RETIREMENT INCOME
GETTING STARTED

A regular income stream from an account-based pension or an annuity can be an effective way to fund your retirement. Some retirees may also be eligible for social security benefits from the Australian Government. It's important to understand how all these options work, to determine which is right for you.

Will I have enough to retire?

With improved life expectancy and advances in medical science, Australians can look forward to a much longer and more active retirement than past generations. A male retiring at age 65 will likely spend around 19 years in retirement and a female 22 years.[1] Enjoying a long and happy retirement, however, may cost more than you think. According to the Association of Superannuation Funds of Australia (ASFA), an individual seeking a comfortable lifestyle needs an annual after-tax income of $42,569 which would require a lump sum of approximately $686,231 at retirement to provide this level of income for 25 years.[2]

Your financial adviser can help you see how you are tracking by determining your future income potential, projecting your final savings at retirement, and taking you through your options.

Transition to retirement – flexibility and choice

Before you retire you have the option to 'transition to retirement' (TTR). This means you can reduce your work hours and supplement your income with potentially tax-effective withdrawals from your super through a pre-retirement pension. Alternatively, you can continue your current level of work, make withdrawals from your super and increase your super contributions. Your financial adviser can help outline your choices and the difference this may make financially, once you retire.

A pre-retirement pension forms part of a TTR strategy and is subject to a maximum annual drawdown of 10%. If you are fully retired, there is no maximum drawdown limit and payments will continue until your account balance is exhausted or you withdraw it in full. You also have a wide choice of investments including low-risk term deposit and cash products, and you can generally switch options at any time should your needs and circumstances change.

How do I access an income in retirement?

The most common ways to access a retirement income stream are:

- Allocated or account-based pensions: using only superannuation savings
- Annuities: using either super savings or ordinary (non-super) money.

Without adequate super or other investments, you may need to rely in part or whole on the government Age Pension for a retirement income. See the 'Social Security' section below for further information.

How does an account-based pension work?

An account-based (or allocated) pension lets you draw a regular income from a superannuation savings lump sum and any investment earnings. Your pension account balance is adjusted in line with market movements, investment returns, pension payments, lump sum withdrawals and fees.

How does an annuity work?

An annuity can be purchased with either super or ordinary (non-super) savings and converts a lump sum into guaranteed income payments for a set period of time.

The two main types of annuities are:

- Fixed term annuities which pay a guaranteed income for a defined period of time eg 20 years
- Lifetime annuities which pay a guaranteed income for the remainder of your life.

By guaranteeing your future income payments regardless of the underlying performance, the annuity provider effectively carries all the investment risk. They also offer flexible ownership options, indexing to protect against inflation and access to capital if required. The trade-off for an investor is you generally have no choice of investments, and can't change your income once the annuity has commenced.

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What happens to your account-based pension or annuity when you die?

The status of the income stream benefits upon your death will depend on whether beneficiary arrangements are in place and the type of product (account-based pension or annuity). Your financial adviser can explain the differences and help you decide which is best for your circumstances. When commencing an account-based pension or annuity, you can nominate a person(s) to whom benefits may be paid (as a lump sum or an income stream) in the event of your death.

There are three types of arrangements for account-based pensions: reversionary nomination, non-binding nomination and (lapsing or non-lapsing) binding nomination. In each case, the nominated person must be either your Legal Personal Representative (LPR), or a 'dependant', which the Superannuation Industry (Supervision) Act 1993 defines as:

- your spouse[3]
- your child (regardless of age)
- a person who was financially dependent on you just before you died
- a person with whom you had an interdependency relationship just before you died.[4]

For super annuities, the above restrictions also apply. Where you have a term annuity, the reversionary beneficiary can continue the regular payments or choose to take a lump sum. For lifetime annuities, the income will continue for the reversionary's lifetime, or may be paid as a lump sum in some circumstances.

It is important to note that death benefits paid to your estate, and adult children (with some exceptions), must be paid as a lump sum.

Annuities (non-super)

If you take out a fixed term annuity and die mid-term, the future income payments may be made to your estate or a reversionary or nominated beneficiary. Alternatively, a lump sum may be paid to your beneficiary or to your estate.

For lifetime annuities, a binding reversionary beneficiary can apply and income payments can continue to the beneficiary for their lifetime; alternatively a lump sum could be paid to your dependants or to your estate if you die within a chosen guaranteed period. Where a lifetime annuity has no reversionary beneficiary and you die outside of any guaranteed period, it will expire upon your death, meaning any residual benefit passes back to the annuity provider.

How are account-based pensions and annuities taxed?

Tax concessions vary depending on your age and circumstances and the type of income stream.

Account-based pensions

- Aged between preservation age and 60 – income received is assessable and taxed at your marginal tax rate. Part of each payment may be tax-free and you may qualify for a 15% tax offset on the taxable component which means you may end up paying little or no tax on your income. Lump sum withdrawals may also be taxed, part of the withdrawal may be tax-free and the remainder taxed at a maximum rate of 15% plus the Medicare levy.[5]
- Aged 60 or above – any income and lump sum withdrawals received are tax-free.[5]

Annuities

If you purchase an annuity using your super savings, it is taxed in the same way as an account-based pension. For annuities purchased with ordinary money, the income you receive will be assessable and taxed at your marginal tax rate. However, part of your payment, generally equal to the return of your original investment will be tax-free.

What happens to my Age Pension entitlements?

The social security income test treatment of your income stream will depend on whether it is an annuity or account-based pension and in some cases when it commenced. For some account-based pensions that commenced prior to 1 January 2015 and many annuities, part of each payment, generally equal to the return of your original investment is not counted. Other account-based pensions, including any commenced on or after 1 January 2015, are assumed to produce a 'deemed' level of income, while actual pension payments are ignored.

In addition, 100% of the value of an income stream purchased from 20 September 2007 is counted as an asset under the social security assets test.[6] For an account-based pension, the amount counted is the account balance of the pension. For an annuity, the amount counted is based on the initial investment used to purchase the income stream, less an allowance for the repayment of your original purchase price over time.

Which is better – account-based pension or annuity?

Your financial adviser can help you decide whether an account-based pension or annuity best meets your personal circumstances and income requirements. The table below provides a basic comparison.

	Account-based pensions	Annuities
Guaranteed income	No	Yes
Choice of investments	Yes	No
Ability to vary income	Yes – above a set minimum[7]	No
Access to capital	Yes	Yes – for fixed term annuities Yes – for lifetime annuities within the guaranteed period
Guaranteed (fixed term)	No	Yes – either lifetime or a chosen fixed term
Purchase with non-superannuation savings	No	Yes
Death benefit payable	Yes – of the remaining account balance	Fixed term – yes, a lump sum or continuing annuity payments Lifetime – yes, when death occurs within a chosen guaranteed period

About social security benefits

Centrelink delivers a range of government funded social security benefits to assist individuals and families. The type and amount of benefits you can receive depend on your personal and financial circumstances and your stage of life.

What is the Age Pension?

The Age Pension is a social security benefit designed to provide a basic retirement income for recipients.

Pension reform – transitional arrangements

A transitional rate arrangement is in place for some pensioners who were adversely affected by changes made to the pension system in September 2009. The transitional rate is based on the income test rules and payment rates (indexed to CPI) that applied before 20 September 2009, and will continue until the current rules provide an equal or better outcome for those affected. For more information on transitional rates and thresholds visit humanservices.gov.au.

What is the Service Pension?

The Service Pension, managed by the Department of Veterans' Affairs, provides income support to eligible veterans and eligible partners, widows or widowers. The Service Pension rates are the same as those for the Age Pension and are generally subject to the income and assets tests.

What is the Work Bonus?

The Work Bonus was introduced on 20 September 2009 to replace the Pension Bonus Scheme which was closed on 19 September 2009. It provides an incentive for pensioners over Age Pension age to participate in the workforce. Customers registered prior to its closure will continue accruing entitlements as previously. To compensate for the closure of this measure, the Work Bonus will operate as a pension income test concession for people of Age Pension age.

The concession means that the first $250 of employment income per fortnight is not counted for income test purposes. This concession equates to a maximum increase in Age Pension entitlement of $3,250 pa (single or couple combined).

Age requirements

Your eligibility for Age Pension depends on your current age and when you were born. If you were born before 1 July 1947, you have reached the qualifying age for Age Pension. From 1 July 2017, the qualifying age for Age Pension will increase from 65 years to 65.5 years. The qualifying age will then rise by six months every two years, reaching 67 by 1 July 2023. In the Federal Budget released in May 2014, the Government has proposed to increase the age pension age to 70 by the year 2035 – at the time of writing, this proposal had not been legislated.

For the latest information visit humanservices.gov.au. Refer to the table below to determine at what age you will be eligible for the Age Pension.

Born	Women eligible for Age Pension at age	Men eligible for Age Pension at age
Between 1 July 1947 and 31 December 1948	64.5	65
Between 1 January 1949 and 30 June 1952	65	65
Between 1 July 1952 and 31 December 1953	65.5	65.5
Between 1 January 1954 and 30 June 1955	66	66
Between 1 July 1955 and 31 December 1956	66.5	66.5
After 1 January 1957	67	67

The amount of Age Pension you receive will depend on the income and assets tests. The Age Pension is treated as taxable income and pension rates are indexed in March and September each year.

The table below shows the maximum Age Pension rates for singles and couples each fortnight.

Age Pension rate per fortnight as at 1 July 2015:

Single	$860.20[8]
Couple	$648.40 each or $1,296.80 combined

The income and assets tests

When determining your eligibility to receive the Age Pension or Service Pension, Centrelink applies two forms of assessment: the income test and the assets test – the one that results in the lowest payment rate will apply.

Understanding the assets test

For the purposes of the assets test, an asset is any property or possession that you fully or partly own. Assets are valued according to their market (sale) value.

Some of the assessable assets covered by the test are:

- funds in bank accounts, shares and managed funds
- superannuation funds (once over Age Pension age)
- motor vehicles, boats and caravans
- household contents and personal effects
- property such as holiday homes
- account-based pensions and other income streams.

Assets exempted under the test are a principal home and some retirement income stream products, such as annuities purchased before 20 September 2007.[9]

For social security purposes the assets test limits differ depending on whether you are single or married and whether or not you own your home. There are also different rates for a couple separated by illness and a couple where only one partner is eligible for the Age Pension. Visit humanservices.gov.au for full details.

Assets test threshold for homeowners as at 1 July 2015:

Family situation	For maximum pension	For part pension
Single	Up to $205,500	< $779,000
Couple (combined)	Up to $291,500	< $1,156,500

Assets test threshold for non-homeowners as at 1 July 2015:

Family situation	For maximum pension	For part pension
Single	Up to $354,500	< $928,000
Couple (combined)	Up to $440,500	< $1,305,500

For every $1,000 of assets over these amounts, the rate of Age Pension payable reduces by $1.50 (singles and couples combined).

Proposed changes

The assets test for pensions will change from 1 January 2017. The "taper rates" where for every additional $1,000 in assets above the minimum threshold for a full pension, fortnightly payments reduce will increase to $3 from the current $1.50. This change will effectively lower the upper asset threshold where the pension ceases to be payable.

The minimum threshold for a full pension will also increase from 1 January 2017.

Understanding the income test

For the purpose of the income test, income is defined as any money earned, derived or received for your use or benefit and includes:

- deemed income from bank accounts, investments, shares and interest
- gross income from salary and wages
- income from business and real estate
- deemed income from superannuation (if you are over Age Pension age)
- Account-based pensions commenced on or after 1 January 2015 (account based pensions commenced prior to 1 January 2015 may be treated differently depending on your circumstances).

Income test for account based pensions

Account-based pensions commenced on or after 1 January 2015 are deemed for income test purposes, like share dividends or interest, when assessing eligibility for the Age Pension. ABPs commenced prior to 1 January 2015 are 'grandfathered' and continue to be assessed under the pre-2015 rules provided you have also received an eligible social security payment (eg the Age Pension) from before 1 January 2015.

Prior to 1 January 2015, only annualised pension payments from an account-based pension that exceed the deductible amount are assessable under the Centrelink/DVA income test.

The deductible amount is broadly the part of your pension payment each year that represents a return of your original purchase price.

If you have a pre-2015 ABP that is grandfathered, you can lose the grandfathering status of your ABP under any of the following three circumstances:

- you cease to qualify for an eligible social security income support payment
- you fully commute and cash out or rollover the grandfathered ABP (eg by changing product providers)
- death.

A pre-2015 ABP will retain its grandfathered status on death if it automatically reverts to a reversionary beneficiary who is in receipt of an income support payment at the time of reversion.

Long term annuities

If you purchase a long term (term of six years or more, or longer than life expectancy if less than six years) and lifetime annuities where there's no residual capital value on termination, part of the annuity payment can be exempt from the Income Test. This is known as the deductible amount and is considered to be the return of your capital.

The deductible amount is generally calculated as:

$$\frac{\text{Purchase price – residual capital value}}{\text{Life expectancy or term}}$$

For the latest information visit www.humanservices.gov.au.

Income test for singles as at 1 July 2015:

Fortnightly income	Up to $160	Over $160
Reduction in payment	None – full payment	50¢ for each dollar over $160
Payment reduces to $0 once fortnightly income reaches this amount		$1,882.40

Income test for couples (combined) as at 1 July 2015:

Fortnightly income	Up to $288	Over $288
Reduction in payment	None – full payment	50 cents for each dollar over $288(combined)
Payment reduces to $0 once combined fortnightly income reaches this amount		$2,881.60

Commonwealth Seniors Health Card

Even if you don't qualify for the Age Pension, you may be eligible to receive the Commonwealth Seniors Health Card (CSHC). The CSHC provides a range of benefits, such as discounts on prescription medicine, Australian government funded medical services and other government concessions, to self-funded retirees who do not qualify for the Age Pension but have an adjusted taxable income of less than $51,500 pa for singles or $82,400 pa (combined) for couples. New account-based pensions commenced on or after 1 January 2015 will be subject to deeming. However ABPs that commenced prior to 1 January 2015 will be grandfathered so that nothing is included in the income test (assuming paid from a taxed super fund) if you are a holder of a CSHC immediately before 1 January 2015 and continuously in receipt of the CSHC.

Pensioner Concessions Card

The Pensioner Concessions Card is available to you if you receive income support payments such as the Age Pension, Disability Support Pension or the Service Pension. Cardholders are eligible for reduced cost medicines under the Pharmaceutical Benefits Scheme (PBS), as well as other concessions, including reduced water rates, energy bills and property rates, a telephone allowance, reduced public transport fares and reduced motor vehicle registration costs.

Why financial advice is important

Talking to a financial adviser before you retire will help put you on the road to financial security and access the following benefits:

- Getting help from a financial adviser can help you decipher complex super and tax legislation and translate them into actionable strategies.
- They follow a proven process to ensure all aspects of your financial well-being are covered.
- They can help you assess the best income stream option and also structure your retirement portfolio to minimise tax.
- They are supported by a network of technical and qualified specialists in super and retirement.
- You can schedule regular reviews to ensure you stay on track before and after you retire so all you need to focus on is enjoying a new more relaxed lifestyle.

1 Australian Government Actuary, Life tables, 2010–12.

2 ASFA Retirement Standard – March 2015. All figures in today's dollars (using 3.75% as a deflator) and assumed investment return of 7% per annum. Assumes retirement age of 65 and retirement duration of 25 years.

3 Includes de facto relationships (whether of the same sex or different sex) or in a relationship that is registered under a law of a State or Territory.

4 Two people are classified as having an interdependency relationship if they have a close personal relationship, they live together, one of them provides the other with financial support, and one or each of them provides the other with domestic support and personal care.

5 Applies to income from a taxed fund only.

6 Some income streams commenced prior to 20 September 2007 have a 50% or 100% assets test exemption. If you think this applies to you, check with your pension or annuity provider or seek financial advice. Complying defined benefits pensions such as a Government Sector Super Scheme pension are 100% assets test exempt.

7 Except pre-retirement pensions, which have a set maximum of 10% of the account balance

8 Including maximum pension supplement and energy supplement.

9 Annuities are 100% assets test exempt if commenced prior to 20 September 2004; 50% assets test exempt if commenced between 20 September 2004 and 20 September 2007; and 100% assets tested if commenced from 20 September 2007.

SPEAK TO US FOR MORE INFORMATION

If you would like to know more about retirement strategies or how to access social security benefits, talk to a financial adviser. They can give you more detailed information on the best approach for your situation.

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