National Information Centre on Retirement Investments Inc.

Redundancy and You

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http://moneymap.nicri.org.au

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Information current from 01/10/10

REDUNDANCY AND YOU

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NICRI

Redundancy and You

Introduction

"Redundancy and You" has been written to help you navigate through redundancy. It is designed to provide a basic understanding of the financial planning process, to introduce you to the maze of regulations surrounding Employment Termination Payments (ETP) and superannuation issues. It outlines your options and highlights some other aspects which you may need to consider along the way.

Jargon

As you face redundancy you are likely to come across many new words and terms you have never heard before. It is important that you understand these new words and terms as any misunderstanding could be detrimental to you financially.

A list of some of the different investment terms follows. The list is not exhaustive and should be used as a guide only.

Accumulation Phase - Monies that remain in superannuation and have not yet been converted to an income stream.

Account Based Income Stream - A structured drawdown of capital and earnings at specified minimum rates delivering tax free income to superannuants aged 60 years and older, concessional taxation to superannuants after preservation age and less than 60, as well as potential concessional assessment under the Income Test for Government Income Support.

Approved Deposit Fund (ADF) - A fund created specifically for the investment and preservation of superannuation and other rollover benefits - seldom open to new contributions now.

Asset - A possession having monetary value.

AWOTE - Average Weekly Ordinary Time Earnings.

Capital - Accumulated wealth including redundancy payments.

Capital Guarantee - Guarantees the return of capital and may also guarantee interest once credited to the account.

Capital Secure or Capital Stable - Refers to a fund where the underlying investments are usually low risk.

Commission - Money paid by an institution to a financial advice provider for placing investments with that particular institution.

Deemed Income - An assumed rate of income applied to financial investments for Government Income Support means testing regardless of actual return.

Deferred Annuity (DA) - An annuity that is purchased with a benefit from a superannuation product where the income stream starts at a later date, usually 65.

Earnings - The overall increase or decrease in the value of an investment including income and positive or negative growth.

Employment Termination Payments (ETP) - Some payments received since 1 July 2007 on retirement, resignation or retrenchment.

Ex gratia Payments - A voluntary payment from an employer on termination of employment, excluding genuine redundancy payments and other payments on termination.

Fees - Amounts that fund managers/trustees and/or financial institutions charge for the administration of the fund and can include entry, ongoing and withdrawal fees.

Gainful Employment - Employed or self employed for gain or reward in any business, trade, profession, vocation, calling, occupation or employment for at least 10 hours per week while under age 65 years. A different definition applies for people of age 65 and up to 75 years.

Golden Handshakes - See ex gratia payments.

Grandfathered (for the purposes of this publication - page 9) - Ensures access to restricted non-preserved and unrestricted non-preserved superannuation benefits accrued as at 30 June 1999 will be accessable on termination of employment after that date.

Immediate Annuity - A contract bought with a single payment and with a specified payout plan that starts immediately. See NICRI leaflet *Introducing Immediate Annuities.*

Interest - Money paid for the use of borrowed money, usually expressed as a percentage return on money invested.

Mortgage - A contractual arrangement where one party (the mortgagor) provides property as security for a loan provided by another party (the mortgagee).

Non-Commutable Pension/Annuity - An income stream that does not permit withdrawal of lump sums.

Parking Fund - A low or no cost product in the superannuation environment with low volatility - cash fund.

Portfolio - A group of investments or investment products held.

Preserved Amounts - The portion of superannuation that cannot be accessed until conditions of release are satisfied.

Preservation Age - The age after which a person may gain access, upon satisfying certain conditions, to accumulated superannuation preserved benefits. It is dependent on the individual's date of birth, to be phased in from 1 July 2015 to 1 July 2025.

People born	Preservation age
Before July 1960	55
July 1960 - June 1961	56
July 1961 - June 1962	57
July 1962 - June 1963	58
July 1963 - June 1964	59
After June 1964	60

Product Disclosure Statement (PDS)/Prospectus - Document issued by a company or fund setting out the fees, terms of investment, objectives of the investment and providing information about the financial and management state of the company or fund.

Restricted Non-Preserved Amounts - The portion of a superannuation benefit that is not subject to preservation requirements but is not accessible until ceasing employment with the employer relating to the benefit.

Retirement - If over the preservation age and less than 60 years of age the arrangement under which a person was gainfully employed has come to an end and the fund trustee is reasonably satisfied the member intends never again to become gainfully employed. If over 60 years of age the person's gainful employment has come to an end.

Risk - Chance or possibility of either loss or performance not meeting an expectation.

Rolling Over - Transferring all or part of a superannuation benefit to another ADF, DA, superannuation fund/scheme or income stream product.

Security - Safety of an investment.

Taxed Fund - A superannuation fund in the accumulation phase which has to pay tax on the income it receives.

Unrestricted Non-Preserved Amounts - The portion of a superannuation benefit that is not subject to preservation requirements and is accessible.

Vested Superannuation Benefits - The inclusion of the total amount of employer superannuation contributions in the member's name.

Volatility - Characteristic of the market to rise or fall sharply in price within a short period of time. High volatility = High risk. Low volatility = Low risk.

Part 1- Personal Financial Planning

If you are about to receive a redundancy package you are no doubt being confronted with a barrage of new information and some difficult financial decisions. You may choose to devise your own financial plan or alternatively you may choose to seek advice from a licenced financial planner.

If you decide to initiate your own financial plan then you should start by sorting your money according to your needs and finding ways to meet those needs. Obviously, all plans differ as they depend on your age, future employment prospects as well as your current financial position and your objectives.

There are several areas you will need to consider.

1. Regular Income

Money used to meet expenses may come from sources such as alternative employment, your spouse's wage, returns from investments or Government Income Support payments. Consideration could be given to using any lump sum payment you receive to minimise expenses by paying off or reducing debts. This will reduce the amount of regular income required for living. These payments can affect eligibility to Government Income Support even if they are used to reduce or clear debt and advice should be sought prior to using the payments. It would be prudent to confirm recommendations in this regard with Centrelink's Financial Information Service (FIS) staff. NICRI's 'moneymap' website *(http://moneymap.nicri.org.au)* has loan and savings calculators as well as a budget sheet which will help you calculate income required.

2. Cash Reserve

You should consider unforeseen expenses such as home or car repairs. Cash for this purpose should not be tied up and should be readily accessible.

3. Capital Growth

If you have money left over after providing for living expenses and reserves you should consider setting aside some for longer term purposes. This surplus should be placed in investments that allow it to grow. This can be achieved by rolling over some of your superannuation into managed investment options or investments with exposure to the equity (stock) and property markets. It can also be done through investments outside the superannuation environment. It is essential that any investments you make are appropriate for you. The level of acceptable risk, taxation and Government Income Support implications should all be taken into account. Refer to 'moneymap' for help prioritising your needs and objectives as well as assessing your risk profile.

4. Estate Planning

This is an area overlooked by many people. Your Will should be current and beneficiaries (if applicable) nominated with regard to superannuation monies to ensure your estate is distributed in accordance with your wishes and to minimise problems and difficulties for those who survive you. Nomination of beneficiaries may be made through your superannuation fund. This can affect the tax effective transmission of your superannuation. You should consider the need for an enduring power of attorney so your affairs are looked after in the case of an unforeseen accident or illness. Where appropriate, the need to establish a testamentary trust should be considered. These are usually required only when the estate is large and there is concern that the assets may not be satisfactorily managed by your beneficiaries. Estate planning is a complex area and professional assistance may be needed from a financial planner and legal adviser.

Checklist of Financial Planning Considerations

- [ ] Assess what assets and liabilities you have.
- [ ] Calculate the amount of income you need for basic living expenses.
- [ ] Decide how you are going to provide this income.
- [ ] Consider paying off your debts.
- [ ] Ensure you have a reserve of money in case of unforeseen circumstances.
- [ ] Place reserve funds into low risk investments.
- [ ] Allow excess funds to be placed in longer term growth investments, as appropriate.
- [ ] Ensure your Will and other estate planning issues are up to date

Not all steps may be necessary but should still be considered. Visit http://moneymap.nicri.org.au

Selecting a Financial Planner

The aim of the financial advice provider should be to match your needs, goals and preferred risk levels with investment products. They need to have relevant information about your personal circumstances and are required to understand the legislation and regulations relating to the investment products available.

The planner's task is not always easy, nor is it always easy to find a satisfactory planner. The NICRI booklet *'The Financial Planning Process'* provides information for those seeking the help of a professional planner.

Most planners try to do a good job but you must be aware that:

- some are limited by experience;
- some are limited by the products they are authorised to sell; and
- fees will vary from planner to planner.

It is best to seek the opinion of several financial planners and to thoroughly research any plan before implementing recommendations.

Purchasing an investment plan can be considered similar to the purchase of a house or car. When looking to buy a house you would normally inspect several houses, ask questions and contact the council to check and confirm details. Some people even hire professionals to give a second opinion e.g. building inspectors or valuers. When it comes to investing large sums of money it is not uncommon for people to see only one planner and go ahead with their recommendations without understanding all the implications of the plan or that there may be other strategies and products that may serve them more effectively. You should use the same approach when deciding on investments as you would when buying a house. NICRI recommends consulting at least three planners.

Financial Planning Fees

When seeking professional advice you should expect to pay for the service provided. In this situation the service is getting to know you, establishing your needs and objectives, discussing possible strategies to address these issues and then providing recommendations in the form of a Statement of Advice (SoA). Obtain a copy of the advice provider's Financial Services Guide (FSG) so you can be aware of the costs before you meet with the prospective advisor. There are three main methods by which fees are calculated or charged for financial planning services. These are as follows:

Commission Based

The planner receives a commission from the institution for placing the investment with that particular institution. The commission is usually calculated as a percentage of the investment and paid from the entry fee or, in some cases, from ongoing fees. In addition to the initial commission payment, financial planners may also be paid an ongoing annual commission (trailing commission) for money retained in the investment.

The danger of the commission based system is that a less ethical planner may recommend investments that pay higher commissions rather than the most suitable investment. Planners who receive commissions should not be overlooked and may be suitable for investors with small amounts to invest or for those who know what they want. Discount brokers who provide a 'no advice' service could also be suitable.

Full commission based services are rare and it is proposed to ban initial and trailing commissions from 1 July 2012.

Percentage of Portfolio

The planner charges a percentage of the total amount you invest. This amount is paid directly to the planner and is usually deducted before the investments are made.

You should be aware that this system of charging may result in your paying for investments that you would have been able to place yourself without advice.

Fee for Service

The planner charges you a fee based on an hourly rate. This system is similar to the method used by other professionals e.g. accountants and solicitors. Commissions may be refunded.

Planners using the fee for service method of charging should be able to give you unbiased advice, but you should check what advice the fee actually covers.

'Bank' based planners will often infer that they are paid by salary or a combination of salary and bonuses. However, in most circumstances the salary must be justified by a predetermined level of sales.

Fee for service based charges are becoming more common.

Combination

A planner may use more than one of the above ways to charge for the service. All charges must be disclosed regardless of the method or combination.

Some may charge a fee for providing a SoA but offer to refund the fee when you proceed with the investments recommended.

A Case Study

John Smith approaches three financial planners to invest $100 000. He enquires about their fees and is told the following information:

Planner A accepts commission paid by product providers and does not charge you directly.

Planner B charges you 3% of all funds invested.

Planner C charges $250 per hour and estimates 12 hours to formulate and produce a SoA.

In all cases the entry fee for the investment is assumed to be 4% of the funds invested and commission payable to planners is 2.5%. It is also assumed that Planners B & C return this commission to you in the form of additional funds in the investment.

What will it cost John to invest his money?

Planner A

After the entry fee of $4 000, the net amount invested is **$96 000** ($100 000 - $4 000). Commission paid is 2.5% of $100 000 ($2 500) which is deducted from the entry fee.

Planner B

Fee paid is $3 000 (3% of $100 000). After the entry fee of $3 880 (4% of $97 000) the net amount invested is $93 120. Following the refund of commission the investment is **$95 545** ($100 000 - {($3 000 + $3 880) - $2 425}).

Planner C

Fee paid is $3 000 ($250 by 12 hours). After the entry fee of $3 880 (4% of $97 000) the net amount invested is $93 120. Following the refund of commission the investment is **$95 545**($100 000 - {$3 000 + $3 880 - $2 425}).

WARNING. You should use the above figures as a guide only. There are many ways in which planners are remunerated and you should do the sums yourself based on the agreed scale of charges and the particular fund manager's method of charging an entry fee.

CARE: If all three planners are seen but no funds are invested, the funds available for investment for planners 'A & B' remains at $100 000. The remaining funds available after seeing planner 'C' is $97 000.

It is common today that each advisor would charge for a Statement of Advice.

Part 2 - Termination Payments

Before being able to make financial planning decisions you will need to have some understanding of rules, regulations and classifications that surround your redundancy payment. The money you receive on termination of employment may represent payments for unused annual leave, long service leave, other leave entitlements and a Genuine Redundancy Payment as well. The various payments may be broken down into components that are taxed differently. Depending on when in the financial year the payments are received and what other taxable income you receive in the remainder of the year, the amount of tax payable could be affected.

Before using the funds paid to you in lieu of leave it is important to check the treatment of these payments from a Government Income Support point of view if applicable. (Refer Part 5)

Redundancy

The reasons an employee receives a redundancy payment can be many and varied and can determine any tax concessions and tax-free components on payments received.

Genuine Redundancy

A Genuine Redundancy occurs when:

• the employer no longer needs the job to be done by anyone because of changes in the operational requirements of the business; and

• the employee's position is made redundant before their 65th birthday; and

• there is no arrangement entered into between the employer and employee or the employer and another entity to employ the dismissed employee after the termination.

Employees can also receive redundancy payments through mutual agreement with their employer. For example if things are not 'working out', or the employee falls ill and cannot fulfill their duties, or other changes in personal circumstances.

In such instances the redundancy may not be classed as 'Genuine' and so any payments received attract fewer concessions.

Employment Termination Payments (ETP)

ETPs were previously known as Eligible Termination Payments and Bona Fide Termination Payments which attracted special tax concessions in respect of superannuation. These concessions have ended (except for transitional ETPs), however concessional tax rates and tax-free components may apply depending on the nature of the redundancy.

An ETP is any amount paid to the employee over and above what they would ordinarily have received had they left work voluntarily. For example, when an employee quits work for another job they will be paid out any entitlement owing to them such as pay for time already worked and unused annual leave and, where applicable, long service leave.

Any other payment made by the amployer such as payment in lieu of notice, a severance payment of a number of weeks' pay for each year of service and a gratuity payment, sometimes known as a 'Golden Handshake', is classified as an ETP.

Transitional Rules

If a written contract, law, legal instrument or workplace agreement existed as at 9 May 2006 then transitional arrangements may apply to payments made between 1 July 2007 and 30 June 2012.

The responsibility of determining whether or not transitional rules apply, rests with your employer. They should provide you with prepayment statements so you can decide whether to take a cash lump sum or to roll the benefit over into superannuation.

Under Transitional rules, if the payment was taken in cash, and you are at or above your preservation age at the end of the financial year in which you get the payment, tax of 15% plus Medicare levy is payable up to the low rate threshold, $160 000 in the 2010/11 financial year, on the taxable component. Payments in excess of this cap up to the higher level non-indexed cap of $1 000 000 are taxed at 30% plus Medicare levy and any excess at the highest MTR plus the Medicare levy.

If you are under the preservation age, amounts up to the higher level cap of $1 000 000 are taxed at 30% plus the Medicare levy while anything in excess will be taxed at the highest MTR plus Medicare levy.

If the payment is rolled over it is known as a Directed Termination Payment and up to $1 000 000 of the taxable component will be subject to tax at the maximum rate of 15% in the hands of the superannuation fund. Any excess will count towards your concessional contribution cap - $25 000 unless over age 50 years, then $50 000.

You must notify your employer within 30 days of the receipt of the pre-payment statement if it is to be a Directed Termination Payment. If not it must be made direct to you.

If an ETP paid on or after 1 July 2012 relates to a termination prior to that date on which a transitional payment had already been made, the cap will be reduced by the amount of the transitional payment whether it was directed to superannuation or received by you personally.

Approved Early Retirement Scheme

An early retirement scheme is genuine if:

- it is offered to all employees within a particular section or class identified by the employer;
- it seeks to rationalise or re-organise the business operation of workforce; and
- it is approved in writing by the Commissioner of Taxation before it is implemented.

Taxation

ETPs can comprise two components - a tax exempt component and a taxable component. The tax exempt component is nade up of payments relating to pre 1 July 1983 service (if applicable) and to genuine redundancies.

If the ETP is due to a genuine redundancy there will be a tax exempt component relating to the employee's years of completed service. For the financial year 2010/11 the maximum amounts are:

- base amount $8 126; plus
- $4 064 for each whole year of completed service.

These amounts are indexed annually to AWOTE.

The remainder of the redundancy payment is the ETP and for the 2010/11 financial year subject to the following tax rates:

ETP	$0 to $160 000	$160 000+
Under 55	31.50%	46.50%
55 and over	16.50%	46.50%

Note: Tax rates include Medicare Levy (1.5%)

Unused Leave Entitlements

Unused leave and long service leave payments are also subject to tax. If they are paid out as a result of a genuine redundancy they are taxed at 31.5% (including Medicare levy). Where a redundancy is not genuine the employee's normal tax rates apply.

NICRI has a range of Fact Sheets covering other redundancy issues at *http://redundancy.nicri.org.au.*

Superannuation

A superannuation benefit is made up of two components. They are:

- A Tax Exempt component; and
- A Taxable component.

For people familiar with the components that made up superannuation prior to 1 July 2007, the term Undeducted Contributions has been replaced with Non-Concessional Contributions which, together with any Pre 1 July 1983 component, Post 1 July 1994 Invalidity component and probably in rare instances a concessional component, form the Tax Exempt component. The Tax Exempt component of a superannuation fund can only grow in value when Non-concessional contributions are made to the fund or benefits from another fund are merged.

The remainder of the fund is the Taxable component and is made up of any Post 30 June 1983 component, concessional contributions (those for which a tax deduction has been claimed, including salary sacrifice contributions), and all the earnings of the fund.

All superannuation benefits contributed on or after 1 July 1999 are 'preserved' until a condition of release is satisfied. Refer to Accessing Superannuation – Page 9. Much of the superannuation benefits contributed prior to that date are also preserved.

Taxation of a Superannuation Benefit that is accessible

The taxation applicable to your superannuation payments is dependent on your age. People over age 60 years who access their superannuation benefit from a taxed fund, subject to a condition of release being satisfied, do not pay any tax on the payment received, whether it is taken as an income stream or as a lump sum.

For those at or over their preservation age (minimum 55 years) and under age 60 years the tax exempt portion is received free of tax. In the 2010/11 financial year, up to $160 000 (the low rate cap) of the taxable component is also received free of tax. The $160 000 cap is indexed annually to AWOTE but the indexation does not apply till it reaches at least $5 000 and then in increments of $5 000. Any amount in excess of this is taxed at 15% plus the Medicare levy. If the benefit is taken as an income stream a tax exempt component is calculated in proportion of the components. The taxable component is taxed at marginal tax rates but delivers a 15% tax offset.

On the rare occasions that someone under 55 gains access to their superannuation benefit as a lump sum the whole of the taxable component is taxable at 20% plus Medicare levy.

Part 3 - Accessing Superannuation

In order to make appropriate financial decisions you must be aware of the preservation requirements which may prevent you from accessing your superannuation money. The components could fall into three categories: a preserved portion; restricted non-preserved portion; and unrestricted non-preserved portion. Each portion has specific preservation and accessibility features. You may need to contact your superannuation fund in order to find out how your superannuation is classified.

Your superannuation benefits must remain in the superannuation environment until you have satisfied a condition of release, as specified in the Superannuation Industry (Supervision){SIS} Regulations. Some employer sponsored superannuation funds require you to withdraw/rollover your superannuation benefit as soon as practicable after termination of employment. If you fail to notify your employer sponsored fund within a reasonable time frame (at the discretion of the fund trustee) your benefit may be transferred to an eligible rollover fund of their choice. Various costs may apply.

The superannuation regulations were amended as at 1 July 1999 requiring all superannuation contributions and earnings on all superannuation benefits to be preserved. Your right to access any restricted non-preserved and unrestricted non-preserved benefits as at 1 July 1999 is grandfathered. The value of these benefits as at 30 June 1999 remain fixed and are not allowed to increase through additional contributions or accumulated earnings.

The Preserved Portion

The preserved portion must remain in an eligible superannuation or rollover fund until you have satisfied a condition of release eg retirement after reaching your preservation age. It can only be accessed before preservation age in cases of severe financial hardship, on compassionate grounds or if you die. To gain access to funds on compassionate grounds an application must be made to the Australian Prudential Regulation Authority (APRA). A person is taken to be in severe financial hardship if they have received specified Government Income Support Payments for a continuous period of 26 weeks. The superannuation fund trustee must receive written evidence from the relevant Government department or agency that the member meets this requirement and be satisfied the member is unable to meet reasonable and immediate family living expenses.

Those over age 55 years and 39 weeks who have been in receipt of specified Government Income Support Payments for a cumulative period of 39 weeks do not need to satisfy the living expenses test if they are not gainfully employed on a full time or part time basis.

On being made redundant you must place the preserved portion of your superannuation benefit in an eligible fund. This will mean leaving the preserved portion in your current superannuation fund or rolling it over into another superannuation fund, superannuation bond, rollover fund or Retirement Savings Account (RSA). The preserved portion may be rolled over into the same fund as the non preserved portion. It is possible to use your preserved portion to purchase a non-commutable income stream that meets the conditions of the transition to retirement initiative that came into effect from 1 July 2005.

The Restricted Non-Preserved Portion

You will be able to access your restricted non-preserved portion on being made redundant. This is because the termination of employment constitutes a condition of release and the restricted non-preserved portion can be accessed once a condition of release has been met. All restricted non-preserved money becomes unrestricted non-preserved money on termination of employment. While access is possible it is not required and it is possible to roll these benefits over. If it is accessed, tax may be payable depending on your age.

The Unrestricted Non-Preserved Portion

The unrestricted non-preserved portion can be accessed by you at any time.

Unless you definitely need the funds as cash it is usually prudent to rollover this portion into a short term (parking) fund within superannuation, until such time as the money is needed or a longer term decision is made. Ideally such a fund would not have entry or exit fees and the underlying assets would not be volatile. A Retirement Savings Account (RSA) might be suitable.

Part 4 - The Choices

Do Nothing

As from 1 July 2007 it is possible to retain benefits within the accumulation phase of superannuation for as long as you want. Earnings are taxed in the fund's hands at a maximum rate of 15% and tax on withdrawals may apply depending on your age at the time.

Take the Money

The most obvious option is to take the accessible money and pay any tax due. The money can then be used as ordinary money, however, you should be aware that once this decision is implemented it is irrevocable.

It will benefit you to do a calculation of the tax payable as often it may be an insignificant amount and can be an unnecessary stumbling block when making decisions. If you anticipate that your income will be low in the next financial year it may be beneficial to delay the receipt of your superannuation money until then as the amount of tax payable may be less. If you are under age 55 years and have an unfunded amount in your taxable component be aware that you may pay less tax if you need to withdraw the money before you turn 55 years by withdrawing it directly from your superannuation fund rather than rolling it over and then withdrawing the money. If it can remain in the rollover until after you turn 55 years, you may save tax by rolling it over first. For further information on this issue you can contact NICRI (see NICRI leaflet *Rolling Over Superannuation)*, your accountant, or speak with a financial planner.

If you fail to provide your employer or superannuation fund with adequate instructions your benefit may, at the payers discretion, be rolled over to an eligible rollover fund or any unrestricted non-preserved benefits be paid in cash. The payer sets the time allowed for you to provide adequate instructions for the treatment of your superannuation benefit. The regulations permit a maximum of 30 days or a shorter time reasonably required by the payer.

Rollover into a Superannuation Fund

Your superannuation benefit may be retained in your existing fund, subject to fund rules, or it can be rolled over to another superannuation fund or RSA.

The amount classified as a tax free Genuine Redundancy Payment cannot be rolled over, but if it is not required for anything else it can be placed in superannuation as a personal contribution, subject to the contribution cap. As from 1 July 1999 any contributions to a superannuation fund will be a preserved benefit until you satisfy a condition of release. (see page 9- The Preserved Portion)

You can contribute to a superannuation fund whether gainfully employed or not if under age 65 years or if you satisfy the work test between the ages of 65 years and 75 years. Gainful employment in this situation is paid work for 40 hours in 30 consecutive days during the financial year of contributing. It is not possible to join a superannuation fund after the age of 75 years.

Superannuation funds and RSAs, subject to their individual rules, have the following features:

- the unrestricted non-preserved money may retain its character and can be accessed as required;
- the preserved money cannot be withdrawn until reaching preservation age and retired or by reaching preservation age and receiving benefits in the form of a non-commutable income stream;
- on death the balance is paid to nominated dependant beneficiary/ies or paid to your estate;

- superannuation money retained in the accumulation phase of the superannuation environment is not assessed by Centrelink or the Department of Veterans' Affairs (DVA) until you are of Age/Service Pension age. After that time the asset is assessable under the means tests. In some situations where a pensioner remains working after Age/Service Pension age their superannuation remains preserved under the fund's rules. Application can be made for special exemption for these superannuation benefits in these circumstances. If a withdrawal is made during the time the superannuation is exempt from assessment it may become assessable depending on what is done with the funds.

RSAs and superannuation funds are designed to accept further contributions of ordinary money. Some funds require contributions on a regular basis. Consideration should be given to the flexibility of making contributions, the investment strategy and the fee structure of the product. Further details are available in the NICRI leaflets *A Super Checklist*, *Introducing Superannuation* and *Superannuation Tax Considerations*.

Superannuation Funds

There are several different forms of superannuation funds available. These include public offer retail superannuation funds and industry funds, employer superannuation funds and Self Managed Superannuation Funds (SMSF). Within the funds various investment options and structures are available.

In addition to ongoing management fees, entry/exit fees may apply. These vary with the funds and their structures. Investment options range from cash to higher growth and can include master trusts and wholesale funds which enable diversification over fund managers. See NICRI leaflet *Master Trusts and Wrap Accounts*.

Retirement Savings Accounts (RSA)

Retirement Savings Accounts are offered by several financial institutions. These accounts are specifically designed to accept superannuation contributions and benefits are guaranteed by the provider. Returns offered are not high and the products are usually not actively marketed. RSAs are more suited for short term superannuation investment or for those who are very risk averse.

Some accounts apply a fee based on the balance held in the account.

Care should be taken not to confuse RSAs with Retirement Statement Accounts that some financial institutions offer as working accounts for retirees.

Self Managed Superannuation Funds (SMSF)

As previously mentioned superannuation benefits can be rolled over into SMSFs. Further information on SMSFs can be obtained from the NICRI leaflet *Self Managed Superannuation Funds.* The ATO has many publications relating to SMSFs and they can be obtained by telephoning their publication distribution service on 1300 720 092 or from their website www.ato.gov.au/super and following the links to publications and fact sheets.

SMSFs can be complex and specialist assistance should be sought before establishing and managing such an investment structure.

Rollover into a Retirement Income Stream Product

If you require a regular income, transferring your superannuation into an Account Based Income Stream or an Immediate Annuity may be an option you could consider. These products provide a tax effective income but need to be considered very carefully particularly with respect to your investment risk profile and the implications for Government Income Support. Further information is available in the NICRI leaflets *Retirement Income Streams-A Comparison, Account Based Income Streams* and *Introducing Immediate Annuities*.

Advantages of Rolling Over

The advantages of rolling over are:

- funds and subsequent earnings accumulate for later use and ultimately for retirement;
- payment of tax, if applicable, is deferred until the money is withdrawn. Tax payable reduces significantly after age 55 and disappears after age 60 years if paid to you or a dependant beneficiary;
- earnings of superannuation in the accumulation phase are taxed at a maximum rate of 15%;
- the ability to access unrestricted non-preserved funds is maintained;
- superannuation money retained in the superannuation/rollover environment is not assessed by Centrelink or DVA until you are of Age Pension/Service Pension age. After that time the asset is assessable under the Means Tests.

If funds are not required, rolling over is often the best strategy available.

How to Rollover

Your personnel department/pay office and superannuation fund trustee will provide you with a Prepayment Statement. This statement details your entitlements and seeks your instructions on how and to whom your benefits are to be paid. These must be completed and returned to the personnel department/pay office. If you are transferring the full amount of your benefit to the one fund the paperwork may be simplified. For details ask at your personnel department or pay office.

If you decide to rollover your superannuation benefit your superannuation fund will comply with your instructions, unless your instructions breach a Commonwealth, State or Territory law. If you rollover all or part of your benefits the payer will provide your chosen fund with a Rollover Statement which contains your personal particulars and the rollover payment details including the amount of preserved, unrestricted non-preserved benefits, tax exempt and taxable components.

A fund requested to transfer a superannuation benefit to another fund is obliged to effect the transfer within 30 days. It is prudent to keep copies of documentation in respect of the transfer in case of any dispute.

A Case Study

Mary Smith was made redundant on 1 July 2010 after 37 years of service. She received termination/separation and superannuation payments of $345 000. She is 56 years old and in the coming financial year her marginal tax rate is 15% plus Medicare levy (1.5%). Her payments comprise:

$45 000 Genuine Redundancy Payment

$100 000 Tax exempt superannuation component

$200 000 Taxable superannuation component

What is her tax payable?

Tax Payable	**$**
$45 000 Genuine Redundancy Payment (up to $158 494 is tax free)	Nil
$100 000 Tax exempt component	Nil
$200 000 Taxable component (first $160 000 is tax free, excess $40 000 taxed at 15% + medicare levy)	$6 600.00

If Mary rolls over the superannuation benefit to an account based income stream and draws the minimum (4% at her age), what is the tax situation?

4% of the total benefit ($300 000) taken as the minimum payment is $12 000. Using the proportioned method to determine the taxable and tax exempt component:

Tax exempt component	$4 000.00
Taxable component	$8 000.00
Tax offset available (15% of taxable component)	$1 200.00

By converting the benefit into an account based income stream before age 60 years the taxable component of the pension payment is added to Mary's other taxable income which could mean that her MTR is increased to 30% depending on other income generated. However the tax offset will reduce her tax liability by up to $1 200.00.

If Mary was aged 60 years or more she would not pay tax on any portion of her benefit whether as a lump sum or via an income stream.

If Mary was under her preservation age her superannuation benefit would be preserved and therefore inaccessible unless she met a condition of release. Her Genuine Redundancy Payment would still be tax free.

Part 5 - Government Income Support Considerations

You may be eligible for Newstart Allowance, the Age Pension or a Service Pension and you should contact either Centrelink or Department of Veterans' Affairs (DVA) to find out about your individual entitlements, eligibility and the current rates of payment.

Centrelink provides a free and confidential Financial Information Service (FIS). Information is provided relating to all social security payments and entitlements as well as investment options and taxation issues. This service can assist in making the best use of your resources and gaining accurate information about the assessment of investments from a social security aspect. The DVA offers a similar service to people eligible to receive payments from them through their Veterans' Affairs Network (VAN) offices.

Newstart Allowance

This allowance is paid to people aged between 21 years and Age Pension age (see page 15) who are temporarily unemployed.

To be eligible to claim Newstart Allowance you must:

- be an Australian resident living in Australia and not subject to the 2 year waiting period for non-residents;
- be unemployed;
- satisfy an Activity Test which includes actively seeking and a willingness to undertake paid work or complying with a requirement of Centrelink to undertake paid work or be involved in an approved training or voluntary work arrangement;
- be temporarily incapacitated for work;
- qualify under the Means Tests for the allowance;
- be registered with Centrelink as being unemployed;
- not associated with industrial action.

There is a minimum waiting period of 1 week before newstart allowance is payable. Proof of identity, tax file number and Employment Separation Certificate are also required.

In addition to the 1 week waiting period, known as the ordinary waiting period, mentioned above there are other waiting periods such as the Liquid Assets Waiting Period and Income Maintenance Period.

Liquid Assets Waiting Period (LAWP)

Single people with liquid assets of more than $2 500 and couples with more than $5 000 can be subject to a further waiting period of 13 weeks which is served concurrently with the ordinary waiting period and the Income Maintenance Period (IMP). For the period from 1 April 2009 to 30 March 2011, the amounts have been doubled to $5 000 and $10 000 respectively. Where liquid assets are greater than these thresholds the excess over these amounts are divided by $500 for singles and $1 000 for couples to establish the additional waiting period (part weeks are rounded down). Liquid assets include money in financial institution accounts including fixed deposits, debentures, shares, managed investments and money on loan. Due to the rounding down of the part weeks the LAWP does not become effective until the liquid assets are $5 500 and $11 000 (combined) respectively.

Income Maintenance Period (IMP)

Payments for leave will be assessed as income from the date of payment. The maintenance period is the period the leave payment covers. The gross leave payment amount is divided by the period covered and the amount assessed as income on a fortnightly basis. You may still be entitled to receive part Newstart Allowance during this period. Payments received as Genuine Redundancy Payments are included to determine the length of the IMP. The IMP is concurrent with the ordinary waiting period and the LAWP.

In cases of severe financial hardship application may be made to have the IMP waived so long as the expenditure causing hardship was reasonable and unavoidable.

If you intend applying for Newstart Allowance and have cash and/or receive any of the foregoing leave payments on termination of employment, the repayment of debts may cause undue hardship as the liquid asset waiting period and income maintenance periods will still apply. If you have debts it is advisable to discuss your circumstances with Centrelink prior to repayment of any outstanding loans.

Under the Income Test single people and each partner of a couple can earn up to $62 per fortnight and qualify for the full allowance. If income earned exceeds this amount, the allowance will be reduced.

Earnings on superannuation savings are exempt from the Income Test until a person reaches Age Pension/ Service Pension age. If you own your home and have assessable assets above the limit of $181 750 for a single person or $258 000 combined for couples you cannot receive the Newstart Allowance. For non home owners these limits are $313 250 and $389 500 respectively. If they are below the limit the rate is calculated under the income test. These thresholds are indexed annually in July.

For those eligible to receive benefits from DVA the assessment criteria are different. For further information contact NICRI, VAN or Centrelink.

Age Pension

The Age Pension is provided to assist older people with limited means. It is payable to women aged at least 64 years and men aged 65 years or over who satisfy the income and assets test and have, in most circumstances, resided in Australia continuously for ten years. The age pension age for women is being increased over twenty years. The first increase occurred on 1 July 1995. (see table below)

Date of Birth	Qualifying Age for Women
1 January 1943 to 30 June 1944	63 years
1 July 1944 to 31 December 1945	63 years 6 months
1 January 1946 to 30 June 1947	64 years
1 July 1947 to 31 December 1948	64 years 6 months
1 January 1949 and later	65 years

The rate of pension paid is calculated under both the Income Test and the Assets Test. The test which results in the lower rate of pension is applied.

The Income Test

Under the Income Test you can earn up to an allowable amount per fortnight and still receive the full pension. Income for social security purposes includes income from all sources such as employment, overseas pensions and *deemed income* on investments.

The amount of allowable income depends on whether you are single or a member of a couple. For singles this is $146 per fortnight and for couples $256 combined per fortnight. A single pensioner will lose 50 cents of pension for every dollar that income exceeds allowable limits if granted Government Income Support on or after 20 September 2009. If granted prior, the reduction is 40 cents per dollar. Each pensioner, as a member of a pensioner couple, will lose 25 cents of pension for every dollar earned above allowable limits. When only one person of a couple receives the pension, the rate is reduced by 25 cents for every dollar above the allowable income for a couple. Pensioners should consider safely maximising income from sources other than the pension as it will always result in a higher overall income. In some circumstances the reduction of pension may be dollar for dollar. If superannuation has been retained in the accumulation phase, deeming applies to the balance.

The Assets Test

Under the Assets Test a homeowner pensioner can have assets up to $181 750 for a single person or $258 000 combined for a couple and still receive the full pension. For non-homeowners the thresholds are $313 250 and $389 500 respectively. An asset for Government Income Support purposes is any property owned partly or wholly by a person and generally includes all possessions except the pensioner's home. The value of the asset is its net market value less any valid debts or encumbrances. The net market value of an asset is the point at which a willing purchaser and a willing, but not anxious, vendor would reach agreement.

Every $1 000 of assets over the threshold reduces the pension by $1.50 per fortnight for both single pensioners and pensioner couples combined.

Other Government Income Support Payments

While the effect of cashing of a superannuation benefit is clearly understood when it comes to its assessment for Government Income Support recipients, it is not as simple when it comes to other Government payments such as family tax payments, maternity allowances etc. The cashing of superannuation benefits may result in these government payments being reduced or withdrawn for 12 months.

If you receive the family tax payment or if you believe you may qualify for the maternity allowance or maternity immunisation allowance you should talk to Centrelink to determine if these Government payments will be affected if you intend cashing your superannuation benefits.

Part 6 - Other Considerations

Capital Guarantees

Products offering capital guarantees are very rare.

An investment offering a capital guarantee usually only guarantees that the initial amount invested, after fees have been deducted, will remain in the account. In most cases the interest once paid to the account is also guaranteed to be returned when the investment is withdrawn. It is still possible for amounts in capital guaranteed funds to decline due to poor returns and high fees.

There are variations to capital guarantees, for instance, some guarantees only offer a guarantee of 80% of the initial amount invested. You should know what the guarantee actually covers and be aware that the guarantee is only as good as the company providing it.

Guarantees are supported in two ways. Firstly, reserves are established and can be used if the fund suffers a loss or if a shortfall occurs and secondly, monies lodged are usuallydeposited through the company's number one fundwhich is traditionally the responsibility of the company's actuaries and supervised by the Australian Prudential Regulation Authority (APRA).

RSAs were introduced in July 1997 and are still offered by 1 bank and 8 credit unions, as listed on APRA's website. It is necessary for the capital in these accounts to be guaranteed.

Capital Stable and Capital Secure

Capital stable/capital secure funds do not have a guarantee as above. The stability or security of the fund comes from the underlying investments which may include term deposits, bank certificate of deposit, bank endorsed commercial bills and Government securities.

Some also have exposure to shares and property.

Most of the portfolio is usually invested in the lower risk investments but there is still a risk that a capital stable/capital secure fund will decrease in value.

Accessing Benefits

Although money in the superannuation environment can be retained indefinitely – until death – some fund rules, particularly with ADFs and DAs may require you to withdraw your benefit or convert it to an income stream. Even where such a choice is voluntary it is prudent to consider the investment options in which the assets are held, with the view to consolidate any gains in the time leading up to when the assets are withdrawn. Where the investments are held in options which can be volatile consideration may need to be given to transferring to a cash option of the fund to shield against possible sudden falls in the markets. While there is an 'opportunity cost' in following such a strategy it could protect you from losing money when you need to get at it. See NICRI publication *Rolling over Superannuation.*

If it is intended to transfer the benefit to an income stream using similar investment options/allocation the investment term is lengthened and volatility in the short term may not be such an issue. Buy/sell margins in the unit price may apply. Where using the same product provider it may be possible to arrange the transfer at the sell price. It would be prudent to seek advice on the strategy to be adopted well in advance of the anticipated event.

Paperwork

Unless you are certain that you need the money in cash it is important to arrange for superannuation benefits to be rolled over directly to the new fund. If it is cashed out it cannot then be rolled over to a superannuation or rollover fund and retain its original characteristics. If the cash is subsequently contributed to a superannuation fund the benefit will be treated as a preserved benefit (see page 9) and a condition of release must be met before the fund can be cashed. Cheques must be made payable to the rollover or superannuation fund.

When filling out paperwork it is important to ensure all the forms, both investment and tax, are read and understood. A product provider will usually offer several investment options within the one product eg a deferred annuity offering the following investment options: cash fund, capital stable fund, balanced fund, share index fund, international fund or property fund. Each option has its own risks but the funds are all deferred annuities. It is easy to place funds in inappropriate investments unless care is taken when filling in the application forms.

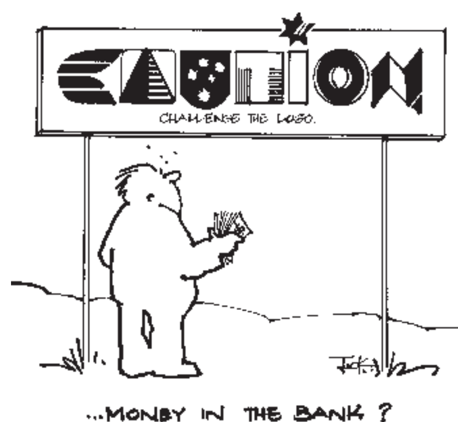
You should be aware of:

- the terms and conditions of the investment;
- the risk that the funds are exposed to (see NICRI leaflet *Safety, Risk & Scams*); and
- any costs associated with early withdrawal or changes in circumstances.

Bank Logos

It is possible to invest in ADFs, DAs, superannuation funds etc at bank branches. These products are generally provided by a subsidiary company of the bank, which is not always clear as the bank's own logo often dominates the product disclosure statements and other information. In the small print the following or similar statement can be found 'The bank does not guarantee the performance of the fund or the repayment of capital'.

Money placed with these bank owned investment companies is exposed to all the normal commercial risks. This means that these products should be considered on their own merits and not those of the parent bank.



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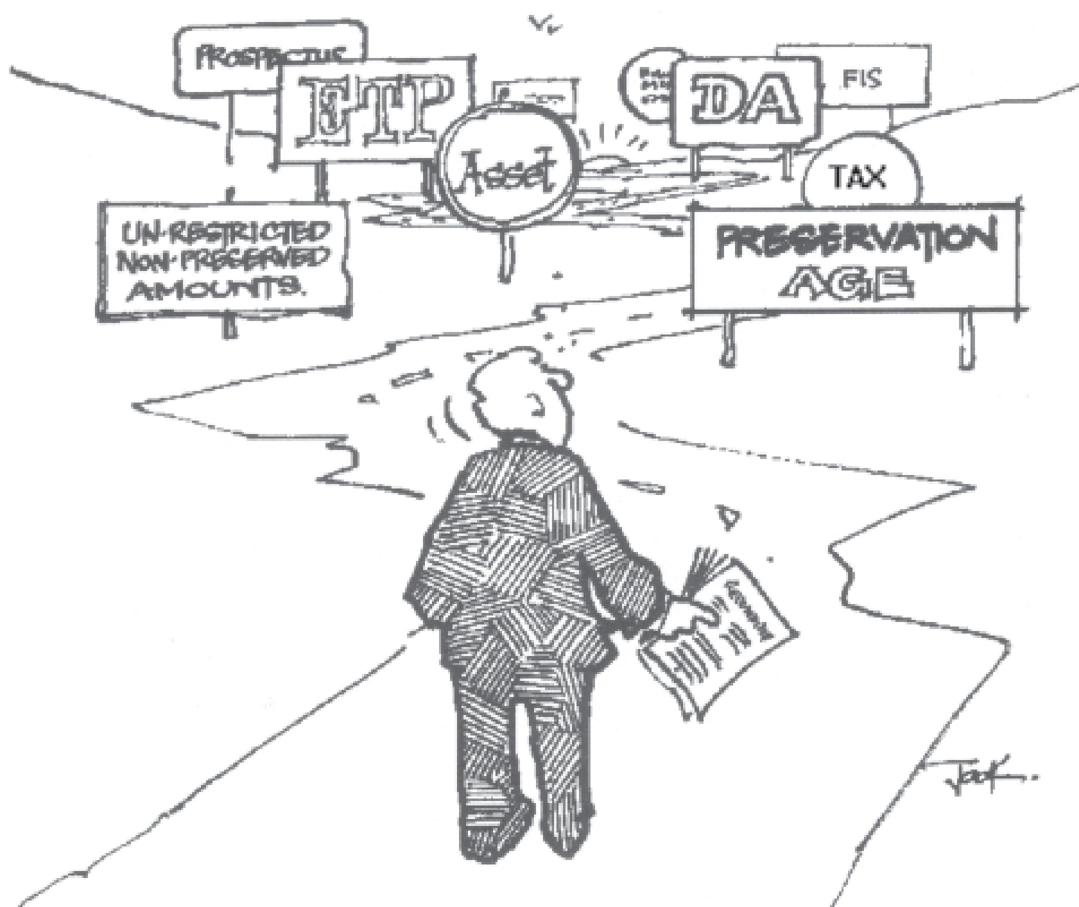
This publication is intended as a guide only and is not in any way an endorsement of any products mentioned. Readers should not rely on this information alone as a basis for making an investment. The information was correct at the time of writing but is subject to change without notice.



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