

What is an *Account Based Pension*?

An account based pension is an investment which pays you a regular and tax effective income in retirement.

How do account based pensions (ABPs) work?

You invest money from a superannuation fund into an ABP. The ABP then pays you a regular income comprised of earnings and capital until your account runs out.

The annual income you choose must be at least equal to the Government's prescribed minimum, based on your account balance.

Here's an example to show you how ABPs work.

Let's say Jack, aged 60, is married to Jenna. Jenna has her own retirement investments and Jack has \$500,000 invested in an ABP. This ABP generates tax free earnings at, say, 8% p.a. which equals \$40,000 in Year 1. If Jack draws an income of, say, \$33,000 (indexed at 3% p.a.), he will pay no tax on that. His account balance at the start of the next year will therefore be \$507,000. And so on and so on, as you can see in Table 1.

In ten years time, Jack's account balance will be \$541,310, with earnings of \$43,305. Jack's income will be \$43,058, and this will be tax free.

Over those 10 years, tax free earnings in the fund would total \$419,865, and the total tax free income Jack would draw would be \$378,308. And Jack would still have an account balance of \$541,310.

Because Jack has been taking less than the fund earns each year the account balance has actually grown over the first 10 years. If he continues to take the indexed pension, his balance will eventually decline but he will still have

\$286,137 in the account by age 85 and will receive a tax free pension payment from it of \$69,095 in that year.*

What are the tax advantages of ABPs?

- ☑ Lump sum tax is deferred when you transfer superannuation money to an ABP. Once you are 60+, lump sum tax will be eliminated.
- ☑ No tax on earnings in the fund.
- ☑ Little or no tax on ABP income. In fact, once you are 60 or more, you will pay no tax on ABP income.

Case study: \$150,000 p.a. tax free

Let's say Evan and Claire, both aged 65, retire with the following:

Super (Evan)	\$1,300,000
Super (Claire)	\$180,000
Cash	\$520,000
	<u>\$2,000,000</u>

The couple require a retirement income of \$150,000 p.a.

We might recommend investing along the lines of Table 2 (see next page).

This type of portfolio would enable Evan and Claire to generate their required \$150,000 p.a. income tax free.

Importantly, the couple would need to choose an underlying asset allocation which met their investment return requirement while satisfying their tolerance to risk.

Table 1: \$500,000 invested in an ABP*

Age	Account balance	Tax free fund earnings	Jack's income	Tax
60	\$500,000	\$40,000	\$33,000	Nil
61	\$507,000	\$40,560	\$33,990	Nil
70	\$541,310	\$43,305	\$43,058	Nil
Totals (to age 70)		<u>\$419,865</u>	<u>\$378,308</u>	<u>Nil</u>

*Assumptions: Earning rate 8% p.a. The income is drawn at end of year and is indexed at 3% p.a. No other assessable income. Jenna's investments, together with Jack's ABP, generate sufficient income for them. Income indexed at 3% p.a.

Table 2: Evan and Claire's tax free retirement income

Investment	Owner	Amount	Income
Account Based Pensions	Evan	\$1,300,000	\$106,121
Account Based Pensions	Claire	\$180,000	\$14,708
Shares (fully franked)	Joint	\$500,000	\$28,571
Cash	Joint	\$20,000	\$600
Totals		\$2,000,000	\$150,000

Income Tax: Nil

Income from shares 4.0% p.a., plus refund of franking credits. Cash earns 3.0% p.a. No other assessable income.

Do ABPs have a Centrelink advantage?

Yes, the income from an ABP is only partially assessed by Centrelink, so if you are subject to the income test an ABP could be of assistance.

For example, let's say George is 65 and has \$300,000 in an ABP from which he chooses to take an income of \$17,000.

Of that, \$16,574 isn't counted for the Age Pension income test, only \$426 is.

PROS

- ▶ Highly tax effective
- ▶ Can make estate planning easier
- ▶ Could help you increase Age Pension benefit
- ▶ Easy to withdraw some or all of your capital
- ▶ Full range of assets in which to invest

CONS

- ▶ Minimum limit on annual income
- ▶ Fully assessed by Centrelink's assets test

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Importantly, our initial advice isn't a 'set and forget' service. Instead we offer you regular financial mentoring and ongoing guidance – in all aspects of your personal finances – to set you, and keep you, on the path to financial wellbeing.

Our team of experienced financial professionals can provide you with a detailed and totally tailored blueprint for financial success in any or all of the following areas:

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- Retirement planning
- Superannuation
- Wealth creation
- Investments
- Home loans

- Commercial loans
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- Personal estate planning
- Personal risk insurance
- Investment loans
- Car finance
- Business estate planning
- Business risk insurance.

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Because knowledge is the first step to creating a secure financial future.

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