

# REVISING RETIREMENT PLANS

While most people are looking forward to the super changes planned to commence from 1 July 2007, there are thousands of people considering retiring before that date who have to make decisions on the existing rules. You may also be considering retiring before the age of 60 after the new rules come into effect which means your super is still potentially subject to benefits tax.

by Trish Power



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**S**uperannuation fund members now fall into four distinct categories when considering the tax treatment of super benefit payments:

1. Planning to retire before 1 July 2007
2. Retiring on or after 1 July 2007 but under the age of 60
3. Retiring on or after 1 July 2007 but aged 60 or over
4. Already retired.

**Friendly warning:** You may need to read these 'simpler rules' more than once.

*Note: If you're planning to make any super contributions during the 2007 financial year you need to be aware of the new limits placed on undeducted contributions (see page 13 for more details).*

## 1. Planning to retire before 1 July 2007

If you're considering retiring before 1 July 2007 then you will need to be mindful of reasonable benefit limits and how you structure your retirement income streams to ensure you meet the current rules. Note that undeducted contributions are not subject to the RBL limits.

Your super fund pays no tax on investment earnings for assets funding an income stream, which continues under the new rules.

You will not automatically receive tax-free super benefits. With the right structure you may still enjoy tax-free benefits for the 2007 financial year. Before 1 July 2007, you can defer any lump sum ETP tax indefinitely by taking an income stream, although remember you can still take advantage of the tax-free threshold on lump sums. And if you've made after-tax contributions you're entitled to a tax-free amount known as the 'deductible amount' to your super fund, which reduces the taxable amount of your pension income.

You're also entitled to a tax offset against your pension income. If you're over the age of 55, a 15% pension offset is available against tax payable on your pension. Income streams from untaxed public sector funds won't be eligible for the pension offset.

From 1 July 2007, your super benefits will

be tax-free if you're aged 60 or over (see later), but if you're under the age of 60, then see the next section for information.

## 2. Planning to retire on or after 1 July 2007 but before you turn 60

Your benefit may still be subject to tax. Your benefit will be made up of only two ETP components — 'exempt' and 'taxable' compared to the eight components that apply prior to July 2007. For some individuals this may mean a lower tax bill than would have been the case under the old laws.

For example, an individual retiring under the age of 60 with a pre-July 1983 component could take his super as a lump sum and pay no tax on this component. If he had retired before July 2007 however, 5% of the pre-July 1983 component would have been included in his taxable income.

You are still eligible for the tax-free threshold on lump sums (\$135,590 for 2006/07 year), as is the case prior to July 2007. Any amount of your 'taxable' component above the tax-free threshold is taxed at 15%, as-

suming you're aged at least 55.

If you take an income stream, the rules that apply are similar to what applies before July 2007. The main difference is that because there are now only two ETP components rather than eight, more of your benefit is likely to be part of the tax-free 'exempt' component, such as your pre-July 1983 component. The 'exempt' component is then used to work out your tax-free or 'deductible' amount, which I explain in section 1 of this article.

When you turn 60, your pension becomes tax-free as explained in section 3.

*Note: Splitting your super contributions with your spouse may still be a tax-effective strategy under the new rules if you're planning to retire before the age of 60. You both may then be entitled to a tax-free*

Current system vs proposed system*		
Component	Current tax treatment	Proposal
Pre-July 1983	5% taxed at marginal rate	
Concessional	5% taxed at marginal rate	
Undeducted contributions	Exempt	Exempt component
Post-June 1994 invalidity	Exempt	
Capital gains tax exempt	Exempt	
Non-qualifying	Marginal rates	Taxable component (See schedule below)
Post-June 1983	Taxed as per schedule below	
Excessive	38%	Abolished
<b>Taxable component</b>		
<b>Taxpayers age</b>	<b>Current tax (for post-83 component)</b>	<b>Proposal</b>
Under 55	20%	20%
Age 55 to 59	Up to threshold* – Nil Over threshold* – 15%	Up to threshold* – Nil Over threshold* – 15%
Age 60 and over	Up to threshold* – Nil Over threshold* – 15%	Exempt

Source: *A plan to Simplify and Streamline Superannuation (May 2006), Commonwealth of Australia 2006.*

\*The threshold for the 2006/07 year is \$135,590. Note that benefits payable from untaxed schemes are subject to higher tax rates (see text).

ETP threshold for your post June 1983 (taxed) component, currently \$135,590 per person.

### Untaxed schemes

The 'nil' tax up to threshold (see above table) does not apply to lump sums from untaxed schemes (such as older public sector funds), which are taxed 15% up to threshold, then 30% for benefit above this amount up to \$700,000 and then marginal tax rates.

If you're taking a pension from an untaxed scheme then your pension income is taxed at marginal rates, although your after-tax contributions will be returned to you over time as tax-free amounts.

### 3. Planning to retire on or after 1 July 2007, and on or after you turn 60

From 1 July 2007, most super benefits taken as a lump sum or as an income stream will be tax-free, provided you are aged 60 years or older. You don't have to worry about exceeding reasonable benefit limits (RBLs) because the Government plans to abolish RBLs after 30 June 2007.

#### Untaxed schemes

If you're a member of one of the older public sector 'untaxed' super schemes, your final benefit will still be subject to tax on or after 1 July 2007 but at a lower rate than previously. The new rates are:

- For a lump sum: 15% tax on untaxed post-June 1983 component valued up to \$700,000, and top marginal tax rate for component amount above the \$700,000 threshold.
- For pension payments: Included in assessable income and taxed at marginal rates but you will be eligible for a 10% tax offset. Presumably your exempt component (see table on page 11) will be treated as tax-free amounts over time.

### 4. You have already retired

Until 30 June 2007, the tax treatment of your income stream/s and any lump sums that you withdraw receive the same treatment as before the 2006 May Budget.

From 1 July 2007, your superannuation benefit payments will be tax-free unless you are:

- under the age of 60, or
- receiving an income stream from an untaxed scheme.

If you fall into one of the categories that may still be liable to pay tax on benefit payments, then refer to earlier sections for the tax treatment of your benefits: the tax-free component of your income stream and/or any pension offset that you're entitled to will continue to be relevant.



For most Australians however who have retired and are receiving an income stream, any tax-free amounts or pension offsets that you were entitled to before July 2007 will become irrelevant because benefits are now exempt from tax.

Note: Earnings on any super fund assets that finance a pension will continue to be tax-free.

### Simpler pension rules from 1 July 2007

From 1 July 2007, all pensions must meet minimum standards, which are as follows:

- Minimum payments made at least annually (see table).
- No maximum payment limits, unless a transitional retirement income stream (TRIP).
- Lump sum death benefits tax-free to dependants but non-dependants pay tax.
- Reversionary pensions are tax-free when primary or reversionary beneficiary are over 60.

*IMPORTANT: Pensions that were commenced before 1 July 2007 and that meet current rules are deemed to meet the new minimum standards.*

### Transitional retirement income streams (TRIP)

Since 1 July 2005, Australians over the age of 55 have been able to access super benefits before retirement provided you take part, or all, of your super as a non-commutable income stream.

Non-commutable means you can't convert the income stream to a lump sum. The current rules enable a fund member to draw down roughly about 10% of the account balance each year.

From 1 July 2007, payment rules for TRIPs will be simplified and the maximum withdrawal will be no more than 10% of the account balance as at the start of each year.

*IMPORTANT: TRIPs that were commenced before 1 July 2007 and that meet current rules are deemed to meet the new standards.* ●

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### Proposed minimum annual pension payments (sample only)

Age	% of account balance (average)
55-64	4
65-74	5
75-84	6
85-94	10
95+	14

Source: *A plan to Simplify and Streamline Superannuation (May 2006)*, Commonwealth of Australia 2006.