Unlocking the door to your pension access

TONY NEGLINE

Pension access is in the headlines in the lead-up to the federal budget on May 12.

It's worth covering how it all works: the rules for accessing super are different and depend on your age. Understanding these rules and how they work has always been important especially for people approaching retirement.

Once you're aged at least 65 you can do whatever you like with your superannuation even if you're working full-time. That is, you can use some or all of it to pay you a pension or take it all out as a lump sum.

Some people claim the longstanding ability to take lump sums from super represents a potential moral hazard. In particular some people will take all their money out of super, waste it on consumables and then head-off to the Centrelink Office to claim the full aged pension: this is the key reason there has been an escalating political debate about both superannuation lump sums and pension access in the last few weeks.

It's true that new retirees are keen to enjoy their new found freedom and travel in Australia and abroad. They might also use some of their super pay off their mortgage and other debts, renovate their home or update their motor vehicle and home furnishings.

But use all of their super savings? Yes, this definitely happens in some cases but in my experience it's rare. Only a minority find that ready access to a large amount of money is something they haven't experienced before and it burns a hole in their pocket.

Most retirees recognise that full aged pensioners aren't particularly well off, retirement might last many years and retirement homes for later infirm years probably have to be funded. These people — who are alert to so-called "longevity risk" watch their pennies.

That said it's unusual when retirees don't seek to access to some government aged pension. At the very least they want the Commonwealth Seniors Health Card. To beat the pension's income and assets tests some will renovate their home because it's fully exempt from these tests.

What about access to super before you reach 65? If you ceased work on or after you turned 60 years of age then full access to your super is immediately allowed. Note you don't have to fully stop work. You just need to stop one job.

A super fund will need proof that you have ceased employment. APRA regulated super funds will typically ask you to sign a declaration. Some of these funds will ask you to execute a statutory declaration. For self-managed super funds you should keep some relevant documentation, such as an appropriately dated exit letter from an employer, in your records.

If you ceased work before you had your 60th birthday then you have to pass two tests before you can access to your super money as a lump sum.

Firstly you must be aged at least your "preservation age". For anyone born before July 1960, that means at least age 55.

For those born during the 1960-61 financial year, their preservation age is 56. This increased preservation age, which was first mooted 23 years ago, takes effect on July 1.

Secondly you must be able to satisfy your super fund trustee that you've ceased work and never intend to work again for more than 10 hours per week. Again APRA regulated super funds will want a signed declaration. If you run your own super fund then you need documentary proof that you've stopped work and that your intention is not to work again.

By making this declaration, can you never return to work? The key issue is your frame of mind when you make the statement.

This doesn't mean your life won't change at some future point in time.

In relation to making these declarations about ceasing work and your future intentions it's important not to be cute.

Super monies accessed illegally can be taxed at the highest marginal tax rate. In addition remember that under our tax laws you have to prove your statements are correct. That is, the burden of proof lies with you. Also SMSF trustees can be fined for these super law breaches.

Once you hit your preservation age then you can elect to take your super money as a Transition to Retirement pension.

A key feature of these pensions is that lump sums aren't allowed until the above access rules are satisfied.

Tony Negline is author of The Essential SMSF Guide 2014-15.

Four ideas better than cash

With rates set to stay lower for longer it may be time to act

ELIZABETH REDMAN

If the RBA's Glenn Stevens endorses a further cut to 2 per cent next month another lift in the share market is likely

Interest rates are at the lowest level in a generation and could fall even further. Whatever slight tweaks the Reserve Bank makes to the official cash rate in the immediate future, interest rates — and returns on term deposits — appear likely to remain at historically low levels for some time.

But don't panic: there are opportunities for savvy investors to take advantage of lower interest rates.

The Australian share market has soared this year on the back of the February cut in rates to 2.25 per cent, which spurred some savers to switch money out of cash into equities in search of better yields. If RBA governor Glenn Stevens endorses a further cut to 2 per cent next month, as most observers expect, another lift in the share market is likely.

In this environment, retirees may want to consider how much of their portfolio to keep in cash. It makes sense to be able to easily cover living expenses, and to be prepared for emergencies such as health issues. Cash is a simple way to do this — but it's also very costly.

Consider an investor keeping $100,000 in cash. The average grossed up dividend yield for the ASX200 is about 6 per cent, meaning that money could be earning a return of $6000 a year in equities. On the average deposit rate of 2.7 per cent, that money would only earn $2700 in a year, leaving the investor some $3300 worse off.

So, what is an investor to do? Here's four potential strategies:

- An investor holding large amounts of cash for liquidity may wish to consider using a credit card with a 55-day interest-free period to manage spending instead. Of course, this is a strategy that requires discipline. It would not make sense to incur the interest rates of 20 per cent or more that credit cards can attract. But used wisely, credit cards could play a role in reducing the cash balance an investor needs.

- Investors who are dissatisfied with the rates of return available on term deposits and savings accounts might be interested to investigate peer-to-peer lending. A number of operations in Australia are targeting wholesale and retail investors, who lend cash to creditworthy borrowers for personal loans. The lenders' platforms remove the traditional middleman of the big banks, offering cheaper debt to borrowers and rates of return of up to 10 per cent for lenders. Despite the impressive track records of many P2P lenders in ensuring savers receive their principal back with interest, any capital placed on the platform is still at risk, in contrast to the government guarantee on bank deposits of up to $250,000.

- For more aggressive investors who take an optimistic view of markets, it might be worth considering whether it's time to borrow to fund investments. Many property investors negatively gear and Prime Minister Tony Abbott has in recent days ruled out any changes to these arrangements. Although property markets have risen strongly over the last two years, there will always be individual suburbs and properties offering better value. Low interest rates make property investment more attractive, although the key question for investors is not whether debt will become even cheaper, but whether a property investment is a good quality option that suits an investor's personal circumstances.

It's also possible to borrow to negatively gear in shares, both inside and outside a self-managed super fund. Again, this is a strategy for investors who are comfortable with debt and who take a bullish view of equity markets. It also makes more sense for investors with a long-term view, keeping in mind that the Australian share market has been the best performing in the world over the past century. Before implementing a gearing strategy, it makes sense to consider how and when to repay borrowings in the future. It's also worth examining products such as protected equity loans, which allow an investor to borrow to buy shares, knowing that if the price of an individual share falls, the investor can hand the share back to the lender to satisfy the loan and not owe money.

- When gearing, investors could also use a "debt recycling" strategy. This involves making extra mortgage repayments of a certain amount, then borrowing that same amount to invest in shares. Over time, homeowners can pay down a mortgage, keep their level of debt constant and accumulate a share portfolio. Steady capital growth would mean the investment portfolio is worth more than the loan by the time the mortgage is repaid, while the share investments provide franking credits to reduce taxable income. The risks are evident — steadily rising share markets are never certain.

If you're considering any complex strategies, seek advice. But with interest rates likely to stay lower for longer, it's worth acting sooner rather than later.

DIY funds' cars must stay in the garage as tax office drives collectables changes

MONICA RULE

Accumulating collectables in a DIY superannuation fund has been a marvellous dimension to personal investing in recent years and a boon to the local art market.

Unfortunately, the rules are about to change for most people most of the time. It does not mean you can't have collectables — such as vintage cars, rare books, wine or stamps in your DIY fund any longer. But it does mean that the acquisition and storage process has changed dramatically, not to mention the paperwork around this aspect of investment, which has now increased.

"Why is this so?" you ask.

The sole purpose of superannuation is to provide retirement and ancillary benefits to members. By investing in and enjoying a collectable or personal use asset, SMSF members gain a pre-retirement benefit that went against the spirit of the sole purpose test.

So, the superannuation law was tightened from 1 July 2011, so that any collectables and personal use assets acquired by an SMSF from this date onwards cannot be used by members or leased to members of the SMSF. Not only that, these assets cannot be stored in a private residence of the members. The trustees of the SMSF must document their decision on where the assets are stored and keep their documented decision for 10 years. On top of that, trustees have to take out insurance for these assets within seven days of their SMSF acquiring them.

However, the government did provide a five-year transitional period for SMSFs that acquired these assets prior to July 1, 2011. These SMSFs do not have to comply with the new restrictions until July 1, 2016. What this means is if you are currently enjoying these items, come July 1, 2016, you will have to comply with the new requirements of storing the items somewhere else apart from your residence and take out insurance on them, if you haven't already done so. You can also no longer lease them from your SMSF.

What happens if you don't comply with the new restrictions?

Non-compliance with the law is an offence that can result in a fine of $1700. Not only that, the tax office can also take other compliance actions on you and your SMSF.

So don't leave things to the last minute. You need to start thinking about whether you want to put plans in place to comply with the superannuation law requirements or sell these assets. If you decide to purchase these assets from your SMSF yourself, then you will need to do so at the market rate prior to July 1, 2016. If you purchase them from your SMSF on or after July 1, 2016, you will need to have them independently valued prior to the purchase.

There has been strong resistance from the art market to these new changes and understandably many in the collectables business are upset with what they regard as tough new regulations. Nonetheless, for collectors who really are specialists and really understand the nature of collectable investments, the ability to invest through a DIY fund is still distinctly possible. But for others, in less than 15 months this type of investment will be something that can no longer by enjoyed.

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FLOAT WATCH

Soccer brand ready to boot up

XPD SOCCER GEAR GROUP LTD
ASX Code: XPD
Shares on Offer: 75 million
Listing Price: $0.20
Market Capitalisation: $85 million
Listing Date: May 12

TIM MORRIS

Is soccer in Australia undervalued relative to other sporting codes?

In terms of TV rights, the sport's current circa $40 million-a-year deal with Foxtel and SBS trails behind the circa $200m-a-year deal currently enjoyed by the AFL, and rugby league, as well as Cricket Australia's $100m-a-year Big Bash League.

Relatively weaker match attendances may be a factor. The A League commands just under 14,000 attendees a match, which is in striking distance of the NRL (16,000), but well short of the AFL (33,000) and Big Bash League (23,000).

However, venue takings fail to recognise the sport's grassroots qualities.

In terms of participation, soccer ranks ahead any other team sport in the country, and more than the other football codes combined.

> Venue takings fail to recognise the sport's grassroots qualities

The sport's ability to command high levels of grassroots engagement is driving the coming listing of XPD Soccer Gear Group.

The sporting goods manufacturer is principally involved in the production and sale of football boots.

Established in 1992, its manufacturing and marketing operations are exclusively focused on China, featuring in 1900 retail outlets.

Proceeds from its initial public offer are scheduled to facilitate an expansion of its manufacturing capacity and increased marketing activities.

The company has increased sales and profits for the past three consecutive financial years, and a planned doubling of its manufacturing capabilities has the potential to extend the trend.

While its growth record and expansion plans are attractive qualities, new investors should not overlook regulatory and transparency risks associated with XPD's China operational base.

The company has not issued any forecasts regarding the payment of dividends and regulated capital controls in China may constrain its capacity to do so.

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