



## Transition to retirement pensions

### From 1 July 2009

#### Introduction

In 2005 the Federal Government introduced a new measure that makes it easier for individuals to stay in the workforce longer and ease into their retirement. Transition to retirement offers individuals with the option of reducing their working hours by supplementing their wages with superannuation pension income, rather than retiring permanently after attaining preservation age simply to access their superannuation benefits.

This has given rise to a popular strategy where an individual at preservation age who is still employed or self-employed can sacrifice all (subject to the new contribution limits effective 1 July 2009) or part of their salary into superannuation and commence a transition to retirement pension using their superannuation to supplement their income.

The key benefit to this strategy is moving current superannuation benefits from an environment where income or earnings are taxed at 15 per cent to the pension environment where earnings are exempt from tax. From ages 55-59 it also allows access to the full 15 per cent tax offset on income that is drawn from the pension, and tax free income from the pension after age 60.

#### Contribution Limits

Period	Concessional contribution cap# (1)	Transitional concessional contribution cap*	Non-concessional contribution cap
1 July 2008 to 30 July 2009	\$50,000	\$100,000	\$150,000
1 July 2009 to 30 July 2010	\$25,000	\$50,000	\$150,000
1 July 2010 to 30 July 2011	\$25,000	\$50,000	6 x (1)
1 July 2011 to 30 July 2012	\$25,000	\$50,000	6 x (1)
1 July 2012 to 30 July 2013	\$25,000	n/a	6 x (1)

# Subject to indexation

\* Applies to individuals who are 50 yrs or over during the relevant yrs

#### Pension Limits

The amount that must be drawn from an account based pension is a certain percentage of your member account balance - either the day before you commence the pension (in the first year) or as at the previous 30 June (from year 2 onwards). For "transition to retirement" pensions there is also an upper limit imposed, which ceases once the pensioner moves to permanent retirement or reaches age 65. The respective limits are as follows:

Age	Lower limit	Upper Limit *
55-64	4%	10% *
65-74	5%	N/A
75-84	7%	N/A
85-89	9%	N/A
90-94	11%	N/A
95 & over	14%	N/A

\* only applies to Transition to retirement pensions

Note:

The Government has announced that it will leave the minimum amounts that must be drawn from account based pensions, allocated pensions and market linked (term allocated) pensions at 50% of the prescribed amounts for the 2009/10 year as applied for the 2008/09 year. This includes transition to retirement pensions.

## How the strategy can work

There are two key ways transition to retirement can work. An individual may choose to continue working on a part time basis, using part of their superannuation to supplement their income instead of having to retire permanently from the workforce simply to access their superannuation.

In addition, individuals can also establish an effective salary sacrifice agreement with their employer whereby they direct a portion of their pre-tax salary as additional contributions to superannuation. This can be done in addition to supplementing their income with a transition to retirement pension.

## Example: Transition to retirement pension and salary sacrifice

John, 55 years old, earns \$150,000 pa (plus \$13,500 in SG), and has \$600,000 in super (all taxable component). He is currently salary sacrificing \$74,876 and drawing down \$60,000 from a TTR pension. This allows him to maintain a net income of \$103,300 pa to meet his living costs and save tax.

The table below compares John's tax position both now and from 1 July 2009. To maintain the same level of income, and stay within the new contribution caps (\$50,000 for over 50s), he must decrease his salary sacrifice to \$36,500 as this cap also includes his \$13,500 SG from his employer.

As a result, he doesn't need to withdraw as much pension income, but the tax benefits decrease slightly compared to the 2008/09 financial year.

However, when compared to doing nothing, this strategy is still beneficial for John.

	No strategy (\$)	Salary sacrifice + TTR pre-July 2009 (\$)	Salary sacrifice + TTR post-June 2009 (\$)
<b>Income</b>			
Gross salary	150,000	150,000	150,000
<b>TTR pension</b>	-	<b>\$60,000</b>	<b>30,000</b>
<b>(Less salary sacrifice)</b>	-	<b>(74,876)</b>	<b>(36,500)</b>
Taxable income	150,000	135,124	143,500
Gross tax payable	46,700	38,797	41,980
(Less pension tax offset)	-	(9,000)	(4,500)
Medicare levy	-	2,027	2,153
Net tax	46,700	31,824	39,633
<b>Net Income</b>	<b>103,300</b>	<b>103,300</b>	<b>103,867</b>
<b>Tax</b>			
Net tax (Including Medicare levy)	46,700	31,824	39,633
Super contributions tax	-	11,231	5,475
<b>Total tax</b>	<b>6,700</b>	<b>43,055</b>	<b>45,108</b>
<b>Additional saving</b>	-	<b>3,645</b>	<b>2,159*</b>

\* Includes the additional \$567 in net income (\$103,867 - \$103,300)

Super guarantee has not been included in this table as it does not affect the taxation outcomes. Contributions tax paid on SG contributions will be the same in all three scenarios (15% x \$13,500 = \$2,025).

The information contained in this document is of a general nature only and is not intended to be personal advice. No person should act solely on the basis of the information contained herein but only after discussing their individual circumstances with their financial Adviser.  
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If you are less than 60 and receive a “transition to retirement” pension the exempt component (ie the portion paid from any undeducted contributions) will be completely tax free, while the taxable component will be taxable at marginal rates but is subject to a rebate of 15%. (ie if you are on the 46.5% tax bracket you will receive a rebate of 15% effectively reducing the rate to 31.5%).

## Tips/Traps

- Income from a non-commutable pension will be assessed as income for social security purposes (an exempt amount applies based on purchase price / relevant number). Therefore some clients may be better off not commencing a pension if social security entitlements are an issue. Alternatively, commencing a pension that replace salary and wages may improve pension entitlements under the income test as it will be treated more favourably due to the exempt amount.
- The condition of release for over 55s may tempt members/trustees of self managed superannuation funds which have significant unrealised capital gains in the accumulation phase to commence a non-commutable pension upon reaching preservation age to sell assets in the pension phase (pension income is exempt), and then commute the pension back into the accumulation phase. Such a strategy could be employed repeatedly to avoid capital gains tax while allowing members to accumulate their superannuation. The purpose of such a strategy could be seen to avoid tax and may fall within the scope of Part IVA of the Income Tax Assessment Act. This is an issue that the ATO will likely monitor very closely.
- On the 17 November 2005 the ATO released guidance on the transition to retirement pensions stating that, “An eligible person may take out a pension under the transition to retirement rules. At the same time, that person may engage in an effective salary sacrifice arrangement and contribute to a complying superannuation fund for their own benefit”.

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