Versatile SMSFs can provide for all occasions

A self-managed super fund offers the flexibility to allow one member to draw a pension and one to keep working, writes **Alexandra Cain.**

The beauty of a self-managed super fund (SMSF) environment is its unique capacity to cater for both accumulation and pension strategies, as well as the ability of members to easily change the structure of the fund year-to-year.

This is especially the case with funds that are partially in the pension phase and partially in the accumulation phase. This is a situation that often occurs if one or more of the members has put in place a transition-to-retirement strategy, or if one member is paid a pension and another member is still working and accumulating super.

AMP financial planner Peter Burke says the key decision when the fund is both paying a pension and accumulating funds is whether to apportion the income the assets within the fund generates on a pro rata basis, or to segregate assets between the two strategies.

"The choice you make will impact the tax outcomes of the fund," says Burke, explaining that "most of the time the pro rata approach is the simplest to administer".

David Shirlow, Macquarie Adviser Services' technical expert for SMSFs, says fund members that choose the segregated route need to ensure "the trust deed allows assets to be earmarked to different accounts".

It is quite typical to also have a separate investment strategy for each pool of assets. Sometimes there might even be a number of different accounts with different investment strategies for both the pension and accumulation parts of the fund.

Shirlow says you also need to "make it clear the pension pool of assets is used solely for pension purposes. You also need separate cash accounts for pension and accumulation assets because all earnings and dividends related to the assets in each pool have to be segregated."

But according to Burke, while there can be many pension accounts, there can only be one accumulation account per member inside the SMSF.

From a tax perspective, Peter Hogan, a financial planner with Plaza Financial, part of the Securitor dealer group, says "15 per cent tax will still be payable on the taxable contributions received and investment income of the accumulation portion of the fund, but on the pension side no tax is payable. It's important that the fund be structured so that that calculation is possible."

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> PETER BURKE, AMP

Interestingly, Hogan says "any franking credits earned by the assets segregated for the pension portion of the fund can still be used to offset the tax liability of the accumulation part of the fund because the fund as a whole is treated as a single entity for tax purposes".

"The other important issue that arises from the fact that the fund is a single entity is that, no matter what arrangements are made to notionally allocate particular assets to particular pensioners or accumulators, they are still assets of the single fund and so must be owned in the names of all the individual trustees or the corporate trustee.

"The Australian Tax Office, as the regulator of SMSFs, has publicly expressed serious concerns with any fund where assets are not properly owned in the names of the current trustees," says Hogan.

Burke says SMSFs that are simultaneously in the accumulation and pension phases need to be mindful of contribution and withdrawal minimums and maximums.

He says "punitive rates of tax apply if you get it wrong, so you really need to be mindful of contribution caps in particular".

If the pension part of the fund does not correctly pay out the minimum pension amount it is supposed to, the fund will be considered to still be in the accumulation phase and there will be tax implications.

Another important consideration according to Burke is the estate planning aspects of the fund. "It can be a challenge to make sure there is as little tax impact as possible created if a non-dependent beneficiary inherits assets from the fund," says Burke.

"The ability to run separate pensions through an SMSF can provide opportunities to quarantine taxable and tax-free superannuation components.

"This can provide tax benefits – particularly from an estate planning perspective.

"Having said that, a similar outcome could be achieved through retail super funds.

"The beauty of SMSFs is that they are very flexible and there's lots of room to move within the rules. You can segment assets, set up multiple pensions for the fund and minimise the tax position easily and cost-effectively."

Versatile tools

- Today's DIY funds offer a high degree of flexibility and can cater for both accumulation and pension strategies.
- Managers need to take care that funds are correctly structured to avoid punitive rates of tax.

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