



ACCOUNT BASED PENSION PAYMENT AGREEMENT

GRANT SUPERANNUATION FUND

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1. Introduction

A member of an SMSF can generally access their superannuation benefits as an SMSF income stream or lump sum when they have satisfied a relevant 'condition of release' under Schedule 1 of the *Superannuation Industry (Supervision) Regulations 1994* (SISR). The most common 'condition of release' is retirement as defined by SISR 6.01(7).

2. Corporations Legislation

The payment of an account-based pension by the trustee of an SMSF is a financial product for the purposes of the *Corporations Act 2001*. As a financial product the *Corporations Act 2001* provides as follows:

- **Product Disclosure Statement (PDS)**

In terms of the information required to be given to the member of an SMSF to make a confident and informed decision in relation to an SMSF financial product, the *Corporations Act 2001*, requires a licensee, their authorised representative and the trustee of an SMSF to provide a member of a SMSF with a PDS. This pension PDS has been issued by the trustee of the fund to the member seeking to commence a pension. The PDS should be reviewed by members on an on-going basis.

- **Statement of Advice (SoA)**

Section 946A of the *Corporations Act 2001* requires that a client be provided with a Statement of Advice where they are provided with a recommendation to acquire or dispose of an SMSF financial product.

3. SMSF Pensions v Lump sums

There are effectively three ways for the trustee of an SMSF to provide payments of member benefits in an SMSF – so careful consideration must be given to how the member chooses to take income from their fund:

Option One: Taking a Pension

The trustee may pay an SMSF pension from the fund with the member's current accumulation benefits. Post 20 September 2007 there are currently two main SMSF pension types that may be paid by the trustee of the fund under the trust deed used by the fund – the transition to retirement income stream and the account-based pension. However, the transition to retirement income stream will no longer benefit from the pension tax concessions from 1 July 2017.

The SMSF pension may be built with a reversionary interest meaning that upon the death of the member the pension continues in the name of the reversionary beneficiary thereby combining SMSF pension planning and SMSF estate planning. Prior to utilising this strategy, careful consideration must be given to the Superannuation Laws, who can be paid a reversionary pension and more importantly the concessional tax rates for death benefit pensions. Advice should be sought by any member seeking to put in place a reversionary pension for a spouse or other eligible dependants.

Option Two: Taking Lump Sums

At the time of retirement, a member of the fund may access their benefits as a lump sum. The SISR provides that a retiree member can leave their benefits in their accumulation account and draw them down gradually as multiple lump sum payments until their death. In essence, income is provided as a series of lump sum withdrawals from a member's accumulation account rather than taking a pension.

Option Three: Taking both Lump Sums and an Income Stream

Upon retirement, a member of a superannuation fund can provide the bulk of their lifestyle income by way of an income stream with a lump sum only taken if and when needed. This may be in the event of a health, family crisis or an unbudgeted expenditure.

With this option, the strategy is for the member to hold some of their superannuation benefits in their accumulation account and some in the pension account. How much is in each account and how the accumulation and pension accounts are to be used between retirement and death is a function of four factors:

- a) what lifestyle income is required – remember this can be drawn down from both sides of the fund;
- b) the minimum pension drawdown rules for the pension. If there is too much in the member's pension side of the fund, excessive income may be required to be withdrawn, thereby taking funds out of a concessional tax environment;
- c) where the trustee invests on behalf of an accumulation account member the fund is subject to tax at a rate of 15% on income and 10% on capital gains in respect of assets held for more than a year. In comparison income earned on assets used by the trustee to fund a pension account is tax-free.
- d) the member's personal Transfer Balance Cap. From 1 July 2021, a member is limited to a cap amount of \$1.7 million that can support retirement income streams. This cap amount is indexed in \$100,000 increments subject to Consumer Price Index (CPI). The excess balance must remain in the accumulation account or leave the superannuation system.

Note: There are estate and tax planning advantages to running both accounts and these should be discussed with the member's SMSF adviser.

4. SMSF Account Based Pension

As the fund is an SMSF and the pension has commenced following, for example, the retirement of the member, the income stream generally is an account-based pension. As an account-based pension, the member must take a minimum payment each year otherwise the Commissioner of Taxation has noted that the income stream would not be a pension thereby jeopardising the fund's tax-exempt status on pension assets.

The minimum draw-down payments under the account-based pension regulations are as follows for the 2023-2024 income year:

Characteristics	Account-based pension
Minimum Payment	Minimum Percentage %
Under 65	4.00%
65 - 74	5.00%
75 - 79	6.00%
80 - 84	7.00%
85 - 89	9.00%
90 - 94	11.00%
95 +	14.00%
Roll back to Accumulation Account	Yes
Lump Sum Commutation	Yes

Where a member has an account-based pension, at any time they may elect to commute the whole or part of the pension into a lump sum payment. The taxation consequences of commuting to a lump sum will depend on the member's age at the time of commutation and are discussed below. On the death of the member, an SMSF Will created by the member may require the commutation of the deceased member's pension for the benefit of a dependant. The taxation consequences in relation to any SMSF estate planning and in particular an SMSF Will should be discussed with a qualified SMSF adviser.

A member may also request the trustee of an SMSF to make the pension auto-reversionary which means that the pension transfers from a deceased member automatically upon their death to a spouse, dependant or legal estate. There are several important reasons for ensuring that account-based pensions are auto-reversionary.

Note: Where a member of an SMSF has an older style allocated pension they may consider rolling the pension back into their lump-sum account and commence one or more account-based pensions. If the member has a defined benefit pension, careful consideration of whether the pension can be rolled back and the consequences of a rollback must take place.

From 1 July 2021, the transfer balance cap measures are in place. The capital value of any existing account-based pensions as at 30 June 2021 become a credit item to the member's personal transfer balance account. An individual is only allowed \$1.7 million in retirement income streams. This cap amount is in relation to the 2021-22 financial year and is indexed in \$100,000 increments based on CPI. It is a per member cap and not per fund. Any excess over the cap amount is required to be transferred to the member's accumulation account or commuted to a lump-sum and cash out of the fund so as to avoid excess transfer balance tax. For account-based pensions commencing after 1 July 2021, the capital value at the time of commencement is the credit item. Full or partial commutations are debit items to the personal transfer balance cap. Earnings and pension payments are excluded.

It should also be noted, that if a member is in receipt of a transition to retirement income stream (TRIS) and the member reaches the age of 65, or notifies their fund that they have satisfied one of the following 'nil' cash restriction conditions of release:

- Retirement
- Permanent incapacity
- Terminal illness

A TRIS will also be in the retirement phase if it starts to be paid to a reversionary beneficiary after the original member's death. At this point, the capital value of the TRIS in the retirement phase will automatically be a credit item to the member's personal transfer balance account and receive tax exemption on earnings.

5. Taxation of Pensions

5.1 Trustee of the Fund

Where the trustee commences to pay an account-based pension, the trustee is entitled to a tax exemption on income and capital gains arising in relation to assets set aside to meet the fund's SMSF income stream liabilities. This is different from the accumulation stage of an SMSF where income is generally taxed at a rate of 15% and capital gains at a rate of 10% if the investment is held for more than 12 months.

Where the trustee runs a pooled investment strategy meaning the assets of the fund are pooled to pay all member benefits including pensions, then the trustee will obtain a proportional tax exemption on income and gains earned by the fund. The exemption proportion is to be determined by reference to the liabilities that the trustee faces in order to pay current pensions versus the fund's total superannuation benefit liabilities. In order to claim the exemption, the trustee of the fund must engage the services of an actuary each year to determine the amount of the fund's SMSF income stream liabilities as well as its superannuation liabilities.

In contrast, where the trustee of the fund runs a separate investment strategy for any SMSF pension (segregating assets from the rest of the fund), then any income or gains earned on these assets is tax-free. The segregation of assets is a simple bookkeeping exercise that can be undertaken by the accountant or administrator of the fund. Importantly if the assets have accrued capital gains in the accumulation side of the SMSF, then the transfer of the assets to a separate pension investment strategy in the fund will not create a tax liability at the time of transfer. Further provided the assets funding the pension are disposed of by the trustee at the time the SMSF pension has commenced there will be no capital or income tax consequences in respect of the disposal of the assets.

Please note, from 1 July 2021, the fund cannot run a segregated method when calculating the exempt current pension income (ECPI) of the fund, if the fund has a member who is in receipt of a retirement income stream and the member's total superannuation balance exceeds the general transfer balance cap (\$1.7 million for the 2021-22 financial year).

As a final point where the trustee of the SMSF as part of the fund's pension assets holds Australian shares paying franking credits, no tax is payable on the dividend. However, the trustee may claim the franking credits to reduce overall tax payable in the fund. If there are excess credits in an income year these will be refunded by the Commissioner of Taxation.

5.2 Pension Beneficiaries

a) Benefits paid to a Member

The Simpler Super regime that commenced on 1 July 2007 introduced the concept of multiple superannuation interests being held by a member who has an accumulation account and at the same time commences a pension. Superannuation interests are important because from these interests flow a superannuation benefit, whether a lump sum from the member's accumulation account or a pension or lump sum from the member's pension account. These benefits when paid will have a taxable/tax-free component. The proportion of taxable/tax-free component is to be determined by the underlying taxable/tax-free proportion of the relevant superannuation interest.

The taxable/tax-free component determination is crucial as it plays an important part for a pre-60-year-old member (such as a member with a transition to retirement pension) as well as for their dependants and other beneficiaries in the event of the member's death.

b) The proportioning rule

Superannuation benefits whether taken as a lump sum or pension are to be divided by the trustee of the fund into a taxable and tax-free component. The proportion used is the same as the underlying superannuation interest from where the superannuation benefit is sourced.

For example, a 60-year-old member of a complying SMSF taking an account-based pension may have a taxable/tax-free component proportion equal to 60/40. Any income stream benefit taken from that superannuation interest will have 60% taxable and 40% tax-free component. This will include any lump sum commutations from the pension.

The taxable/tax-free component of any lump sum or pension payment can easily be determined by your SMSF adviser or accountant at the time of commencement of the pension or when a lump sum or pension commutation amount is taken from the fund.

c) The taxation of benefits to a member

Where a superannuation benefit is paid to a member, either as a lump sum, a commutation of the pension or direct pension payment it will be taxed as follows:

- Tax-free Component - Any tax-free component payable is always tax-free in their hands irrespective of their age. This includes both lump sums and income streams.
- Taxable Component - Table A highlights the taxation treatment of benefits payable to a member. It should be noted that the preservation age for a person born prior to 1960 is aged 55.
- Untaxed Component – untaxed component is only found in SMSFs with life-insurance and a lump sum is paid to a dependant or the member's legal estate in the event of the member's death.

Table A – Taxation of the Taxable Component

Type of Benefit	Under preservation age	Between preservation age and age 60	Age 60 and over
Lump sum	20%	Tax free up to the <u>low rate cap amount</u> with any remainder taxed up to a maximum rate of 15% (excluding Medicare levy)	Tax-free
Income stream	Marginal tax rate	Marginal tax rate - 15% tax offset	Tax-free

Note: The taxation of superannuation death benefits is different from that above and advice should be sought regarding SMSF Wills from an SMSF adviser.

SMSF Trust Deed

The fund's trust deed is the key determinant to what type of pension may be paid from the fund. The trust deed may allow pensions to be continued where they may have been established many years ago as well as the account-based and transition to retirement pensions of modern times. Flexibility is a must in superannuation and particularly SMSFs.

APPLICATION BY KATHLEEN GRANT TO COMMENCE AN ACCOUNT-BASED PENSION

Date: 1/7/2023
Name of Fund: Grant Superannuation Fund
Members Name: Kathleen Grant
Age of Member: 68

Request to commence an Account-based Pension:

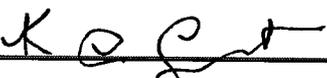
The Member hereby requests the Trustee to commence an Account-based Pension with an amount from the Members Accumulation Superannuation Interest having satisfied the relevant Condition of Release as per Schedule 1 of SISR.

Pension Account Balance:	\$290,000	Approximate balance. Actual amount to advised when 2023 year processing completed.
Date of Commencement:	1 July 2023	
Condition of Release:	Reaching Age 65	
Minimum Annual Income Payment:	\$14,500	Approximate. Actual minimum to be advised.
Current Year Pension Payment:	\$14,500	
Tax-free / Taxable Component Proportions:	85%/15%	Approximate. Actual to be advised.
Reversionary Beneficiary Name:	Alan Grant	

Signed by the Member:

The Member

Signed by Kathleen Grant in the presence of:



Kathleen Grant
Member



CAROLE A WOODLAND
Witness Name / Signature

TRUSTEE MEETING: COMMENCEMENT OF AN ACCOUNT-BASED PENSION

Date: _____

Name of Fund: Grant Superannuation Fund

Attended by: Alan Grant and Kathleen Grant

Held at: 8 WINTERGREEN CLOSE, BRACKEN RIDGE, QLD 4017

Chairperson: Alan Grant

Table a Motion to commence an Account-based Pension:

Purpose of the Account-based Pension:

To commence an Account-based Pension for Kathleen Grant under the governing rules of the Fund. The Chairperson confirms that the condition of release corresponds with one or more of the conditions of release under Schedule 1 of the SISR and acknowledges the Member's request to commence an Account-based Pension subject to the payment limits and standards as prescribed by Schedule 1AAB and 7 of the SISR.

The Pension is to have the following terms and conditions:

Pension Account Balance: \$290,000

Date of Commencement: 1 July 2023

Condition of Release: Reaching Age 65

Minimum Annual Income Payment: \$14,500

Current Year Pension Payment: \$14,500

Tax-free / Taxable Component Proportions: 85%/15%

Reversionary Beneficiary Name: Alan Grant

Trustee Resolutions:

It was resolved by the Trustee to commence an Account-based Pension on behalf of the Member. The Trustee is to forward this trustee minute to the Member as notification of the commencement of the Pension.

EXECUTED BY:

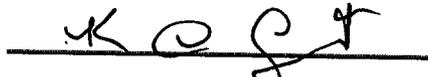
Grant Superannuation Fund

The Trustee

Executed by A&K GRANT PTY LTD - ACN 604 097 485 by:



Alan Grant
Director



Kathleen Grant
Director