

Asgard

“Your guide to allocated pensions”



You've accumulated a healthy balance in your superannuation account and you're looking forward to those retirement years you've been dreaming about. But what happens now? How do you make sure you're going to get the most out of your superannuation?



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In the May 2006 federal budget the government announced proposals to make significant changes to superannuation and these changes may affect the way that allocated pensions work. Full details will be released by the government closer to the date that changes will come into effect (1 July 2007). For a full summary of the proposals, visit www.asgard.com.au or speak to your financial adviser.

What is an allocated pension?

An allocated pension is a superannuation account that will provide you with a regular income stream from your superannuation savings. The income stream will generally be available to you once you've retired from the workforce. In some circumstances, you may be able to access it pre-retirement.

Currently, you can elect to receive a pension payment between a minimum and maximum limits as set by the Government. These limits may change from 1 July 07 as announced in the May 06 budget.

You can hold a range of assets in your allocated pension account, including shares, managed investments, fixed interest and cash, depending on your investment strategy.

One of the best things about an allocated pension is that it is generally much more tax effective than taking your super as a lump sum.

Case study

What are the tax benefits?

- You don't pay any tax on any returns earned by the investments in your account. These tax-free earnings remain in your account to increase the value of your investment, so you can potentially receive more income or increase the life of your superannuation funds.
- Rolling your super straight into an allocated pension means you defer the payment of lump sum tax, possibly indefinitely.
- Payments from your allocated pension account are assessed at ordinary marginal tax rates, but if you're over 55 or permanently incapacitated, you're also entitled to a tax rebate of up to 15% tax on income received, plus the Medicare levy.
- Contributions that you or your spouse made into superannuation (on your behalf and for which no tax deduction was claimed) are returned to you tax-free over the life of your pension.
- Generally, Centrelink treats only part of the income received from an allocated pension as income, so you may still be eligible for social security payments depending on your individual circumstances.
- Any unrealised capital gains in your superannuation account may be able to be rolled into your allocated pension account. No tax is payable upon rolling over and best of all, the investments can later be sold free of tax!

Doing it right

Let's say George, aged 65, has just retired and has \$350,000 in superannuation. After sitting down with his financial adviser, he decides to roll his super into an allocated pension. Under the levels set by legislation, for the first year of the allocated pension, George must draw a minimum pension of \$20,230 and no more than \$35,350.

Let's assume George wants to receive \$35,000 pa as income and draws this amount from his pension. At marginal rates, \$35,000 of income results in tax payable of \$6,375 (including Medicare). However, George will be entitled to the 15% rebate (\$5,250), as he hasn't exceeded his Reasonable Benefit Limit. This reduces George's ultimate tax liability (ignoring other rebates) to \$1,125 – an effective tax rate of only 3.2%.

Getting it wrong

Jenny is also retiring at 65 and has the same superannuation balance as George. However, instead of rolling her super into an allocated pension, she withdraws the whole \$350,000 from her super account as a lump sum. As this is treated as an eligible termination payment, Jenny pays tax of \$9,259* on this withdrawal. She then also has to pay tax (including CGT) on any income she made from reinvesting the lump sum in her own name. *Ouch!*

In comparison...

George would be in an even better position compared to Jenny if he had also made undeducted contributions to his superannuation account, as these are returned tax-free over the life of the pension. The balance of the pension is taxed, but he can still take advantage of the 15% tax rebate.

“Because George has undeducted contributions in his pension, some of the income drawn will be returned tax-free.”

Let's say 12 months before his retirement, George met with his financial adviser and they decided that George should make an undeducted contribution of \$100,000 to his superannuation account. At retirement, George now has \$450,000 in superannuation to purchase an allocated pension. For the first year of the allocated pension, George has to draw a minimum of \$26,010 but no more than \$45,450.

Because George has undeducted contributions in his pension, some of the income drawn will be returned tax-free. This amount or 'deductible amount' is calculated as the total of George's undeducted contributions (\$100,000) divided by his life expectancy at the start of the allocated pension (in this case 17.7 years). This gives George an annual tax-free (or deductible) amount of \$5,650 which will be available for the life of his allocated pension.

This means that only \$29,350 of the \$35,000 pension will be taxed. Tax (including Medicare) ordinarily payable on this amount would be \$4,595. However, George will be entitled to a rebate of \$4,403 (or 15% of \$29,350), which will reduce his overall tax liability to \$440 (Medicare levy only) – an effective tax rate of 1.3%.

*Assuming an equal pre/post 83 split and a 30% marginal rate

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For more than 20 years, we've been working behind the scenes with financial advisers to create products and services to match your financial needs. In fact, we're one of Australia's largest financial services groups, managing more than \$34 billion for 400,000 Australians. For more information go to www.asgard.com.au

Want to be more flexible?

Through an allocated pension, you can:

- choose the investments in your account according to your particular risk profile and requirements, rather than having no say over where your money is invested (as is the case with some other types of pensions)
- vary the amount of income you receive and the frequency and timing of each payment,
- depending on your changing needs. This is especially useful if you're balancing your allocated pension income against other income sources
- draw a lump sum at any time (if you've retired), say for a holiday or emergency. You'll have access to your money if and when you ever need it.

What about estate planning?

An allocated pension can run for your own lifetime (assuming the money doesn't run out!) or transfer to a beneficiary (generally your spouse) after your death. Allocated pensions are a good way to secure an income stream for your spouse, giving you peace of mind knowing that you can provide for your family in the future.

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Interested?

To get started, you first need to speak to your financial adviser. Allocated pensions are just one of the options available and your adviser will help you make the best decision for your personal circumstances.

Important information

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