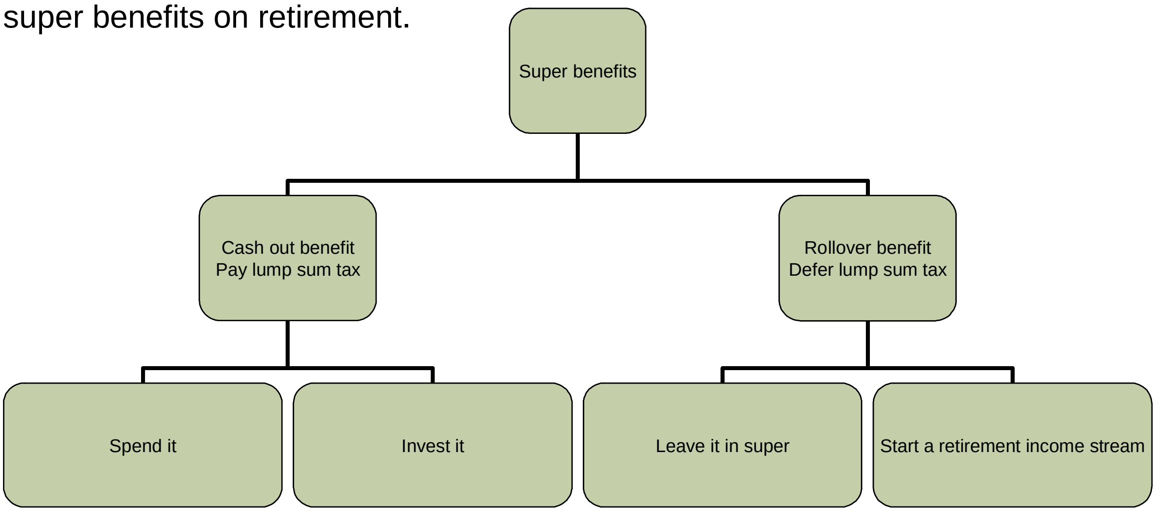
Retire in style with allocated pensions

As you plan for your retirement, you will come to realise that the choices available to you for investing your superannuation savings are extensive, and perhaps even a little daunting. It's important to know well ahead of your actual retirement day what decisions you need to make and how they will affect your retirement lifestyle - after all you'll only retire once.

The diagram below illustrates your key decision points in dealing with your super benefits on retirement.



Your first decision point is whether to stay invested in the super system through your retirement or whether you want to cash out your benefit.

Cashing out may be necessary if you need funds for immediate expenditure and don't have other investments. You may also want to cash out some super so you can invest it yourself (shares, investment property). Whether this is appropriate will depend on your particular situation, however remember that you have a wide range of investment opportunities in the super system, so you don't necessarily have to cash out to get a good return. The downside with both of these choices is that you'll lose part of your super benefit to lump sum tax.

If you're under 65 and don't need an income straight away, you can rollover to a super or rollover fund. Alternatively, you can rollover directly into a retirement income stream, such as a pension or annuity. In both cases, you don't pay any lump sum tax at the time of rolling over; you'll only be taxed if later you decide to cash out some of your benefit.

<u>7 reasons to invest in an allocated pension</u>

The checklist below contains 7 questions for you to consider as part of your retirement planning in determining whether an allocated pension is suitable for you.

Checklist question	How allocated pensions can help
☑ Do you want to defer lump sum tax?	No lump sum tax payable on direct rollover to an allocated pension.
☑ Is investment choice in retirement important to you?	Your account balance can be invested in any of the investment portfolios available to you, from cash to diversified to growth.
☑ Do you want to be able to set and change your income payments?	You can choose the level of your allocated pension payments, between government-set limits, and can change the amount at any time.
☑ Is tax-effective income important to you?	• No tax on investment earnings. • Part of pension payment may be tax free. • 15% tax offset on taxable payment.
☑ Do you want your retirement investments to help with your age pension eligibility?	Part of each pension payment is not counted in the Income Test. Account balance is counted in the Assets Test.
☑ Do you want access to your capital?	Your allocated pension account balance can be withdrawn as a lump sum at any time.
☑ Is flexible estate planning important to you?	Your dependants can receive any allocated pension account balance remaining on your death as either an allocated pension or a lump sum.

<u>Case study</u>

Mike has just retired from his job at age 65. He's married to Angela, age 63, who doesn't work and together they're planning their retirement.
Mike has a super benefit of $250,000 as well as a $30,000 term deposit earning 3.5% pa. He and Angela also have a car worth $20,000 and home contents of $20,000. Angela doesn't have any super or investments of her own.
Mike wants to know whether an allocated pension is a good choice for his retirement, taking into account the 7 reasons listed above.

1. Deferral of lump sum tax

If Mike cashes out[1]

- Undeducted (after-tax) contributions are tax-free
- First $112,405 of post 83 super is also tax-free
- Pays lump sum tax of $14,938
- $235,062 to invest

[1] Assumptions: pre 83 component $20,000; post 83 component $200,000; undeducted contributions component $30,000; marginal tax rate 47% + 1.5% Medicare levy

If Mike rolls over

- No lump sum tax
- Full $250,000 to invest

2. Investment choice

By rolling into an allocated pension, Mike can choose the investment portfolios his benefit is invested in. He chooses to invest:

- $50,000 in a cash portfolio
- $75,000 in a balanced portfolio
- $125,000 in a growth portfolio

This gives the bulk of Mike's retirement savings more time to grow before they're actually needed for his pension payments.

3. Flexible income payments

Mike can choose his starting income payment, provided it's more than the minimum of $15,920 and less than the maximum of $30,860. He can also change the amount at any time, including choosing to have his payment increase by inflation each year, between these limits, and can vary the frequency of the payment.

4. Tax-effective income

Allocated pensions receive the benefit of a range of tax concessions on income payments, including an annual tax-free amount and a 15% tax offset on the taxable part of the payment.

Example of Mike's overall tax situation using an allocated pension

Allocated pension payment	$25,000	
Bank interest	$1,200	
Total gross income	**$26,200**	
Tax-free pension payment	$1,850	($30,000 undeducted contributions / 16.21 yrs life expectancy)
Taxable income	**$24,350**	
Tax payable	$3,685	
15% tax offset	$3,472	[15% of ($25,000 - $1,850)]
Senior Australians tax offset	$596.50	
Final tax bill	**NIL***	
Total net income	$26,200	
Effective tax rate	**0%**	

* Medicare levy of $365.25 payable

5. Social security friendly

Allocated pensions are assessed favourably under the Centrelink Income Test, as part of each payment is not counted.

In Mike's case only $9,577 of his $25,000 allocated pension payment is assessed for the Income Test.

Under the Assets Test, the allocated pension account balance is fully counted.

6. Access to capital

Mike wants to make sure that if he needs to upgrade his car in a few years, he can access a lump sum of $20,000 to do so. Because he has his own account in an allocated pension, he has full access to his account balance whenever he needs it. Provided he's got sufficient funds in his account balance for the withdrawal, he simply makes a withdrawal request, pays any lump sum tax that applies and receives his money.

7. Flexible estate planning

Mike can nominate Angela as a beneficiary for his allocated pension, so she can take over his pension account on his death and either continue to receive pension payments or cash out a lump sum. If Angela pre-deceased Mike and was unable to inherit Mike's pension, then his family will still benefit. The amount[2] of death benefit Mike's dependants can receive equals the allocated pension account balance at the time of his death.

<u>Summary</u>

To **retire in style**, you need to know what you want to get out of your retirement and what your choices are to help you get there.

Once you know where you want to get to, use the 7-point checklist discussed above to help you decide which is the right product for your retirement. Each of the issues in the checklist is important, and you may have to weigh up some against others to get the result that's right for you.

A financial plan can help you bring this together and is a sound first step in making your retirement lifestyle achievable.

Remember that, although you'll have many choices on retirement, often the simple solutions are the best. That's where an allocated pension can be a simple and flexible way for you to convert your super savings into retirement income and enjoy your retirement years.

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[2] Note that in some instances, lump sum tax or excess benefits tax may reduce the net death benefit paid