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DIY SUPER JOHN WASILIEV

Popular pension under scrutiny

The government is reconsidering the allowable levels of income paid from allocated pensions.

Change is impossible to escape in superannuation and allocated pensions are the latest area to come under government scrutiny.

In a response earlier this month to suggestions by a Senate committee, the government accepted there should be a review of rules that state what minimum income must be paid each year from an allocated pension.

In fact, the government said it was considering the appropriateness of both the minimum and maximum regulated pension income rules for allocated pensions.

It is a major issue given that allocated pensions are without question the most popular superannuation retirement income arrangement, other than taking your super as a lump sum.

Allocated pensions are popular, says Peter Crump, chief executive of Adelaide-based financial planner Portfolio Planning Solutions, because they are promoted by financial institutions and the large super funds that sell off-the-shelf pensions. Financial advisers and accountants also recommend allocated pensions be set up within DIY super funds.

Allocated pensions are simple to run, the administration is not complicated and they have been around for nearly 20 years. While they were not officially introduced in their present form until the early 1990s, they were around unofficially for a number of years before they were regulated.

Allocated pensions operate as an extension of a superannuation savings account where instead of making contributions you make regular income withdrawals.

There are tax concessions for the pension income (there is a special tax rebate that reduces income tax) and no tax on the investments in a super fund that is paying an allocated pension. The amount of income that can be drawn is determined by so-called pension factors that set minimum and maximum levels. You must take the minimum each year and cannot withdraw more than the maximum.

These income levels are calculated annually by dividing the pension factors into your super account when you start the pension and thereafter into the balance at the start of every financial year.

Crump says the trouble with the current pension factors is that the minimum levels they produce are probably too generous for current political thinking. Maximum amounts probably are too restrictive.

Many people draw only the minimum income at least when they first start their allocated pension - because they want their super savings to last as long as possible. Taking the minimum stretches an allocated pension longer than most people would live. It could still be paying you income if you lived to 100.

On the other hand, taking the maximum pension will see an allocated pension run out at about age 80. Crump says the current average life expectancy for a 65-year-old Australian male is nearly 18 years. So if retirees take the maximum every year, at least half of them would run out of money while they could still have quite a number of retirement years ahead of them.

A 65-year-old woman's average life expectancy is 21 years, so the chance that her superannuation will run dry at a maximum pension rate is even greater. Many retirees try to manage their income withdrawals between the minimum and maximum levels.

But many people in government, both politicians and public servants, consider the rules and regulations should be regularly adjusted to reflect changing times.

With superannuation, it has always been government thinking that the tax concessions are granted during both the savings and retirement income phases to encourage some retirement income independence. The thinking is also that this money should be spent in retirement rather than accumulated for future generations.

Crump says allocated pensions are the least sophisticated but the most flexible of the official retirement income options that are available through superannuation. You can, for example, make lump sum withdrawals if you require.

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