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FINANCIAL PLANNING

Retirement Income Streams

A Financial Advice Technical Guide

Contents

If you like the idea of receiving regular income in retirement, then a retirement income stream may be the answer for you. However, there are many kinds of retirement income streams to choose from. This guide is designed to help you understand how the main options work, their relative merits and special features.

The following information is current as at 1 July 2021.

Income stream overview

What is an income stream?

Income streams are generally available as either pensions or annuities. The main difference between a pension and an annuity is the provider:

- Pensions are generally provided by superannuation funds. They can generally only be purchased with accumulated superannuation monies.
- Annuities are provided by life insurance offices, friendly societies or trade unions. They can generally be purchased with accumulated superannuation monies, or with non-superannuation (ordinary) monies.

Types of income streams

There are four main types of income streams available:

- Account based. Account based income streams can only be purchased with superannuation monies. Each year you are required to take a minimum payment which is based on your age at commencement and at each subsequent 1 July. No maximum income limit applies unless it is a Transition to Retirement (TTR) income stream, where a maximum of 10% of the account balance applies. Your money is invested for you, and lasts as long as there is money left in your account.
- Non-account based. As the name suggests, a non-account based income stream is one for which there is no account balance attributable to you. These are generally fixed term and lifetime pensions and annuities.
  - Fixed term. As the name suggests, the term is fixed generally according to your life expectancy and the income level is also fixed at commencement, though it may increase in line with inflation.
  - Lifetime. These income streams generally last as long as you do. As with a fixed term, the income level is pre-agreed. Unlike the other types, the income is guaranteed for your lifetime – no matter what investment returns are generated and no matter whether you outlive your life expectancy.
  - Asset test exempt. These income streams allow the recipient favourable social security treatment under the asset test. These were only available until 19 September 2007 and came in the form of lifetime, fixed term and market-linked income streams. Asset test exempt income streams may, subject to meeting certain conditions, be purchased from 20 September 2007 from the commutation of existing asset test exempt income streams.
- Market linked. Market linked income streams can only be purchased with superannuation monies. The term is fixed at commencement and the income level can vary from plus or minus 10% from the annual calculated amount. Public offer superannuation funds offered these types of income streams up until 19 September 2007. They may, subject to meeting certain conditions, still be purchased from public offer superannuation funds from the commutation of existing market linked pensions and complying fixed term pensions/annuities. It is also possible for a Self Managed Superannuation Fund to pay this type of income stream.

Each of these types of income stream have their relative merits and special features. These are set out for you on the following pages.

<table>
<tr><th></th><th>Market Linked Income Streams (Limited availability after 20 September 2007)</th><th>Account Based Income Streams</th></tr>
<tr><td>What income do you receive?</td><td>Income is calculated by reference to your account balance at commencement and subsequently every 1 July, divided by a payment factor.

The amount calculated can then normally be varied up or down 10%. However from 2019-20 until 2021-22 the amount can be varied up to 110% or down to 45% as part of the governments response to COVID-19.</td><td>Income is subject to a minimum payment per year expressed as a percentage of your account balance based on your age at the commencement date and each subsequent 1 July as follows:
<table>
<tr><th>Age</th><th>%*</th></tr>
<tr><td>Under 65</td><td>2</td></tr>
<tr><td>65–74</td><td>2.5</td></tr>
<tr><td>75–79</td><td>3</td></tr>
<tr><td>80–84</td><td>3.5</td></tr>
<tr><td>85–89</td><td>4.5</td></tr>
<tr><td>90–94</td><td>5.5</td></tr>
<tr><td>95 or more</td><td>7</td></tr>
</table>
No maximum annual income limit applies unless a TTR income stream (10% of the account balance).

* Minimum draw down percentages have been reduced by 50% for the 2019-20 and 2021-22 as part of the governments response to COVID-19.</td></tr>
<tr><td>Can you withdraw money?</td><td>Not generally accessible.</td><td>Ability to make withdrawals at any time subject to fund rules with the exception of a TTR income stream.</td></tr>
<tr><td>How long do payments last?</td><td>You can choose from a term that lies between:
– Your life expectancy at purchase
– The life expectancy of a person five years younger at purchase
– The number of years between your current age and 100.

If you have a spouse with a longer life expectancy who will continue to receive the pension on your death, the term can be based on the above rules using their life expectancy.</td><td>Until the money in your account runs out.</td></tr>
<tr><td>Can you choose how the money is invested?</td><td>You have a number of choices about how your money is invested.</td><td>You generally have a number of choices about how your money is invested.</td></tr>
<tr><td>What happens if you die?</td><td>The market linked income stream will continue to be paid to your reversionary beneficiary (if any), or may be paid to your other beneficiaries or your estate as a lump sum.</td><td>Certain tax dependent beneficiaries may receive the remaining balance as an income stream or lump sum. Alternatively, it can be paid to other beneficiaries via your estate as a lump sum.</td></tr>
</table>

Non-Account Based Income Streams		
	Lifetime Pensions/Annuities	**Fixed Term Pensions/Annuities**
What income do you receive?	Income is fixed but may increase annually in line with a fixed percentage or CPI.	Income is subject to a minimum payment per year expressed as a percentage of your account balance based on your age at the commencement date and each subsequent 1 July as follows:.
Can you withdraw money?	Not generally accessible.	Not generally accessible.
How long do payments last?	Until you die (or where you have a reversionary beneficiary – until you both die).	You can choose the length of the term for the payments.
Can you choose how the money is invested?	Not relevant as income is fixed.	Not relevant as income is fixed.
What happens if you die?	There are two options: Where you have a reversionary beneficiary, they may continue to receive income payments until they die. When you have a guaranteed period, if you die within the period, the residual value is paid to your beneficiaries or your estate.	The remaining income payments flow to the reversionary beneficiary for the remainder of the term or the residual value is paid to your beneficiaries or your estate.

Transition to retirement

If you have reached your preservation age, subject to the rules of your fund, you may be able to draw on your super without having to retire permanently from the workforce.

Under these rules, if you are still working, you will have to receive your super as a particular type of pension. These pensions, known as TTR income streams, will generally not be “commutable”. Broadly speaking, this means you will not be able to withdraw lump sum amounts from the income stream. They include account based pensions and market linked pensions. For an account based pension, a maximum income limit of 10% per annum of the account balance will apply.

If you select a TTR income stream, you will be allowed to take a lump sum once you meet a full condition of release such as retirement or reaching the age of 65. Alternatively, you can stop the pension and roll back your benefits to the accumulation phase at any time.

Taxation of income streams

How is an income stream taxed?

From your preservation age to 59

Not all income received from an income stream from a taxed superannuation fund is necessarily taxable for income tax purposes. The following table is a guide to how income streams are taxed.

Taxable Income	Income stream payment (assessable income) less tax free portion*.	= Taxable income
Tax Payable	You pay tax on taxable income at marginal tax rates, less a 15% tax offset for superannuation pensions. The tax offset is not available for income streams that are not from taxed superannuation funds.	= Net tax paid limited to zero where offset exceeds tax

* This is the portion of the pension payment that is not taxed.

Your preservation age is determined by your date of birth as follows:

Date of Birth	Preservation Age
Before 1 July 1960	55
1 July 1960—30 June 1961	56
1 July 1961—30 June 1962	57
1 July 1962—30 June 1963	58
1 July 1963—30 June 1964	59
On or after 1 July 1964	60

Age 60 and over

The income you receive from an income stream from a taxed superannuation fund (i.e. a pension) will be tax free and is not required to be included in your tax return.

Income streams and social security

Which income streams are asset or income test exempt?

The income and assets test are both used by Centrelink and the Department of Veterans' Affairs to determine eligibility for social security payment.

For social security purposes, income streams are divided into three assessment as summarised in the following table.

Income Stream	Income Test	Assets Test
Asset test exempt income stream – eligible lifetime, fixed term, market linked income streams*.	Annual Payment – PP/RN	Eligible lifetime and fixed term income streams: – 100% of the purchase price is exempt if purchased before 20 September 2004; – 50% of the reduced value~ of the purchase price is exempt if purchased 20 September 2004 – 19 September 2007 – Market Linked income streams – 50% of ongoing account balance is exempt if purchased before 19 September 2007.
Asset-tested long term^ and grandfathered# account based income streams.	Annual Payment – (PP-RCV-Commutations)/RN	Non-account based: – If 100% RCV, purchase price – If RCV<100%, reduced value of purchase price~ Account-based - remaining account balance.
Asset-tested lifetime purchased before 1 July 2019	Annual Payment – (PP-RCV-Commutations)/RN	Reduced value of purchase price~.
Asset-tested lifetime purchased after 1 July 2019	Non-deferred income stream: 60% of payments are assessed Deferred income stream: 60% of payments are assessed once the deferral period ends and payments commence	Those that meet a declining capital access schedule: – 60% of the purchase price counted from 'assessment day' to 'threshold day'+. – 30% of the purchase price thereafter.
Asset tested fixed term income streams with an initial term of 5 years or less; Non- grandfathered# account based income streams.	Deemed	Fixed term income streams: – 100% RCV, purchase price. – RCV<100%, reduced value of purchase price~. Account-based - remaining account balance.
Non-purchased defined benefit pensions	Annual payment, less tax free portion (but no more than 10% of the annual payment unless the payer is a military/ defence super fund)	100% exempt if employment related and paid from a pre 20 September 1998 public or private sector superannuation fund; otherwise: – Annual payment x Pension valuation factor†.

* Asset tested market linked income streams receive the same income test.

^ Long term income streams have a term greater than 5 years or at least the life expectancy if the term is 5 years or less but excludes lifetime income streams.

\# To be grandfathered, the account based income stream needs to have commenced before 1 January 2015 and the recipient has also continuously received an income support payment since prior to 1 January 2015.

~ Calculation of reduced value: PP [(PP - RCV) x (term elapsed/RN)].

\+ Assessment day is the later of:
- the day the client first satisfies a condition of release;
- the day the first amount was paid for the income stream;
- the day the client acquired the income stream, if no amount of money is identifiable as having been used to pay for the income stream, for example, collective defined contribution streams.

The 'threshold day' is currently the later of either age 84 or a minimum of five years from 'assessment day'. Where the lifetime income stream is reversionary, there are additional definitions for 'assessment day' and 'threshold day'.

† Pension valuation factors can be found here https://guides.dss.gov.au/guide-social-security-law/4/9/5/50

Where:

PP is the Purchase Price and means the full purchase price less any commuted amounts.

RN means the Relevant Number and is the term at purchase for a market linked or fixed term income stream. It is your life expectancy for account based and lifetime income streams.

RCV means the Residual Capital Value.

Eligibility for Age Pension

Who is eligible for the Age Pension?

For some people Age Pension will make up most of their retirement income. For others it works out to be a handy bonus. Some do not receive it at all. So, understanding your eligibility is a crucial part of retirement planning.

Presently both males and females must be aged 66.5 if they did not reach age 66 by 30 June 2021 to apply for the pension. The required age pension age for both males and females born on or after 1 July 1955 is as follows:

Born between	Age pension age
1 July 1955 to 31 December 1956	66½
1 January 1957 and later	67

The person claiming Age Pension must be an Australian resident.

Generally, a person qualifies if they have always lived in Australia. A person who has lived overseas can also qualify if they either:

– Have lived in Australia for at least 5 years continuously and have, in total, lived in Australia, on or off, for more than 10 years
– Have lived in a country with which Australia has an international Social Security Agreement that counts towards Australian residence
– Have a qualifying residence exemption (i.e. they are, or were, a refugee)
– Are a woman who was widowed here, and both she and her partner were Australian residents at the time, and she has lived in Australia for 104 weeks immediately before the claim
– Were receiving Widow B pension, Widow Allowance or Partner Allowance immediately before turning age pension age.

A person's Age Pension entitlement is calculated by Centrelink by applying the income and assets tests. The method that produces the lowest entitlement will determine the amount of Age Pension a person will receive. The Centrelink rules provide specific definitions of assets and income and it is important that you have an understanding of these rules. You should discuss with your financial adviser whether you may qualify for Age Pension.

For more information on Centrelink payments, please call 132 300 or visit your nearest Centrelink office. For more information on Veterans' Affairs call the Department of Veterans' Affairs general enquiries on 133 254.

Payments

The Age Pension — As at 1 July 2021	
Single* (full rate)	$944.30** per fortnight
Couple (full rate)	$1,423.60** (combined) per fortnight

Source: Centrelink website.
* Includes couples separated due to ill health.
** This payment includes all supplements plus the pharmaceutical allowance.

Asset test

The more assets you have, the less pension you will be entitled to. While the family home is normally not included in the assets test, non home-owners are entitled to a higher threshold because they have to pay rent in retirement.

As you can see, if you are single and a homeowner you may be able to receive a full pension if your other assets (such as cash and investments) are less than $270,500. For every $1,000 above this amount your pension payment is reduced by $3.00 per fortnight. When your assets reach $588,250 you will no longer qualify for any pension. The same principles apply to the other categories.

Assets Test – For Homeowners – As at 1 July 2021		
Family situation	**To receive full pension**	**To receive part pension[1]**
Single	Up to $270,500	Less than $588,250
Partnered (combined)	Up to $405,000	Less than $884,000
Illness separated couple (combined)	Up to $405,000	Less than $1,040,500
One partner eligible (combined)	Up to $405,000	Less than $884,000

Source: Centrelink website.

[1] Lower cutoff thresholds will apply to persons receiving Age Pension under transitional rules.

Assets Test — For Non-homeowners — As at 1 July 2021		
Family situation	**To receive full pension**	**To receive part pension**
Single	Up to $487,000	Less than $804,750
Partnered (combined)	Up to $621,500	Less than $1,100,500
Illness separated couple (combined)	Up to $621,500	Less than $1,257,000
One partner eligible (combined)	Up to $621,500	Less than $1,100,500

Source: Centrelink website.

Income test

The more income you earn, the less pension you will be entitled to.

The maximum you can earn before you no longer qualify for a pension entitlement is $2,085.40 per fortnight for a single person and $3,192.40 (combined) per fortnight for a couple. Note that income includes earnings from salaries or wages, rent, interest, dividends and any money you are deemed to earn (see 'deeming' below). As you can see, a single person can earn up to $180 per fortnight ($320 combined for a couple) before they start to have their pension entitlements reduced.

Income Test – As at 1 July 2021		
Family situation	For full payment (per fortnight)[1]	For part payment (per fortnight)[2]
Single	Up to $180	Less than $2,085.40
Couple (combined)	Up to $320	Less than $3,192.40
Illness separated couple (combined)	Up to $320	Less than $4,130.80

Source: Centrelink website.

1 Income over these amounts reduces the rate of Age Pension payable by 50 cents in the dollar.

2 Limits increase if Rent Assistance is paid with your Pension.

Deeming

Deeming assumes your capital from financial investments is earning a given rate of return (income) – regardless of what return those investments actually generate.

The current deeming rules are as follows:

- If you are single and receiving a pension or allowance, the first $53,600 of your financial investments are deemed to earn income at 0.25% pa. Any amounts over that are deemed to earn income at 2.25% pa.
- If you are part of a couple and at least one of you is getting a pension, the first $89,000 of your combined financial investments is deemed to earn income at 0.25% pa. Any amount over that is deemed to earn income at 2.25% pa.
- If you are part of a couple and neither receives a pension, the first $44,500 for each of you and your partner's financial investments is deemed to earn income at 0.25% pa. Any amount over that is deemed to earn income at 2.25% pa.
- Deeming rates are determined by the Minister for Families and Social Services and reflect rates of return available on a range of financial products.