

Superannuation Q&A

By Andrew Quinn

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This week:

- SMSFs and warrants
- Calculating pensions.
- Defining an 'eligible person'.

Warrants your attention

I keep hearing about how I can use my SMSF to invest in property through warrants. Are these the same kind of warrants that are available in equity markets or something entirely different? Is it an off-the-shelf product or something that is tailor-made for each individual investor?

An instalment warrant is an agreement that enables you to purchase an asset over time. Under the agreement, the buyer makes an initial payment and then pays one or more instalments plus interest in the future to fund the asset. According to the tax office, warrants are very much like a loan, which has been a problem for super funds because they are not supposed to borrow.

To make the rules consistent across all asset classes, the government amended the Superannuation Industry Supervision Act in September 2007 to allow super funds to invest in warrant-style arrangements as long as certain conditions were met.

In particular:

- The borrowed funds must be used to purchase an asset (such as real estate) that is held in trust for the SMSF
- The fund must have the right to acquire legal ownership of the asset by making payments.
- The lender can only have recourse against the underlying asset, not other assets of the SMSF.

This means that the door is now open to a range of SMSF borrowing strategies as long as they have the features of a warrant. There are many banks and lending institutions that will set up SMSF loans that are tailor-made to your situation and will allow you to qualify under the new rules. You can also provide the funding yourself if you have appropriate legal documentation and trust arrangements in place.

If you are interested in exploring these options, you should get professional advice because there are lots of boxes to tick.

DIY dilemma

My husband and I have been advised to set up a DIY fund and then pay ourselves an allocated pension. We are currently transferring cash and assets, including shares into a fund. I am little confused about how the pension amount is calculated. Also, especially at the start, if there is not enough cash in the account, how is a pension paid out?

Superannuation pensions are fairly straightforward to set up and can provide some excellent tax outcomes but the rules regarding payments can sometimes be tricky to grasp. The amount of pension that you can, or must, take will primarily depend on your age, employment status and the type of pension you are taking.

If you are still working, your account-based (allocated) pension will be a transition-to-retirement income stream and you will need to draw a minimum pension based on the percentages set out below. Pensions commenced during the year should be pro-rated unless they were started in June.

For these pensions, a maximum limit of 10% of the account balance will apply until you retire or reach age 65.

Minimum pension drawdowns

Age	% of account balance for 2009-10	% of account balance for 2010-11 onwards
Under 65	2.0%	4%
65-74	2.5%	5%
75-79	3.0%	6%
80-84	3.5%	7%
85-89	4.5%	9%
90-94	5.5%	11%
95 or more	7.0%	14%

The rules on pension payments are very flexible. The key is to make at least one payment per annum and to ensure that you have kept within the pension limits. If there is not enough cash in your SMSF to start a pension immediately, you can delay the payment until later in the relevant financial year if you wish or wait until you have sufficient cash available. I'm sure your accountant or financial adviser can assist you with these details.

The definition of eligible

I have been receiving WorkCover payments for the past 10 years, having been incapacitated by an accident at work. My accountant tells me that changes in the definition of income mean I can no longer obtain a deduction for contributions to my SMSF as I am not an "eligible person". This is because "I received or was entitled to receive superannuation benefits in respect of eligible employment for the year of income". While I have no problem accepting that the income from WorkCover is taxable, I do not believe I received any "superannuation benefits" to render me ineligible. Do you have a better explanation for this?

Generally speaking, a taxpayer is an "eligible person" as long as their assessable income, exempt income and reportable fringe benefits from the employment are less than 10% of their total assessable income and reportable fringe benefits for the year.

For the purposes of the 10% rule, it has been found that if an employee receives periodic workers compensation payments from an insurer as a result of an injury suffered while engaging in eligible employment, and the payments are included in the employee's assessable income, those payments are "attributable to" that eligible employment.

Without more details about your situation, it is difficult to say whether your compensation payments are still "attributable to" your employment of a decade earlier. Your eligibility to contribute and claim a deduction will also depend on your age and whether you are engaged in any of the other eligible activities described in s290 –160 of the Income Tax Assessment Act. Please note this does not constitute legal advice.



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