to exercise his discretion. The dividends paid on 1 June 2003 and on 1 June 2005 to the Toby Superannuation Fund are not consistent with an arm's length outcome and will therefore be special income under subsection 273(2). In the absence of other factors, if full market value had been paid for the shares, the Commissioner would have exercised his discretion not to treat the dividend as special income.

11.7 BORROWING WITHIN AN SMSF

There are strict rules associated with borrowing within an SMSF.

Section 67 of SISA states:

“The trustees of the fund must not borrow any money or maintain an existing borrowing (not listed as an exemption).

Section 67A-67B of SISA then goes on to explain the provisions for borrowing under Limited-recourse borrowing arrangements (LRBA).

The ATO issued a ruling in respect of the borrowing provisions, SMSFR 2012/1. This is a final ruling which provides clarity around the following key concepts of the legislation:

- what constitutes a ‘single acquirable asset’
- the distinction between ‘maintaining’ or ‘repairing’ the acquirable asset compared to ‘improving’ it
- when a single acquirable asset is changed to the extent that it becomes a different asset

The following examples are extracts from SMSFR 2012/1 issued by the ATO:

<u>**SINGLE ACQUIRABLE ASSET**</u>

Example 1 - two adjacent blocks of land

As part of the investment strategy of an SMSF, the trustees of the SMSF want to acquire two adjacent blocks of land under a single LRBA. While the vendor will only sell the two

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blocks together, there are no physical or legal impediments to the two blocks of land being sold separately.

The two blocks of land are not a single acquirable asset. As a result, the two blocks of land cannot be acquired under a single LRBA. However, the blocks of land could be acquired under separate LRBAs.

Example 2 - a factory complex on more than one title

A trustee of an SMSF wants to enter into an LRBA to acquire a factory which is constructed across three titles. The existence of the factory adds considerably to the value of the land and thus is a significant part of the value of the asset. The factory is therefore relevant as a unifying physical object.

The factory and the land comprised of the three titles, is a single acquirable asset and can be acquired under a single LRBA.

However, if the factory was derelict and thus not of significant value relative to the land this asset could not be acquired under a LRBA as the factory is not relevant as a unifying physical object and thus the assets are the three titles .

Example 3 - apartment with separate car park

The trustee of an SMSF wants to enter into an LRBA to purchase an apartment with a separate car park on the same strata plan that contains a notice of restriction. The apartment and car park are each on a separate legal title. As the strata plan contains a notice of restriction, if the car park and apartment are not transferred together the transfer of title of the apartment cannot be registered according to the relevant law of the State.

As the two titles must both be transferred if the transfer of title of the apartment is to be registered, this effectively means that the two assets must be dealt with together under a law of the State. In these circumstances the apartment and car park comprise a single acquirable asset that may be acquired under a single LRBA.

Example 4 - serviced apartment and furnishings

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The trustees of an SMSF want to enter into an LRBA to purchase a serviced apartment that will be leased to a provider of short-term residential accommodation. The purchaser of the apartment is required by the vendor to also purchase a furnishings package.

The apartment without the furnishings package is a single acquirable asset and its acquisition could be funded under an LRBA. However, the apartment and the furnishings package, even if purchased together under the one contract, is not a single acquirable asset. The furnishings package, even if purchased under a separate contract, is still not a single acquirable asset as it would include multiple items.

Example 5 - purchase of residential premises

The trustees of an SMSF want to acquire land that has an existing residential house on it. A deposit is paid to the vendor on signing the contract to acquire that land with the house. The balance of the purchase price is paid at settlement 60 days later. The relevant asset acquired is the land along with the existing house.

The land with the existing house is a single acquirable asset and the deposit and the payment at settlement is applied for the acquisition of that asset. The trustees of the SMSF can enter into a single LRBA to fund both payments.

Example 6 - completed 'off-the-plan' apartment.

The trustees of an SMSF enter into a contract to purchase a strata titled apartment 'off-the-plan'. A deposit is required upon entering into the contract with the balance to be paid upon settlement for the completed strata titled apartment.

A single LRBA can be entered into to fund both the deposit and the balance to be paid under the contract upon settlement. Both the deposit and the settlement payment are applied for the acquisition of a single acquirable asset being the completed strata titled apartment.

MAINTAINING, REPAIRING OR IMPROVING THE ACQUIRABLE ASSET

Subparagraph 67A (1) (a)(i) provides that borrowings under an LRBA cannot be used to fund improvements. However, money from other sources can be used to improve (or

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repair or maintain) a single acquirable asset. For example, accumulated funds held by the SMSF may be used to fund the improvements. However, any improvements must not result in the acquirable asset becoming a different asset.

Example 1

Repair or Maintenance

A fire damages part of the kitchen (cooktop, benches, walls and ceiling).
Restoration (replacement) of the damaged part of the kitchen with modern equivalent materials or appliances would constitute repair or restoration of a part of the entire asset being the house and land.
If superior materials or appliances are used it is a question of degree as to whether the changes significantly improve the state or function of the asset as a whole.
For example, the addition of a dishwasher would not amount to an improvement, even if a dishwasher was not previously part of the kitchen, on the basis that this is a minor or trifling improvement to the state or function of the asset as a whole

Improvement

If the house was extended to increase the size of the kitchen this would be an improvement.
If as well as restoring the damaged part of the internal kitchen (a repair) a new external kitchen was added to the entertainment area of the house the external kitchen would be an improvement.

Example 2

Repair or Maintenance

- The guttering on the house is replaced with the modern equivalent and the house is repainted. If in replacing the guttering a leaf guard is also fitted this would not amount to an improvement on the basis that this is a minor or trifling addition to the entire asset being the house and land.
- A fence is replaced using modern equivalent materials. If part of replacing the fence also included the addition of a gate to provide another access point, this would not be regarded as an improvement on the basis that this is a minor or trifling addition to the entire asset being the house and land.

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- A fire alarm is installed to comply with new requirements of the local council. This would not be regarded as an improvement on the basis that this is a minor or trifling addition to the entire asset being the house and land.

Improvement

- A pergola is built to create an outdoor entertaining area.
- The addition of a swimming pool or a garage.
- An integrated home automation system is installed including electronically controlled lighting, multi room audio-visual distribution and security system.
- A house extension to add a further bathroom.

Example 3

Repair or Maintenance

A cyclone damages the roof of the house. Replacement of the roof in its entirety with the modern equivalent is a repair as it is restoring the asset to what it was.
If superior materials are used it is a question of degree as to whether the changes significantly improve the state or function of the asset as a whole.

Improvement

The addition of a second storey to the house at the time of also replacing the roof would be an improvement.

Example 4

Repair or Maintenance

A fire destroys a three bedroom residential house. Rebuilding a broadly comparable house is not an improvement as it restores the asset to what it was before the fire.
If superior materials, fittings or appliances are used it is a question of degree as to whether the changes significantly improve the state or function of the asset as a whole.

Improvement

Rebuilding a residential house that is not broadly comparable to that destroyed is an improvement.
However, if the funds to rebuild are from an insurance company and not from borrowings this does not affect the LRBA.

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Example 5

Repair or Maintenance

A residential house is acquired under an LRBA and is rented out for a number of years. As the area is now a real estate hot spot a decision is taken to renew the kitchen which, although functional, is significantly out of date and showing wear and tear.

The design of the kitchen is improved and modern equivalent, rather than superior, materials and appliances are used.

The changes made do not significantly improve the state or function of the asset as a whole.

Improvement

A residential house is acquired under an LRBA and is rented out for a number of years. As the area is now a real estate hot spot a decision is taken to demolish the house.

Rebuilding a residential house that is not broadly comparable to that demolished is an improvement.
However, if the funds to rebuild are not from borrowings this does not affect the LRBA.

WHETHER IT IS A DIFFERENT ASSET

The single acquirable asset identified when the LRBA is put in place must continue to be the asset that is held on trust under that LRBA, unless its replacement is covered by section 67B.

The following examples illustrate whether a change to a single acquirable asset results in a different asset(s).

Example 1

Single acquirable asset

Vacant block of land on single title

Whether it is a different asset

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A vacant block of land is subsequently subdivided resulting in multiple titles. One asset has been replaced by several different assets as a result of the subdivision.

Example 2

Single acquirable asset

Vacant block of land on single title

Whether it is a different asset

A residential house is built on vacant land which is on a single title. The character of the asset has fundamentally changed from vacant land to residential premises. This is a different asset.

Example 3

Single acquirable asset

Residential house and land

Whether it is a different asset

While each of the following changes would be improvements each (or all) of the changes would not result in a different asset:

- an extension to add two bedrooms;
- the addition of a swimming pool;
- an extension consisting of an outdoor entertainment area;
- the addition of a garage shed and driveway;
- the addition of a garden shed.

Example 4

Single acquirable asset

Residential house and land

Whether it is a different asset

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A 'granny flat' is to be constructed in the backyard of a property which already has a four bedroom residence established on it. The granny flat will have two bedrooms, a family room, a kitchen and a bathroom and will be connected to utilities such as electricity, water and sewage.
The character of the asset would remain residential premises and thus the construction of the granny flat would not result in there being a different asset.

Example 5

Single acquirable asset

Residential house and land

Whether it is a different asset

A house is demolished following a fire and is replaced by three strata titled units. The character of the asset has fundamentally changed along with the underlying proprietary rights. This has created three different assets.

NOTE: You can access the full SMSFR 2012/1 ruling on the ATO website.

Further to the above provisions:

- The asset acquired with borrowed funds must be held in trust with the SMSF having a beneficial interest and a right, but not an obligation, to acquire the legal ownership of the asset, or any replacement, through the payment of further instalments;
- Security can only be given over the asset being bought and in the event that the value of the property falls below the loan value, the lender will not have recourse to any other assets of the SMSF (i.e. the loan will be a Limited Recourse Borrowing Arrangement);
- Other assets of the Super Fund cannot be used as security, so as to ensure that other assets of the fund are not at risk.

A separate trust (called a Bare Trust) needs to be created to hold the asset to be acquired as a result of the borrowing where the super fund is the beneficial owner. The Bare Trust has no purpose other than to hold the asset for the SMSF until such time as the loan has been repaid and the title then transfers from the Bare Trust to the SMSF.

The lender can use the asset held by the Bare Trust as security for the borrowing.

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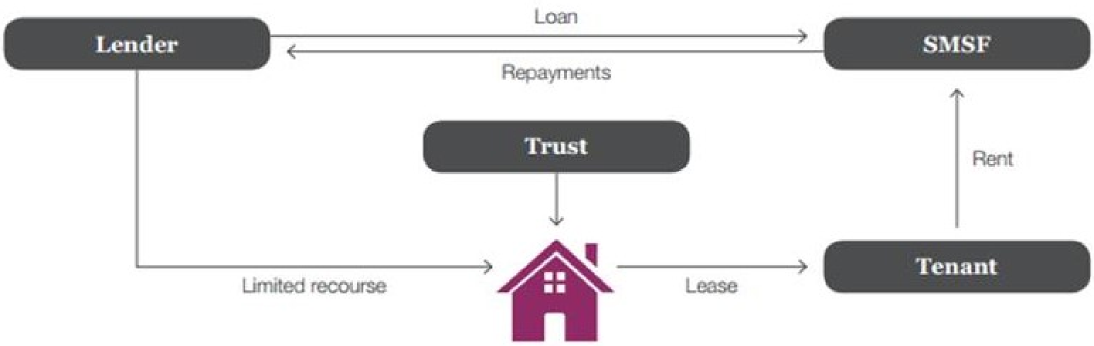
The super fund borrows the money and collects any revenue generated by the asset (i.e. rent or dividends).There is a very specific way in which the trust and loan arrangements need to be undertaken in order to qualify under the superannuation rules.

The following diagram from Strategy Steps summarises the parties involved in the Limited Recourse Borrowing Arrangement:



When the loan is eventually paid off, ownership of the asset is transferred back to the Super Fund. There is no further stamp duty or capital gains tax event at this time as the super fund was always the beneficial owner of the asset.

When a Limited Recourse Borrowing Arrangement has been repaid, the property must either be transferred from the Bare Trust to the SMSF as soon as practicable or the SMSF trustee could arrange for the property to be sold to a third party. Otherwise, the SMSF may be faced with an in-house assets test issue, as described below.

When a property is part of a Limited Recourse Borrowing Arrangement, the Bare Trust which holds the property will not be treated as a related trust and the value of the property will not count for the purposes of the in-house asset rules.

However, if the property remains in the Bare Trust with no remaining loan, it will no longer be considered to be part of the Limited Recourse Borrowing Arrangement. Without the LRBA exemption, the Bare Trust will then become a 'related party' trust and the value of the property will be counted for the purposes of the 5% in-house assets holding rule.

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If the market value of the in-house assets at the next balance date exceeds 5% of the total market value of all SMSF assets, the trustee must prepare a plan by which the excess amount of in-house assets (i.e. amount over 5%) will be reduced by way of asset divestment. The plan must be prepared within 12 months of the balance date and must be implemented.

Here is a great you tube video on borrowing, from evolve my super:

https://www.youtube.com/watch?v=EB32_1RSXfg

BESIDES A LIMITED RECOURSE BORROWING ARRANGEMENT, CAN AN SMSF BORROW UNDER ANY OTHER CIRCUMSTANCES?

In addition to limited recourse borrowing arrangements, SMSFs may also borrow under the following conditions:

- To pay a beneficiary if the SMSF would otherwise be unable to make the required payment, provided that the payment is required by law or under governing rules of the fund. The borrowing period must be for a maximum of 90 days and the amount of borrowing must not exceed 10% of the market value of the SMSF.
- To cover settlement transactions for up to 7 days if the trustees did not expect there be a need to borrow at the time of the transaction. The amount of borrowing must not exceed 10% of the market value of the SMSF.

PROPERTY INVESTMENTS USING BORROWED FUNDS

Case Study

Aneka and Darcy wish to acquire a commercial property as an investment for the A & D Superannuation Fund. They do not have sufficient cash for the purchase so will arrange a **limited recourse loan.** The SMSF takes out the loan and contributes cash to pay the deposit for the property, meet the legal costs and pay stamp duty. The property is held in the Bare Trust and the SMSF then manages the property in the same way as any other real estate investment. The borrowing is a **limited recourse loan** which means that the

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newly acquired property is the only asset that can be used as security. In the event of loan default, the lender and any other person's rights are limited to that asset. No claim can be made on any other assets of the A & D Superannuation Fund.

Assets such as property can be leased from an SMSF on commercial terms. Rental payments, superannuation contributions (e.g. SGC and salary sacrifice) and other income enable an SMSF to meet loan repayments and expenses associated with the property. All income and expenses are received and paid by the fund not the Custodial Trustee (Bare Trust) holding the asset. For a commercial property, the tenant can be a related party or an unrelated party under lease. For a residential property, the tenant must be an unrelated party.

When the loan is repaid, legal ownership of the property is transferred from the Bare Trust to the SMSF.

WHO IS THE LENDER TO THE SMSF?

Superannuation law allows for the lender to be any one who can ordinarily lend money. Many financial institutions now have SMSF loan products available. Members and others can also lend money to an SMSF on an arms-length basis.

NON-BANK LENDERS

When entering into an LRBA with a non-bank lender important consideration must be given to the 'arms-length' rule.

Section 109 of SISA states that:

'All investment transactions must be made and maintained at arm's-length – that is, purchase, sale price and income from an asset reflects a true market value/rate of return.'

To this end, income that does not reflect dealing at arm's-length will be considered to be 'non arms-length income', which is taxed at 47% (2017-2018) regardless of whether the fund is in accumulation or pension mode.

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In the past the ATO has issued a number of interpretative decisions (ATO ID….) as well as NTLG minutes around the issue of interest free or low interest loans to SMSF trustees.

There was a stage where a low or no interest loan was considered *not* to be non arms-length; however it is now apparent that the ATO considers this arrangement (interest free or low interest loan) to be in breach of S109.

So, if the terms of an LRBA are not consistent with dealing at arm's-length, the income generated from the asset within this structure may be subject to the highest MTR.

The ATO has now issued some Practical Compliance Guidelines (PCG 2016/5) which sets out the safe harbour terms which are consistent with an arms-length dealing.

Here is an outline of the safe harbour terms in simplified terms from the *DBA Lawyers SMSF newsfeed dated 06/04/2016*.

Type of asset being acquired	**Real property (any kind)**	**Listed securities**
Interest rate	RBA Indicator Rates for banks providing standard variable housing loans for investors (5.75% for 2015 – 2016)	Same as real property + 2%
Term of loan	15 years for original loan (any refinancing will be reduced by duration of the previous loan(s))	7 years for original loan (any refinancing will be reduced by duration of the previous loan(s))
Maximum LVR	70%	50%
Security	A registered mortgage	A registered charge/mortgage or similar security (that provides security for loans for such assets)
Personal guarantee	Not required	Not required
Nature and frequency of	Monthly repayments on a 'principal and interest' basis	Same as real property

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payments		
Loan agreements	Written and executed	Written and executed

From a compliance perspective the ATO requires all existing LRBAs to be on terms consistent with an arms-length dealing by 30 June 2016.

The following examples from *Practical Compliance Guidelines (PCG 2016/5)* give guidance on applying the safe harbour.

Example 1 - Real Property

A complying SMSF borrowed money under an LRBA on terms consistent with section 67A of the SISA. It used the funds to acquire commercial property valued at $500,000 on 1 July 2011.

The borrower is the SMSF trustee.

The lender is an SMSF member's father (a related party).

A holding trust has been established, and the holding trust trustee is the legal owner of the property until the borrowing is repaid.

The loan has the following features:

- The total amount borrowed is $500,000.
- The SMSF met all the costs associated with purchasing the property from existing fund assets.
- The loan is interest free.
- The principal is repayable at the end of the term of the loan, but may be repaid earlier if the SMSF chooses to do so.
- The term of the loan is 25 years.
- The lender's recourse against the SMSF is limited to the rights relating to the property held in the holding trust, and
- The loan agreement is in writing.

At 1 July 2015, the property was valued at $643,000.

The SMSF has not repaid any of the principal since the loan commenced.

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The income earned from the property, which is rented to an unrelated party, gives rise to non arms-length income. To avoid having to report non arms-length income for the 2015-16 year (and prior years) the Fund has a number of options.

Option 1 - Alter the terms of the loan to meet guidelines

To bring the terms of the loan into line with Safe Harbour 1, the trustees of the SMSF must ensure that: ·

The 70% LVR is met (in this case, the value of the property at 1 July 2015 may be used). Based on a property valuation of $643,000 at 1 July 2015, the maximum the SMSF can borrow is $450,100. The SMSF needs to repay $49,900 of principal as soon as practical before 30 June 2016.

·

The loan term cannot exceed 11 years from 1 July 2015. The SMSF must recognise that the loan commenced 4 years earlier. An additional 11 years would not exceed the maximum 15 year term.

·

The SMSF can use a variable interest rate. Alternatively, it can alter the terms of the loan to use a fixed rate of interest for a period that ensures the total period for which the rate of interest is fixed does not exceed 5 years. The loan must convert to a variable interest rate loan at the end of the nominated period.

·

The interest rate of 5.75% p.a. applies from 1 July 2015 to 30 June 2016. The SMSF trustee must determine and pay the appropriate amount of principal and interest payable for the year. This calculation must take the opening balance of $500,000, the remaining term of 11 years, and the timing of the $49,900 capital repayment, into account.

After 1 July 2016, the new LRBA must continue under terms complying with the ATO's guidelines relating to real property at all times. For example, the SMSF must ensure that it updates the interest rate used for the loan on 1 July each year (if variable) or as appropriate (if fixed), and make monthly principal and interest repayments accordingly.

Option 2 - Refinance through a commercial lender

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Option 3 - Pay out the LRBA

Example 2 - collection of listed shares

A complying SMSF borrowed money under an LRBA on terms consistent with section 67A of the SISA. It used the funds to acquire a collection of stock exchange listed shares valued at $100,000 on 1 July 2011.

The borrower is the SMSF trustee.

The lender is an SMSF member (a related party).

A holding trust has been established, and the holding trust trustee is the legal owner of the collection of shares until the borrowing is repaid.

The loan has the following features:

- The total amount borrowed is $80,000·
- The SMSF met all the costs associated with purchasing the shares, and provided $20,000 from existing fund assets towards the purchase price.
- Interest was payable, but only at a fixed rate of 2% p.a. for the entire term of the loan.
- The principal is repayable at the end of the term of the loan, but may be repaid earlier if the SMSF chooses to do so.
- The term of the loan is for 10 years.
- The lender's recourse against the SMSF is limited to the rights relating to the collection of shares held in the Holding Trust, and
- The loan agreement is in writing.

The dividend income earned from these shares gives rise to non arms-length income.

Option 1 - Alter the terms of the loan to meet guidelines

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The SMSF and the related party could alter the terms of the loan to comply with Safe Harbour 2, for a collection of stock exchange listed shares.

To bring the terms of the loan into line with Safe Harbour 2, the trustees of the SMFS must ensure that:

- The 50% LVR is met (in this case the value of the collection of shares at 1 July 2015 may be used). Based on a market valuation of $120,000 at 1 July 2015, the maximum the SMSF can borrow is $60,000. The SMSF needs to repay $20,000 of principal as soon as practical before 30 June 2016.
- The loan term cannot exceed 3 years from 1 July 2015. The SMSF must recognise that the loan commenced four years earlier. An additional three years would not exceed the maximum 7 year term.
- The interest rate must be a variable interest rate, as the loan has already been fixed for 4 years from when it commenced (that is, 1 July 2011).

The interest rate of 7.75% p.a. applies from 1 July 2015 to 30 June 2016. The related party and the SMSF must determine the appropriate amount of principal and interest payable for the year. This calculation must take the opening balance of $80,000, the remaining term of three years, the timing of the $20,000 capital repayment, and the interest already paid into account.

After 1 July 2016, the new LRBA must continue under terms complying with the ATO's guidelines relating to listed shares at all times. For example, the SMSF must ensure that it updates the interest rate used for the loan on 1 July each year, and make monthly principal and interest repayments accordingly.

Option 2 - Refinance through a commercial lender

Option 3 - Pay out the LRBA

Pro Tip

The safe harbours outlined in PCG 2016/5 apply to real property; shares in a stock exchange listed company and units in a stock exchange listed unit trust.

Therefore in the case of an LRBA established to invest into a managed fund or a unit trust, the trustee/s of the SMSF must ensure that they have the appropriate

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documentation to provide evidence that the terms of the arrangement satisfy the arms-length rule.

IMPORTANT BORROWING CONSIDERATIONS

The following issues need to be considered when borrowing to acquire property within an SMSF:

Separate Bare Trust documents are required to be prepared for each property. The law allows only for a 'single acquirable asset' or collection of identical assets for each Bare Trust purchase.

A parcel of 100 CBA shares would be considered a single acquirable asset but a parcel of shares made up of several companies' shares would NOT be considered as a single acquirable asset.

Certain properties such as an apartment may have a car park on separate title which may require more than one Bare Trust arrangement.

As the rights of the lender are limited to the property, financial institutions will typically request a personal guarantee by the member (to protect against default on the loan).

Property held within a custodian trust (Bare Trust) that was acquired using a limited recourse borrowing cannot be developed or subdivided.

The property asset must be one which the SMSF trustee is permitted to acquire and hold directly.

SETTING UP A BARE TRUST

The Bare Trust is established by a Settlor, who is usually an acquaintance, lawyer or accountant who knows the parties. A quaint but essential requirement is that the Settlor provides a gift of a small amount such as $5 or $10 to the Bare Trustee to establish the Bare Trust. If this money isn't actually paid, the Bare Trust is invalid. The Settlor can't get the money back either; it sits in the Bare Trust's books as an asset.

The ancillary documents include resolutions and authorisations by the SMSF trustee and the Bare Trustee that the Bare Trust be established and the property purchased. These resolutions and authorisations are also necessary in order to comply with the super rules.

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The SMSF can require the property to be transferred to it by the Bare Trustee at any time, but only if there are no borrowings against it. In practice, the property is often sold before the loan is paid out, so the Bare Trustee will still be the owner and will be the seller in the sale contract.

If the property is transferred to the SMSF, there is no duty payable on the transfer.

SMSF BORROWING BENEFITS

Borrowing within an SMSF allows members to accelerate their wealth accumulation through making loan repayments with pre-tax contributions. Investment income is concessionally taxed and there is no CGT if the asset in sold in retirement.

WHAT ABOUT PROPERTY DEVELOPMENT?

We have already established from SMSFR2012/1 that the acquirable asset identified when the LRBA is put in place must continue to be the asset that is held on trust under that LRBA.

Therefore to the extent that a single acquirable asset becomes a different asset; for example, a house with land is purchased; the house is demolished; and a block of units is constructed - this would be classed as property development which is not allowable using borrowed funds.

However, there are ways that an SMSF may become involved in property development; one of those being an investment via a unit trust.

This is a specialised area which requires a high level of expertise and is best undertaken in consultation with a suitably qualified SMSF lawyer.

WHAT ABOUT BUYING OVERSEAS PROPERTY?

The complexity of buying property overseas depends upon the jurisdiction in the country where the property is being purchased. Many overseas jurisdictions require the property to be held by a company in that country. This would require the SMSF to acquire shares in the company, and for the company to purchase the property.

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However if the investments do not satisfy the 13.22C exceptions covered earlier, the SMSF investment in the shares of a company overseas will constitute a breach in the in-house asset rule.

If the jurisdiction allowed the SMSF to invest directly in the property without using a company, this would overcome the compliance aspect.

The process can be further complicated if borrowings are required and the investment is made via a foreign company.

On summary, buying overseas property through your SMSF is allowable however there are a number of compliance issues to be navigated resulting in higher costs.

As such, expert tax and legal advice in both jurisdictions would be required before undertaking this strategy.

REAL PROPERTY INVESTMENTS PROS AND CONS

The clarification of the borrowing rules has seen an increased investment into the direct property market by SMSF investors.

Whether or not this is a good thing depends upon the individual client circumstances.

Consideration should also be given to other structures outside the superannuation environment to ensure that this is in the best interests of the client.

Some things that should be considered are:

- Consider both the income and capital consequences of a property investment.
- With a negatively geared property in an SMSF you are working with a 15% income tax rate in accumulation and transition to retirement (TTR) and 0% in retirement income stream phase. If a client's Marginal Tax Rate is, say, 37% then negative gearing from an income perspective would be more beneficial at the client's Marginal Tax Rate.
- Consider a property which can be positively geared in an SMSF.
- Depending on when a capital gain is realised, the lower CGT rate in super (10% if asset is held longer than 12 months in accumulation or transition to retirement; or 0% in retirement income stream phase) should be compared with other

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options. Remember that an individual receives a 50% CGT discount when the asset is held longer than 12 months.

So a client with an effective Marginal Tax Rate of 20% will pay 10% with the CGT discount and a client with an MTR of 45% will pay 22.5% with the CGT discount, outside of super.

- Direct property is an illiquid asset which may make up a large part of the SMSF. This needs to be considered if a member leaves the fund whether by choice or on death. It may also affect pension payments, for example, if you cannot find a tenant to rent the property.

DERIVATIVES &LEVERAGE

Leverage, or gearing, involves a higher exposure to investment returns than the amount invested. This can increase returns on the upside as well as increasing the downside risk.

As there are borrowing restrictions for SMSFs and limited recourse borrowing arrangements can be expensive and complex, some SMSF trustees choose to obtain leverage by alternative methods such as investing in geared funds or derivatives such as Contracts for Difference (CFDs). These derivatives are becoming increasingly popular.

Any such leverage would need to be consistent with the SMSF's investment strategy and the trustees must meet other requirements to invest in derivatives.

The regulator disallows SMSFs from using derivatives for speculation purposes on the basis that this can result in significant risk for the superannuation fund's assets due to the in-built leverage of derivatives.

However, trustees may use derivatives for hedging purposes to minimise risk by protecting assets against changes in the market provided that this is consistent with the fund's investment strategy and the Derivatives Risk Statement which the trustees will also need to prepare.

The Derivatives Risk Statement must contain the following:

- Policies for the use of derivatives including analysis of risks;
- Restrictions and controls on the use of derivatives considering staff expertise (i.e. expertise of trustees and their advisers); and
- Compliance procedures to ensure effective controls (e.g. reporting procedures, internal and external audits and staff-management procedures).

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11.8 CGT CALCULATIONS FOR SMSFs

WHAT IS THE COST BASE?

The cost base of a CGT asset is generally the cost of the asset when you bought it. However, it also includes certain other costs associated with acquiring, holding and disposing of the asset. For most CGT events, you need the cost base of the CGT asset to work out whether or not you have made a capital gain. If you have made a capital loss, you may need the reduced cost base of the CGT asset for your calculation.

ELEMENTS OF THE COST BASE

The cost base of a CGT asset is made up of five elements:

1) money or property given for the asset
2) incidental costs of acquiring the CGT asset or that relate to the CGT event
3) costs of owning the asset
4) capital costs to increase or preserve the value of your asset or to install or move it
5) capital costs of preserving or defending your ownership of or rights to your asset.

You need to work out the amount for each element, then add them together to work out the cost base of your CGT asset.

CAPITAL GAIN

You may make a capital gain from a CGT event such as the sale of an asset. Generally, your capital gain is the difference between your asset's cost base (what you paid for it) and your capital proceeds (what you received for it). You can also make a capital gain if a managed fund or other unit trust distributes a capital gain to you.

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Any capital gains realised upon sale of assets or from distributions of realised capital gains from managed funds are usually entitled to a 1/3 discount if the underlying asset sold by the SMSF or underlying managed fund has been held for over 12 months. If the asset has been held for a period of less than 12 months, the full 15% superannuation tax would apply with no discount.

Case Study

Jessica has an accumulation account in her SMSF which includes an investment in a managed international share fund. The managed fund was initially purchased three years ago for $80,000. She now sells the managed fund for $100,000 and realises a $20,000 capital gain. As the units in the managed fund were purchased over 12 months ago, her SMSF will incur Capital Gains Tax of $20,000 X 15% X 2/3 = $2,000.

Case Study

Greg has an accumulation account in his SMSF which includes an investment in a managed international share fund. During the year, the managed fund sells an underlying share and realises a gain. The managed fund provider initially purchased the underlying share three years ago. The managed fund distributes income and the realised capital gain to unitholders including Greg's SMSF. Greg's SMSF will be assessed for tax at 15% on the income component from the managed fund's distribution relating to share dividends distributed. Greg's SMSF will also be assessed at 15% for two-thirds of the realised capital gains component of the managed fund distribution. The managed fund will report the income component and realised capital gains component to the unitholders such as the SMSF as part of the annual tax reporting. This will include reference to which components of the realised capital gains relate to investments held less than 12 months and those held for more than 12 months.

CAPITAL LOSS

Generally, you may make a capital loss as a result of a CGT event if you received less capital proceeds for an asset than its reduced cost base.

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SMSFs can offset capital losses against capital gains realised during the financial year in order to maximise the value of the losses. If realised capital losses exceed any realised capital gains in the financial year, the net loss can be carried forward to the future financial years to offset future years' capital gains.

Case Study

Jeremy has an accumulation account in his SMSF and during the year, his SMSF account sells three shares. Shares A and B were purchased four years ago whilst Share C was purchased 10 months ago. Upon selling the shares, the SMSF realises a $12,000 capital gain for Share A, $5,000 capital loss for Share B and $15,000 capital gain for Share C.

The most tax-effective way which the SMSF can offset the realised loss from Share B would be to offset the loss against the gains from Share C. This is because the SMSF would not be entitled to a 1/3 capital gains tax discount for Share C given they had been owned for less than 12 months. Share A on the other hand had been owned for more than 12 months so the SMSF would be entitled to the full 1/3 capital gains tax discount.

The net capital gains would be as follows:

- Share C capital gains = $15,000
- Minus Share B loss = ($5,000)
- Equals Net Capital Gains which are fully taxable at 15% = $10,000
- Plus Share A capital gain = $12,000, taxable at only 10% because of the 1/3 capital gains tax discount.

Total capital gains tax = $10,000 x 15% + $12,000 x 10% = $2,700

SUPER REFORMS – CGT RELIEF

Provisions for CGT relief were made available to fund members who were required to commute their existing pensions in order to comply with the new super reforms which became effective from 1 July 2017.

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That is, members with a pension balance greater than $1.6million would need to commute the excess amount back to the accumulation phase or withdraw it as a lump sum.

Likewise, members with a transition to retirement pension in place could decide to commute their pension back to the accumulation phase before the 1 July 2017 commencement date of the reforms.

The CGT relief allows the cost base of the assets funding the pension to be reset to market value so that those who were required to commute their pension as a result of the new transfer balance cap were not disadvantaged.

An election must be made by the due date of the lodgement of the SMSF's 2016/17 annual return and the decision is irrevocable.

The CGT relief provisions are complicated and an individual analysis of each client's circumstances is required, in consultation with a tax accountant.

11.9 WHEN A PENSION ACCOUNT MEMBER DIES

When an SMSF member dies, the trustees must pay out the death benefit as either a lump sum or income stream to the beneficiaries as soon as possible after the death of the member.

This process involves the following steps:

1. Identify the beneficiaries – this could be in accordance with the trust deed, a valid binding nomination or a trustee's side agreement, or alternatively, at the trustees' discretion if there is no nomination, a non-binding nomination or an invalid binding nomination. The beneficiary must be someone who is eligible to receive the benefit, i.e. a "dependant" as defined in the SIS Act or to the member's legal personal representative.

2. Calculate the amount of death benefit – this will be based on the members' SMSF balance with consideration provided to contributions and pension payments made prior to death, net income and capital growth attributable to the member until the payment date and any life insurance proceeds.

3. Determine whether to pay the death benefit as a lump sum and/or pension – this will be based on what the trust deed allows, whether the member has a legally binding

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nomination in place and whether the beneficiary will be eligible to receive an income stream under the regulations.

4. Complete required paperwork – this may include a PAYG form for a new pension recipient and membership form and ATO notification of a new SMSF member.

5. Pay the benefit

When a pension member dies and there is a reversionary beneficiary, the pension will continue and will be paid to the reversionary beneficiary. No tax on earnings or capital gains tax will apply for the pension.

When a pension member dies and no reversionary beneficiary has been arranged, any capital gains realised or earnings received from pension assets following the death of the pension member will be exempt from tax even if the benefit is paid as a lump sum, provided that the trustee pays the benefits to the beneficiary as soon as practical.

If the beneficiaries are non-dependants e.g. adult children, then those non-dependants will be taxed on the taxable component of the death benefits.

Example

A married or de facto couple are members of an SMSF. A member has a binding death benefit nomination in place at the time of the member's death, and the nomination entitles the beneficiary (a dependant) to a reversionary pension. At the time of death, the member has already commenced a pension. In this situation, the pension would continue to be paid to the member's spouse (or other nominated dependant) including the tax-exempt status of the pension account.

For such a pension entitlement to continue, the rules of the income stream must specify that the pension will be automatically transferred to the beneficiary (a dependant). The rules must also specify both the person to whom the benefit will become payable and that it will be paid in the form of a pension.

11.10 SEGREGATED VS UNSEGREGATED ASSETS AND ALLOCATING EARNINGS & WITHDRAWALS TO TAX COMPONENTS

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SMSFs can hold separate accounts to easily differentiate assets for one member's account from another account of the member or another member of the SMSF. Such treatment of assets is known as having 'segregated 'assets. Alternatively, an SMSF can combine various members' accounts into one pool, which is known as 'unsegregated' assets.

Trustees may choose to segregate assets between members if each member has different risk profiles. Trustees may choose to have unsegregated assets to reduce administration costs or where there is a large asset in the SMSF such as a property which would represent a combination of more than one account.

The appendix contains more information on the difference between segregated and unsegregated assets in terms of the allocation of earnings and withdrawals to tax components.

In recent years, there has been a significant increase in the adoption by SMSF members who have reached their preservation age and still working to utilise a Transition to Retirement strategy. This involves commencing a pension via their SMSF as well as contributing personal or employer-funded superannuation contributions to their SMSF accumulation account.

Where a member has established a pension account, they are unable to add funds to that pension account. Any future contributions will either be added to their accumulation account or a separate pension account via their SMSF (i.e. a newly created pension account). If the member wants to consolidate more than one pension account or a pension and accumulation account into a new pension, the trustees will be able to arrange this in accordance with legislation and the trust deed.

Case Study

Mark is 58 and is undertaking a Transition to Retirement strategy via his SMSF whereby he has an accumulation account (account number 1) which receives his employer contributions and a pension account (account number 2) which provides him with tax-effective earnings and income to supplement his lifestyle expenses. Mark inherits $200,000 and wants to contribute these funds as a non-concessional contribution to his SMSF and ensure that the funds are added to the pension component of his SMSF as he does not want these funds to attract 15% earnings tax in the accumulation phase.

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Mark is unable to add the $200,000 to his existing pension account (account number 2). However, Mark can create a second pension account (account number 3) to contribute the $200,000 as no further contributions can be added to an existing pension account. He would then have three SMSF accounts (i.e. 1 accumulation account and 2 pension accounts).

If he would prefer to only hold 1 accumulation account and 1 pension account, he could alternatively choose to create the second pension account (account number 3) and fund this pension account from a combination of the full transfer from the existing pension account (account number 2) and the $200,000 contribution (i.e. both transactions would be recorded at the same time). He would then have two open SMSF accounts comprising an accumulation account (account number 1) and a pension account (account number 3), whilst account number 2 would be closed.

Case Study

The AXY SMSF has assets of $2,000,000. Member A (who is receiving a super income stream benefit that is not an allocated, market-linked or account-based pension) has an account balance of $1,200,000, and member B (who is still in the accumulation phase) has an account balance of $800,000. The trustees have identified specific assets of the SMSF that total $1,200,000 as having been set aside for member A($500,000 in shares, $500,000 in property and $200,000 in a bank deposit), and these SMSF assets are used to pay his income stream benefit. These assets are segregated current pension assets. The trustees of the SMSF must get an actuarial certificate to verify that those assets, and the earnings that the actuary expects will be made from them, are sufficient to pay, in part or in full, member A's income stream benefit.

The income that is earned from these assets is exempt from tax. For the above SMSF, if we assume that assets set aside for member A ($1,200,000) earned $100,000 in income and the other assets of the SMSF earned $60,000 in income, then exempt current pension income is $100,000. This would be shown on the SMSF annual return as follows:

Total assessable income	$160,000 (included at item 10 label V of the SMSF annual return)

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less ECPI	$100,000 (the fund claims this exemption by including this amount at item 11 label K of the SMSF annual return)
equals Taxable income	$60,000 (included at item 11 label O of the SMSF annual return)

(Source: ATO)

Effective from 1 July 2017, SMSF's are not able to use the segregated assets method if:

- there is at least one retirement phase interest in the fund during the year and
- a member has a total superannuation balance > $1.6 million at the prior 30 June and is receiving a retirement phase income stream from any fund

11.11 TRANSFERRING AN ASSET OUT OF AN SMSF

Transferring an asset out of your SMSF may or may not create a taxable capital gain. It depends on:

- the value of the cost base
- selling price
- what phase you are in

If your super account is in the retirement income stream phase, that is, you're receiving an income stream from your SMSF account and you have retired, then no tax is payable on earnings from fund assets financing an SMSF retirement pension. The tax exempt treatment of fund earnings financing a retirement pension also includes any capital gains.

If you have not yet started a retirement phase income stream, that is, your super account is in accumulation phase, or transition to retirement phase, then tax is payable on fund earnings, including any capital gains.

The SMSF pension payments must be in cash, rather than assets. An individual can however withdraw assets as a lump sum payment.

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11.12 INSURANCE WITHIN AN SMSF

As part of the fund's investment strategy, trustees must consider the insurance needs of their members. The sample investment strategy in the appendix contains an example paragraph which may be included in relation to insurance.

Example

The SMSF Investment Strategy can include a statement such as the following after the Trustees consider whether members require insurance:

'The trustees have considered the insurance needs of the members of the fund. They have determined that the insurances held by the members within the fund remain appropriate.'

When considering the insurance needs of the members', trustees need to consider the restrictions that were introduced on new policies acquired on or after 1 July 2014.

The Trustee's also have a duty to protect the assets of the fund from loss or damage.

If a residential or commercial investment property is owned by the fund then building and contents insurance is required, as well as adequate levels of public liability insurance.

In a 2010 court case where a property was owned by an SMSF the court held the owner of the property (the SMSF) liable for the death of a tradesman who was electrocuted after coming into contact with an exposed wire from a decommissioned solar hot water system. Damages of $350,000 were awarded to the widow of the deceased.

Also, if a fund invests in collectibles the trustee must ensure that the assets are insured in the fund's name within 7 days of the purchase.

Who owns the insurance policy?

If the trustee of an SMSF takes out an insurance policy on a member of the fund, the policy must be owned by the trustees on behalf of the fund. The premiums which are paid for the insurance policies on the life of the members must be deducted from the relevant member's account, and any insurance proceeds received must also be allocated to the relevant member's account.

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Case Study- SMSF Insurance

Kirsty and Darryl are members of the same SMSF. Darryl's life insurance is held in the SMSF so the fund is the owner of the policy on Darryl's life. The premiums paid in respect of the policy relate specifically to Darryl so they must be deducted from his account. If Darryl dies, Kirsty must ensure that100% of the proceeds from the insurance policy are allocated to Darryl's account.

Trustees should regularly review whether the members have appropriate insurance covers via the SMSF or if any changes should be implemented, and document their decisions based on their analysis. It would be prudent to review the insurance levels annually or when a new member joins the fund, or a major life event such as birth of a child or transition to pension phase occurs for a member.

Trustees may be liable to third parties for the decisions they make in relation to insurance cover for their members.

For example, if an SMSF member dies, the deceased's family members could then claim that the trustees should have arranged higher insurance cover for that member. If trustees' documentation of the members' insurance needs assessments is too brief, they risk the potential for future claims from the deceased's family members. Trustees can reduce this risk by documenting detailed analysis of the members' insurance needs in a separate document such as a Statement of Advice from a financial planner.

Life insurance, Total and Permanent Disability (TPD) and income protection can all be purchased within an SMSF. It is important to ensure that the policy is in the fund trustee's name ("as trustee") not in the name of the individual member.

TERM LIFE INSURANCE

Term life insurance was covered in detail in section 10.0of this module. If a term life policy includes a payout for a terminal medical condition the terms of the policy must align with the SIS condition of release for terminal illness.

The Trustee of an SMSF must understand that from 1 July 2104 they are prohibited from acquiring an insurance policy which provides a payout on a condition that does not align with the SIS definition.

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TOTAL AND PERMANENT DISABILITY (TPD)

Earlier in this module we discussed TPD in relation to 'own' occupation and 'any' occupation.

The Trustee of an SMSF should be aware that from 1 July 2014 they are prohibited from acquiring a TPD policy with an 'own occupation' TPD definition or a TPD policy which provides ancillary lump sum benefits

INCOME PROTECTION INSURANCE

A Trustee is prohibited from acquiring an income protection policy which provides ancillary lump sum benefits such as rehabilitation and home care benefits.

The terms and conditions of the income protection policy must also satisfy the definition of temporary incapacity contained in the SIS Regulations which requires the member to have:

- ceased to be gainfully employed due to ill-health, or
- have temporarily ceased to receive any gain or reward under a continuing employment arrangement due to ill-health.

Further, the Trustee of an SMSF cannot hold a policy which pays a partial benefit when a member reduces their work hours as a result of accident, illness or injury, rather than ceasing work completely.

Pro Tip

Some insurers have designed policies specific for SMSF's which take into account the insurance changes which came into place on 1 July 2014.

CAN PERSONAL LIFE INSURANCE POLICIES BE TRANSFERRED INTO AN SMSF?

No. Where a member purchases a life insurance policy outside a super fund, and then attempts to transfer the policy ownership to the SMSF at a later stage this is treated as a transfer of ownership of an asset which is prohibited under s 66(2)(A) of the SIS Act.

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However, it is possible to approach a member's insurer to request that they cancel the existing personal policy and reissue it in the name of the SMSF trustee without further underwriting. It would be important to check that the terms and conditions would be the same as some insurers may change the benefit features over time for new policies. The same issues apply to TPD and Income Protection Insurance.

An SMSF can also purchase life insurance cover on behalf of members.

11.13 WINDING UPAN SMSF

The winding up of an SMSF can occur for a number of reasons:

- the fund has no assets left (the SMSF has paid out all money in the fund either as a lump sum or as pension payments to members)
- the death of a member
- the members decide they no longer want the responsibility
- a key member/trustee is moving overseas

WHAT IS REQUIRED TO WIND UP AN SMSF?

There are a number of steps necessary to correctly wind up an SMSF.

1. Check the trust deed to identify what needs to be done to wind up the fund.
2. Ensure that all trustees have a written agreement to wind-up the fund (e.g. all trustees could sign the minutes of meeting confirming the date the fund will start to be wound-up and how the benefits will be paid).
3. Each member must notify how and where they want their benefits to be paid, specifically whether they want their benefits to be rolled over to another super fund or paid out as a lump sum.

   The wind up of an SMSF means that there will be no assets left in the fund. To move these assets out, you need to comply with both the SIS laws and your trust deed.

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This generally means paying out lump sums to members, provided they can satisfy a condition of release, or rolling over the members' benefits to another complying superannuation fund.

Be aware that if the SMSF sells assets to pay out benefits or roll over benefits to another fund, there may be capital gains tax issues.

4. Notify the ATO of the decision to wind-up the fund before starting to wind-up the fund.
5. Arrange for the SMSF's final wind-up set of accounts and audit before lodging the final annual return.
6. Pay any outstanding tax and charges.
7. In the case of a corporate trustee, the directors must decide whether the company should remain running or be wound up.
8. Rollover or pay out any SMSF benefits.
9. The ATO will confirm that the SMSF has been would up and will send a letter stating that they have cancelled the SMSFs ABN, and closed the SMSF records on their system.
10. Once confirmation from the ATO has been received, the SMSF bank accounts need to be closed. If an amount needs to be retained to cover expenses such as income tax which will be due in the future, the bank account can still be closed and the money retained in a trust by the former trustees to be paid when the expenses are due. This will avoid the requirement for the SMSF to complete a potential additional year's income tax return and accounts.
11. The ATO needs to be notified in writing within 28 days of the fund being wound up, with details of:
    - the name and ABN of the SMSF
    - the date the SMSF was wound up
    - a contact person, with contact details such as name, phone number, email etc.

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CONCLUSION

Superannuation for most people will be the largest asset outside of their home. Leading up to retirement is a very important period in which thoughtful planning is required. The complexity of superannuation legislation means that those who not only have the knowledge, but importantly how to best apply it, will position themselves to fully realise the available opportunities.

IMPORTANT

You must now complete **both** Part C and Part D of your Multiple Choice assessments for Module 3.

A few tips:

- You can access the Multiple Choice Questions at monarch.mywisenet.com.au
- Press "Ctrl F" if you want to search the pdf course materials for any key words or terms.
- You have 2 attempts. Please note, if you require a second attempt, the answers are shuffled so read them carefully. The highest score counts.
- If you are unsuccessful after 2 attempts, please contact our office on 1300 738 955.

Once you complete the Multiple Choice assessments, you should complete the assignment and the workplace simulation for Module 3.

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APPENDIX

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APPENDIX 1 – FAILING THE SOLE PURPOSE TEST - IT'S A CRIME

APPENDIX 1 - FAILING THE SOLE PURPOSE TEST - IT'S A CRIME

Kassongo Case

On 4 January 2007, ASIC initiated civil proceedings against a Sydney man, AtanOnaKassongo, following allegations he was involved in the operation of an unlicensed financial services business offering people early access to their superannuation funds. On 5 August 2008, Mr Kassongo, was further charged with a criminal offence of dishonestly failing to ensure a self-managed superannuation fund (SMSF) known as the Kassongo Superannuation Fund (KSF) was maintained in accordance with the sole purpose test. Mr Kassongo was trustee of the fund at the time of the alleged offence. This is the first time criminal charges have been laid against a trustee of a self-managed superannuation fund under the SIS Act. This criminal charge followed an investigation conducted with the assistance of the Australian Taxation Office and was the first, and not expected to be the last, to be laid against a trustee of a self-managed superannuation fund under the SIS Act.

ASIC said that it had pursued the action against Kassongo on the basis that he had allegedly dishonestly failed to ensure that the KSF was maintained in accordance with the sole purpose test. Under the SIS Act, SMSF trustees must operate their fund for the sole purpose of providing retirement savings for the fund's members. ASIC alleged that the preserved superannuation benefits of 192 superannuates totalling $4,055,043 were deposited into the bank accounts of KSF. It was alleged that these funds were rolled over from 56 complying superannuation funds and that Kassongo then used KSF to obtain early access to these benefits by withdrawing and distributing the funds to the superannuants and agents engaged by him to assist in the early release scheme. ASIC also alleged that, at the time the KSF received the superannuation benefits from the complying superannuation funds, Mr Kassongo was aware that he had an obligation to preserve these benefits until the superannuants had satisfied a condition of release but had no intention of doing so. For his service, Kassongo had retained over $600,000 for himself by way of commission.

Mr Kassongo pleaded guilty to the criminal charges brought by the regulator and pursued by the Director of Public Prosecutions. He was sentenced to two years imprisonment, to be released after eight months, for unlawfully allowing the early access of superannuation benefits.

http://www.bartier.com.au/publications/publicationDetail.aspx?PublicationID=208

Little Case

The Kassongo prosecution was closely followed by the identical scenario of the Little case. This action is the second such case where ASIC has used a breach of the sole purpose test to prosecute an SMSF trustee. ASIC brought charges against Gerard Little, an SMSF trustee for a breach of the SIS Act. Little was charged under sections 62 and 202 of the SIS ACT for failing to ensure his SMSF, called Little Super Fund (LSF), was maintained in a manner that satisfied the sole purpose test.

The regulator alleges Little, as trustee of LSF, accepted the preserved benefits of 121 superannuants, worth $3.5 million, into the bank account of the fund. These monies were then rolled over into 11 other complying superannuation funds.

ASIC claims Little breached the SIS Act when he used LSF to access these funds illegally, withdrawing a portion and distributing it among the original superannuants. It is also alleged that from this transaction Little retained $685,000 for himself as a commission for his services. The corporate watchdog has alleged Little knew the rolled over super benefits had to be preserved until retirement age, but had no intention of abiding by the conditions.

On 24 March 2009, Mr Gerard Little pleaded guilty in the Downing Centre Local Court to criminal charges under section 62 and 202 of the SIS Act. Gerard Little was sentenced to two years imprisonment, to be released after eight months, for unlawfully allowing the early access of superannuation benefits

APPENDIX 2 – REQUEST TO ROLLOVER SUPERANNUATION BENEFIT

Completing the form *Rollover initiation request to transfer whole balance of superannuation benefits between funds*

Australian Government

By completing this form, you will initiate a rollover request to transfer the **whole** balance of your super benefits between funds. This form can **not** be used to transfer part of the balance of your super benefits.

You can **not** use this form to transfer your benefits to your own self-managed super fund (SMSF). You must use the form *Rollover initiation request to transfer whole balance of superannuation benefits to your self-managed super fund* (NAT 74662).

This form will not change the fund to which your employer pays your contributions. The *Standard choice* form must be used by you to change funds.

BEFORE COMPLETING THIS FORM

- Read the important information below.
- Check that the fund you are transferring your benefits **TO** can accept this transfer.

WHEN COMPLETING THIS FORM

- Refer back to these instructions where a question shows a message like this: ❯
- Print clearly in BLOCK LETTERS.

AFTER COMPLETING THIS FORM

- Sign the authorisation.
- Send the request form to either your **FROM** fund or your **TO** fund

IMPORTANT INFORMATION

! This transfer may close your account – you will need to check this with your **FROM** fund.

This form can **not** be used to:

- transfer part of the balance of your super benefits
- transfer benefits if you don't know where your super is
- transfer benefits from multiple funds on this one form – a separate form must be completed for each fund you wish to transfer super from
- change the fund to which your employer pays contributions on your behalf
- open a super account
- transfer benefits under certain conditions or circumstances – for example, if there is a super agreement under the *Family Law Act 1975* in place

CHECKLIST

- ☐ Have you read the important information?
- ☐ Have you considered where your future employer contributions will be paid?
- ☐ Have you checked your **TO** fund can accept the transfer?
- ☐ Have you completed all of the mandatory fields on the form?
- ☐ Have you signed and dated the form?

WHAT HAPPENS TO MY FUTURE EMPLOYER CONTRIBUTIONS?

Using this form to transfer your benefits will not change the fund to which your employer pays your contributions and may close the account you are transferring your benefits **FROM**.

If you wish to change the fund into which your employer contributions are being paid, you will need to speak to your employer about super choice. For the appropriate forms and information about whether you are eligible to choose the fund to which your employer contributions are made, visit **ato.gov.au** or call the Australian Taxation Office (ATO) on **13 10 20**.

THINGS YOU NEED TO CONSIDER WHEN TRANSFERRING YOUR SUPERANNUATION

When you transfer your super, your entitlements under that fund may cease – you need to consider all relevant information before you make a decision to transfer your super. If you ask for information, your super provider must give it to you.

Some of the points you may consider are:

- **Fees** – your **FROM** fund must give you information about any exit or withdrawal fees. If you are not aware of the fees that may apply, you should contact your fund for further information before completing this form. The fees could include administration fees, and exit or withdrawal fees. Your **TO** fund may also charge entry or deposit fees on transfer. Differences in fees that funds charge can have a significant effect on the super you will have to retire on – for example, a 1% increase in fees may significantly reduce your final benefit.
- **Death and disability benefits** – your **FROM** fund may insure you against death, illness or an accident which leaves you unable to return to work. If you choose to leave your current fund, you may lose any insurance entitlements you have – other funds may not offer insurance, or may require you to pass a medical examination before they cover you.
- When considering a new fund, you should consider checking the costs and amount of any cover offered.

WHAT HAPPENS IF YOU DO NOT QUOTE MY TAX FILE NUMBER (TFN)?

You are not required to provide your TFN to your super fund. However, if you do not provide your TFN, your fund may be taxed at the highest marginal tax rate, plus the Medicare levy, on contributions made to your account in the year, compared to the concessional tax rate of 15%. Your fund may deduct this additional tax from your account.

If your super fund does not have your TFN, you will not be able to make personal contributions to your super account. Choosing to quote your TFN will also make it easier to keep track of your super in the future.

Under the *Superannuation Industry (Supervision) Act 1993*, your super fund is authorised to collect your TFN, which will only be used for lawful purposes. These purposes may change in the future as a result of legislative change. The TFN may be disclosed to another super provider when your benefits are being transferred, unless you request in writing that your TFN is not to be disclosed to any other trustee.

TRANSFERS TO SELF-MANAGED SUPER FUNDS

You must use the form *Rollover initiation request to transfer whole balance of superannuation benefits to your self-managed super fund* (NAT 74662) to transfer your benefits to your own self-managed super fund (SMSF).

HAVE YOU CHANGED YOUR NAME OR ARE YOU SIGNING ON BEHALF OF ANOTHER PERSON?

If you have changed your name or are signing on behalf of the applicant, you will need to provide a certified linking document – a linking document is a document that proves a relationship exists between two (or more) names.

The following table contains information about suitable linking documents:

Purpose	Suitable linking documents
Change of name	Marriage certificate, deed poll or change of name certificate from the Births, Deaths and Marriages Registration Office
Signed on behalf of the applicant	Guardianship papers or Power of Attorney

CERTIFICATION OF PERSONAL DOCUMENTS

All copied pages of **original** proof of identification documents (including any linking documents) need to be certified as true copies by any individual approved to do so (see below).

The person who is authorised to certify documents must sight the original and the copy and make sure both documents are identical, then make sure all pages have been certified as true copies by writing or stamping '**certified true copy**' followed by their signature, printed name, qualification – for example, Justice of the Peace or Australia Post employee – and date.

The following people can certify copies of the originals as **true and correct** copies:

- a person enrolled on the roll of a State or Territory Supreme Court or the High Court of Australia as a legal practitioner
- a judge of a court
- a magistrate
- a Chief Executive Officer of a Commonwealth court
- a registrar or deputy registrar of a court
- a justice of the peace
- a notary public officer
- a police officer
- an agent of the Australian Postal Corporation who is in change of an office supplying postal services to the public
- a permanent employee of the Australian Postal Corporation with two or more years of continuous service
- an Australian consular officer or an Australian diplomatic officer
- an officer with two or more years of continuous service with one or more financial institutions
- a finance company officer with two or more years of continuous service (with one or more finance companies)
- an officer with, or authorised representative of, a holder of an Australian Financial Services Licence (AFSL), having two or more years continuous service with one or more licensees
- a permanent employee of the Commonwealth with two or more years continuous service
- a permanent employee of the State or Territory, or State and Territory authority with two or more years continuous service
- a permanent employee of a local government authority with two or more years of continuous service
- a member of the Institute of Chartered Accountants in Australia, CPA Australia, or the National Institute of Accountants, with two or more years continuous membership.

WHERE DO I SEND THE FORM?

You can send your completed and signed form to either the transferring or the receiving fund.

MORE INFORMATION

For more information about super, visit the:

- Australian Securities & Investments Commission (ASIC) website at **moneysmart.gov.au**
- ATO website at **ato.gov.au/super**

For more information about this form, phone the ATO on **13 10 20**.

Australian Government

Rollover initiation request to transfer whole balance of superannuation benefits between funds

under the *Superannuation Industry (Supervision) Act 1993*

COMPLETING THIS FORM

- Read the important information pages
- Refer to instructions where indicated with a
- This form is only for whole (not part) balance transfers.

AFTER COMPLETING THIS FORM

- Sign the authorisation
- Send form to **either** your **FROM** (transferring) or **TO** (receiving) fund.

Personal details

Title: Mr Mrs Miss Ms Other

*Family name

*Given names

Other/previous names

*Date of birth Day / Month / Year

Tax file number

Under the *Superannuation Industry (Supervision) Act 1993*, you are not obliged to disclose your tax file number, but there may be tax consequences.

See 'What happens if I do not quote my tax file number?'

*Sex Male Female

Contact phone number

Residential address

*Address

*Suburb

*State/territory *Postcode

Previous address

If you know that the address held by your **FROM** fund is different to your current residential address, give details below.

Address

Suburb

State/territory Postcode

Fund details

FROM (Transferring fund)

*Fund name

Fund phone number

*Membership or account number

Australian business number (ABN)

Unique Superannuation identifier

If you have multiple account numbers with this fund, you must complete a separate form for each account you wish to transfer.

TO (Receiving fund)

*Fund name

Fund phone number

*Membership or account number

Australian business number (ABN)

Unique Superannuation identifier

You must check with your **TO** fund to ensure they can accept this transfer.

Authorisation

Print form Reset form

By signing this request form I am making the following statements:

- I declare I have fully read this form and the information completed is true and correct.
- I am aware I may ask my superannuation provider for information about any fees or charges that may apply, or any other information about the effect this transfer may have on my benefits, and have obtained or do not require such information.
- I consent to my tax file number being disclosed for the purposes of consolidating my account.
- I discharge the superannuation provider of my **FROM** fund of all further liability in respect of the benefits paid and transferred to my **TO** fund.

I request and consent to the transfer of superannuation as described above and authorise the superannuation provider of each fund to give effect to this transfer.

***Name** (Print in BLOCK LETTERS)

***Signature**

***Date** Day / Month / Year

*** Denotes mandatory field. If you do not complete all of the mandatory fields, there may be a delay in processing your request.**

APPENDIX 3 – INTENTION TO CLAIM A TAX DEDUCTION

Australian Government
Australian Taxation Office

Notice of intent to claim or vary a deduction for personal super contributions

COMPLETING THIS STATEMENT

- Print clearly using a black pen only.
- Use BLOCK LETTERS and print one character per box.
- Place X in ALL applicable boxes.

The instructions contain important information about completing this notice. Refer to them for more information about how to complete and lodge this notice.

Section A: **Your details**

1 Tax file number (TFN)

The ATO does not collect this information provided on this form. This form is to assist you in providing details to your super fund. Your super fund is authorised to request your personal details, including your TFN, under the *Superannuation Industry (Supervision) Act 1993*, the *Income Tax Assessment Act 1997* and the *Taxation Administration Act 1953*. It is not an offence not to provide your TFN. However, if *you* do not provide your TFN, and your super fund doesn't already hold your TFN, they will not be permitted to accept the contribution(s) covered by this notice. For more information about your privacy please contact the entity you are providing this form to.

2 Name

Title: Mr Mrs Miss Ms Other

Family name

First given name

Other given names

3 Date of birth Day / Month / Year

4 Current postal address

Suburb/town/locality

State/territory (Australia only)

Postcode (Australia only)

Country if outside of Australia

5 Daytime phone number (include area code)

Section B: **Super fund's details**

6 Fund name

7 Fund Australian business number (ABN)

8 Member account number

9 Unique Superannuation Identifier (USI) (if known)

Section C: **Contribution details**

10 Personal contribution details

Is this notice varying an earlier notice? No ☐ Yes ☐

If you answered 'No' complete the **Original Notice to Claim a Tax Deduction** section below.
If you answered 'Yes' complete the **Variation of previous valid notice of intent** section below.

ORIGINAL NOTICE TO CLAIM A TAX DEDUCTION

11 Financial year ended 30 June 20☐☐

12 My personal contributions to this fund in the above financial year $ ☐☐☐,☐☐☐.☐☐

13 The amount of these personal contributions I will be claiming as a tax deduction $ ☐☐☐,☐☐☐.☐☐

Section D: **Declaration**

This form has a declaration where you say the information in it is correct and complete. Please review the information before you sign the declaration. If you provide false or misleading information, or fail to take reasonable care, you may be liable to administrative penalties imposed by taxation law.

INTENTION TO CLAIM A TAX DEDUCTION

Complete this declaration if you have **not** previously lodged a valid notice with your super fund for these contributions.

I declare that at the time of lodging this notice:

- *I intend to claim the personal contributions stated as a tax deduction*
- *I am a current member of the identified super fund*
- *the identified super fund currently holds these contributions and has not begun to pay a superannuation income stream based in whole or part on these contributions*
- *I have not included any of the contributions in an earlier valid notice.*

I declare that I am lodging this notice at the earlier of ***either****:*

- *before the end of the day that I lodged my income tax return for the income year in which the personal contributions were made,* ***or***
- *before the end of the income year following the year in which the contribution was made.*

I declare that the information given on this notice is correct and complete.

Name (Print in BLOCK LETTERS)

Signature

Date
Day / Month / Year

Send your completed notice to your super fund. **Do not send it to us**. The information on this notice is for you and your super fund. We don't collect this information; we only provide a format for you to provide the information to your super fund.

VARIATION OF PREVIOUS VALID NOTICE OF INTENT

14 Financial year ended 30 June 20☐☐

15 My personal contributions to this fund in the above financial year $ ☐☐☐,☐☐☐.☐☐

16 The amount of these personal contributions claimed in my original notice of intent $ ☐☐☐,☐☐☐.☐☐

17 The amount of these personal contributions I will now be claiming as a tax deduction $ ☐☐☐,☐☐☐.☐☐

Declaration

This form has a declaration where you sign to indicate that the information in it is correct and complete. Please review the information before you sign the declaration. If you provide false or misleading information, or fail to take reasonable care, you may be liable to administrative penalties imposed by taxation law.

> Complete this declaration if you have already lodged a valid notice with your fund for these contributions and you wish to **reduce** the amount stated in that notice.

VARIATION OF PREVIOUS VALID NOTICE OF INTENT

I declare that at the time of lodging this notice:

- *I intend to claim the personal contributions stated as a tax deduction*
- *I am a current member of the identified super fund*
- *the identified super fund currently holds these contributions and has not begun to pay a superannuation income stream based in whole or part on these contributions.*

I declare that I wish to vary my previous valid notice for these contributions by ***reducing*** *the amount I advised in my previous notice and I confirm that either:*

- *I have lodged my income tax return for the year in which the contribution was made, prior to the end of the following income year, and this variation notice is being lodged before the end of the day on which the return was lodged,* **or**
- *I have not yet lodged my income tax return for the relevant year and this variation notice is being lodged on or before 30 June in the financial year following the year in which the personal contributions were made,* **or**
- *the ATO has disallowed my claim for a deduction for the relevant year and this notice reduces the amount stated in my previous valid notice by the amount that has been disallowed.*

I declare that the information given on this notice is correct and complete.

Name (Print in BLOCK LETTERS)

Signature

Date

Day / Month / Year

> Send your completed variation notice to your super fund. **Do not send it to us**. The information on this notice is for you and your super fund. We don't collect this information; we only provide a format for you to provide the information to your super fund.

APPENDIX 4 – CONTRIBUTION SPLITTING FORM

Instructions and form for super fund members

Contributions splitting

How to complete your *Superannuation contributions splitting application*.

BEFORE COMPLETING THIS APPLICATION

Contact your superannuation (super) fund before completing this application, to check whether your fund:

- offers contributions splitting
- needs you to use a different application form
- charges a fee for contributions splitting to recover costs.

You can only apply once to split contributions made to a particular super fund in a particular financial year.

> ! If you want to apply to split deductible personal contributions, you must give your super fund a *Notice of intent to claim or vary a deduction for personal super contributions* (NAT 71121) **before** you lodge your *Superannuation contributions splitting application*.

WHO SHOULD COMPLETE THIS APPLICATION?

You should complete this application if you want to increase your spouse's super by giving them some of your super. When you split your contributions, you transfer or roll over a portion of the contributions you recently made to your super account to your spouse's super account.

For this application, the definition of a spouse includes a person:

- you are legally married to
- you are in a relationship with that is registered under certain state or territory laws (including registered same-sex relationships)
- of the same or of a different sex, who lives with you on a genuine domestic basis in a relationship as a couple (known as a 'de facto spouse').

> ! Contributions splitting does not reduce the amount counted towards your concessional contributions cap. Your super fund reports to us all the contributions that were made for you, including any contributions that were later transferred to your spouse after a contributions splitting application.

NAT 15237-02.2014

Australian Government
Australian Taxation Office

WHEN CAN YOU APPLY TO SPLIT YOUR CONTRIBUTIONS?

You can apply to split your contributions when you are any age, but your spouse must be either:

- less than the preservation age that applies to them, **or**
- aged between their preservation age and 65 years, and not retired.

You lodge this application with your super fund in the:

- financial year immediately after the financial year in which the contributions were made
- financial year the contributions were made, **only** if your entire benefit is being withdrawn before the end of that financial year as a rollover, transfer, lump sum benefit or combination of these.

WHEN WOULD YOUR APPLICATION BE INVALID?

Your application to split your contributions is invalid if any of the following applies:

- you have already applied in that financial year and the trustee of your fund has received your application
- the amount of benefits you have applied to split is more than the maximum amount that can be split
- your spouse is 65 years old or over
- your spouse has reached their preservation age and is retired.

WHAT CONTRIBUTIONS CAN BE SPLIT?

The maximum amount that can be transferred to your spouse each financial year usually depends on the amount and type of contributions made by or for you in the *previous* financial year.

It can also depend on the contributions made in the *current* financial year, but only if your entire benefit will be rolled over, transferred or withdrawn in that financial year (see When can you apply to split your contributions?).

There are two main types of contributions that can be split with your spouse:

- taxed splittable contributions
- untaxed splittable employer contributions.

Other contributions types cannot be split.

Taxed splittable contributions

You can ask your super fund to transfer to your spouse up to 85% of a financial year's 'taxed splittable contributions'. These are generally:

- any contributions your employer made for you (your before-tax contributions), including any salary sacrifice contributions
- any personal contributions you made for yourself that you have advised your super fund you will claim a tax deduction for – usually only self-employed people can make this type of contribution.

These contributions can include other amounts, such as amounts allocated by your super fund from a reserve or surplus to meet an employer's liability to make contributions. Contact your super fund for details of what contributions were made for you and whether they can be split.

> ! The maximum amount of taxed splittable contributions you can apply to split is the lesser of 85% of the concessional contributions for that financial year and the concessional contributions cap for that financial year. Refer to *Super contributions – too much super can mean extra tax* (NAT 71433) to check the current cap.

Untaxed splittable employer contributions

If you are a member of a public sector super scheme, the employer contributions that are made for you may be 'untaxed splittable employer contributions'.

You can transfer to your spouse 100% of untaxed splittable employer contributions made for you in a financial year, if that amount is less than the concessional contributions cap for that financial year.

> ! Some public sector schemes are not able to offer contributions splitting. You should contact your super scheme for advice about splitting untaxed contributions before completing this application.

WHAT CONTRIBUTIONS CANNOT BE SPLIT?

Any contributions that are not taxed splittable contributions or untaxed splittable employer contributions cannot be split with your spouse – for example, splitting is not available for personal contributions you cannot claim a deduction for.

TABLE 1: What contributions can be split

Type of contribution	Can they be split?
Employer contributions	Yes
Salary sacrifice contributions	Yes
Personal contributions that you can claim a deduction for (self-employed people may be able to claim this deduction)	Yes
Personal contributions that you can't claim a deduction for (employees usually cannot claim this deduction)	No
Contributions you make with a capital gains tax (CGT) cap election for small business or with a personal injury election	No
Contributions made by your spouse to your super	No
Contributions made for you if you are under 18 years old (unless made by your employer)	No
Contributions made by family and friends (other than those made by your spouse or for a child under 18 years old)	Yes
Transfers from foreign funds	No
Allocations from reserves that are assessable, such as allocations to meet an employer's obligation to contribute	Yes
Other allocations from reserves	No
A rollover super benefit	No
A contribution that has already been split	No
Government co-contribution payment	No
First home saver account payments and government contributions	No
Temporary resident contributions	No
Trustee contributions	No
A super interest that is subject to a payment split (due to relationship breakdown)	No

EXAMPLE 1: Typical splitting arrangement

John's employer contributed $10,000 to his super fund in the 2011–12 financial year. John talks to his super fund about splitting his 2011–12 contributions with his wife Mary, who works part-time. The fund advises him he is eligible to apply after 30 June 2012.

John completes the *Superannuation contributions splitting application* and lodges it with his fund in August 2012. He puts $7,000 at question 22 'taxed splittable contributions' to split his employer contributions.

His super fund accepts his application and determines that it is valid because $7,000 is:

- less than 85% of the $10,000 contributed by his employer, and
- less than the concessional contributions cap.

His super fund transfers $7,000 to Mary's super fund in September 2012.

EXAMPLE 2: Effect on the contributions caps

In 2011–12, Marita had a salary sacrifice arrangement and the super contributions made for her for the financial year are as follows:

Salary sacrifice contributions:	$20,000
Employer contributions:	$10,000
Total employer contributions	**$30,000**

After the end of the financial year, Marita and her partner Ken visited an investment adviser who advised her to cut back her salary sacrifice to only $15,000 and advised her she would need to pay excess contributions tax because she had contributed more than the $25,000 concessional contributions cap for 2011–12.

A friend later told Marita about contributions splitting. Marita and her friend thought that splitting her contributions with Ken might eliminate the excess contributions made in 2011–12. However, when she gave a *Superannuation contributions splitting application* to her super fund requesting that 85% of her 2011–12 employer contributions be split with Ken, her fund advised:

- they could not accept the application, because she was not permitted to split $25,500 (85% x $30,000) with Ken because this amount is more than the $25,000 concessional contributions cap
- they could accept a new application for a split of 83.33%, but they were required by law to report that $30,000 had been contributed for her
- she should seek professional advice about excess contributions tax.

Marita goes ahead with the 83.33% split. She later receives an assessment of excess contributions tax from us based on her concessional contributions of $30,000.

HOW DO YOU COMPLETE THIS APPLICATION?

Section A: Your details

Provide your details.

You don't have to provide your tax file number (TFN) to your super fund on this form, but it may help your super fund identify your account if you do.

If your super fund does not have your TFN, they cannot accept personal contributions (and other member contributions) and extra tax may be deducted from your employer contributions (and other assessable contributions).

Section B: Your fund's details

Provide the name of your super fund, the fund's Australian business number (ABN) and your member account number.

This information will help your super fund identify your account. Providing your super fund's ABN will help an administrator of a number of separate funds make sure they have the correct fund.

You will find your fund's ABN on your product disclosure statement or member statement. You can search for their details by visiting Super Fund Lookup at **superfundlookup.gov.au** or find it on your super fund's website. You can also phone your super fund to ask them for their ABN.

Section C: Your spouse's details

Provide your spouse's details – your spouse does not have to provide their TFN to **their** super fund. However, if the super fund does not have their TFN, the fund cannot accept personal contributions (and other member contributions), and extra tax may be deducted from employer contributions (and other assessable contributions).

Section D: Your spouse's fund details

Amounts cannot be transferred to a super account that has been closed, or to an account a pension is being paid from.

Your spouse can open a new account to receive the contributions and may need to complete a membership application to open a new account.

Provide the name of your spouse's super fund. Providing the fund's ABN will prevent confusion between funds with similar names and may allow electronic processing of the transfer.

Provide your spouse's member account number – this is the account the split contributions will be transferred to. If you do not provide the correct information, your spouse's super fund may not be able to accept the payment.

Section E: Contributions splitting details

Question 21
Financial year ending

Provide the financial year in which the super contributions were made to your account.

This must be either this current financial year or the previous financial year. You cannot apply to split contributions made to your account in any other financial year – see 'When can you apply to split your contributions?' on page 2.

For example, if you are applying in the 2012–13 financial year, the super contributions to be split must have been made on or after 1 July 2011.

Question 22
Taxed splittable contributions

Provide the amount or percentage of 'taxed splittable contributions' you received in the financial year that you want to transfer to your spouse.

See 'What contributions can be split?' on page 2 for the limits for 'taxed splittable contributions' and what contributions this category includes.

Question 23
Untaxed splittable employer contributions

Only complete this question if you are a member of a public sector super scheme that treats employer contributions as 'untaxed'.

Provide the amount or percentage of 'untaxed splittable employer contributions' you want to transfer to your spouse.

See 'What contributions can be split?' on page 2 for the limits for 'untaxed splittable employer contributions' and what contributions this category includes.

Section F: Your request and declaration

Read the declaration. Check that the information you provided in the application is correct before printing your full name and signing and dating the declaration.

Section G: Your spouse's declaration

Your spouse should read the declaration and check that they meet the age requirements before printing their full name and signing and dating the declaration.

Your super fund may ask for evidence to demonstrate that your spouse is either:

- less than 55 years old, or
- 55 to 64 years old and not retired.

Send this application to your super fund, not to us.

MORE INFORMATION

For information about whether your super fund allows contributions splitting, you must contact them.

For more information about super or to obtain copies of our publications:

- visit our website at **ato.gov.au**
- phone us on **13 10 20** between 8.00am and 6.00pm, Monday to Friday
- write to us at
  Australian Taxation Office
  PO Box 3100
  PENRITH NSW 2740

If you do not speak English well and need help from the ATO, phone the Translating and Interpreting Service on **13 14 50**.

If you are deaf or have a hearing or speech impairment, phone us through the National Relay Service (NRS) on the numbers listed below, and ask for the ATO number you need:

- TTY users, phone **13 36 77**. For ATO 1800 free-call numbers, phone **1800 555 677**.
- Speak and Listen users, phone **1300 555 727**. For ATO 1800 free-call numbers, phone **1800 555 727**.
- Internet relay users, connect to the NRS at **relayservice.com.au**

OUR COMMITMENT TO YOU

We are committed to providing you with accurate, consistent and clear information to help you understand your rights and entitlements and meet your obligations.

If you follow our information in this publication and it turns out to be incorrect, or it is misleading and you make a mistake as a result, we must still apply the law correctly. If that means you owe us money, we must ask you to pay it but we will not charge you a penalty. Also, if you acted reasonably and in good faith we will not charge you interest.

If you make an honest mistake in trying to follow our information in this publication and you owe us money as a result, we will not charge you a penalty. However, we will ask you to pay the money, and we may also charge you interest. If correcting the mistake means we owe you money, we will pay it to you. We will also pay you any interest you are entitled to.

If you feel that this publication does not fully cover your circumstances, or you are unsure how it applies to you, you can seek further assistance from us.

We regularly revise our publications to take account of any changes to the law, so make sure that you have the latest information. If you are unsure, you can check for more recent information on our website at **ato.gov.au** or contact us.

This publication was current at **February 2014**.

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PUBLISHED BY

Australian Taxation Office
Canberra
February 2014

JS 24870

Australian Government
Australian Taxation Office

Superannuation contributions splitting application

WHEN COMPLETING THIS FORM
- Print clearly in BLOCK LETTERS using a black pen only.
- Place X in ALL applicable boxes.

Section A: **Your details**

1 Tax file number (TFN)

You don't have to provide your TFN to your superannuation fund. However, if your superannuation fund does not have your TFN, they cannot accept personal contributions (and other member contributions) and extra tax may be deducted from your employer contributions (and other assessable contributions).

2 Full name

Title: Mr Mrs Miss Ms Other

Family name

First given name

Other given names

3 Address

Suburb/town

State/territory

Postcode

4 Date of birth Day / Month / Year

5 Sex Male Female

6 Daytime phone number (include area code)

7 Email address

Section B: **Your superannuation fund's details**

8 Fund's name

9 Australian business number (ABN)

10 Member account number

Section C: **Your spouse's details**

11 Tax file number (TFN)

You don't have to provide your TFN to your superannuation fund. However, if your superannuation fund does not have your TFN, they cannot accept personal contributions (and other member contributions) and extra tax may be deducted from your employer contributions (and other assessable contributions).

12 Full name

Title: Mr ☐ Mrs ☐ Miss ☐ Ms ☐ Other

Family name

First given name

Other given names

13 Address

Suburb/town

State/territory

Postcode

14 Date of birth Day / Month / Year

15 Sex Male ☐ Female ☐

16 Daytime phone number (include area code)

17 Email address

Section D: **Your spouse's superannuation fund details**

18 Fund's name

19 ABN

20 Member account number

Sensitive (when completed)

Section E: **Contributions splitting details**

21 Financial year ending

This must be either this current financial year or the previous financial year. You cannot apply to split contributions made to your account before the beginning of last financial year.

Day / Month / Year

30 / 06 / ____

22 Taxed splittable contributions

Write the amount or percentage that your spouse is to receive. It cannot be more than 85% of the contributions you made in this category or more than the concessional contributions cap for the financial year.

The contributions in this category include:

- employer contributions (including salary sacrifice contributions)
- personal contributions you have advised your fund you will claim as a tax deduction (for example, because you are self-employed).

Dollar amount $ ___,___.~~00~~ **OR** percentage __ %

23 Untaxed splittable employer contributions

Write the amount or percentage that your spouse is to receive.

These can only be employer contributions to your public sector superannuation fund that you are requesting be split with your spouse.

Dollar amount $ ___,___.~~00~~ **OR** percentage ___ %

Section F: **Your request and declaration**

I request that you split the contributions detailed in section E to the superannuation account of my spouse as detailed in section D. I declare that the information provided on this form is correct.

Name (Print in BLOCK LETTERS)

Signature

Date

Day / Month / Year

Section G: **Your spouse's declaration**

I declare that at the date of this application I am the spouse of the applicant and I am either:

- *less than 55 years old*
- *55 to 64 years old and not retired.*

Name (Print in BLOCK LETTERS)

Signature

Date

Day / Month / Year

Privacy

The ATO is a government agency bound by the *Privacy Act 1988* in terms of collection and handling of personal information and tax file numbers (TFNs). For further information about privacy law notices go to **ato.gov.au/privacy**

Send your completed application to your superannuation fund. You don't send this form to the ATO.

APPENDIX 5 – CAPITAL GAINS TAX CAP ELECTION FORM

Australian Government
Australian Taxation Office

Capital gains tax cap election

WHEN COMPLETING THIS FORM
You can complete this form electronically or with a pen.
If you choose to use a pen:
- Print clearly in BLOCK LETTERS, using a black pen.
- Place **X** in ALL relevant boxes.

You must give your signed and dated election to your super fund either with your contribution or before your contribution is made. It's not valid if the contribution has already been made.

Section A: **Your fund's details**

1 Fund's name

2 Australian business number (ABN)

3 Member account number

Section B: **Your details**

4 Tax file number (TFN)

The ATO does not collect the information provided on this form. This form is to assist you in providing details to your super fund. Your super fund is authorised to request your personal details, including your TFN, under the *Superannuation Industry (Supervision) Act 1993* (ie, s299E, 299F and 299G). It is not an offence to provide your TFN. However, if you do not provide your TFN, and your super fund doesn't already hold your TFN, they will not be permitted to accept the contribution covered by this election. For more information about your privacy please contact the entity you are providing this form to.

5 Full name

Title: Mr Mrs Miss Ms Other

Family name

First given name

Other given names

6 Address

Suburb/town

State/territory

Postcode

7 Date of birth Day / Month / Year

8 Daytime phone number (include area code)

Section C: **Payer details**

9 Name

10 ABN

11 Contact name

Title: Mr Mrs Miss Ms Other

Family name

First given name

Other given names

12 Contact phone number (include area code)

Section D: **Election**

This election is only valid for personal 'after-tax' contributions. If a payer is not acting for you and on your behalf the contribution may not be a personal contribution. For example, if your employer makes the contribution under an obligation to contribute for you it may be treated as an employer contribution and be counted towards the concessional contributions cap.

13 Election and amount

Place an **X** in the appropriate box to show the CGT concession(s) that applies to you. In each case provide the amount you choose to exclude from your non-concessional contributions cap because of your entitlement to the CGT concession.

Small business retirement exemption amount Provide amount $, , .

Small business 15-year exemption amount Provide amount $, , .

There are limits on the amounts you can claim. If you exceed them your election will not be effective. For details of these limits visit our website at **ato.gov.au** and refer to *CGT cap election*.

14 Is this election for a further contribution of a financial benefit from a look-through earnout right from an earlier CGT event? (See instructions)

Yes **No**

Financial benefits provided under look-through earnout rights must generally be made within 5 years of the end of the income year in which the CGT event occurred.

Section E: **Declaration**

Providing false or misleading information in this election may result in the ATO imposing an administrative penalty.

I declare, that:

- *the personal contributions for which this election is to apply will be made by me or on my behalf*
- *I am eligible for one or both of the following CGT concessions*
  - *the small business 15-year exemption*
  - *the small business retirement exemption*
- *I have met all the requirements of section 292-100 of the* Income Tax Assessment Act 1997 *to elect to have the contributions excluded from the non-concessional contributions cap.*

If the personal contribution for which this election is to apply is a financial benefit from a look-through earnout right and I would otherwise be ineligible to make this personal contribution into superannuation, then:

- I was under 65 years old when the underlying CGT event happened, or
- I was between 65 and 74 years old and gainfully employed for at least 40 hours in a period of not more than 30 consecutive days during the financial year in which the CGT event happened, and
- the amount of the contribution does not exceed my CGT cap amount.

Name (Print in BLOCK LETTERS)

Signature

Date

Day / Month / Year

Print form

Save form

Reset form

APPENDIX 6 – PRESERVATION COMPONENTS

APPENDIX 6- PRESERVED, RESTRICTED NON-PRESERVED & UNRESTRICED NON-PRESERVED COMPONENTS

As mentioned earlier, most superannuation benefits are ‘preserved’ until a member reaches preservation age and satisfies a condition of release.

A member may have a ‘restricted non-preserved’ benefit relating to contributions made by a member to an employer sponsored fund before 1st July 1999 if the member did not claim a tax deduction for that contribution. Restricted non-preserved benefits have an additional condition of release than preserved benefits which is when a member stops being employed by the employer sponsor of the fund. If a member has a ‘restricted non-preserved’ benefit of a retail or industry fund and has left the employment of the employer sponsor, before rolling over that fund into the SMSF, it would be beneficial for the member to inform the existing superannuation fund that they have changed employment so that the fund can record the component as ‘unrestricted non-preserved’ prior to rolling over the funds. Otherwise, upon rolling over the benefits, a separate condition of release will need to be met before the SMSF can pay out any benefits to the member as it is unlikely that the previous employer would be an employer sponsor of the SMSF.

Upon meeting a condition of release, the component will change from ‘preserved’ or ‘restricted non-preserved’ to ‘unrestricted non-preserved’. Unrestricted non-preserved benefits will include earnings in the pension phase, except transition to retirement pensions.

APPENDIX 7 – PAYG LUMP SUM PAYMENT SUMMARY

Australian Government
Australian Taxation Office

PAYG payment summary – superannuation lump sum

For important information see reverse of page.

You must complete all sections of this form. For help completing this form, visit our website at **ato.gov.au/paymentsummaries**

Payment summary for year ending 30 June ☐☐☐☐

If you are **amending a payment summary** you have already sent, place X in this box ☐

Section A: **Payee details**

Tax file number ☐☐☐ ☐☐☐ ☐☐☐

See reverse of page for information about tax file numbers.

Surname or family name

Given name(s)

Residential address

Suburb/town/locality

State/territory

Postcode

Date of birth (if known) Day / Month / Year

Section B: **Payment details**

Date of payment Day / Month / Year

TOTAL TAX WITHHELD $ ☐☐,☐☐☐,☐☐☐.~~00~~

Taxable component

Taxed element $ ☐☐,☐☐☐,☐☐☐.~~00~~

Untaxed element $ ☐☐,☐☐☐,☐☐☐.~~00~~

Tax-free component $ ☐☐,☐☐☐,☐☐☐.~~00~~

Place an X in the appropriate box for each field below.

Is this payment a death benefit? **No** ☐ **Yes** ☐

Type of death benefit Trustee of deceased estate ☐ or Non-dependant ☐

Section C: **Payer details**

You **must** also complete this section

Australian business number (ABN) or withholding payer number (WPN) ☐☐ ☐☐☐ ☐☐☐ ☐☐☐ Branch number ☐☐☐

Name (use the same name that appears on your activity statement)

Privacy – For information about your privacy visit our website at **ato.gov.au/privacy**

DECLARATION – *I declare that the information given on this form is complete and correct.*

Signature of authorised person

Date Day / Month / Year

Payee's copy

Sample only

NAT 70947-02.2014

ABOUT THIS PAYMENT SUMMARY

INFORMATION FOR PAYEES

Under the pay as you go (PAYG) withholding system, your super fund or payer withholds amounts from certain types of payments made to you and sends these withheld amounts to us.

Your super fund or payer must also provide you with a payment summary that shows the details of the payments made to you and the amounts withheld.

If this payment summary shows that tax has been withheld, you need to lodge a tax return with us for the year shown on the payment summary. If no tax is withheld, you may still have to lodge a tax return.

If you need to lodge a tax return, a credit for the tax withheld, shown on this payment summary, will reduce any liability raised in your assessment.

> There is no requirement for you to attach a copy of this payment summary to your tax return.

> You must keep all payment summaries you receive for five years, or two years if you are an Australian resident and have simple tax affairs (you can visit our website at **ato.gov.au** or contact us to see if this applies to you).

LODGING YOUR TAX RETURN

You can lodge:

- online at **ato.gov.au/etax**
- through a registered tax agent
- by mail.

AMENDED PAYMENT SUMMARY

If there is an error in the original payment summary provided to you, your super fund or payer must give you an amended payment summary. If this is the case, the amended payment summary box on the top of this form will be marked with an X.

If you have received an amended payment summary and have not yet lodged your tax return, use the information on the amended payment summary – not the original – to complete your return.

If you have already lodged your tax return and you then receive an amended payment summary, you may need to lodge an amendment to that tax return.

> If you want to know more about your payment summary, lodging your tax return, or lodging an amendment to your tax return, visit our website at **ato.gov.au** or phone **13 28 61** between 8.00am and 6.00pm, Monday to Friday.

TAXABLE COMPONENT

The taxable component of a super lump sum consists of two elements:

- the element taxed in the fund, and/or
- the element untaxed in the fund.

If you are under 60 years of age, the taxable components of super lump sums are assessable income and should be shown in your tax return.

If you are 60 years or over, only the element untaxed in the fund of the taxable component is shown in your tax return. The element taxed in the fund is not assessable income and is not shown in your tax return.

TAX-FREE COMPONENT

This is the amount of the super lump sum that is tax-free. It consists of the contributions segment and the 'crystallised' segment of the payment. The contributions segment consists of contributions made to your fund on or after 1 July 2007, which have not been included in the assessable income of your fund. The 'crystallised' segment consists of the following amounts as at just before 1 July 2007:

- the pre-July 1983 component
- the concessional component
- undeducted contributions
- the post-June 1994 invalidity component
- the capital gains tax (CGT) exempt component.

Tax free components of super lump sums are not required to be shown at any label on your tax return.

DEATH BENEFIT

A death benefit is a super lump sum paid to another person after a member has died. The payment may be made to a dependant, non-dependant or the estate of the deceased.

TAX FILE NUMBERS

The *Taxation Administration Act 1953* authorises your payer to ask you to provide your tax file number (TFN). While it is not compulsory to provide your TFN to your payer, they may have withheld at a higher rate if you did not. We will use your TFN to identify you in our records.

APPENDIX 8 – PAYG SUPER INCOME STREAM PAYMENT SUMMARY

Australian Government
Australian Taxation Office

PAYG payment summary – superannuation income stream

For important information see reverse of page.

You must complete all sections of this form. For help completing this form, visit our website at **ato.gov.au/paymentsummaries**

Payment summary for year ending 30 June ☐☐☐☐

If you are **amending a payment summary** you have already sent, place X in this box ☐

Section A: Payee details

Tax file number ☐☐☐ ☐☐☐ ☐☐☐

See reverse of page for information about tax file numbers.

Surname or family name

Given name(s)

Residential address

Suburb/town/locality

State/territory

Postcode

Date of birth (if known) Day / Month / Year

Section B: Payment details

Period during which payments were made Day / Month / Year **to** Day / Month / Year

TOTAL TAX WITHHELD $ ☐☐,☐☐☐,☐☐☐.00

Taxable component

Taxed element $ ☐☐,☐☐☐,☐☐☐.00

Untaxed element $ ☐☐,☐☐☐,☐☐☐.00

Tax-free component $ ☐☐,☐☐☐,☐☐☐.00

Tax offset amount $ ☐☐,☐☐☐,☐☐☐.00

Lump sum in arrears – taxable component

Taxed element $ ☐☐,☐☐☐,☐☐☐.00

Untaxed element $ ☐☐,☐☐☐,☐☐☐.00

Lump sum in arrears – tax free component $ ☐☐,☐☐☐,☐☐☐.00

Payee's copy

Sample only

Section C: Payer details

You **must** also complete this section

Australian business number (ABN) or withholding payer number (WPN)

Branch number

Name (use the same name that appears on your activity statement)

Privacy – For information about your privacy visit our website at **ato.gov.au/privacy**

DECLARATION – *I declare that the information given on this form is complete and correct.*

Signature of authorised person

Date Day / Month / Year

ABOUT THIS PAYMENT SUMMARY

INFORMATION FOR PAYEES

Under the pay as you go (PAYG) withholding system, your super fund or payer withholds amounts from certain types of payments made to you and sends these withheld amounts to us.

Your super fund or payer must also provide you with a payment summary each year that shows the details of the payments made to you and the amounts withheld during the year.

If this payment summary shows that tax has been withheld, you need to lodge a tax return with us for the year shown on the payment summary. If no tax is withheld, you may still have to lodge a tax return.

If you need to lodge an tax return, a credit for the tax withheld, shown on this payment summary, will reduce any liability raised in your assessment.

There is no requirement for you to attach a copy of this payment summary to your tax return.

You must keep all payment summaries you receive for five years, or two years if you are an Australian resident and have simple tax affairs (you can visit our website at **ato.gov.au** or contact us to see if this applies to you).

LODGING YOUR TAX RETURN

You can lodge:

- online at **ato.gov.au/etax**
- by phone, if you have simple affairs
- through a registered tax agent
- by mail.

AMENDED PAYMENT SUMMARY

If there is an error in the original payment summary provided to you, your super fund or payer must give you an amended payment summary. If this is the case, the amended payment summary box on the top of this form will be marked with an X.

If you have received an amended payment summary and have not yet lodged your tax return, use the information on the amended payment summary – not the original – to complete your return.

If you have already lodged your tax return and you then receive an amended payment summary, you may need to lodge an amendment to that tax return.

If you want to know more about your payment summary, lodging your tax return, or lodging an amendment to your tax return, visit our website at **ato.gov.au** or phone **13 28 61** between 8.00am and 6.00pm, Monday to Friday.

Sample only

TAXABLE COMPONENT

This is the total amount of the payment less the tax free component, and is used to calculate the amount of tax withheld from your payments. This amount may be comprised of an element taxed in the fund (or taxed element), an element untaxed in the fund (or untaxed element) or both and these amounts need to be included in your tax return.

TAX-FREE COMPONENT

This is the amount of the payment which is tax free. Tax free components of super income streams are not required to be shown at any label on your tax return.

TAX OFFSET AMOUNT

The tax offset amount may reduce the amount of tax you have to pay. This amount needs to be included in your tax return.

LUMP SUM IN ARREARS – TAXABLE COMPONENT

This amount is the taxable portion of a lump sum payment in arrears of a super income stream that accrued in earlier financial years. This amount may be comprised of an element taxed in the fund (or taxed element), an element untaxed in the fund (or untaxed element) or both and these amounts need to be included in your tax return.

LUMP SUM IN ARREARS – TAX FREE COMPONENT

The amount is the tax free portion of a lump sum payment in arrears of a super income stream that accrued in earlier financial years. There is no requirement to show this amount at any label on your tax return.

TAX FILE NUMBERS

The *Taxation Administration Act 1953* authorises your payer to ask you to provide your tax file number (TFN). While it is not compulsory to provide your TFN to your payer, they may have withheld at a higher rate if you did not. We will use your TFN to identify you in our records.

APPENDIX 9 – SAMPLE BINDING DEATH BENEFIT NOMINATION

Binding death benefit nomination

first state super

Use this form if you want to make a new lapsing or non-lapsing binding death benefit nomination for your accumulation account.

Please use a dark pen and CAPITAL letters, or type directly into this form online, print it and send it to us. Use (✗) to mark boxes. Forms are located on our website at **firststatesuper.com.au/forms**.

If you have any questions, please refer to the *Member Booklet Supplement: Nominating beneficiaries* on our website or call us on **1300 650 873**.

IMPORTANT!
We must receive a valid nomination in writing prior to death.

1. Your personal details

Member number

Account number F S S U

Date of birth

Title

Last name

Given name(s)

Address

Suburb

State

Postcode

Daytime contact number

Mobile number

M F

Email (for security reasons, please ensure that your nominated email address is your personal email address and not a role-based email address such as employee_title@company.com.au)

You MUST select ✗ either lapsing or non-lapsing.

2. Type of nomination

I would like my binding nomination to be: ☐ lapsing OR ☐ non-lapsing

3. Details of beneficiaries

IMPORTANT!
If you nominate more than one beneficiary and/or your legal personal representative, your nominations MUST add up to **100%**.

If you wish to nominate more than four beneficiaries, please provide the necessary beneficiary and witness details on another form or in a separate letter attached to this form.

You can nominate one or more beneficiaries and/or your legal personal representative. Please record the percentage of your benefit you would like to go to each. **IMPORTANT! We cannot accept forms that have alterations. If you make a mistake in this section please complete a new form.**

Beneficiary #1

Last name

Given name(s)

Title

M F

Date of birth (DD-MM-YYYY)

Relationship (cross ✗ one) ☐ Spouse/ de facto ☐ Child ☐ Financial dependant ☐ Interdependency relationship

% of benefit %

(see over for additional beneficiary nominations)

FSS Trustee Corporation (Trustee) ABN 11 118 202 672 AFSL 293340 **First State Superannuation Scheme** (Fund) ABN 53 226 460 365

3. Details of beneficiaries (continued)

Beneficiary #2

Last name

Given name(s)

Title M F Date of birth (DD-MM-YYYY)

Relationship (cross ✗ one) ☐ Spouse/de facto ☐ Child ☐ Financial dependant ☐ Interdependency relationship

% of benefit %

Beneficiary #3

Last name

Given name(s)

Title M F Date of birth (DD-MM-YYYY)

Relationship (cross ✗ one) ☐ Spouse/de facto ☐ Child ☐ Financial dependant ☐ Interdependency relationship

% of benefit %

Beneficiary #4

Last name

Given name(s)

Title M F Date of birth (DD-MM-YYYY)

Relationship (cross ✗ one) ☐ Spouse/de facto ☐ Child ☐ Financial dependant ☐ Interdependency relationship

% of benefit %

My legal personal representative

Your legal personal representative is the executor or the administrator of your estate.
We **do not** need a name or any other details.

% of benefit %

TOTAL NOMINATIONS 1 0 0 %

4. Privacy

The personal information you provide on this form is collected by and held for First State Super by the fund administrator, Pillar Administration, in accordance with the Australian Privacy Principles of the *Privacy Act 1988 (Cth)*, for the purpose of administering your account and providing you with services associated with your fund membership.

For further information about how your personal information is handled, please call us on 1300 650 873 or visit firststatesuper.com.au/privacy to view the privacy policy (a hard copy of the policy may also be provided on request). The policy contains information about how you may access and seek correction of your personal information, how you may complain about a breach of your privacy and other important information about how your personal information is collected, used and disclosed.

IMPORTANT!
You must sign and date this declaration in the presence of two witnesses, who must also sign and date the witness declarations ON THE SAME DAY AS YOU. The witnesses must be over the age of 18 and must not be beneficiaries nominated on this form.

5. Member and witness declarations and signatures

Member declaration

- I have read the information in this form and in the *Member Booklet Supplement: Nominating beneficiaries* and I understand the terms on which this nomination is made.
- This nomination will only be valid if the beneficiaries listed are my spouse, child, financial dependant, interdependent or legal personal representative of my estate when I die, and the nomination is signed by me in the presence of two witnesses who are 18 years of age or older and not listed as beneficiaries.
- I can amend this nomination by completing a new *Binding death benefit nomination* form.
- I can cancel my nomination by completing a *Binding death benefit cancellation* form.
- If this nomination is invalid or has not been received by First State Super when I die, my death benefit will be paid at First State Super's discretion as guided by superannuation law.
- My beneficiaries and I will be bound by the provisions of First State Super's trust deed, and that First State Super accepts no responsibility for the correct nomination of beneficiaries.
- I have read and understood the First State Super privacy policy.

Please sign and date form here.

Member signature

Date (DD-MM-YYYY)

This MUST be the same date that the form is witnessed

Witness declarations

I declare that I am over the age of 18 and this nomination was signed and dated by the member in my presence.

Witness 1

Name

Signature

Date (DD-MM-YYYY)

This MUST be the same date that the form is signed by the member

Address

Suburb

State

Postcode

Witness 2

Name

Signature

Date (DD-MM-YYYY)

This MUST be the same date that the form is signed by the member

Address

Suburb

State

Postcode

Send the form to this address.

6. Where to send your completed form

Return the completed form to **First State Super PO Box 1229 WOLLONGONG NSW 2500**. If you have any questions, please call us on **1300 650 873**.

Save form | Print form | Clear form

FSS Trustee Corporation (Trustee) ABN 11 118 202 672 AFSL 293340 **First State Superannuation Scheme** (Fund) ABN 53 226 460 365

Notes for completing the binding death benefit nomination form

Before you make a decision about making a death benefit nomination, you should read the current *Member Booklet Supplement: Nominating beneficiaries*. This supplement is available on our website or if you require a paper copy, please contact us and one will be mailed to you free of charge.

Forms are located on our website at **firststatesuper.com.au/forms**. You can type data directly into these forms, print them and send them to us. If you prefer to write on the forms, please use a dark pen and print clearly.

Only originals or certified copies of this form will be accepted. If you have more than one account, you must complete a separate death benefit nomination for each account. A binding nomination can only be cancelled by completing a *Binding death benefit cancellation* form and returning it to us.

Your personal details

Email address

The email address you provide will replace any email address we currently hold for you. For security reasons, please ensure that your nominated email address is your personal email address and not a role-based email address such as employee_title@company.com.au.

Type of nomination

Lapsing and non-lapsing nominations

A binding nomination can be either lapsing or non-lapsing. A lapsing binding death benefit nomination is valid for up to three years from the day after the date it was first signed, or last confirmed or amended. For the nomination to remain valid, you must confirm the nomination in writing every three years before the three-year period expires. We will send you a renewal notice shortly before the three-year expiry date so you can confirm your nomination. You must sign and date the confirmation but it does not need to be witnessed.

A non-lapsing binding death benefit nomination does not expire, so it does not need to be confirmed every three years. However, we will still send you a courtesy letter every three years to give you an opportunity to update the details of your nomination.

Details of beneficiaries

For the initial nomination to be valid, you must complete, sign and date this form correctly. The form must be signed and dated by two witnesses on the same date that you sign the form. The people you may nominate under a binding nomination must have been one or more of the following at the time the trustee pays the benefit:

- your spouse or de facto
- your children, including step, adopted and ex-nuptial children
- any person(s) financially dependent on you
- a person in an interdependency relationship with you
- your legal personal representative – the executor or administrator of your estate.

The total of your nominations (whether you make one or more nominations) MUST add up to 100%. Your nomination(s) will be invalid if the total is not 100%. No decimals are allowed. If, for example, you want to split your death benefit into thirds, you should round the split to the nearest whole percentage e.g. 33%, 33% and 34%.

You should ensure that you review your nomination when your personal circumstances change.

Member and witness declarations and signatures

You must sign and date this declaration in the presence of two witnesses, who must also sign and date the witness declarations ON THE SAME DAY AS YOU. The witnesses must be over the age of 18 and must not be beneficiaries nominated on this form.

FSS Trustee Corporation (Trustee) ABN 11 118 202 672 AFSL 293340 **First State Superannuation Scheme** (Fund) ABN 53 226 460 365
FSS048 08/16

APPENDIX 10 – SMSF TRUSTEE DECLARATION

Trustee declaration

To be completed by new trustees and directors of corporate trustees of self-managed super funds.

Read this declaration in conjunction with *Key messages for self-managed super fund trustees* at **ato.gov.au/smsfessentials**

NAT 71089-08.2014

Australian Government
Australian Taxation Office

Who should complete this declaration?

You must complete this declaration if you become a trustee or director of a corporate trustee (trustee) of:

- a new self-managed super fund (SMSF)
- an existing SMSF.

You must sign this declaration within 21 days of becoming a trustee or director of a corporate trustee of an SMSF.

A separate declaration is required to be completed and signed by each and every new trustee.

You must also complete the declaration if you:

- have been directed to do so by us
- are a legal personal representative who has been appointed as trustee on behalf of a:
  - member who is under a legal disability (usually a member under 18 years old)
  - member for whom you hold an enduring power of attorney
  - deceased member.

Information you need to read

Make sure you read *Key messages for self-managed super fund trustees* at **ato.gov.au/smsfessentials**. It highlights some of the key points from the declaration and some important messages.

Before completing this declaration

Before you complete and sign this declaration, make sure you:

- read each section
- understand all the information it contains.

If you have any difficulties completing this declaration or you do not fully understand the information it contains:

- speak to a professional adviser
- visit **ato.gov.au/smsf**
- phone us on **13 10 20**.

When completing this declaration

When you complete this declaration, remember to:

- insert the full name of the fund at the beginning
- sign and date it
- ensure it is signed and dated by a witness (anyone 18 years old or over).

What should you do with the declaration?

You must keep your completed declaration for at least 10 years and make it available to us if we request it.

We recommend that you keep a copy of your completed declaration and refer to it and the information in *Key messages for self-managed super fund trustees* when making important decisions, such as those relating to choosing investments, accepting contributions and paying benefits.

Do not send your completed declaration to us.

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You are free to copy, adapt, modify, transmit and distribute this material as you wish (but not in any way that suggests the ATO or the Commonwealth endorses you or any of your services or products).

Published by

Australian Taxation Office
Canberra
August 2014

JS 32597

Australian Government
Australian Taxation Office

Self-managed super fund trustee declaration

I understand that as an individual trustee or director of the corporate trustee of

Fund name

I am responsible for ensuring that the fund complies with the *Superannuation Industry (Supervision) Act 1993* (SISA) and other relevant legislation. The Commissioner of Taxation (the Commissioner) has the authority and responsibility for administering the legislation and enforcing the fund's compliance with the law.

I must keep myself informed of changes to the legislation relevant to the operation of my fund and ensure the trust deed is kept up to date in accordance with the law and the needs of the members.

If I do not comply with the legislation, the Commissioner may take the following actions:
- impose administrative penalties on me
- give me a written direction to rectify any contraventions or undertake a course of education
- enter into agreements with me to rectify any contraventions of the legislation
- disqualify me from being a trustee or director of a corporate trustee of any superannuation fund in the future
- remove the fund's complying status, which may result in significant adverse tax consequences for the fund
- prosecute me under the law, which may result in fines or imprisonment.

Sole purpose

I understand it is my responsibility to ensure the fund is only maintained for the purpose of providing benefits to the members upon their retirement (or attainment of a certain age) or their beneficiaries if a member dies. I understand that I should regularly evaluate whether the fund continues to be the appropriate vehicle to meet this purpose.

Trustee duties

I understand that by law I must at all times:
- act honestly in all matters concerning the fund
- exercise skill, care and diligence in managing the fund
- act in the best interests of all the members of the fund
- ensure that members only access their super benefits if they have met a legitimate condition of release
- refrain from entering into transactions that circumvent restrictions on the payment of benefits
- ensure that my money and other assets are kept separate from the money and other assets of the fund
- take appropriate action to protect the fund's assets (for example, have sufficient evidence of the ownership of fund assets)
- refrain from entering into any contract or do anything that would prevent me from, or hinder me in, properly performing or exercising my functions or powers as a trustee or director of the corporate trustee of the fund
- allow all members of the fund to have access to information and documents as required, including details about
  - the financial situation of the fund
  - the investments of the fund
  - the members' benefit entitlements.

I also understand that by law I must prepare, implement and regularly review an investment strategy having regard to all the circumstances of the fund, which include, but are not limited to:
- the risks associated with the fund's investments
- the likely return from investments, taking into account the fund's objectives and expected cash flow requirements
- investment diversity and the fund's exposure to risk due to inadequate diversification
- the liquidity of the fund's investments having regard to the fund's expected cash flow requirements in discharging its existing and prospective liabilities (including benefit payments)
- whether the trustees of the fund should hold insurance cover for one or more members of the fund.

Accepting contributions and paying benefits

I understand that I can only accept contributions and pay benefits (income streams or lump sums) to members or their beneficiaries when the conditions specified in the law and the fund trust deed have been met.

Investment restrictions

I understand that, as a trustee or director of the corporate trustee of the fund, subject to certain limited exceptions specified in the law, I am prohibited from:
- lending money of the fund to, or providing financial assistance to, a member of the fund or a member's relative (financial assistance means any assistance that improves the financial position of a person directly or indirectly, including the provision of credit)

- acquiring assets (other than business real property, listed securities, certain in-house assets and acquisitions made under mergers allowed by special determinations or acquisitions as a result of a breakdown of a relationship) for the fund from members or other related parties of the fund
- borrowing money (or maintaining an existing borrowing) on behalf of the fund except in certain limited circumstances (while limited recourse borrowing arrangements are permitted, they can be complex and particular conditions must be met to ensure that legal requirements are not breached)
- having more than 5% of the market value of the fund's total assets at the end of the income year as in-house assets (these are loans to, or investments in, related parties of the fund – including trusts – or assets subject to a lease or lease arrangement between the trustee and a member, relative or other related party)
- entering into investments that are not made or maintained on an arm's length (commercial) basis (this ensures the purchase or sale price of the fund's assets and any earnings from those assets reflects their market value).

Administration

I understand that the trustees of the fund must:

- keep and retain for at least 10 years
  - minutes of all trustee meetings at which matters affecting the fund were considered (this includes investment decisions and decisions to appoint members and trustees)
  - records of all changes of trustees, including directors of the corporate trustee
  - each trustee's consent to be appointed as a trustee of the fund or a director of the corporate trustee
  - all trustee declarations
  - copies of all reports given to members
- ensure that the following are prepared and retained for at least five years
  - an annual statement of the financial position of the fund
  - an annual operating statement
  - copies of all annual returns lodged
  - accounts and statements that accurately record and explain the transactions and financial position of the fund
- appoint an approved SMSF auditor each year, no later than 45 days before the due date for lodgment of the fund's annual return and provide documents to the auditor as requested
- lodge the fund's annual return, completed in its entirety, by the due date
- notify the ATO within 28 days of any changes to the
  - membership of the fund, or trustees or directors of the corporate trustee
  - name of the fund
  - contact person and their contact details
  - postal address, registered address or address for service of notices for the fund
- notify the ATO in writing within 28 days if the fund becomes an Australian Prudential Regulation Authority (APRA) regulated fund.

DECLARATION

By signing this declaration I acknowledge that I understand my duties and responsibilities as a trustee or director of the corporate trustee of the self-managed superannuation fund named on this declaration (or if the fund's name changes, that name). I understand that:

- *I must ensure this document is retained for at least 10 years or while I remain a trustee or director of the corporate trustee (whichever is longer) and, if I fail to do this, penalties may apply.*
- *I may have to make this document available for inspection by a member of staff of the ATO and, if I fail to do this, penalties may apply.*
- *I do not have access to the government's financial assistance program that is available to trustees of APRA regulated funds in the case of financial loss due to fraudulent conduct or theft.*

Trustee's or director's name

Trustee's or director's signature

Date
Day / Month / Year

Witness' name (witness must be 18 years old or over)

Witness' signature

Date
Day / Month / Year

SENSITIVE (when completed)

APPENDIX 11 – SAMPLE INVESTMENT STRATEGY

APPENDIX 11- SAMPLEINVESTMENT STRATEGY

Investment Strategy

The SMSF Investment Strategy is detailed below.

Investment Objectives

The objective of the Fund is to maximise benefits for the purposes of providing Retirement Benefits to the Fund Members in accordance with the Trust Deed governing the Fund's operations. The Investment Objectives which have been considered by the Trustees of the Fund in formulating the Investment Strategy include:

The Trustees will act prudently to pursue the maximum rate or return possible, subject to acceptable risk and diversification parameters.

The Trustees will take into account the number of years to retirement of the Members when considering investment options.

The Trustees will establish a tolerance within the Fund to short term fluctuations in income and capital values given the profile of the Member's ages.

The Trustees will have proper regard to the risks associated with the investments given the Fund's Objectives and cash flow requirements.

The Trustees will invest to ensure sufficient liquidity is retained within the Fund to meet benefit payments and other liabilities as they fall due.

The Trustees before investing in a particular asset will have proper regard to the balance between the risk and return, so as to maximise the rate of return on Members' entitlements subject to an appropriate level of risk.

Investment Review

The Investment Objectives of the Fund will be reviewed annually and at such other times as a significant event occurs which affects the Fund.

Investment Strategy

With regard to the investment objectives outlined above the Trustees have adopted to pursue an Investment Strategy aimed at accumulating over the long term some or all of the following asset classes:

- ASX Listed Securities
- ASX Listed and Exchange Traded Options

- ASX Listed Warrants
- International Listed Securities
- Australian and International CFDs
- Australian and International Managed Funds
- Cash
- Term Deposits
- Bonds
- Debentures
- Other Cash Based Investments
- Property Investment with or without borrowings
- Physical Metals and Commodities
- Foreign Exchange
- Other Assets that the Trustees consider appropriate to the extent permitted by the Trust Deed and Superannuation Law.

Percentage Investment Range

The Trustees consider that no specific range for each of the above asset classes should be adopted but each asset class should be considered on its own investment merits having regard to an appropriate degree of diversification.

Single Asset Investment Strategy

A single asset strategy may be adopted by the Fund if the asset proposed to be invested in is considered by the Trustees to satisfy a core purpose of the Fund's Investment Objectives and provided that the Trustees are satisfied that no other benefit (excepting incidental benefits) is conferred upon members or associated parties.

Arm's Length Basis

All investments by the Fund shall be on an arm's length basis and will be acquired, maintained or disposed of on commercial terms at market rates of returns.

Maximising Member Returns

The Trustees consider that this Investment Strategy will fulfil the principal objective of maximising member returns having regard to risk and is consistent with the investment objectives of the Fund.

Insurance

The Trustees have considered the insurance needs of the members of the fund. They have determined that it remains appropriate for the fund not to hold insurance policies for the members.

Date: ________________.

Trustee: ________________.

Signature: ________________.

Trustee: ________________.

Signature:

APPENDIX 12 – REQUEST TO ADJUST CONCESSIONAL CONTS.

Australian Government
Australian Taxation Office

Request to adjust concessional contributions

WHO SHOULD COMPLETE THIS FORM?

Only members of a self-managed superannuation fund (SMSF) can complete this form for contributions they made to their SMSF.

COMPLETING THIS FORM

The instructions contain important information

- Print clearly using a black pen only.
- Use BLOCK LETTERS and print one character per box.

! The instructions contain important information about completing this form. Refer to them for more information about how to complete and lodge this form.

Section A: **Your details**

1 Tax file number (TFN)

! You don't have to provide your TFN to us. However, if you do, it will help us identifiy you correctly and process your form quickly. For more information on privacy, refer to **ato.gov.au/privacy**

2 Full name

Title: Mr Mrs Miss Ms Other

Family name

First given name

Other given names

3 Date of birth Day / Month / Year

4 Current postal address

Street address

Suburb/town/locality

State/territory (Australia only)

Postcode (Australia only)

5 Daytime phone number (include area code)

Section B: **Self Managed Superannuation Fund Details**

The SMSF to which the concessional contributions to be adjusted were made:

6 What is your Australian business number (ABN)?

7 Fund name

Section C: **Details of the financial years in which concessional contributions will be adjusted**

8 Year 1 – The financial year in which the contributions referred to in Section D were **made** to the SMSF but not allocated to you:

Year ending 30 June

9 Year 2 – The financial year in which the contributions referred to in Section D were **allocated** to you by the SMSF's trustees:

Year ending 30 June

Section D: **Details of concessional contributions to be adjusted**

10 Personal Contributions – The amount of the personal contributions you made to the SMSF in Year 1, which were not allocated until Year 2, and for which you will be claiming a tax deduction in Year 1.

$, .

In the SMSF annual return for Year 1, these contributions will be included as 'assessable personal contributions' in Section B and as 'personal contributions' made by you in Section F or G.

11 Employer Contributions – The amount of the employer contributions, including salary sacrifice contributions, your employer made to the SMSF in Year 1 and which were not allocated to you until Year 2.

$, .

In the SMSF annual return for Year 1, these contributions will be included as 'assessable employer contributions' in Section B and as 'employer contributions' made on your behalf in Section F or G.

Sensitive (when completed)

Section E: **Declaration**

Privacy

The ATO is a government agency bound by the Privacy Act 1988 in terms of collection and handling of personal information and TFNs. For further information about privacy law notices go to **ato.gov.au/privacy**

Complete the declaration that applies to you. Print your full name then sign and date the declaration.

INDIVIDUAL DECLARATION

I declare that the information contained in this form is true and correct.

Name (Print in BLOCK LETTERS)

Signature

Date
Day / Month / Year

AGENT OR AUTHORISED OFFICER DECLARATION

complete this declaration if you are an authorised representative of the individual shown in Section A.

I declare that:

- *I have prepared the form with the information supplied by the individual*
- *I have received a declaration made by the individual that the information provided to me for the preparation of this statement is true and correct*
- *I am authorised by the individual to give the information in this form to the Australian Taxation Office.*

Signature

Date
Day / Month / Year

Tax agent number (if applicable)

Name of organisation (if applicable)

Agent or Authorised Officer name

Title: Mr Mrs Miss Ms Other

Family name

First given name

Other given names

Agent or Authorised Officer phone number (include area code)

Agent or Authorised Officer address

Street address

Suburb/town/locality

State/territory (Australia only)

Postcode (Australia only)

Lodging your form

Print form

Reset form

Post or fax your completed and signed form to:

- fax on **1300 139 024**
- mail to
  Australian Taxation Office
  PO Box 3578
  ALBURY NSW 2640

APPENDIX 13 – SEGREGATED VS UNSEGREGATED ASSETS

APPENDIX 13–SEGREGATED VS UNSEGREGATED ASSETS AND ALLOCATING EARNINGS & WITHDRAWALS TO TAX COMPONENTS

The body of this module's course notes include some information on segregated vs unsegregated assets. Below is further information in this area including allocating earnings and withdrawals to tax components.

Net earnings after expenses from assets funding a pension will be exempt from tax and this exemption is referred to as 'exempt current pension income'. SMSFs using the unsegregated assets method will need an actuarial certificate for each year they claim the exempt current pension income.

An actuarial certificate will not be required to claim exempt current pension income if the segregated assets method is used and at all times that pensions were payable during the financial year, the SMSF only paid allocated pensions, market-linked pensions or account-based pensions, and no other type of pension. However, under the segregated assets method, an actuarial certificate will be required if the SMSF pays a different type of income stream or the market value of the pension exceeds the account balance supporting the benefit.

Where an SMSF has more than one member or where one member has more than one account, trustees must allocate any investment returns and expenses between the various members and accounts in a fair way. Any realised capital losses associated with a member's pension account cannot be used to offset realised capital gains from an accumulation account.

If each member's accounts are segregated, such investment earnings and many of the SMSF expenses may be easily differentiated between each account, although this may be more difficult for unsegregated accounts.

For example, where an SMSF has unsegregated assets and there are two members, the trustees may apply any earnings and administration and investment expenses to each member's accounts in accordance with their respective member balances. Where an expense clearly relates to one member's account, such as insurance premiums, those expenses can be applied to that particular member's account to adjust that member's balance. Similarly, any rollovers, contributions or pension payments into or out of a particular member's account can be applied to that account.

Where SMSF assets are invested in a portfolio comprising more than one member's account balance, trustees should consider the timing of transactions such as contributions and withdrawals to derive at a fair allocation of earnings between members' accounts.

Example 1

The XYZ Super Fund has two members, Jim and Jenny. As at 30th June 2012, their SMSF was valued at $500,000, of which each member's balance was $250,000. At that time, their respective balances were therefore 50% each. Jim contributes $100,000 to the SMSF on 2nd July 2012 and Jenny does not make any contributions during the 2012/13 financial year. If the SMSF generates $30,000 net earnings during the year, Jim's proportion of the combined earnings would be higher than 50% as a result of his contribution early in that year. However, if Jim made the contribution on 30th June 2013, approximately 50% of the earnings would be attributable to both Jim and Jenny.

Example 2

The ABC Super Fund is a sole member fund where the member is Robert. Robert has two accounts in the ABC Super Fund – an accumulation account which is worth $30,000 and a pension fund which is worth $400,000 at the start of the financial year.

The earnings and withdrawals associated with the pension account will need to be fairly determined as the earnings will be exempt from taxation and any increase or decrease in the pension balance will be apportioned across the tax-free and taxable components based on the pro-rata component percentages which applied upon the commencement of the pension.

No such earnings exemption will apply for the earnings attributable to the accumulation account. The earnings and contributions attributable to the accumulation account will need to be fairly determined to be added to the taxable component and to get appropriately assessed for tax purposes.

If the ABC Super Fund applies a segregated investment method, the expenses and income from each account can be easily determined and applied.

However, if the ABC Super Fund applies an unsegregated investment method, the average value of the pension assets out of the average value of the total SMSF assets during the course of the year will generally be applicable for determining the percentage of the earnings which will be exempt from tax (i.e. relating to the pension), whilst the residual will be allocated to the accumulation account and taxed accordingly.

Earnings, pension payments and "commutations" (lump sum withdrawals) on any pension component will be allocated in accordance with the taxable and tax-free proportions which applied at the commencement of the pension. For the accumulation account, earnings will be allocated to the taxable component, whilst any commutations will be proportioned between the taxable and tax-free components based on the pro-rata proportions at the time of withdrawal. Any contributions will be allocated to either the taxable component (e.g. concessional contributions) or tax-free component (e.g. non-concessional contributions) depending on the type of contribution being made.

APPENDIX 14 – SMSF AUDIT COMPLIANCE

Appendix 14 – SMSF audit compliance section

This is a summary of the SISA provisions which an auditor must consider for compliance purposes. It has been extracted from the ATO form NAT11466 –Self-managed superannuation fund independent auditor's report.

Section or Regulation	Explanation
S17A	The fund must meet the definition of an SMSF
S35AE	The trustees must keep and maintain accounting records for a minimum of five years
S35B	The trustees must prepare, sign and retain accounts and statements
S35C(2)	The trustees must provide the auditor with the necessary documents to complete the audit in a timely and professional manner; and within 14 days of a written request from the auditor
S62	The fund must be maintained for the sole purpose of providing benefits to any or all of the following: • fund members upon their retirement • fund members upon reaching a prescribed age • the dependants of a fund member in the case of the member's death before retirement
S65	The trustees must not loan monies or provide financial assistance to any member or relative at any time during the financial year
S66	The trustees must not acquire any assets (not listed as an exception) from any member or related party of the fund
S67	The trustees of the fund must not borrow any money or maintain an existing borrowing (not listed as an exception)
S67A & 67B	The fund must comply with the limited recourse borrowing arrangement rules when borrowing to purchase single acquirable asset or replacement assets (not listed as an exception to the borrowing rules)

S82-85	The trustees must comply with the in-house asset rules
S103	The trustees must keep minutes of all meetings and retain the minutes for a minimum of 10 years
S104	The trustees must keep up to date records of all trustee or director of corporate trustee changes and trustee consents for a minimum of 10 years
S104A	Trustees who became a trustee on or after 1 July 2007 must sign and retain a trustee declaration
S105	The trustees must ensure that copies of all member or beneficiary reports are kept for a minimum of 10 years
S109	All investment transactions must be made and maintained at arms-length – that is, purchase, sale price and income from an asset reflects a true market value/rate of return
S126K	A disqualified person cannot be a trustee, investment manager or custodian of a superannuation fund
Sub Reg 1.06 (9A)	Pension payments must be made at least annually, and must be at least the amount calculated under Schedule 7
Reg 4.09	Trustees must formulate, regularly review and give effect to an investment strategy for the fund
Reg 4.09A	The assets of the SMSF must be held separately from any assets held by the trustee personally or by a standard employer sponsor or an associate of the standard employer sponsor
Reg 5.03	Investment returns must be allocated to members in a manner that is fair and reasonable
Reg 5.08	Member minimum benefits must be maintained in the fund until transferred, rolled over, allotted (to the member's spouse) or cashed out in a permitted fashion
Reg 6.17	Payments of member benefits must be made in accordance with Part 6 or Part 7A of the regulations and be permitted by the trust deed

Reg 7.04	Contributions can only be accepted in accordance with the applicable rules for the year being audited
Reg 8.02B	When preparing accounts and statements required by subsection 35B(1) of SISA, an asset must be valued at its market value
Reg 13.12	Trustees must not recognise an assignment of a super interest of a member or beneficiary
Reg 13.13	Trustees must not recognise a charge over or in relation to a member's benefits
Reg 13.14	Trustees must not give a charge over, or in relation to, an asset of the fund
Reg 13.18AA	Investments in collectables and personal use assets must be maintained in accordance with prescribed rules