ACCOUNT-BASED PENSIONS

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Account-based pensions provide tax-effective regular income to help meet your income needs using your superannuation savings.

BENEFITS

- Pension income is completely tax-free if you are aged 60 or over.
- Some of the income may be taxable if you are under age 60 but you will be entitled to a 15% tax offset if you are over preservation age or the pension is paid due to disability.
- Pension payments are flexible and can be varied at any time but you need to ensure you take the minimum each year.
- You retain flexibility by continuing to have a wide range of investment options and the ability to stop the pension at any time.
- You can nominate a reversionary or beneficiaries to receive the benefits upon your death under various estate planning strategies.

HOW IT WORKS

The most tax-effective source of income for retirees is an account-based pension. An account-based pension is an income stream paid from a superannuation fund. To commence an account-based pension, you first need to meet a condition of release or have unrestricted non-preserved funds in your superannuation account.

Account-based pensions are tax-effective compared to other sources of income because:

- Pension income paid to you from age 60 is not taxable.
- Pension income paid to you between preservation age and age 60 or due to disability is taxable, but you will be entitled to a 15% tax offset to help reduce tax payable.
- Within the pension account, all earnings and capital gains from investments are tax exempt this can boost the effective returns compared to other similar investments.

Your pension-account balance will increase with investment earnings and decrease because of pension payments, negative returns, fees and charges. These factors ultimately determine how long your account-based pension will last.

PENSION INCOME

An account-based pension is very flexible, allowing you to vary the amount of income you take. One of the few requirements is that you must take at least a minimum amount of income each year. There is no maximum and lump sums can be withdrawn at any time.

The minimum amount is based on your age and calculated as a percentage of your account balance when you commence the pension. The minimum amount is then recalculated every 1 July based on your age and account balance at that time.

TAXATION OF YOUR PENSION

When you commence an account-based pension the balance is split into a taxable component and a tax-free component. This is based on the split that was in your superannuation account just before you commenced the pension.

All future pension payments, lump sums and death benefits are split in the same proportions. For example, if your account balance at commencement consisted of $80,000 taxable and $20,000 tax-free, then 80% of all pension payments, lump sum withdrawals and your final death benefit would be made up of the taxable component.

Whilst you are under age 60, the taxable component is included in your assessable income with a 15% tax offset to help reduce your tax if you are over preservation age. But once you turn age 60, all pension income is tax free.

The Transfer Balance Cap will limit the amount of superannuation held in retirement (pension) phase. Pension balances and notional earnings in excess of the Cap can be subject to an excess transfer balance tax. Excess amounts can instead be retained in accumulation phase. where superannuation tax rates continue to apply or retained outside superannuation.

CENTRELINK

Account-based pensions are now assessed under deeming rules for the Centrelink income test. This means the income assessment is calculated using a deeming rate (set by the government) against your account balance.

However, if you commenced your account-based pension before 1 January 2015 and have been continuously receiving a means-tested payment from Centrelink or Veterans' Affairs (DVA) since 31 December 2014 your account-based pension may continue to be assessed under the deductible amount rules. These rules may be more favourable and only assess a portion of the income payments received. If you switch to a new pension provider or your Centrelink/DVA entitlements reduce to nil your account-based pension will revert to deeming rules.

Regardless of when your account-based pension commenced, lump sums withdrawn do not count as income for Centrelink/DVA purposes but under the deductible rules these withdrawals reduce how much of each income payment is not assessable going forward.

The account balance of an account-based pension counts as an assessable asset.

WHAT YOU NEED TO CONSIDER

- If you have made personal superannuation contributions in the current year for which you wish to claim a tax deduction, you must lodge a notice of deductibility form with your superannuation fund (and wait for confirmation that they have received the notice) prior to commencing an account-based pension.
- In the financial year that you either start or stop your account-based pension the minimum pension required for that financial year is pro-rated. If the pension is commenced in June, you do not need to take any income in that financial year.
- If you do not take the required minimum income, tax will apply on earnings of the account for the whole year.
- Your account-based pension is not guaranteed and pension payments can only be made while there are funds in your account. There is a risk that your pension income may cease (or reduce) if you draw your income too fast or if investment returns are poor.
- Upon death, any remaining account balance will be paid to your nominated beneficiary or to your estate or payments can continue to a nominated reversionary.
- If you are a Centrelink/DVA customer, you are required to notify Centrelink/DVA within 14 days about the commencement of the pension as it may affect your payment or any significant changes to the account-balance.

- If you have an existing account-based pension which is assessed by Centrelink/DVA under the deductible amount rules, switching to a new account-based pension will trigger a shift to deeming rules. In some circumstances this may be less favorable under the income test and can affect your Centrelink/DVA entitlements as well as aged care fees.
- If the value of your pension interests is greater than the transfer balance cap, you are required to withdraw the excess either by rolling back to accumulation phase or withdrawing the excess from superannuation, or a combination of both.
- Pension balances and notional earnings in excess of the Cap can be subject to an excess transfer balance tax Excess amounts can instead be retained in accumulation phase. where superannuation tax rates continue to apply or retained outside superannuation. Fees may be charged for your superannuation contributions. You should check the details in the fee section of your Statement of Advice and the Product Disclosure Statement (PDS) for your superannuation fund.

REFERENCES

You may wish to refer to the following websites for further information about account based pensions:

- www.ato.gov.au
- www.moneysmart.gov.au
- www.servicesaustralia.gov.au

The information in this document is of a general nature and does not take into account your own financial objectives, circumstances or needs. You should consider your own personal situation and requirements before making a decision.

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