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Pensions – Getting them right

The implications of the new financial year

July 2021

But first…. You need to know

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AGENDA

- Impact of indexation on Transfer Balance Caps
- Meeting minimum pension rules
- Maintaining your pension account balance
- When a pensioner dies

Impact of indexation on Transfer Balance Caps

Indexation of the Transfer Balance Cap (TBC)

- General transfer balance cap (TBC) was introduced on 1 July 2017 at $1,600,000
- First time since introduced TBC is indexed by $100,000 to $1,700,000 from 1 July 2021
- Entitlement to indexation is proportional for anyone who has already commenced a pension based on highest proportion of TBC used
- If all the TBC was used prior to 1 July 2021 then no entitlement to indexation

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Indexation of the Transfer Balance Cap (TBC)

- If Larry has not commenced a retirement phase pension prior to 1 July 2021 then his TBC is $1,700,000

- If Harry commenced a retirement phase pension on 1 April 2020 with $1,200,000 then on 1 July 2021 his TBC is $1,625,000

- If Gary commenced a retirement phase pension on 1 April 2020 with $1,200,000 and commuted $100,000 from his pension on 1 December 2020 then on 1 July 2021 his TBC is $1,625,000 even though his TBA is $1,100,000

Meeting the minimum pension standards

Meeting minimum pension rules

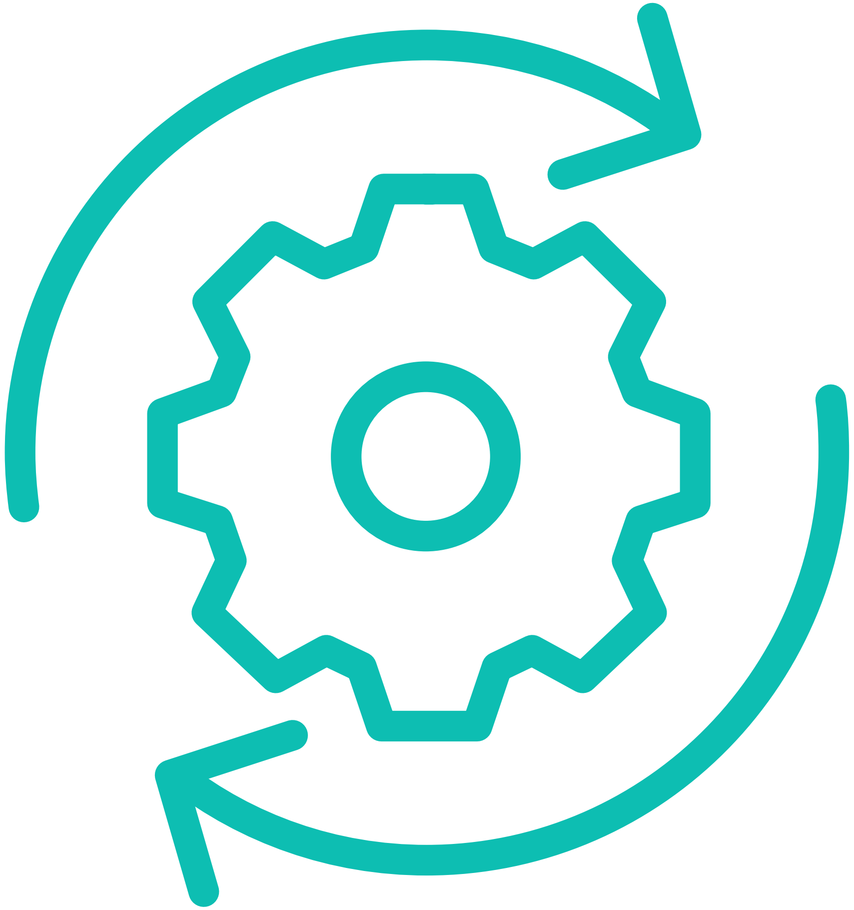
If the minimum pension payment level is not met there can be serious consequences

- Pension is deemed to not exist for full financial year – No exemption on tax on earnings
- Payments to member treated as lump sums not pensions - major issue for transition to retirement pensions
- Transfer Balance Account debit value at date pension fails the standards – end of year not beginning
- Possible administrative penalties for trustees $4,440 ($222 per penalty unit)

Note for 2021/22 the minimum is reduced by 50% for account-based pensions

Pension shortfalls

- If the minimum pension payment shortfall is small , there can be a catch up made in the next year
- Only available once per fund on self assessment
- Shortfall must represent no more than 1/12th of a particular pension’s shortfall
- If it occurs again then needs to be due to reasons outside trustee's control, and trustee must apply to ATO for discretion



Maintaining your pension account balance

Maintaining pension balances

- Since 1 July 2017, a $1.6 million Transfer Balance Cap (TBC) has been imposed
- Purpose of the cap is to limit the amount of superannuation that will produce Exempt Current Pension Income (ECPI)

- Pension purchase prices are measured against TBC on commencement
- Earnings and pension payments do not affect the TBC
- Lump sum transactions from pension accounts reduce Transfer Balance Account

Clients with a single pension

For clients taking the minimum amount the key thing is to ensure the minimum is met

- If not, payments become lump sums & fund will not be able to claim Exempt Current Pension Income (ECPI) for the financial year
- May be able to use shortfall rule once

For clients taking more than the minimum how are these payments treated

- All as pension payments but total pension payments must meet minimum or
- Some as pension payments up to the minimum and lump sums for the balance
- Lump sums but member must elect prior to payment

Let's consider

- Natasha is age 60 and commenced an Account Based Pension with $1.6 million
- She intends to draw $100,000 per annum over the next five years and has no other money in superannuation
- The fund is expected to achieve a 6% return over that period
- How should the payments be treated?

Natasha's pension account

Year	Account Balance	Return @ 6%	Min Pension	Extra Drawing	Account Balance	Transfer Balance Account Alternatives	
Yr 1	$1,600,000	$96,000	$64,000	$36,000	$1,596,000	$1,600,000	$1,564,000
Yr 2	$1,596,000	$95,760	$63,840	$36,160	$1,591,760	$1,600,000	$1,527,840
Yr 3	$1,591,760	$95,506	$63,670	$36,330	$1,587,266	$1,600,000	$1,491,510
Yr 4	$1,587,266	$95,236	$63,490	$36,510	$1,582,502	$1,600,000	$1,455,000
Yr 5	$1,582,502	$94,950	$63,300	$36,700	$1,577,452	$1,600,000	$1,418,300
						All wdls = pension pmts	Wdls = min pension pmts + partial com

Nominating drawings over the pension minimums as lump sum drawdowns will enable potential future pension top ups.

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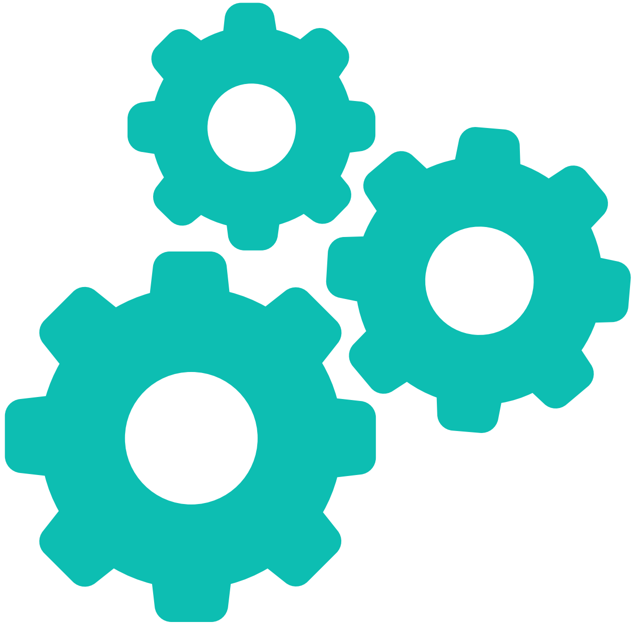
Clients with a single pension

TBAR requirements

- Pension payments not reported
- Partial commutations TBAR event – quarterly or annually

Documentation requirements

- Satisfy minimum pension before any lump sums?
- Prospective lump sum instruction
- Standing instruction possible?



Clients with multiple pensions

For clients taking the minimum amount the key thing is to ensure the minimum is met

- If not, payments become lump sums & fund will not be able to claim Exempt Current Pension Income (ECPI) for the financial year
- May be able to use shortfall rule once

For clients taking more than the minimum how are the payments treated

- Which pension should the excess amount be drawn from?
  - Consider tax free proportion, death benefit beneficiary, pre-1 January 2015 grandfathering rules
  - Lump sums but member must elect prior to payment

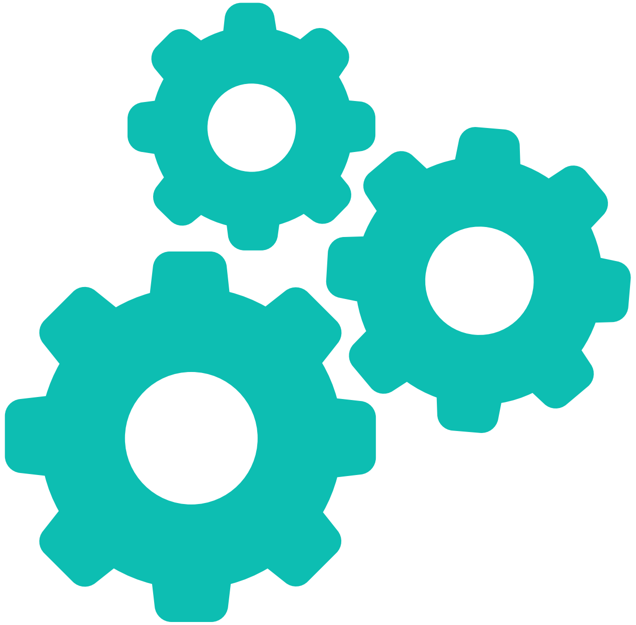
Clients with a multiple pensions

TBAR requirements

- Pension payments not reported
- Partial commutations TBAR event – quarterly or annually
- TBAR needs to identify pension account

Documentation requirements

- Satisfy minimum pension before any lump sums?
- Prospective lump sum instruction
- Standing instruction possible?



Clients with multiple accounts

For clients with a pension and an accumulation account

If only taking the minimum amount the key thing is to ensure the minimum is met

- If not, payments become lump sums & fund will not be able to claim Exempt Current Pension Income (ECPI) for that pension in the financial year
- May be able to use shortfall rule once

For clients taking more than the minimum how are the payments treated

- pension payments but total pension payments must meet minimum or
- Lump sums but member must elect prior to payment
- Order of treatment may change ECPI calculation

Let's consider

- Bruce, aged 60 is the only member of his SMSF
- has an account-based pension on 1 July 2018 of $1.6 million and an accumulation balance of $400,000

- Bruce draws $80,000 each year from his superannuation fund
- Needs to draw minimum amount from pension account
- What about the balance - from pension account or accumulation account

- Does order of payments matter?

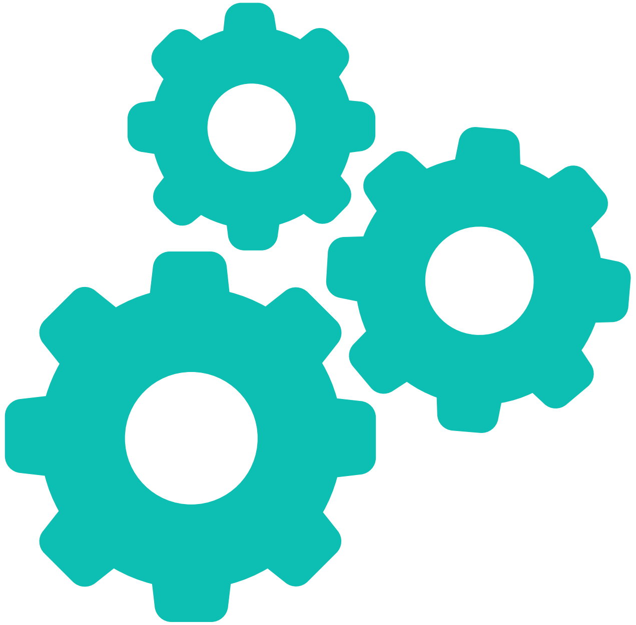
Clients with multiple accounts

TBAR requirements

- Pension payments not reported
- Partial commutations TBAR event – quarterly or annually
- Lump sums from accumulation accounts not reported

Documentation requirements

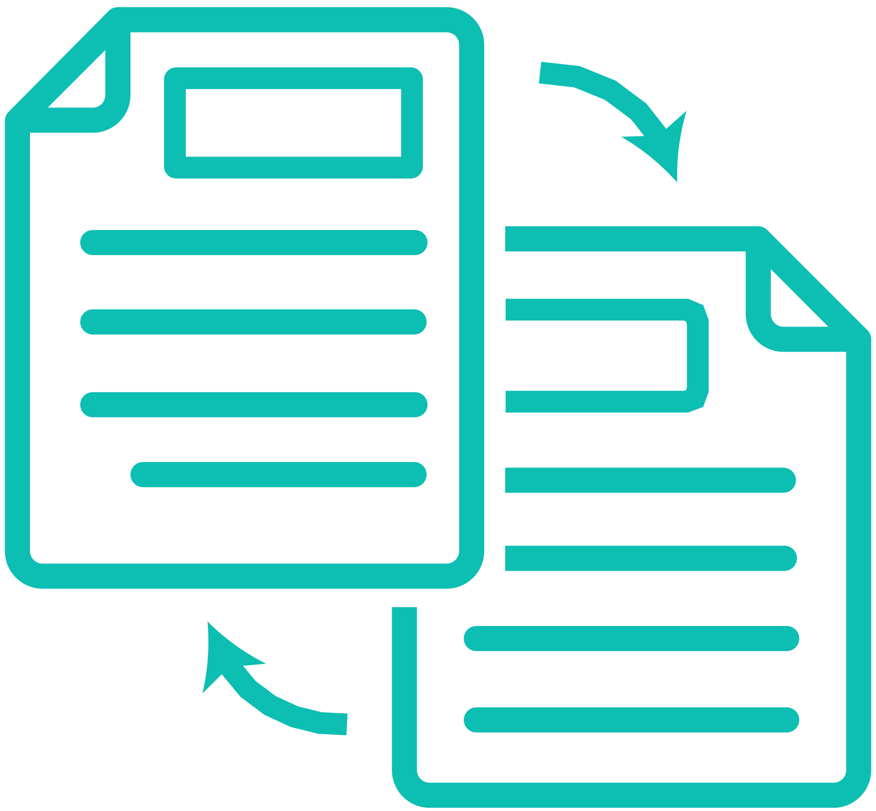
- Satisfy minimum pension before any lump sums?
- Prospective lump sum instruction
- Standing instruction possible?



When a pensioner dies

Death benefit pensions

- Reversionary pensions paid to nominated dependants automatically on the death of a deceased member in pension phase
- Death benefit pensions to allowed dependants based on trustee & dependent agreement where the deceased was in pension phase
- Death benefit pensions to allowed dependents based on trustee & dependent agreement where the deceased was in accumulation phase



Key issues

- Reversionary pension must meet the minimum payment as based on prior 1 July and is not recalculated on death
- Other death benefit pensions calculate minimum on commencement and deceased does not need to have met minimum payment in year of death

- If the minimum pension level is not met for any death benefit pension (reversionary or non-reversionary) then
  - it cannot be rolled back to accumulation phase,
  - the fund will lose the ECPI exemption from the start of the financial year, and
  - the benefit must be paid out as a lump sum superannuation death benefit

Let's consider

Peter Parker

- Account based pension on 1 July 2019 worth $1.8 million – was $1.6 million at 1 July 2017 for TBC
- Pension is Reversionary to his spouse Mary Jane
- Also has an accumulation account of $1 million

Mary Jane Parker

- Account based pension on 1 July 2019 worth $1.9 million – was $1.6 million at 1 July 2017 for TBC
- Pension is Reversionary to her spouse Peter
- Also has an accumulation account of $500,000

Let's consider

- Peter dies on 1 November 2019

- Mary Jane becomes entitled to his pension as an automatic reversion
- Death is a compulsory cashing event so Peter's benefits must be paid

- What are Mary Jane's options?

Option 1 - maintain her pension

- Mary Jane could decide to maintain her pension
- As such she has no capacity under her TBC
- She would be obliged to withdraw ALL of Peter's superannuation including his pension as a lump sum death benefit
- This would leave Mary Jane with
  – Pension account with $1.9 million
  – Accumulation account with $500,000
  – $2.8 million outside of superannuation

Option 2 - commute her pension

- Mary Jane could commute her pension and transfer it to her accumulation account
- She would have capacity under her TBC to maintain Peter's pension
- She could also take part of Peter's accumulation as a non-reversionary death benefit pension
- She would withdraw the balance of Peter's accumulation account as a lump sum death benefit
- This would leave Mary Jane with
  - Reversionary Pension account with $1.8 million
  - Non-reversionary pension account of $100,000
  - Accumulation account with $2.4 million
  - $900,000 outside of superannuation

Mary Jane’s Transfer Balance Account

DATE	TRANSACTION	DEBITS	CREDITS	TRANSFER BALANCE ACCOUNT	MEMBER PENSION BALANCE 1 July 2019
1/7/2017	Pension value @ 1/07/2017		$1,600,000	$1,600,000	$1,900,000
1/11/2019	Commutation of pension	$1,900,000		-$300,000	0
1/11/2019	New account based death benefit pension		$100,000	-$200,000	$1,800,000
1/11/2020	Pension value @ 1 July 2019 (Peter’s reversionary pension)		$1,800,000	$1,600,000	$1,900,000
1/11/2019	Accumulation phase (not counted for TBA purposes)			-	$2,400,000

Mary Jane withdraws Peter’s death benefit of $900,000 as a lump sum

Event based reporting concerns

- Reversionary pension is reported effective the date of death but counts 12 months after date of death
- Non-reversionary pension counts from date pension commences
- Commutation are reported effective date taken

BUT

- Watch out for your reporting cycle – commuting close to the 12-month death date may still result in an excess determination being issued!!

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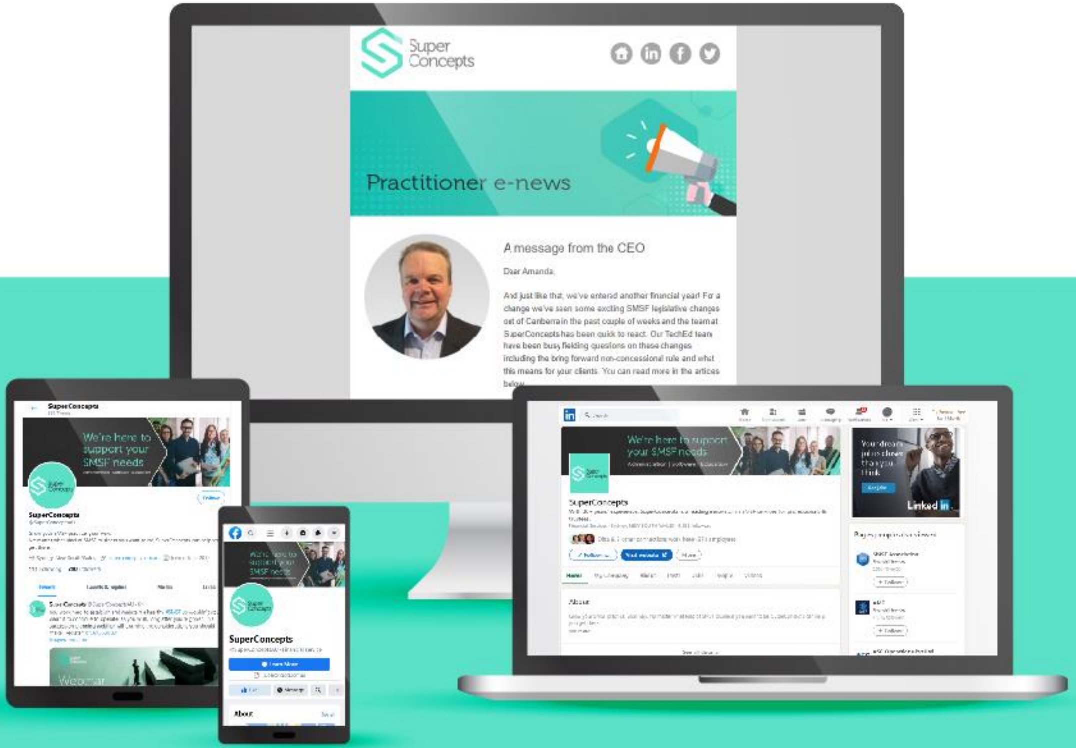

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