WIND UP AN SMSF

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#NC2020

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Peter Crump is a financial adviser and actuary who has worked in superannuation all of his career, well over 30 years. He is a private client adviser at AMP Advice in their Wayville office (formerly known as ipac south australia). He provides financial advice and expert superannuation advice to his and AMP Advice's clients. Until 2018, he served as a non-executive director of the SMSF Association for 8 years, including 2 as Chairman. He has a few formal qualifications, covering taxation, financial advice and actuarial, as well as being a Graduate member of the Australian Institute of Company Directors. He is a published co-author and has made numerous presentations and authored papers on superannuation and SMSF related issues.

What we will address and will not address

Will address

- Member, beneficiary and trustee issues on wind up
- Prospective rather than retrospective consideration of these issues
- Process of final actions leading up to wind up
- Checklist of issues to be considered or addressed

Will not address

- Complex legal issues such as validation of deed, missing deed, final trustee appointment

What affects wind up considerations

These need to be better understood

- ASIC Report 575
- ASIC Information Sheet 205
- TBC reporting (TBAR)
- Different approaches for actuarial certification of ECPI
- Taxation Ruling 2013/5 – when does a pension stop and start ?
- FASEA Ethics Code

ASIC Report 575 – Improving the quality of advice and member experiences
ASIC Information sheet 205 – Advice on self managed superannuation funds, disclosure of risks

- Need to consider an exit strategy at the time of recommending new SMSF
- Need to consider process, cost and risk of exiting SMSF
- Should this be an ongoing (annual) discussion with members and their families ?
- Significant planning goes into SMSF related strategies for wealth creation and succession, but what can go wrong ?
- What is the eventual exit strategy and how will we cope if exit is brought forward ?
- Importance of the conversation, documentation to the client and documentation on file

What causes a wind up ?

Voluntary and involuntary

Voluntary / controlled

- Member/trustee can address structure and strategies for optimised outcome
- Member transfers balance to public offer fund
- Member quits superannuation totally

Involuntary

- Relies on existing structures and strategies, limited optimisation opportunity
- Death of final member
- Incapacity of final member, move to alternative structure

Key steps in wind up

1. Discussion between member and adviser about potential wind up and actions
2. Review documents - trust deed, pension contracts, asset ownership
3. Member and adviser confirm actions
4. Member confirms with / instructs trustee in writing
5. Trustee formally records instructions in minutes
6. Trustee implements instructions / actions, including documentation
7. After actions to transfer balances, formal wind up of fund occurs as consequence or as part of actions (refer deed)

Administrative issues on wind up

1. Which assets are to be sold or transferred / rolled over
2. Tax management strategies
3. Contributions in current and previous year – deductions ?
4. Member to ensure that employer contributions are directed to new fund
5. Minimum pension requirements
6. Payment of or provision for final expenses
7. What to do with final tax liability or credit
8. Extinguish member liability
9. Rolling over requires calculation of tax and preservation components
10. Member reporting
11. TBAR
12. Final financial statements, tax return and audit

Why so complicated ?

Taxation

- Capital gains tax outcomes
- Ensure ECPI continues throughout wind up and is not lost when important
- Careful management of accumulation and pension balances

Asset management

- Overlaps with tax
- Succession, especially with family assets, commercial property

Documentation and reporting

Trust deed needs to be considered at each step

Locating and reading the deed and related documents (e.g. pension contracts)

Actuarial certificates for ECPI

Rollover – benefit preservation and taxation components

Lodgement of final financial statements and tax return after audit

Accumulation , cash only

Case study 1

Harry (aged 34) is sole member of Royal SMSF and director of corporate trustee

Wants to rollover to public offer fund

- No opportunity for forward planning to address tax or asset succession
- Personal contributions, previous and current year – deductions ?
- Final fees determined and paid
- Rollover majority of balance, provision for second rollover on completion, leave working balance
- Completion of tax return, tax refund or payment made
- Final rollover exhausts cash account

Complications with new super account

Pull or push rollover ?

New super account includes ability to authorise/instruct new trustee to request ("pull") rollover from previous fund

Easier for new fund, but harder for old fund

Problematic with more complex arrangements

Prefer "push" rollover initiated by old fund – SMSF to control

Pension, cash only

Case study 2

Cammie (aged 62) is sole member of Senior Royal SMSF and and director of corporate trustee

Fund is fully pension supporting

Wants to quit superannuation totally

- When does the pension cease ?

When does the pension cease ?

TR 2013/5 – para 24 to 27

24	A request to fully commute a superannuation income stream takes effect as soon as the trustee's liability to pay periodic superannuation income stream benefits to the member or a dependant beneficiary is substituted with a liability to pay that member or dependant beneficiary a superannuation lump sum.
25	As the liability to pay the commutation lump sum arises as a consequence of the full commutation having taken effect, the superannuation income stream ceases before the time the lump sum payment to the member or dependant beneficiary is made.
26	The payment made to the member or dependant beneficiary following a full commutation of a superannuation income stream is a superannuation lump sum for income tax purposes as the superannuation interest no longer supports a superannuation income stream at the time the payment is made.
27	A superannuation income stream does not cease when a member or dependant beneficiary applies to partially commute some of their entitlements to future superannuation income stream benefits for an entitlement to a lump sum.

Pension, cash only

Case study 2

- Arrange minimum pension payments
- Majority of pension to be treated with partial commutations
- Residual to be treated as full commutation

If rolling over to new pension arrangements

- Potential problem with second rollover for commencement of pension
- TBAR to be considered – when will SMSF report v new fund reporting

Accumulation – market exposed investments

Case study 3

Harry (aged 34) is sole member of Royal SMSF and director of corporate trustee

Wants to rollover to public offer fund

- Look out for 12 month holding period for 1/3 CG discount
- Allow for carried forward unused losses (if any)
- If assets are all sold prior to rollover, final rollover components easy to finalise
- If in-specie rollover, estimates required for finalisation of tax and benefit components

Accumulation but condition of release satisfied

An opportunity for retro tax planning ?

Can a pension account be commenced just prior to wind up to take advantage of ECPI ?

- What is purpose of the strategy ?
- Need for formal advice
- Pension must have a series of payments to meet definition
- FASEA Ethics Code Standard 1
- Possible ability for ATO to observe process end to end:
    - TBAR for new pension
    - SMSF wind up, ECPI claimed
- Would ATO request copy of advice, consider refer to FASEA ?

Pension– market exposed investments

Case study 4

Charlie (aged 67) is sole member of Royal SMSF and director of corporate trustee

Wants to rollover to public offer fund, shares showing large unrealised gain

- Sale of shares and partial commutation to rollover protects ECPI, then full commutation with residual cash
- Full commutation to accumulation followed by asset sales would not protect ECPI

Pension and accumulation hybrid

Managing the process is important

Requires awareness of:

- ECPI process being followed with actuary
- CG content of specific asset parcels
- Sequencing of treatment of accounts

Pension and accumulation hybrid

Case study 5

Philip (aged 92) is sole member of Patient Partner SMSF and director of corporate trustee

Wants to quit superannuation

Pension = $1,800,000 ($1,600,000 for cap purposes at 1 July 2017)

Accumulation = $600,000

- So that makes ECPI % = $1,800,000 / $2,400,000 = 75% ?
- Or does it ?

Pension and accumulation hybrid

Case study 5

Assets:

Asset	Market Value	Cost base	Unrealised gain (loss)
Cash	$200,000	$200,000	n/a
Property	$600,000	$200,000	$400,000
Managed funds	$200,000	$300,000	($100,000)
ABC shares	$400,000	$150,000	$250,000
DEF shares	$400,000	$200,000	$200,000
GHI shares	$600,000	$450,000	$150,000
Total	**$2,400,000**	**$1,500,000**	**$900,000**

All in one go = taxable income = (1 - 75%) x $900,000 x 2/3 = $150,000

And tax payable of $22,500

Pension and accumulation hybrid

Case study 5

Take accumulation ($600,000) first – the opportunity

Asset	Market Value	Cost base	Unrealised gain (loss)
Cash	$200,000	$200,000	n/a
Property	$600,000	$200,000	$400,000
Managed funds	$200,000	$300,000	($100,000)
ABC shares	$400,000	$150,000	$250,000
DEF shares	$400,000	$200,000	$200,000
GHI shares	$600,000	$450,000	$150,000
Total	**$2,400,000**	**$1,500,000**	**$900,000**

Pension and accumulation hybrid

Case study 5

Take accumulation ($600,000) first

Asset	Market Value	Cost base	Unrealised gain (loss)
Cash	$150,000	$150,000	n/a
Managed funds	$200,000	$300,000	($100,000)
GHI shares	$250,000	$187,500	$62,500
Total	**$600,000**	**$637,500**	**($37,500)**

Taxable income = 0

Pension and accumulation hybrid

Case study 5

After accumulation is drawn, fund is 100% pension

Which ECPI approach will actuarial certificate follow ?

Full year unsegregated % will not be of value

ATO preferred segregated / unsegregated periods will be of value

First period has ECPI of 75%, second period has auto 100% as segregated current pension assets

BUT

ATO preferred ECPI approach will have 0% ECPI on/after full commutation

Illiquid assets and hybrid funds

Case study 6

Elizabeth (aged 88) is sole member of Boss SMSF and director of corporate trustee

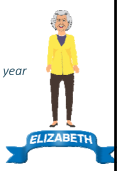
Wants to quit superannuation, but retain the property personally

Pension = $1,800,000 ($1,600,000 for cap purposes at 1 July 2017), minimum met this year

Accumulation = $200,000

Assets:

Asset	Market Value	Cost base	Unrealised gain (loss)
Cash	$100,000	$100,000	n/a
Property	$1,900,000	$1,000,000	$900,000
Total	**$2,000,000**	**$1,100,000**	**$900,000**



Illiquid assets and hybrid funds

Case study 6

Insufficient cash to pay out accumulation balance fully, so full commutation of pension will occur during hybrid status

Which ECPI approach to use ?

- ATO preferred (segregated) approach will provide for 90% ECPI on income prior to commutation of pension and full exposure on commutation of pension
- Industry preferred approach (unsegregated ECPI for full period) will calculate full year proportionate ECPI allowing for pension to exist for full period less 1 day – close to 90%

Involuntary wind up

Limited time to prepare

Most common cause is death of remaining member and no death benefit pension recipients

If there are death benefit pension recipients, opportunity exists to use unsegregated ECPI approach to manage CGT and other investment tax outcomes

ECPI continues while pension account remains to be paid (TR 2013/5) in reasonable period

Death benefits required to be paid as no more than 2 lump sums, but this still provides opportunity for major asset disposals to occur with first payment

Winding up a SMSF
Final tidy up

- Lodge final ATO return
- Final tax refund/payment
- SMSF bank account closed down
- Close down special purpose trustee company

Winding up a SMSF
Checklist

Checklist covers areas of:

- Preliminary – trustee based
- Preliminary – member based (before trustee involvement)
- Member to trustee to member
- Trustee

Winding up a SMSF
Are you ready ?

ASIC provides guidance on prior advice on winding up an SMSF, we should learn from that

Are we sure that our clients are informed of their options and opportunities for wind up

Winding up is not hard to do

It's just hard to do if you have not planned for it

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