

Insights

Tools for sound decision making

February 2009

Don't get caught short in retirement

Your guide to minimising tax and maximising
your super leading up to your retirement,
through a Transition to Retirement strategy



In this issue:
Maximising your income
towards retirement and beyond

Synopsis

If you're over 55 and still working, taking advantage of a Transition to Retirement strategy might just be the thing to give your retirement savings a boost. Whether you're working full or part time, the strategy allows you to access your superannuation savings, while also giving you the opportunity to access some attractive tax benefits.

Transition to retirement

Most people don't realise that their investment strategy post retirement is proportionately more important than their pre-retirement plan.

In fact, accumulating wealth before your retirement is only half the story. Your focus should be equally placed on generating income for your retirement years. We should keep in mind that one of the biggest risks of investing for retirement is running out of money once you have stopped working.

On average, an individual Australian saves a constant percentage of pay through superannuation, from age 25 to 65, then decumulates for around 25 years. The Russell 10/30/60 retirement rule derives its name from the fact that every dollar decumulated consists of roughly:

- » 10 cents of savings from your working years;
- » 30 cents of investment return earned during the accumulation phase; and
- » a whopping 60 cents of investment growth earned during the decumulation phase.

The 'Transition to Retirement' (TtR) strategy is closely aligned to the Russell 10/30/60 rule as it focuses on maximising your ability to save for retirement, regardless of your level of employment. Whether you're employed full time or part time, a TtR strategy could be an ideal way to assist you to achieve your retirement planning goals sooner.

What is a TtR strategy?

The strategy involves commencing a TtR pension from superannuation and, at the same time, salary sacrificing any surplus income back into a new superannuation fund.

The concept was originally devised to provide financial assistance to those wishing to transition to retirement by working part time for a period before finally leaving the workforce. As there are currently no requirements for those accessing a TtR pension to prove working status, this strategy has become popular with full-time workers looking for an opportunity to boost their retirement savings.

The benefits of commencing a TtR pension arise for three reasons:

1. Once a pension has commenced, the tax on earnings within the fund reduces from 15% to nil.
2. Pension payments are usually taxable, but are accompanied by a 15% rebate for those under age 60, and are totally tax free for those over 60, whereas salary is fully taxable.
3. Excess income can be salary sacrificed back into superannuation, which boosts your tax position even further, thus helping you build even more for your retirement nest egg.



Bevan Green
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In a nutshell, a TtR strategy creates the opportunity for you to restructure the way your income is received so that, whilst your day-to-day income may remain basically the same, your superannuation balance upon retirement can be significantly increased.

What is a TtR pension?

A TtR pension is an income stream that enables you to access your superannuation without actually retiring. For people under the age of 65, the minimum amount received as income each year is 4% of the account balance. There is

also a maximum income cap of 10% of the account balance, which is calculated at the start of each new financial year. Careful planning is required to optimise a TtR pension, so speak to your financial adviser to ensure that it remains suitable for you both now and into the future.

Also, while you will receive regular payments from a TtR pension, it's important to know that these pensions can't be accessed as a lump sum, which can only be accessed upon your retirement or reaching age 65 (whichever comes first), or other permitting circumstances.

Case Study

Jim provides a good example

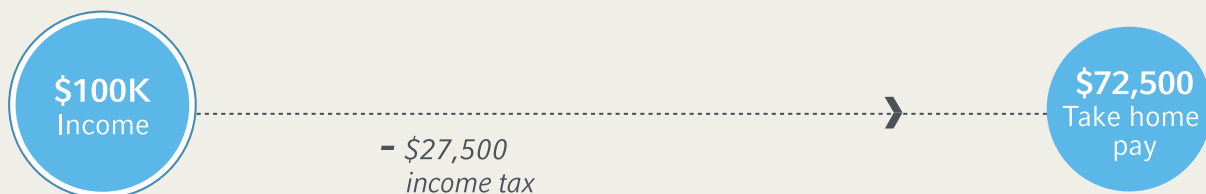
He is 60, works full time, and earns \$100,000 a year.

His income tax payment of \$27,500 leaves him with \$72,500 to meet his living expenses. Jim decides to salary sacrifice \$50,000 a year to superannuation, dropping his taxable income to \$50,000. He now only pays \$9,750 in income tax.

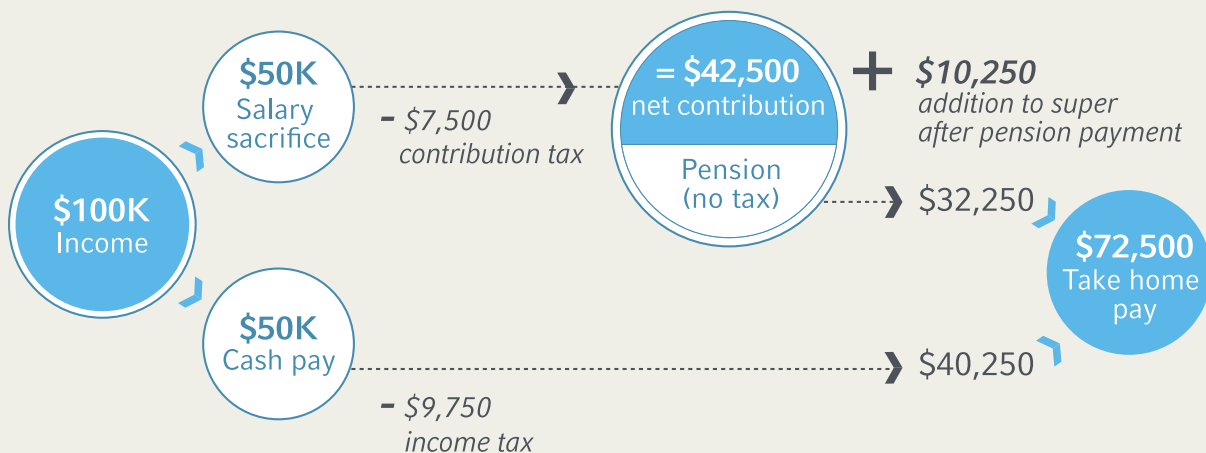
To make up the shortfall in income, Jim starts a TtR pension, and he only needs to receive \$32,250 from the pension to maintain his current lifestyle. As he is over 60 his pension will be tax free.

His contribution to superannuation will be taxed at 15%, but that still leaves \$42,500 in his account. In other words, Jim is adding \$10,250 more a year to his superannuation account than he was before he implemented the strategy, but still taking home the same income.

WITHOUT TtR STRATEGY



TtR STRATEGY



Note: This is a general example and is not specific to your personal situation. The figures in this example are based on the income tax rates that apply in the 2008/09 financial year.

Who can access a TtR pension?

You can access a TtR pension if you are 55 years of age or older. Regardless of whether you are working full time and looking to reduce your hours, or working full time and loving it, you can access a TtR pension. Remember, if you do commence a TtR pension but no longer need the income, there is even the flexibility to roll back your pension to the accumulation phase, assuming you meet the eligibility criteria.

Why adopt a TtR strategy?

As mentioned, the biggest investment risk you face in retirement is running out of the capital you will need to fund the rest of your life. Determining how long you need your money to last is a vital component that will impact your standard of living in retirement. Investors cannot rely on the law of averages to estimate longevity. If you find you need your income to stretch for an additional ten years to what you were expecting, you will need to squeeze an extra 2-3% each year from your investments - which can be a difficult task for any investor!

The lesson here is that longevity uncertainty becomes a greater concern than investment risk the older you get and this should be factored into investment strategies during the accumulation and decumulation phases.

Keep in mind that if you retire at 65, you may live another 20 years or more, which means you still need to be in long-term planning mode. A TtR strategy is an ideal way to maximise your super savings, while reducing the tax you pay – which ultimately means more money in your pocket for your retirement!

So, if you're young at heart and want to keep working, a TtR strategy may well be the answer to helping you achieve your financial goals upon retirement.

“A TtR strategy is an ideal way to maximise your super funds, while reducing the tax you pay – which ultimately means more money in your pocket for your retirement!”

To learn more, speak to your adviser

Making a financial choice is an important decision. While TtR strategies are an effective way for those over 55 years who are either in the workforce or retired, you should speak with your financial adviser about whether the strategy is right for your particular circumstances. Your adviser will help you calculate how much to salary sacrifice and how much your pension balance should be. He or she can also advise on the amount you may need to draw down each year, and can assist in establishing what is the best portfolio mix to suit your risk profile.

Your adviser is there to answer any questions you may have regarding TtR strategies and superannuation in general.

You can also visit russell.com.au to access a range of support material and information on TtR strategies including a webcast and a TtR calculator, which shows how starting a TtR pension could impact your income and tax situation for one year.