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Pension income streams within an SMSF

An income stream from your self-managed super fund ensures regular, flexible and tax-effective income as a pensioner. These streams can be received as a series of benefit payments from your SMSF.

Income streams from an SMSF are usually account-based, which means that the amount allocated to the pension comes directly from a member's account. Once an account-based pension commences, there is an ongoing requirement for the trustees of the superannuation fund to ensure the pension standards and laws are met.

A super income stream exists when:

- A member is entitled to a series of payments that relate to each other.
- The payments are periodic, whether paid annually or more frequently.
- The payments are made over an identifiable period of time.

Minimum payment standards of the Superannuation Industry Supervision (SIS) Regulations must be met in order for SMSFs to pay income stream pensions. These requirements are:

- The minimum amount must be paid at least once a year.
- Once the pension has started, the capital supporting the pension cannot be increased by using contributions or rollover amounts.
- When a member dies, their pension can only be transferred to a dependent beneficiary if they have any.
- The capital value of the pension or the income cannot be used as security for borrowing.
- Before you completely change a pension, you must pay a minimum amount in certain circumstances.
- Before you partially change a pension, you must make sure there are sufficient assets to pay the minimum amount.
- Once they have satisfied these minimum standards, the pension will be treated as super income stream benefits for tax purposes. The funds may then be able to claim an exemption for the income earned on pension assets. This is known as an exempt current pension income (ECPI).

From the commencement of the income stream, there are a number of compliance obligations that need to be met. Records of the pensions starting value must be kept along with taxable elements, earnings from assets and any pension payments made. SMSF trustees may need to amend trust deeds to satisfy these requirements. For more information on how to do this, you should consult a financial advisor.

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High-risk SMSF areas being monitored by the ATO

Self-managed super funds are closely monitored by the ATO to ensure regulations are being met across all areas. It is the responsibility of SMSF trustees to comply with all related super and tax laws.

The ATO is looking into a number of high-risk areas within SMSFs this year, specifically, limited recourse borrowing arrangements (LBRAs), transfer balance account reporting (TBAR) and attempts at accessing super before preservation age.

Limited recourse borrowing arrangements:

The ATO this year announced plans to contact trustees with high concentration risks in their funds. LRBAs allow a superannuation fund to borrow under strict conditions. The existing population of SMSFs that have entered into LRBAs, potentially on the basis of poor or conflicting advice, has been rated a medium to high-risk by the ATO. In 2017, $42.2 billion of LRBAs accounted for 5.6% of total SMSF assets. The most popular of these assets were property, with approximately 95% of the LRBAs for this purpose. Due to this prevalence, the ATO has concerns about the risk of members' retirement savings in the event of a property decline.

Transfer balance account reporting:

The ATO has identified a number of key concerns in TBAR since its commencement in July 2018. TBAR is used to advise the ATO when a transfer balance account event occurs within an SMSF, enabling an individual's transfer balance cap and total superannuation balance to be recorded and tracked. One area the ATO will be monitoring is the reporting of capped defined benefit income streams. In 2018, approximately 86% of SMSFs had failed in their reporting obligations in this area. These errors identify a lack of awareness among SMSFs of their reporting obligations to the tax office.

SMSFs being accessed before preservation age:

Another area of concern for the ATO regarding SMSFs is that these types of funds are being used to gain access to super before preservation age. Preservation age is dictated by the year in which you were born and super cannot legally be accessed before you reach this age. A growing number of investors in their 30s, far off from their preservation age, are moving their super into an SMSF in an attempt to gain access to their super early. The ATO has noticed an increase in this strategy in the last five years. If found to be doing this, penalties can include funds being wound up, a 45% tax impost being applied, administrative penalties which have a cost attached, or being disqualified from running a fund.

Further SMSF contraventions:

The ATO is also looking into possible problem areas in relation to SMSF contraventions. Loans to SMSF members, in-house assets, investing in related party assets and a failure to keep assets separated have accounted for the bulk of contravention reports. The ATO also lists administrative errors, sole purpose breaches, borrowings, operating standards and acquisitions of assets from related parties as categories also seen in contravention reports.

To avoid these issues in your funds, make sure that your SMSF keeps detailed records to help substantiate transactions. It would further benefit trustees to have in place an adequate strategy that deals with the potential risks involved in borrowing arrangements and be aware of their reporting obligations for transfer balance accounts.

Super contributions splitting

Super contribution splitting enables you to increase your spouse's retirement savings with the addition of some of your own funds.

A spousal contribution strategy allows you to roll over a portion of your super and personal deductible contributions into your spouse's account. Splitting your super contributions can be an option if your partner has a low or limited income, resulting in tax advantages that will help you grow your joint retirement funds.

The two main types of contributions that can be split with your spouse are taxed splittable contributions (TSCs) or untaxed splittable contributions (USCs). You can transfer up to 85% of a financial year's TSCs, although you must advise your super fund on personal contributions you will be claiming a tax deduction for.

You must meet the eligibility requirements to avoid incurring penalties from the ATO. Some advantages gained from contribution splitting include:

- Gaining earlier access to concessionally taxed or tax-free lump sum super withdrawals.
- Increase non-concessional contributions you can make by reducing your total super balance.
- Gain earlier access to contributions.
- Maximise tax-free pension benefits.

Your ATO application will only be deemed valid if:

- The person you are splitting your contributions with is a spouse defined by marriage, a registered relationship or a de facto relationship.
- Your spouse is less than the preservation age listed on the ATO or aged between their preservation age and 65 years and not retired.
- You have not already applied in the financial year where the trustee of your fund has received your application.
- The amount of benefits you have used does not exceed the maximum amount that can be split.

SMSF trustee investment strategy checklist

Although small, trustees of self-managed super funds are required to prepare and implement an investment strategy for the purpose of providing retirement benefits to the fund members.

Maximising your retirement nest egg depends on how well your investment strategy functions at different phases in your working life. Consistent monitoring of implementation and growth of the strategy will help determine any shifts in accordance with changing financial circumstances.

Here is a checklist to get you started.

- Map your risk profiles.
- Consider risky circumstances.
- Take out insurance for members.
- Comply with super laws under a trust deed.
- Regularly review your investment strategy.
- Document decisions about investment strategy.
- Know how to discontinue an SMSF, if it arises.