

Transition to retirement pensions

Transition to retirement pensions can help ease the move from full-time to part-time work while offering significant tax and savings benefits.

What's a transition to retirement pension?

A transition to retirement pension is a type of account based pension that allows people between the ages of 55 and 64 to access part of their super through a pension while still working.

They can transition more easily from full-time to part-time work and supplement their earned income with pension income.

The good news is that it can also be used if working full-time and, when combined with a salary sacrifice strategy, can provide significant tax and savings benefits.

What are the benefits?

- ▶ **Supplement your income.** If you want to work fewer hours, a transition to retirement pension can supplement your part-time income so that you can maintain your current lifestyle.
- ▶ **Maximise your super.** As you are still working you can keep contributing to your super while using a transition to retirement pension. This includes 9% employer super guarantee and salary sacrifice.
- ▶ Also, it's not essential to need extra income to benefit from a transition to retirement pension. In combination with a salary sacrifice strategy, you can save considerable tax and boost retirement savings (see case study).
- ▶ **Tax-effective income.** Income that you receive from a transition to retirement pension is favourably taxed compared to your earned income. If you're aged 60 and over, the pension income is tax-free and if you're between 55 and 59, it is taxed at your marginal tax rate and receives a 15% tax offset.
- ▶ **Flexibility.** If your circumstances change, you can stop this type of pension and revert to simply accumulating your super.

Who is it suitable for?

A transition to retirement pension may be suitable if:

- you're between age 55 and 64
- you're still working
- you want to supplement your income or
- you want to boost your super and save tax.



Case study – Maximising super

David, aged 55, is an IT Manager earning \$150,000 pa which provides a net income of \$103,300. He plans to continue working full-time until age 65 and is exploring ways to boost his retirement savings. He also wants to maintain his current lifestyle which requires \$100,000 pa.

David has a superannuation balance of \$400,000 invested in a balanced investment option returning an average of 6.8% pa (after fees and taxes).

After speaking to his financial adviser, David decides to salary sacrifice \$36,500 into super. To supplement his reduced salary, David uses part of his super to start a transition to retirement pension, drawing down \$29,248 in the first year.

This strategy allows David to receive the same net income of \$103,300, but with significant savings. In the first year, this amounts to \$1,682.

This is partly because the money he salary sacrifices, is only taxed at 15% when it enters his super account. If taken as salary, this would be taxed at his marginal tax rate of up to 46.5% (including Medicare levy). In addition, David's pension income receives a 15% tax offset while he is aged 55 to 59 and is tax-free when he reaches age 60.

Table 1 – David’s financial position

	No strategy	Salary sacrifice + pension (\$)
Income position		
Gross salary	\$150,000	150,000
Pension income		29,343
Gross income	\$150,000	179,343
Less salary sacrifice		36,500
Taxable income	\$150,000	142,843
Net tax (includes Medicare Levy)	\$45,700	38,543 (includes 15% pension tax offset)
Net income	\$104,300	104,300
Superannuation		
Employer SG contribution	\$13,500	13,500
Salary sacrifice contribution		36,500
Total contribution	\$13,500	50,000
Less contributions tax	(\$2,025)	(7,500)
Less pension payment		(29,343)
Net position	\$11,475	13,157
Additional benefit year 1		1,682

Had David been age 60, he could have decreased his pension to \$22,448 while continuing to maintain his after-tax income of \$104,300. This would have increased the net benefit of this strategy by \$8,577.

Strategy considerations

A transition to retirement pension and associated strategies can be complex. Here are a few things to consider:

- **Tax position.** A transition to retirement pension and salary sacrifice strategy will generally be most effective if you are in a high marginal tax bracket and are salary sacrificing more than you are drawing down from a pension.
- **Impact on retirement savings.** If you use part of your super to access a transition to retirement pension, this may impact your future lifestyle. One way to avoid eroding your retirement savings may be to combine the pension with a salary sacrifice strategy.
- **Super contribution limits.** If you are salary sacrificing in combination with a transition to retirement pension, it’s important to contribute within the allowed limits to avoid paying excess tax. Until 30 June 2012, concessional super contribution caps (which include salary sacrifice and super guarantee) for anyone 50 or over are \$50,000 pa, however, after this date they will reduce to just \$25,000 pa. Any excess over the cap will be effectively taxed at the top marginal tax rate.

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