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Tax advantages, a superannuation boost and a simpler transition to retirement!

Case study
Doug, aged 55, earns $70,000 per annum and has $350,000 in his current super account and other investments. Doug enjoys his job and is looking forward to working full-time until he reaches the age of 65.

Doug's financial adviser suggests he begin salary sacrificing some of his income in order to build the amount of funds available for his retirement. But Doug explains he cannot currently afford to lessen his take-home income. Despite this, his financial adviser explains that by beginning an NCAP he can supplement his income via his current superannuation fund, while sacrificing the equivalent amount into his super.

Doug expressed surprise at the suggestion. How can taking money from super and putting it back in from his income boost the amount in his super? The confusion is understandable because Doug still receives the same income and so he believes the net result would be the same.

Doug's financial adviser explains that the tax advantages of the strategy arise because the NCAP's investment gains are tax free. The NCAP payment attracts a 15 per cent tax offset while Doug is aged 55 – 59, and is tax free from age 60. **He shows Doug that the strategy could have a net benefit, by the time he is 65, of more than $90,000.**

Thanks to changes in legislation, the jump from work to retirement need no longer be a dramatic event. In fact, taking advantage of 'transitioning to retirement' rules can provide significant tax benefits and give your superannuation a helping hand.

If you have reached preservation age (currently age 55), you are able to access your super as an income stream without having to retire permanently.

Accessing funds while still in the workforce can be done using a non-commutable allocated pension (NCAP), which provides you with a regular payment. The annual amount received can be between 4 per cent and 10 per cent of your account balance, as selected by you.

How does an NCAP work?
When it comes to understanding the value of an NCAP strategy, the benefit results from the differing tax rates applied to regular income, superannuation and pensions. Essentially, there are three levels of taxation that can be applied to your income and retirement benefits:

1. Ordinary assessable income is taxed at your marginal tax rate.
2. Superannuation is generally taxed at a concessional rate – up to 15 per cent on entry and 15 per cent on any investment earnings received by the fund. Withdrawals are tax free for those aged 60 or over.
3. Pension payments are tax free if aged 60 and over. If aged 55–59, all or part of the pension income may be taxable, but a tax offset of up to 15 per cent applies. In addition, there is no tax on any investment earnings in the pension account.

Tax advantages and a boost to your retirement nest egg.
The innovative transition to retirement strategy enables you to access significant tax advantages and to give your superannuation a substantial boost.

An NCAP can allow you to salary sacrifice a significant proportion of your income into superannuation and to supplement this amount with a regular income stream from a newly created NCAP.

An NCAP advantage emerges because of the lower rates of taxation generally applied to superannuation, compared with the marginal tax rates on income. This advantage is further increased because any investment earnings within an NCAP (ie where super money is now in pension phase) will be tax free.

An important feature of an NCAP strategy is that your take-home income can be structured to be exactly the same as was received prior to the strategy.

Not surprisingly, when the strategy first emerged, some were worried that the Australian Taxation Office (ATO) might see it as tax avoidance. But concerns have been laid to rest, with the Commissioner of Taxation confirming on 17 November 2005 that such a strategy would not be considered avoidance.

Assumptions - The projections in this strategy are based on various assumptions, including but not limited to: maximum pension payment = $35,000 in year 1; salary sacrifice = $43,394 in year 1; no change in take-home pay before/after strategy; no change in risk profile; estimated investment return (balanced portfolio) = 5.9% pa (super), 6.8% pa (pension); all investment earnings figures are after tax and after fees; no change in Super Guarantee contributions, ie 9% of $70,000; ongoing administration fees are not included. Note that payment received from an NCAP is eligible for a tax offset of up to 15 per cent if aged 55–59. The payment is tax-free if over age 60.