The SMSF Academy Podcast – Transcript

Episode	29
Topic	Documenting decisions in taking more than the minimum pension
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Aaron Dunn: You're listening to The SMSF Academy podcast and this is episode 29.

Speaker 2: Welcome to The SMSF Academy podcast, the show designed to help professionals stay ahead of the curve. Now, here's your host, the man that's in the know and shows you how SMSF is Dunn right, Aaron Dunn.

Aaron Dunn: Hi there, folks. Aaron Dunn here from The SMSF Academy and thank you for joining me in this week's podcast, our second for 2018. We had some wonderful feedback from our first podcast of the year. It's actually been one of the highest viewed podcast that we've actually had where we looked at 8 things that you should be focusing on with your SMSF business in 2018. So if you haven't spent the time, look at that, I would strongly suggest that you do so.

Today, I want to delve in a little bit deeper into this requirement around taking pension payments post (super) reforms. We have spoken about this at length through some webinar training late in 2017, but more importantly, I wanted to really delve into the documentation that is required based upon the decisions that an individual may make where they intend on taking more than the minimum pension, because I continue to see when we speak to practitioners a lack of understanding when it comes to the documentation and the prioritisation that we're putting in play around, again, where that individual wants to take more than the minimum pension.

We did of course see the ATO provide us with some important, guidance in the lead up to the introduction of the superannuation reforms in practical compliance guidance, PCG 2017/5 and in particular what the Commissioner deemed to be a valid commutation. In that approach, they provided us with the expectation upon the Commissioner as to what they would see as being a valid request by the member to commute and acceptance by the trustee in respect to that commutation, and importantly didn't require any specific amounts to be determined at that point in time but it did require a process to be followed which talked about the requirements of it being:

- made in writing, whether it was a documented resolution;
- It had to be prospective in its nature, so it needed to be documented before the 1st of July 2017.
- It needed to specify a methodology that allowed for that precise quantum of the amount committed to be calculated which it could include that that such amount be ascertained at a later point in time.
- It needed to specify the income strain that would be subject to that commutation and where there was a request that covered one or more pensions that requested an acceptance needs to specify that different income strain that maybe covered and the order of priority in which that commutation was to occur, and (finally),
- didn't conflict with any other agreement.

Now, we've spoken about in the past how that guidance there has really set out a precedent in which we can follow where individuals are going to be taking more than the minimum pension, and in particular, want to create a claw-back event against the members transfer balance cap. Importantly though we need to

distinguish, and we've spoken again in the past about this prioritisation of cashing benefits where there is more than the minimum pension to be taken for the year, because we may have in some instances individuals that have had to comply with the transfer balance cap, but they've retained benefits inside the accumulation account.

Therefore, when we look at this prioritisation of taking benefits, we would be:

1. Establishing that we are going to be taking the minimum pension obligation because of course that is going to give us our earnings tax exemption on our retirement phase income streams; and
2. We are then going to focus on drawing down benefits from the member's accumulation account - the rationale behind that is that we're wanting to increase the level of tax exemption going forward.

In respect to the remainder of that income year and then also in future years by basically drawing down on the accumulation benefits until such a time that those accumulation benefits have been fully utilised. Then, when we have exhausted the capital that is sitting inside that member's accumulation account, we would then look towards undertaking a partial commutation. When we have that partial commutation, the pension doesn't cease, so referencing back to the Commissioner's views in TR 2013/5, what we are therefore doing here is then complying with what the Commissioner has previously indicated within PCG 2017/5.

In respect to that view we're looking to ensure that we get that debit against the transfer balance cap, which is important for specific members where either they are over the transfer balance cap, either themselves or is utilised the transfer balance cap or where we have a husband and wife situation in particular where the combination of those two, from an estate planning point of view, where the combination of those amounts is greater than that transfer balance cap will mean that if that pension wants to revert either automatically as a reversion or a beneficiary or where that text dependent beneficiary would have the right to commence an income stream with that death benefit, it is going to therefore create (potentially) a transfer balance cap issue for that member that they would need to resolve.

By undertaking these partial commutations it would be of course allowing us to reduce the benefit of that member and therefore if they were to receive any future benefit themselves, they would be able to absorb a greater amount of that reversionary income stream or death benefit pension to them.

One of the things that I've seen, like I mentioned is that we're getting a lot of confusion in the conversations with individuals around the documentation that needs to occur and what we've now done.

We've included this inside the blog post as well, in addition to what we have now incorporated into the documents that we prepare, is to really understand how you need to be documenting each of these processes because first and foremost when we prepare our annual calculation around our annual pension

review, we do of course create the necessary annual trustee minute that states the minimum pension obligation.

Regardless of the decisions that are happening in respect to any above minimum payments amounts, we do need to of course document the decisions and calculation that has occurred in respect to that member's income stream for the coming year. We'd be looking clearly at their account balance of that superannuation income stream interest multiplying it by the pension valuation factor based upon that member's age at the first of July and notating that as part of that trustee minute or resolution as I spoke about. We would then to look to get some form of confirmation around that.

Now, this is where it becomes important around what has to happen next...

If there is a decision that any amount is above the minimum are just to be treated as pension payments. Then what we want to ensure is that we have established an acceptance by the member of that pension obligation for the year and that they've indicated therefore that they do intend on taking an amount above the minimum and those amounts are therefore just going to be treated as pension payments, which of course have no influence on the transfer balance cap for the remainder of that year. It is a straight forward process and in essence would continue as has always been the case.

If we look at it in the context where the individual only has or have an accumulation account in addition to their pension and they're only going to be drawing from that accumulation interest for the above minimum amounts. This is where there's been a lot of confusion because a lot of people are saying, "I need to be out to generate not only our annual trustee document but we need to put in place a member request that says, Now, I'm going to take more than the minimum but I'm going to be drawing this from accumulation account."

What I've been saying to people is well, you don’t have to reference inside your income stream the fact that you’re going to be drawing benefits from the accumulation interest because the accumulation interest has no bearing on the calculation that has to come from that specific income stream. Therefore, if it has no bearing on the income stream, there is no further action that is required in respect to amounts that are going to come out of that accumulation account in respect to here, the annual reporting or the annual calculation of that pension.

However, when the event occurs where the individual is wanting to take an amount out of the accumulation account, of course, we should therefore then be putting in the specific request for that amount to be coming out as a lump sum payment. The only other documents here in essence that would need to be created are at the time where the lump sum request would be occurring because we are no longer impacting the pension because we've satisfied the minimum for that particular year and that is all that we're intending on doing. Of course if we are not impacting the pension, there is going to be no requirements around the transfer balance cap either.

Now, in going through that process of having explained it on many occasions to individuals once you go through that process it does make sense. What we’ve

narrowed down is look at how can we incorporate some middle ground here, because when we look at the partial commutation approach where we're only taking it by partial commutation or we're taking it from accumulation and partial commutation, it did provide some level of confusion.

So, alternatively what you do, and this is something we've now introduced into our documents, if you want to incorporate the accumulation account into that documentation process it's not going to have a bearing on the pension but what I would suggest you do is put in place a member request that notes that any additional withdrawals will not actually impact the pension but rather come from the accumulation account. Importantly where this is done would be done prospectively and ensuring therefore that if you wanted to make a change to that in the future you could do so, because where we have this commutation requirement in PCG 2017 it talks about that it needed to be made before the first of July 2017. Therefore, it talked about the prospective nature in how that needed to be done. Importantly, that agreement that was put in place could not be subsequently revoked after the date of the agreement. If you did have any discretion to do so, it would be questionable in the eyes of the Commissioner that that subsequent revoking of that agreement therefore meant that you didn’t have a commutation at all and therefore those amounts would be deemed to be pension payments.

It is very important in the context of a partial commutation that it is a set in ‘stone decision’ but in respect to the members accumulation account if you then wanted to ultimate treat it as a pension payment or maybe even as a commutation as long as you take a prospective approach to it and don't try and do it after the fact, you could arguably therefore make a change in the future if you didn't want to have it as an accumulation account withdrawal.

Just to summarise there, I don't see it being particularly important that you need to prepare another document other than the minimum pension obligation until the point in time where that withdrawal actually comes out as an amount to be debited out of the accumulation account because it has no bearing on that account based pension that may be being paid, otherwise and this is where we've now introduced this document, we then incorporate a member request that notes that any additional withdrawal is not going to impact the pension but will be subject to a withdrawal that is going to come out of the accumulation account of that member. But it would provide some level of flexibility if they want to in the future to be able to change that decision prospectively.

This is then where the shift occurs when we now look at where we may not have an accumulation account and therefore we're taking a partial commutation to strike that debit against the transfer balance cap.

Of course we have our annual preparation of the trustee minute that states what that minimum pension obligation is. Then what we're going to do is again referencing back to the PCG 2017/5, we need to put in place a member request and trustee acceptance. The second step here is to put in place the member request notifying the trustee of their intention to treat the above minimum pension requirement in such a way and that trustee resolution therefore needs

to confirm acceptance of that decision, again following that framework that the Commissioner has previously provided to us.

Then, as we move down the path and we get to that point in time where we've taken our minimums and we're looking to strike that debit against the transfer balance cap as a commutation, we would then provide the further trustee minute and notification to the member at the time of that payment which would of course also incorporate the transfer balance account reporting (TBAR) requirements but as I mentioned before the decision that is being done here if we follow to the letter of the law, the requirements that the Commissioner has put out in that practical compliance guidance, the agreement here could not be subsequently revoked or altered by the member after the date of the agreement has been made. That is because if it was therefore deemed to be changed after the fact, the Commissioner could clearly then go back and say, "It is just but the pension payment and therefore you would have no right or entitlement to create that transfer balance debit in respect to that partial commutation."

When we get to the final one here which where we might have a combination of both accumulation and partial commutation, so an amount is to be taken from the accumulation and ultimately exhaust that accumulation account and therefore any subsequent amounts would come out of partial commutation where we need to combine these two things. This is where we would be looking at some form of prioritisation being established in that documentation, so again, above and beyond the calculation that's done by the trustees around the minimum pension obligation, the member request he would need to establish their intention or in terms of how they're going to take that amount, also establishing the prioritisation of how those benefits are to be applied. The resolution would accept those decisions and again in terms of the way in which that treatments is to occur, and then finally we would have that further notification and trustee minute that would occur at the time of both the lump sums that are occurring out of the accumulation account and where a partial commutation would be occurring we would have a similar requirement in addition to the transfer balance account reporting that would need to be done as well.

We have four different ways in which we need to deal with these above minimum pension payments and therefore how you actually create the documentation in respect to these distinct decisions is going to be critically important to ensure that you are not only achieving the outcomes of what your client wants, but ensure that you satisfy what the commission has stated is rightly a valid commutation as well.

If you want to find out a little bit more in respect to how these documents are created inside our SMSF Academy campus platform, you can do so by contacting us (1300 95 94 76) or you can register online or look at one of those documents or inquire with us about a 14-day trial as well.

Hopefully that helps to clarify. Like I said, we've had a lot of questions and trying to get an understanding around why certain documents need to be created based upon the different scenarios that occur. That table (above) I think is really important because it gives you some clarity in respect to the decisions that need

to be made. Other than that, if you have any other questions in respect to this specific matter, you can get in contact with me either through our website or through our various social media channels as well.

The other thing I just wanted to quickly mention, and we'll get into more detail in this over the coming weeks, but we have now seen very early in the year, Treasury release a consultation paper around some of the superannuation taxation integrity measures in particular for issues impacting a member's total superannuation balance. This was expected, and we have now seen the first measure as part of this consultation is looking at the inclusion of the member's share of an outstanding balance of an LRBA in the total superannuation balance (TSB) definition and the second measure within these consultation form is Incorporating the non-arm's length expenditure being taken into account when determining whether the non-arm's length taxation rules would apply to such a transaction.

I just wanted to make you aware that but of those measures form part of this consultation. It was released on the 11th of January, so we are currently in a stage of consultation. Submissions do close on the 9th of February. We will be going through this over the coming week or so and we'll look to talk about these topics in some detail in one of our coming podcasts. (for now), just wanted to make you aware that this was currently in play and if you wanted to find out a little it more, you can go to the Treasury website and look under consultations and download the consultation paper.

https://treasury.gov.au/consultation/t243169/

That's it. Thank you for joining me in this week's podcast. I look forward to you joining me in next week's podcast. Have a great rest of the week and bye for now.

Speaker 2: Thanks for listening to The SMSF Academy Podcast. Please note that the podcast provides general advice only and is based upon our understanding of the law at the time of the recording. If you have any comments or questions from this podcast or wish to subscribe to the series, you can find us at thesmsfacademy.com.au. Tweet us at The SMSF Academy. Like us on Facebook or connect with us on LinkedIn.