

maintaining pensions post super reforms





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Changes to ECPI calculations and Actuarial Certificates

...and other current ECPI issues.



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...and other current ECPI issues.

with Andy O'Meagher
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One of the most common issues with ECPI calculations



Insufficient Pension Benefits paid in the Income Year (failure to meet the minimum Pension requirements)

The ATO position:

Google “pension minimum not met” one of the first things to show up is a link to the

ATO website: [SMSFs: Minimum pension payment requirements – FAQs](#)

The ATO used to be OK with the ‘catch up’ method until about 5 – 6 years ago.

Not anymore:

‘Can the trustee record the underpayment of the pension as an ‘accrual’ in the accounting records of the fund?’

No, for a trustee to meet the minimum pension payment standards they must meet the payment requirements both in form and effect.’



Failure to meet Pension Min.



If a fund **fails to meet the minimum pension payment requirements** in an income year, the super **income stream will be taken to have ceased at the start of that income year** for income tax purposes.



From the start of the income year the account is no longer supporting a super income stream. Any payments made in the year must be considered as super lump-sum payments for both income tax and SIS Regulations purposes.

If the relevant rules are again complied with in a following income year, this results in the commencement of a new pension. The trustee will need to revalue assets at market value and recalculate the minimum pension payment required at the start of the new pension.



Exceptions to Pens. Min. rule?



The Commissioner of Taxation can make an exception if:

- 1 Honest mistake (small underpayment) or out of the Trustees control
- 2 Entitlement to ECPI would have continued but for failure to meet minimum
- 3 Catch-up payment *is* made in the subsequent year (when oversight noticed)
- 4 Min payment would have been met if that catch-up was in previous income year
- 5 Catch-up payment is treated as if it were in previous income year

AND

Small underpayment is no more than one-month of pension benefits (1/12th of minimum)

Trustee has not previously applied this exception

i.e. This is a 'one-off' for each Trustee over the life of the SMSF

Apply to Commissioner for exception if necessary.



What should administrators do?



Not allow Superannuation Funds to just 'catch-up' in the following income year.

Ensure that Trustees are made aware of:

- Annual pension drawdown requirements
- Tax consequences of failing to meet these
- The fact that the onus is on the Trustees



Are **you** doing the right thing?

Help Trustees apply to the Commissioner to grant an exception if those conditions were met.

NOT apply for an actuarial certificate treating a pension account as being in retirement phase when they know that the minimum was not met.



What are Act2 doing?



- Don't immediately issue certificate if Minimums not all met.
- Contact the client for clarification on the circumstances.
- Point out the FAQ section of ATO website for reference.
- Issue certificate on the basis of pension commutation 1st July.
- Recommend the administrator/Trustees discuss with auditor
- If auditor recommends just catching up in next year...

...happy to recommend they find a new auditor 😊



Legislative/Regulatory Changes



Eligibility to claim ECPI using the Segregated Method [s295-387]

Beginning from 1 July 2017, an SMSF will be ***unable to use the segregated assets method for claiming ECPI*** in a given financial year if all of the following circumstances are satisfied:

- At any time during the given financial year there is **at least one superannuation interest supporting retirement phase** within the SMSF
- Just prior to the start of the given financial year, a member within the SMSF has a **Total Superannuation Balance that exceeds \$1.6 million** and they are also a **recipient of a retirement phase income stream** (where it is inside or outside the SMSF), and
- At any stage during the financial year in question, **the same member holds a superannuation interest** (accumulation or retirement phase) **within the SMSF.**



Using the Segregated Method



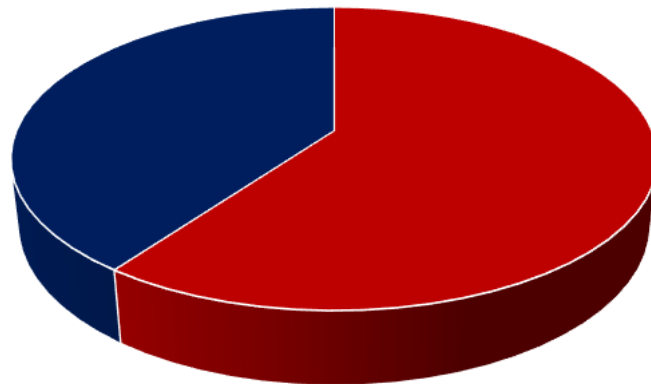
Eligibility to claim ECPI using the Segregated Method

What is the Segregated Method (segregated assets method)?

Essentially allocating or 'tagging' specific assets as being solely for the purpose of supporting a Retirement Income Stream.

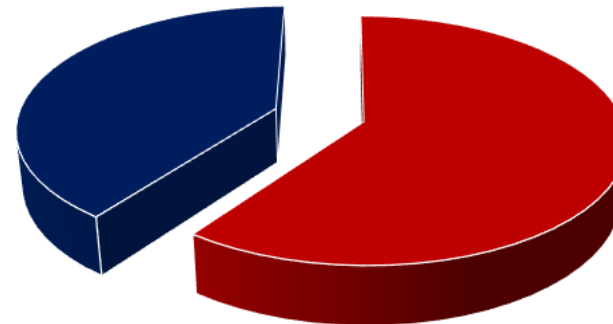
This separates those Pension Assets from any Accumulation Assets and earnings are easily identified as being 100% tax exempt.

Unsegregated (pooled) Assets



■ Pension ■ Accumulation

Segregated Assets



■ Pension ■ Accumulation

Legislative/Regulatory Changes



Eligibility to claim ECPI using the Segregated Method

What impact on the Superannuation Fund?

Most significant when there is a combination of Pension & non-Pension Accounts with segregated assets.

If cannot use Segregated Method to claim ECPI, then, if claiming ECPI, must use the Unsegregated Method, and obtain subsequent actuarial certificate s295-390.

Great news for actuarial certificate providers, not so great for affluent retirees.

Main purpose of this change – to prevent Trustees from playing switcheroo with assets between Pension & Accumulation Phase.

However – 100% Pension will also require certificate!



ATO Changes to ECPI calculations

Are you ready for this???

Deemed Segregation

For actuarial certificates prepared for the 2017/18 year onwards, the ATO have enforced a change to the calculation approach for the Unsegregated Method.

Any period during the income year where the Superannuation Fund holds ONLY Retirement Phase accounts (Pensions), this period is to be known as a **Deemed Segregation Period (DSP)** and ECPI on earnings received within this period must be claimed using the Segregated Method (assuming eligible to do so).

The '**period**' can be as small as just one day and as large as the entire financial year. If the DSP is less than the entire year and the Unsegregated Method is used to claim ECPI for the Unsegregated Periods, a single Actuarial Certificate is required to support the ECPI claim.



Deemed Segregation



So, for a fund where there is at least one period during the year with all balances being in 'pension phase' and at least one period where there is a combination of pension and accumulation phase balances (non-zero), claiming exemption from income tax won't be as simple as just obtaining an actuarial certificate.

A certificate must be obtained that uses transaction data from the Unsegregated Period/s to calculate a single percentage, this percentage is to be ***applied only to the income received outside of the DSP/s***. Earnings received during any DSPs must be exempted using the Segregated Method (i.e. entirely tax exempt).

All periods of the income year (other than any Deemed Segregated Periods) must be used in the calculation of the tax exempt percentage and that percentage must be applied to all earnings **received** during those Unsegregated Periods.

Effectively the calculation is performed by **excluding** data from the DSPs.



Deemed Segregation

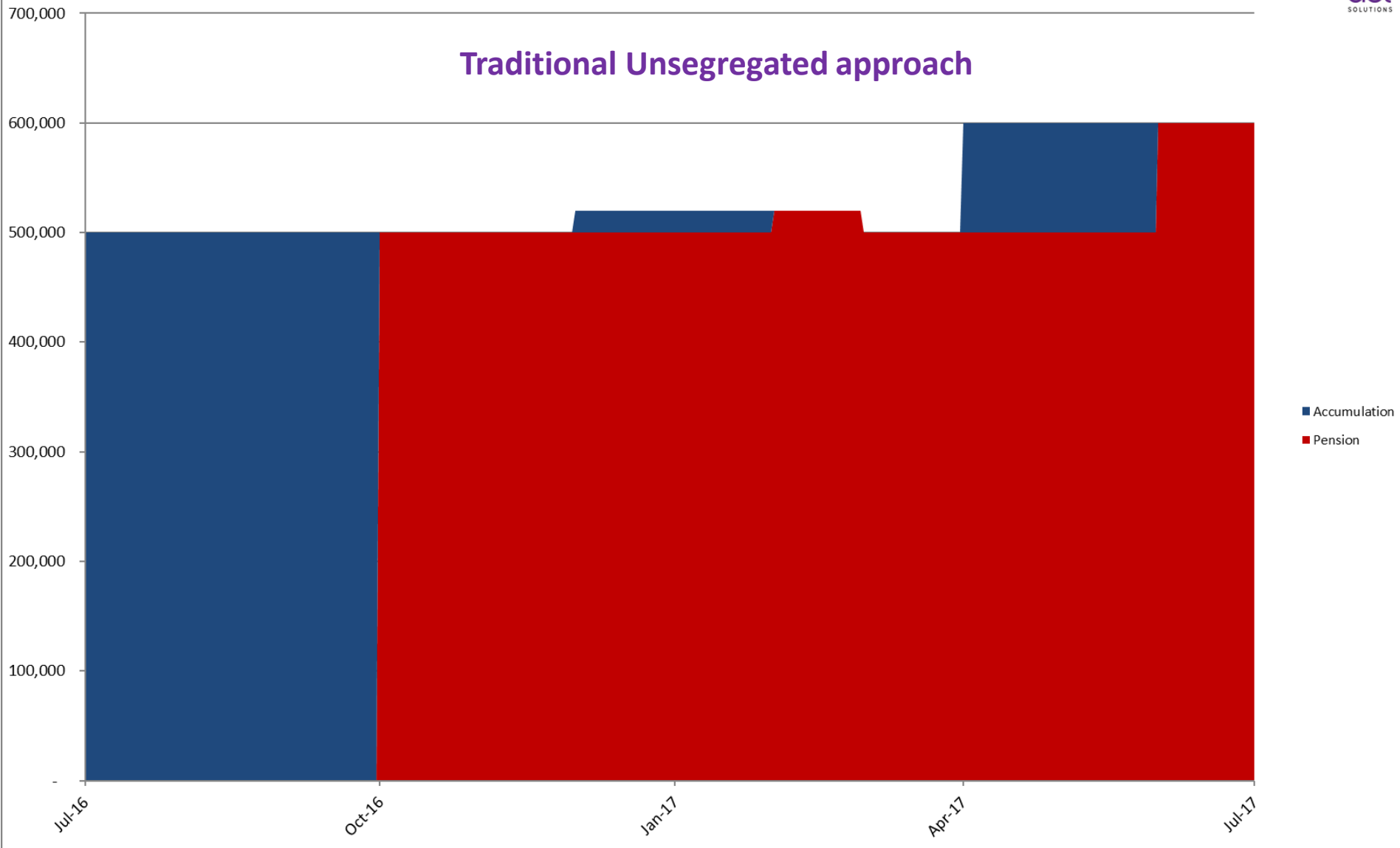
Example

- Single member Fund, \$500K in Accumulation at 1st July
- 1st October – converts entire balance to Retirement Phase (starts pension)
- 1st December – Contributes \$20K
- 1st February – converts that \$20K to Retirement Phase (starts new pension)
- 1st March – takes out \$20K in Pension Benefits
- 1st April – Transfers In \$100K from external Superannuation Fund
- 1st June – converts that \$100K to Retirement Phase (starts new pension)

Reasonably straightforward, let's see what happens.



2016/17 Account Balances for Whole Fund



Tax exempt percentage = 72.420%
Applies to all income received in the 2016/17 year



2016/17 Account Balances for Whole Fund

Deemed Segregation approach



Tax exempt percentage = 53.553%
Applies to income received outside of DS Periods
Income received during DSPs is fully exempt



Example

If earnings received during the year are:

- 10K in share distributions during the 'fully pension' periods (DSPs)
- 10K in share distributions outside of the DSPs
- 15K interest from Term Deposit on 20th June
- 5K in other earnings *distributed evenly throughout the year*

Old method

\$40K x 72.420% = \$28,968 exempted, so \$11,032 is taxable @15% = \$1,655 tax

New method

\$10K x 0% (segregated)

\$10K x 53.553% = \$5,355.30 exempted, so \$4,644.70 is taxable @15% = \$696.70

\$15K x 0% (segregated)

\$5K x 7/12 (unseg for 7 months) x 53.553%, so \$1,354.70 @15% = \$203.21

Total of \$899.91 (\$900) in income tax payable.

What if TD matured outside of the DSPs?

Extra \$1,045 in tax payable.



CGT Example

What if an asset is sold during the year realising a capital gain of \$40K?

Old method

\$40K x 72.420% = \$28,968 exempted, so \$11,032 is taxable @15% = \$1,655 tax

New method

Depends on the timing of the realisation of the gain.

If gain is realised during a Deemed Segregation Period – **fully exempted**.

If gain is realised outside of the DSP, **income tax percentage is applied** per usual.

\$2,787 in CGT payable

Don't forget Capital Losses!

Can carry forward using Unsegregated method.



Timing becomes significant



The two different approaches use different timing techniques.

Unsegregated method

With the calculation of the tax exempt percentage, we're looking at the timings of when the income was *earned*.

Segregated method

The segregated method works with the timing of the *receipt* of the income.

Example – Segregation by Default

With the DSP approach it's now a combination of these two methods.

The difference is quite significant. This means that Deemed Segregation potentially opens the way for strategies.



New requirements



NOTE ALSO:

Those Superannuation Funds where they are not eligible to use the Segregated Approach to claim ECPI (i.e. at least one member with a TSB in excess of \$1.6m and receiving a Retirement Phase Income Stream) will NOT use the Deemed Segregation Method.

These funds will have to have an actuarial certificate determining the income tax exemption on the full income year (as we're used to).

Significantly, this also includes those funds that are ***entirely in Pension Phase for the full year***, they will require an actuarial certificate stating the income to be 100% exempt from income tax if fund is ineligible to use segregated method.



Act2 Solutions... what do we do?



We provide Actuarial Certificates with:

- A simple, efficient and accurate process
- Competitive prices (\$120 +GST)
- Fast turnaround times (15 mins)
- Support (phone and email)



We donate quarterly to worthy causes.
(local, national & international charities)

We are currently developing an updated version of our Web Interface with member area & other features.

Fully integrated with BGL, Class and SuperMate

Give the Act2 Team a call or drop us an email.





The Act2 Team



Come and see me today to find out more...



Thank you for your time and attention



TRIS to the
retirement phase

Converting a TRIS to the retirement phase

- ATO view that TRIS always a TRIS

“Our view is that the current law does not facilitate an ‘auto conversion’ of a TRIS to a different or new pension or income stream. The same TRIS continues on and remains a TRIS until such time as it ‘ceases’.

Super changes – Frequently asked questions (QC 51875)
<https://www.ato.gov.au/Individuals/Super/In-detail/Super-changes---FAQs/#Transitiontoretirementincomestreams>

Maintaining pensions post super reforms

Converting a TRIS to the retirement phase

- To move to the retirement phase must satisfy requirements in subsection 307-80(3) of ITAA 1997:

Nil cashing restriction satisfied	Requirement
Retirement	Meet condition and notify the trustee
Terminal Medical Condition	
Permanent Incapacity	
Attains age 65	Meet condition only

TRIS to the retirement phase

Written notice

- Constructive notice or knowledge is **not sufficient**
 - important step to complete before qualifying for tax exemption, but also prevents transfer balance credit from arising before the trustee is ready
- Written notice is more than simply meeting a condition of release – the law requires notification, which can be made by the member or LPR of the member
- Importantly, reference to the Deed that would authorise the TRIS to enter retirement phase

TRIS to the retirement phase

Governing Rules

- Rule 25.1(c) – Accessing Member Superannuation Benefits

- Specific benefits payable by the Trustee of the Fund

c) Subject to the Fund maintaining its complying status, Where the member has commenced a Transition to Retirement Income Stream and subsequently meets a nil cashing restriction, they may request the Trustee to:

i) shift the Transition to Retirement Income Stream into Retirement Phase in accordance with the Superannuation Laws and continue to pay the Transition to Retirement Income Stream in accordance with the original terms and conditions of the Superannuation Income Stream; or

ii) convert such income stream to an Account Based Pension as a replacement superannuation income stream and upon the Trustee so agreeing, there shall be a deemed commutation and rollback of the Transition to Retirement Income Stream to a new and separate replacement superannuation income stream as an ordinary Account Based Pension in Retirement Phase made in compliance with the Superannuation laws.

← Move the TRIS to a TRIS(RP)

← Replace the TRIS to an ABP via commutation and rollover



[TRIS to Retirement Phase docs](#)

TRIS to the retirement phase

TRIS rules

- Within the TRIS definition (SISR 6.01) the 10% maximum pension 'falls away' where a CoR with nil cashing restriction has been satisfied
- Be wary of pension documents and deeds that may 'hard wire' the maximum pension (e.g. definition of TRIS includes 10% maximum)
 - May need to update deed to remove any specific TRIS requirements

Member-directed investments

Member-directed investments

Active pension account

- Member choice is still available post 1 July 2017
- Allows for separate 'pools' of investments to be created for different purposes
 - Different risk profiles and/or different timeframes for different members
 - Different pensions & accumulation profiles of accounts belonging to a member
 - Overall investments must be within the SMSF investment strategy
 - May need multiple investment strategies, which may cause unnecessary complication for the fund

Member-directed investments

Active pension account

(-)'s of maintaining separate investment pools	(+) 's of maintaining separate investment pools
Administration complexity & higher costs	Value of assets supporting pension liabilities can exceed TBC
Negative investment returns which are not a TBA debit	Potential higher ECPI % (where must use proportionate method) if assets in pension pool grow faster than accumulation assets
Resulting reduction in proportion of total SMSF assets supporting pension liabilities for ECPI calculations	Can use segregated method for tax also?

Member-directed investments

Active pension account

(-)'s of maintaining separate investment pools	(+)'s of maintaining separate investment pools
Value of assets support pension liabilities larger than TBC only lasts while member is alive	Both growth & income relating to assets in the pension pool are not a credit against TBA
Valuation methods of assets more closely scrutinised by ATO	Not penalised for good investment performance whilst pension is still alive

Member-directed investments

Active pension account

- Minimum pension payment based on value of pension assets at 30 June each year, not value of credit against TBC
- Value for pool of assets supporting pension liability of particular member must be paid out of SMSF if in excess of relevant TBC on member's death
- Artificial segregation of pension assets using multiple SMSFs will be regarded as potentially tax avoidance by ATO
 - Rationale for decision in multiple SMSFs