Super caps looming

DIY SUPER

Monica Rule

People with more than $1.6 million in their superannuation pension account have a lot of decisions to make before July 1.

The new $1.6 million transfer balance cap will place a limit on pension accounts in the retirement phase that receive tax-free investment earnings.

If you have more than $1.6 million in your pension account, you must either retain the excess in your accumulation account (where the investment earnings are taxed at a maximum of 15 per cent) or withdraw the money.

If the excess is not removed, your pension will be deemed as not being a pension from the start of the financial year. You will lose the tax exemption and the amount you receive will be treated as a lump sum superannuation benefit instead of a pension.

SMSF members, currently receiving a transition-to-retirement income stream (TRIS), will also lose the tax exemption on earnings from assets supporting their pensions from July 1. These assets will be treated as being in the accumulation phase with earnings taxed at 15 per cent. Once a member turns 65 or fully retires, their TRIS will become an ordinary account-based pension and will count towards the $1.6 million limit.

IMPORTANT CONSIDERATIONS

- Members under 60 with multiple pensions need to consider whether to commute the pension with the higher taxable component to minimise the tax on their pension income.
- Members with a pension which commenced before January 1, 2015, need to decide whether they wish to preserve their entitlements to the age pension and the Commonwealth Seniors Healthcare Card.
- If a member is withdrawing the excess amount from their SMSF, then they need to weigh up the benefit of the $18,200 tax-free income threshold and their marginal tax rate compared with the 15 per cent superannuation tax rate.
- The new reduced contribution limits may make future contributions more difficult.
- Members must decide whether to maintain assets with unrealised capital losses at their original cost base, and reset the cost base of assets with big gains.

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SMSF members who are currently receiving a TRIS or who have retirement pensions in excess of $1.6 million can apply for capital gains tax relief on their pension assets.

The CGT relief is not automatic and their SMSF will need to make an irrevocable election, in the tax office's approved form, before the 2016-2017 tax return is lodged.

The relief deems an asset to be sold on June 30 for its market value and repurchased at that price. This ensures only gains from July 1 onwards will be taxed.

If the CGT relief is applied and an SMSF asset was segregated prior to November 9, 2016, then the entire capital gain arising from the segregated assets will be disregarded.

If an SMSF uses the unsegregated method (because it has assets that support both a pension account and an accumulation account) then the notional capital gain on the non-exempt portion will be included in the SMSF's assessable income for 2016-2017.

SMSF members also need to be aware that by choosing the CGT relief, they must wait a further 12 months before the CGT discount can be claimed on the elected asset.

If there are plans to sell assets soon, it may be more tax effective not to apply the relief due to the 12 month waiting period to claim the CGT discount.

You have to consider whether choosing the CGT relief will produce the best tax result.

For example, if a member is within the $1.6 million cap and will retire soon, it means their SMSF will wholly convert to pension mode.

Applying the relief to an asset may cause the SMSF to be taxed on the deferred notional capital gain when the asset is sold.

If the relief was not chosen, this tax may not arise as the pension's earnings exemption would otherwise apply.

Monica Rule is an SMSF specialist and author of The Self Managed Super Handbook – monicarule.com.au

Time the big ally for DIY funds

Self-employed personal trainer Sherree Rylands is proof that DIY superannuation isn't for everyone.

She plans to close her self-managed super fund after nine years of stagnant performance.

Ms Rylands, below, opened the fund in 2008 because she wanted to take control of her retirement savings but found she didn't have the necessary expertise and couldn't dedicate the time required.

A former nurse, Ms Rylands said she attended financial courses, read about stockmarkets, kept abreast of changes in the regulatory landscape and stayed informed about stockmarket and economic developments.

While pleased with the education experience gained, her returns have been disappointing because of the lack of time she could dedicate to managing the fund, and the high audit and accounting fees (more than $3000 last year).

"If someone asked for advice I would tell them a SMSF takes a lot of time, so it's not something to do if you do not have the expertise or are time-poor," she said.

Ms Rylands will shift her assets into a managed fund with Australian-Super once the SMSF has been closed.

Important decisions if moving out of your SMSF

Michael Ward

There are some vital components that I implore people to consider if they are thinking of making the transition from SMSF to an industry fund or a platform.

These include understanding the latest Federal Government updates including pension draw-down requirements, investment portfolios and the impact the global financial crisis that we seem to have all forgotten about can have on "bucket portfolios", estate planning and the cost comparison of this transition.

Bucket portfolio's are typically labelled balanced or growth, etc and, while they usually include a well diversified approach across shares, property, bonds and cash, clients are unable to specify where their pension income payments should be paid from.

Each dollar of pension income payment made is drawn proportionately from each investment sector. The biggest devastation I witnessed during the financial crisis was to clients who were in these bucket portfolios and while they were simple, they were bleeding capital losses as markets tumbled.

Having the ability to draw income payments from specified sectors is vital and needs to be carefully considered against simplicity. Most platforms and even industry funds allow you to select a portfolio of investments rather than bucket funds.

Other important items that are usually missed are the estate planning consequences. A well established SMSF provides incredible control to ensure funds are distributed as the trustee wishes.

Some platforms and more specifically industry funds do not offer non-lapsing binding death benefit nominations or reversionary nominations.

This is more significant than most people take for granted. If the death benefit nomination is not binding then the trustee of the fund has the discretion to pay the death benefits (super balance) how they see fit.

This does not provide a great deal of peace of mind to the member.

If the nomination isn't non-lapsing then usually every three years the member needs to complete a new nomination otherwise the nomination becomes non-binding.

So if you are chasing a "set and forget" approach then a non-lapsing binding death benefit nomination is essential.

In addition to these, costs are usually cited as a driving factor behind this transition. The irony is, particularly if the SMSF balance is in excess of $1.5 million, that even industry funds are likely to be a more expensive solution.

Most industry super funds have internal fees which are typically about 0.7 per cent of the balance. Platform or wrap accounts are upwards towards one per cent or even 2 per cent including investment management fees.

Added to this is the cost of transitioning the portfolio. Selling share portfolios attracts brokerage, property attracts agents fees and settlement costs and purchasing managed investments even in industry funds attracts a transaction fee known as a buy/sell cost of 0.2 per cent.

That's an additional $3000 just to buy the investments in the new fund. This is usually comparable with the tax, compliance, admin and portfolio costs associated with a SMSF but without the support of professionals to stay abreast of legislative changes, portfolio updates or other retirement income support.

Chasing simplicity and reducing the stress associated with being fully responsible for one's own retirement is understandable and, when set up correctly, most platforms and even industry funds can provide the structure required to achieve this.

Do your research, understand the impact and understand what you can do now to ensure you really can have a simple and stress-free retirement.

Michael Ward is a financial planner with Maxim Private Wealth