

Super Facts

Essential tips for managing your superannuation

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Benefits of superannuation

1. Make salary sacrifice contributions

This is a method by which you can direct what would otherwise be fully taxable salary to your superannuation fund on a pre-tax basis or if you are self-employed, direct pre-tax business income to superannuation. The benefits of adopting this strategy can be substantial and we would recommend to most clients with surplus disposable income that they consider salary sacrifice arrangements as a great way to save more for their retirement.

Example: Let's say you are over age 50, you earn a reasonable income (your top marginal rate of tax is 37%) and you have surplus income of \$25,000 (before tax) that you can invest annually. You can take the after tax income and invest it or you could ask your employer to reduce your taxable income (salary sacrifice, or you do this personally if you are self-employed) and contribute the gross amount into your superannuation fund. The benefits of this strategy are demonstrated below.

	Take surplus income in cash	Contribute surplus income to superannuation
Income	\$25,000	\$0
Tax @ 37% + Medicare @ 1.5%	\$9,625	\$0
Income sacrificed to superannuation	\$0	\$25,000
Tax in super fund	\$0	\$3,750
Net amount invested	\$15,375	\$21,250
Improvement of superannuation over personal investment		\$5,875

By simply directing where your gross income is invested you could have an additional \$5,875 pa. working for you.

2. Self-employed and unemployed

Similar to employees being able to salary sacrifice, self-employed people can direct their gross business income to superannuation and save tax. But what isn't as well understood is that anyone who is self-employed or even unemployed and between 18 and 65 (or between 65 and 75 and working 'part-time' and 'substantially self-employed' - less than 10% of your assessable income comes from employment) can make personal contributions to superannuation and claim these contributions

against personal taxable income (including dividends, rental income, interest and realised capital gains).

For example: Let's say you are over age 50, you earn investment income (your top marginal rate of tax is 30% once franking credits are taken into account) and you realise a capital gain of \$100,000. The asset(s) sold have been held for 12 months or more so you are facing tax on 50% of your capital profits only ie. a \$50,000 taxable gain that pushes you up into the 37% tax bracket. You can pay the full tax on the taxable capital gain or you could contribute part of the gain into your superannuation fund and claim the amount contributed as a tax-deductible (concessional) superannuation contribution. The benefits of this strategy are demonstrated as follows.

	Take gain in cash and pay full tax	Contribute 50% of gain to superannuation
Capital gain	\$100,000	\$100,000
Assessable gain (after 50% discount)	\$50,000	\$50,000
Contribution to superannuation	\$0	(\$50,000)
Taxable income resulting from capital gain	\$50,000	\$0
Tax @ 37% + Medicare @ 1.5%	\$19,250	\$0
Tax in super fund	\$0	\$7,500
Net capital proceeds to invest	\$80,750	\$92,500
Tax saving by contributing \$50,000 to superannuation		\$11,750

Assuming that these capital proceeds were only going to be reinvested, almost \$12,000 of investment capital has been retained by making a tax-deductible contribution to superannuation.

3. Non-concessional contributions

Non-concessional contributions (formerly known as undeducted contributions) provide an avenue by which you can transfer your after-tax cash and certain assets into your superannuation fund.

With very few exceptions most people can see the value in making salary sacrifice or other pre-tax contributions into superannuation, as there is an immediate tax saving, but most question the benefits behind contributing their after-tax funds into superannuation especially when they have to lock them away until age 55 (or even up to age 60 in the case of younger people).



Put quite simply it is the lower rates of tax payable on investment earnings that make it attractive to invest after-tax funds through your superannuation fund. Investment earnings in superannuation are taxed at a maximum of 15%, or 10% on capital gains realised on investments held for 12 months or more, or 0% on income and gains earned on investments which support current pensions payable from your superannuation fund. These rates of tax compare favourably to personal marginal rates of tax that would otherwise be payable on income and gains earned on investments held outside superannuation eg. if an individual is on the 30%, 37% or even 45% (plus Medicare) personal tax rate then investing via their superannuation fund, at a maximum rate of tax of 15%, can confer considerable tax savings on them.

On a non-concessional (after-tax) basis you are permitted to contribute up to \$150,000 pa. to superannuation or if you are under age 65 and you have a lump sum to invest you can contribute up to \$450,000 by paying three years at once, but if you contribute the full \$450,000 you then cannot make further non-concessional contributions for the next two financial years.

As you can see demonstrated in the table below, the lower tax rate inside superannuation enhances your return over time, versus the return you would achieve after paying marginal rates of tax on investments:

\$150,000 non-concessional contributions annually Tax rates: Superannuation 15%, Personal 38.5% Return 7% pa. before tax			
Year	Superannuation	Personal	Improvement
1	\$158,925	\$156,458	\$2,468
2	\$327,306	\$319,650	\$7,656
3	\$505,706	\$489,869	\$15,837
4	\$694,720	\$667,415	\$27,305
5	\$894,981	\$852,605	\$42,376
10	\$2,089,846	\$1,905,230	\$184,616
15	\$3,685,076	\$3,204,798	\$480,278
20	\$5,814,824	\$4,809,243	\$1,005,581

Instances when you can contribute more than \$150,000 (or \$450,000) of non-concessional contributions

There are two instances where individuals could contribute non-concessional contributions in excess of the standard limits:

1. Up to \$1.2 million (life-time limit) can be contributed upon the sale of a qualifying 'small business'; and
2. Certain payments received under a structured settlement, personal injury payment or lump sum workers compensation payment of any amount can be contributed providing certain conditions are met.

4. In-specie contributions

As well as contributing cash to your superannuation fund, if you have a self-managed superannuation fund (SMSF) you can even make contributions in-specie to your fund.

Under Superannuation Law you are permitted to contribute the following assets to your SMSF (in addition to cash), provided they are acquired by the SMSF at 'market value':

- Listed securities (shares, property and fixed interest securities listed on any recognised exchange throughout the world);
- Business Real Property – property that is wholly and exclusively used in the operation of one or more businesses (potentially your own business, and special rules apply for rural property); and,
- Units in Widely-Held trusts – most retail and wholesale managed funds; that you or your associates hold personally.

Contributing assets to your superannuation fund can be beneficial in two ways:

1. It could allow you to make contributions when current cash-flow may not permit; and
2. It provides an avenue to transfer assets out of your personal name(s) into your SMSF and potentially shelter future earnings in the low-tax environment of superannuation.

IMPORTANT NOTE: Transferring assets to your SMSF will be a deemed sale and will almost certainly be assessable for capital gains tax (CGT), and in some cases stamp duty and other costs may also be payable.

5. Spouse contributions

If you have a non-working spouse or one that earns a relatively low income (less than \$13,800 total income and reportable fringe benefits, plus certain contributions to superannuation) then you should consider making a spouse contribution of up to \$3,000 pa. for your spouse, as a spouse contribution can attract a tax rebate to you of up to \$540 pa.

To qualify for this rebate you and your spouse need to meet the following conditions:

1. You must be a married couple (legally married or de-facto) and living together;
2. You must be Australian residents;
3. The contributing spouse can be of any age but the spouse for whom the contribution is made must be under 65 years of age or under 70 and working on at least a 'part-time' basis; and
4. Your spouse's assessable income (income and reportable fringe benefits, plus certain contributions to superannuation) needs to be less than \$10,800 pa. to attract the full tax rebate of \$540.

The rebate reduces as your spouse's assessable income increases above the \$10,800 limit and phases out completely once this assessable income reaches \$13,800 pa.

For the relatively simple exercise of investing \$3,000 pa. into your spouse's superannuation fund you could enjoy a tax rebate/refund of up to \$540 annually.

6. Government Co-contributions

The Government Co-contribution is another Government funded benefit that you could pursue for a low-income spouse but it is particularly appealing to anyone who is working and on a relatively low income (eg. casual/part-time employees, children who are starting out in work) as you must be in some form of gainful employment to qualify for this benefit.

Anyone who is working and under 71 (and earns at least 10% of their income from employment) can qualify for the Government's Co-contribution if their total assessable income (income and reportable fringe benefits, plus certain contributions to superannuation) falls below \$61,920* pa.

In return for a personal contribution to superannuation of \$1,000 pa. the Government will pay up to \$1,000 into the superannuation fund of your choice – a return of up to 100%. If you are working and under 71, and your assessable income is less than \$31,920* pa. then the Government will pay the full 100% Co-contribution on up to \$1,000 of personal superannuation contributions that you make (a maximum of \$1,000 on \$1,000 of contributions). As your assessable income increases the amount of Co-contribution decreases and cuts out completely when your assessable income reaches \$61,920* (*these thresholds are proposed to be fixed for the next financial year).

The great thing about this Government benefit is that you don't even have to apply for it. The ATO pays it automatically once your taxation return for the year has been lodged and your fund has reported the contributions it has received. If you have made personal contributions for the financial year the ATO provides you with an assessment and pays the Co-contribution directly into your superannuation fund.

Though \$1,000 does not sound like a lot, if say your children were to contribute \$1,000 pa. of personal contributions to superannuation between the ages of 18 and 25 and receive an additional \$1,000 of Co-contribution in each of these years, and if their superannuation fund earns 7% pa. after tax, then this would add up to an additional \$153,000 of retirement savings by the time they were age 60. This is an example of the power of compounding returns.

7. Low tax rate on investments

Generally your superannuation fund will pay a lower rate of tax than you do personally on earnings on investments made.

Investing in your personal name can see you paying tax of up to 37% or even 45% (plus Medicare Levy) versus 15% or even 10% that you could be paying on investments held in your superannuation fund.

Most superannuation funds pay a maximum of 15% tax on investment earnings, and if you sell an asset that the fund has held for 12 months or more the rate of tax payable on the capital gain can be as low as 10% by virtue of a 1/3 discount that is applied to the capital gain.

If you compare these rates of tax to what you could pay personally if your investments are held in your own name as opposed to your superannuation fund, then you can see that over time the savings that add up can be quite substantial.

Comparison of superannuation v. personal investing
\$1,000,000 portfolio
Tax rates: Superannuation 15%, Personal 38.5%
Return 7% pa. before tax

Year	Superannuation	Personal	Improvement
1	\$1,059,500	\$1,043,050	\$16,450
2	\$1,122,540	\$1,087,953	\$34,587
3	\$1,189,331	\$1,134,790	\$54,542
4	\$1,260,097	\$1,183,642	\$76,454
5	\$1,335,072	\$1,234,598	\$100,474
10	\$1,782,418	\$1,524,233	\$258,186
15	\$2,379,657	\$1,881,815	\$497,842
20	\$3,177,015	\$2,323,285	\$853,729





8. No tax on investments supporting pensions

This has got to be one of the most powerful incentives for investing in (and where possible, transferring assets to) your superannuation fund. Once you move into retirement and commence a pension(s) from your superannuation fund then all the assets that support your pension payments are exempt from tax on the income they earn and on capital gains they realise.

What this means is that once you commence your private pension you will not pay tax again on your investments (those that support your pension), potentially for the remainder of your life and possibly your spouse's life as well.

Following is a table showing how the 0% tax would apply to the superannuation fund in pension mode versus investing personally, assuming you achieve a net rate of return in both cases of 7% pa, after drawings are taken each year.

Comparison of superannuation (in pension mode) v. personal investing
\$1,000,000 portfolio
Tax rates: Superannuation 0%, Personal 38.5%
Return 7% pa. before tax

Year	Superannuation	Personal	Improvement
1	\$1,070,000	\$1,043,050	\$26,950
2	\$1,144,900	\$1,087,953	\$56,947
3	\$1,225,043	\$1,134,790	\$90,253
4	\$1,310,796	\$1,183,642	\$127,154
5	\$1,402,552	\$1,234,598	\$167,954
10	\$1,967,151	\$1,524,233	\$442,919
15	\$2,759,032	\$1,881,815	\$877,217
20	\$3,869,684	\$2,323,285	\$1,546,399

9. Transition to retirement pensions

This is a strategy by where you can activate your superannuation pension before you retire (minimum of 4% and maximum of 10% of the value of your super fund each year).

Generally you cannot access your superannuation savings until you retire or reach age 65. However, you can commence a transition to retirement pension once you reach your preservation age (currently 55 but increasing to 60) even whilst you are still working full-time, and begin drawing down a superannuation pension to supplement your income.

And if you are already 60 this means you could even be drawing a tax-free income from your superannuation fund (note: pensions paid from unfunded superannuation schemes – mostly Public Sector schemes – are still taxed at marginal tax rates but carry a 10% tax rebate for recipients aged 60 and over).

What many people over 60 are beginning to do now is salary sacrifice the maximum salary they can, or divert the maximum business income they can, as contributions to superannuation and take a transition to retirement pension to supplement their remaining income.

The table below demonstrates how this strategy could work for someone aged 60 and over.

	Take entire salary in cash	Contribute \$50,000 to superannuation and commence pension
Total cash income	\$130,000	\$80,000
Tax (and Medicare @ 1.5%) payable	(\$38,000)	(\$18,750)
Transition to retirement pension	\$0	\$30,750
Total income after tax	\$92,000	\$92,000
Contribution to superannuation	\$0	\$50,000
Tax on superannuation contribution	\$0	(\$7,500)
Net benefit of transition to retirement pension – retained in superannuation fund		\$11,750

By simply exchanging taxable salary for a non-taxable transition to retirement pension, additional savings of \$11,750 pa. were achieved in this example.

10. No tax on superannuation benefits – age 60 onwards

This is by far and away one of the most amazing changes that the Government has made to superannuation in the last 25 years.

Anyone who takes their superannuation after reaching age 60 will now receive their benefits completely free of tax (apart from individuals who are members of untaxed superannuation schemes – mostly Public Sector Schemes, where benefits are still taxable).

Whether you take your superannuation in the form of a lump sum or as a pension benefit you will no longer pay any tax on the amounts you withdraw after your 60th birthday – you could in fact withdraw 100% of your superannuation completely tax free once you retire.

Between 55 and 60 you can get the first \$165,000 of your lump sum benefits tax-free (as long as you are retired and have reached your preservation age) and you can commence a pension (or a transition to retirement pension if you are not yet retired) which is taxable at standard rates less a 15% rebate, but once you reach age 60 all your benefits are tax free.

As stated earlier, once your superannuation fund converts to pension mode, all income and capital gains earned on assets supporting the pension(s) are exempt from tax and now once you turn 60 all your distributions (lump sum or pension benefits) are tax free as well.

Add to this the fact that reasonable benefit limits (RBLs) have now been abolished, and your superannuation fund (and in particular your self-managed superannuation fund) becomes an extremely valuable vehicle in which to hold your investments.

11. Draw out tax-free lump sums and re-contribute them to superannuation

Once you turn 60 and have retired (and in some circumstances even age 55 and retired) and still under age 65 (or less than 75 and still working ‘part-time’) you should consider withdrawing lump sums from your superannuation and re-contributing these as non-concessional contributions to your fund. This is generally referred to as a withdrawal and re-contribution strategy.

Why would you employ a withdrawal and re-contribution strategy? Your superannuation benefits will always have a taxable component and possibly a tax-free component (if you have made non-concessional contributions or you have some other component that is exempt from tax) and whilst the taxable component may not be of any concern to you once you are 60 and drawing down your funds tax-free, it could have an adverse affect on the tax your beneficiaries pay on your death. One way to reduce the effects of this tax is to increase your tax-free component through withdrawing and re-contributing.

Let’s say you have \$1,000,000 in your superannuation fund at age 60 – approximately \$890,000 taxable and \$110,000 tax-free components. If you were to die and your only beneficiaries at that time were your adult children, then they would be liable for tax at 15% plus Medicare Levy on the taxable component ie. 16.5% of \$890,000 or \$147,000 tax. But if you were to withdraw \$450,000 (\$400,000 taxable and \$50,000 tax-free component) and then re-contribute the \$450,000 back to your fund you would change the mix of the taxable and tax-free components in the fund to \$500,000 each. Then if you were to die, those same beneficiaries would only be liable for tax on \$500,000 of taxable component ie. 16.5% of \$500,000 or \$82,500 tax. This results in an overall tax saving of over \$64,000 which certainly makes it worthwhile employing this strategy if you can.

12. Passing on pension funds on death

Once you begin retirement and enter the pension phase of superannuation then it is important to ensure you have your estate planning in place.

1. Have a Reversionary Pension in place (where appropriate). This will ensure that your pension continues to your spouse (and possibly other financial dependants) upon your death. Note that if you are over 60 at that time when you die or your spouse is over 60 then the pension continues tax-free until the death of your spouse.

2. Have a Binding Death Benefit Nomination in place (if necessary). By default, if you have no spouse and no financial dependants to pass your superannuation benefits to, then your adult children will receive your superannuation benefits (usually in equal amounts, after paying tax). If you have no children, then your superannuation will usually be paid to your estate and divided amongst the beneficiaries of your estate in accordance with your Will. If either of these outcomes are not in accordance with your wishes then you may want to put a Binding Death Benefit Nomination in place. This will enforce your trustee to pay benefits, for example to your children, in the proportions you want, select which of your children receive your superannuation and even allow you to elect to have your superannuation (or part thereof) paid into your estate and be dealt with by your Will, for the benefit of the beneficiaries of your estate.

IMPORTANT NOTE: You can only make a Binding Death Benefit Nomination in favour of someone who is considered your dependant under Superannuation Law (commonly your spouse or partner and children) or in favour of your estate. The nomination must be valid both at the time it is made and also at the time of your death, so it is important to review it and update it on a regular basis (every 3 years for some superannuation funds).

13. How much do I need to retire comfortably?

This is probably the one question we get asked more often than any other about superannuation, and not surprisingly it can sometimes be the most difficult to answer.

How much you need for a comfortable retirement depends largely on your living needs. If you (and your spouse) live on \$100,000 pa. after tax or even \$50,000 pa., then you will probably need a similar amount when you retire, albeit it should be easier to generate this after tax income through superannuation given the tax concessions available.

As a general rule of thumb though; we work on the premise that drawings of 6.0% pa. are sustainable from a reasonably well balanced portfolio, therefore:

- If you need \$60,000 pa. after tax and you want to maintain capital, then your starting capital at retirement needs to be \$1,000,000. Under this scenario your capital would grow modestly, in turn growing your income which should then keep pace with inflation, and by the time you die your beneficiaries should inherit \$1,000,000 (before tax, in today's dollars); or
- If you need \$60,000 pa. after tax and you are happy to spend your capital, then you would need starting capital of about \$750,000 at retirement. Under this scenario your capital should run out at about the end of your expected lifetime.

14. Small business CGT concessions

If you operate a small business and qualify for the small business CGT concessions that currently apply (aggregated annual turnover of less than \$2 million or your 'net assets' are less than \$6 million) then you could be entitled to substantial savings in CGT on the sale of your business.

The Government has recognised that most small business owners put a substantial amount of their annual profits back into their business and see their business as the main asset they will sell to provide themselves with capital from which to fund their retirement.

In light of this recognition the Government has put in place a number of CGT concessions which small business operators can avail themselves of to avoid paying CGT on the profit they receive from the sale of their 'active' business assets. Those concessions which specifically apply upon retirement are:

1. The 15 year exemption rule – this provision provides the greatest concessions, as the whole of the capital gain that is realised on 'active' business assets is exempt. To qualify the asset must be held for at least 15 years, the business owner(s) must be 55 years of age and the sale of the business must be in connection with retirement.
2. CGT retirement exemption – up to \$500,000 (lifetime limit) reduction in capital gains (on the sale of 'active' business assets) is available to anyone who elects to use the proceeds of the sale of their business for retirement purposes. If the individual is under 55 (or their preservation age) then the CGT exempt amount must be rolled over to their superannuation fund.

Note, you are permitted to contribute up to \$1.2 million (lifetime limit) to superannuation, from the sale of a qualifying small business, in addition to the standard non-concessional contribution caps that apply, ie. \$150,000 pa. or \$450,000 where three years contributions are paid at once.

IMPORTANT NOTE: As Patersons Securities and its Advisers are not qualified tax agents you should check these small business CGT concessions with your accountant.



15. Hold life insurance through your superannuation fund

Many people need life insurance (and total and permanent disability insurance), especially if they have liabilities and/or young families to provide for. However many people still pay for their insurance privately when they could have their insurance set up, and pay their premiums, through their superannuation fund and potentially make some substantial savings.

It can be possible to get cheaper rates of premiums through superannuation funds (by virtue of group life insurance plans) but where the real savings come about is that you can pay your insurance premiums with pre-tax income via your superannuation fund as opposed to paying them with after tax income personally.

For example, let's say your employer is already paying \$20,000 pa. in super contributions on your behalf (salary sacrifice and the 9% superannuation guarantee), and you pay \$2,000 p.a. in life insurance premiums. You could pay your insurance premiums personally or you could set up your insurance through your superannuation fund and increase your salary sacrifice by \$2,000 pa. to cover your premium payments. The benefits of running insurance through a superannuation fund for someone on 38.5% tax rate (including Medicare Levy) is demonstrated in the table below.

	Take salary and pay premium after tax	Salary sacrifice \$22,000 to superannuation and pay premium through fund
Total cash salary required for premium payment	\$3,252	\$2,000
Personal tax payable	(\$1,252)	\$0
Superannuation fund tax	\$0	*\$0
Net income to pay insurance	\$2,000	\$2,000
Net benefit of paying insurance through superannuation fund	\$1,252	

*No tax is payable in the superannuation fund as the insurance premium would generally be considered a deduction against the fund's taxable income.

16. Hold your business premises through your Self-Managed Superannuation Fund (SMSF)

If you have an SMSF then you can hold a broad range of investments through your fund, and providing your trust deed permits it, and you have a properly constituted investment strategy which provides for investment in direct property, then potentially your fund could hold a business premise and this could even be the premises through which your own business operates.

Providing the property is used wholly and exclusively for business purposes (exceptions apply for rural property) and you transact with your fund at market

rates (purchases and sales of the property and rental payments are in line with what you would pay if dealing with an independent 3rd party on normal commercial terms) and you have a lease agreement between your superannuation fund and your business, then you could even operate your own business from the premises that your superannuation fund owns.

This can confer benefits to you and potentially allow your business to direct greater profits to your SMSF than would otherwise be allowable under maximum contribution rules. For example if your company is already paying the maximum of \$50,000 pa. in pre-tax contributions on your behalf (\$25,000 pa. each for you and your spouse) and your SMSF holds your business premise, worth \$500,000 and yielding 8% in rental, then an additional \$40,000 pa. could be directed from the business to your superannuation fund and taxed at the low rate of 15% as it applies to complying superannuation funds.

17. Superannuation benefits are protected from creditors

With very few exceptions when you are sued personally or you are declared bankrupt, your creditors can seize your assets and force their sale in payment of your liabilities.

One significant exception to this is superannuation – that is, as a general rule, balances in complying superannuation funds are protected from creditors – providing you can demonstrate you have not contributed to your fund in order to defeat creditors and you can demonstrate a history of legitimate contributions, then balances held in complying superannuation funds cannot be redeemed by creditors in order to settle your debts, and will remain as your retirement savings to fund your future retirement. Of course if you were to redeem your superannuation funds (assuming you are over your preservation age and retired or age 65), prior to your bankruptcy being discharged, then once this money moves out of your fund your creditors would generally then have access to these funds.

18. Contribute payments made from personal injury claims to superannuation

Generally, personal (non-concessional) contributions to superannuation are limited to \$150,000 pa (or \$450,000 over 3 years if under age 65). This however is not the case if you receive certain payments for personal injury or workers compensation – there is no limit in this instance – and for most people who qualify to contribute under these provisions, they can even begin to withdraw their funds if necessary.

If you receive a compensation payment:

- Paid under a structured settlement, an order for personal injury payment or a lump sum workers compensation payment; and
- You contribute the payment to superannuation within 90 days of receipt; and
- You do not claim a tax deduction for the contribution; and

- You notify your superannuation fund that you are claiming an exemption from the standard contributions cap; then providing that two medical practitioners (one being a specialist) certify that you are unlikely to be able to be gainfully employed in a capacity for which you are reasonably qualified by education, training or experience, you should qualify not only to make contributions above the \$150,000 cap (up to the amount of your compensation payment) you should also qualify for a condition of release due to permanent incapacity.

For example: let's say that you are 50 years of age and you receive a compensation payment for \$500,000, assuming you qualify (as outlined above), you could contribute the entire \$500,000 to superannuation and then immediately commence an account based pension even though you are not yet 55. And assuming you commenced a new superannuation fund with your \$500,000 you could commence a pension which is entirely tax free even though you are not yet 60, because the \$500,000 would count as tax-free benefits and in turn make the pension it generates tax free. Added to this the fact that any investment earnings (both income and capital gains) in your pension fund are free of tax, this could be a very financially rewarding strategy for you.

For more information on Superannuation and Retirement Planning contact your Patersons Adviser, call 1300 582 256 or visit www.psl.com.au.

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