FACT SHEET

Introducing Immediate Annuities

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What are Immediate Annuities?

Immediate annuities are income stream products purchased with a single lump sum of money which return the earnings and in some cases the capital and earnings in a structured regular manner over an agreed period of time. Immediate Annuities can be purchased with either superannuation or ordinary money. The purchase price for an annuity is dependent on the desired income, current interest rates and whether capital is to be utilised or preserved. Annuities can be tailored to suit particular needs. Minimum investment is usually $10,000.

Immediate annuities are offered mainly by life insurance companies. Immediate annuities can be used to meet or supplement income needs.

Features

- Annuities are payable for a fixed term or for life
- If purchased with ordinary money, annuities may be in single or joint names
- Annuities purchased with superannuation money must be in the name of the person who owns the superannuation
- Nomination of a reversionary annuitant at the time of purchase allows payments to continue in full, or in part, to another person in the event of the prior death of the principal (original) annuitant
- Unless otherwise specified, payments continue in full to the principal annuitant in the event of the prior death of the reversionary annuitant
- If purchased with superannuation money the reversionary annuitant must be a dependant of the principal annuitant. A spouse is always considered a dependant
- From 1 July 2007 superannuation based annuities must pay a minimum percentage (based on the annuitant's age) of the balance of the annuity at commencement and thereafter at 1 July each year as income. This may result in a reduction of the residual value
- Income payments may be received monthly, quarterly, half-yearly or annually
- The amount of capital to be returned as a lump sum at the end of the fixed term or on death can be nominated. This is called the Residual Capital Value (RCV) and cannot exceed the purchase price
- Payments may remain the same each year or be increased at a chosen yearly rate, e.g. in line with inflation. This is called indexation
- A guarantee period may be available for lifetime immediate annuities which ensures some money is paid to the annuitant's estate in the event of death within the period
- Fixed term annuities are guaranteed by the provider for the term
- Taxation advantages may be significant. They should be fully investigated before purchasing the annuity
- Some features may reduce the amount of income offered so options should be carefully chosen and their importance assessed

But Remember...

- The use of Annuities and other tax free retirement income streams purchased with superannuation is subject to the member's available Transfer Balance Cap. From 1 July 2017 an individual's transfer balance cap is $1.6M
- Immediate annuities may use up capital by returning it as part of the payment over the term of the annuity
- For Lifetime annuities, no payment is made to the estate when death occurs after the guarantee period expires
- Usually the contract cannot be varied once the annuity is purchased
- Capital withdrawals (commutations) may be restricted. Life annuities do not usually allow commutations after 6 months
- Interest rates at the time of commencing an immediate annuity have a major impact on payments made for the life of the annuity. Low interest rates at the time of purchase mean low payments for the duration

Fees

Costs are usually accounted for when providing an annuity quote and may not be shown separately. The income or rate of return is net of costs. When comparing annuities obtain quotes with identical options, from different providers and compare the income offered. Quotes from the same provider can vary depending on the adviser used, if applicable, and term chosen.

Taxation

A withholding (tax) declaration is usually completed enabling tax to be withheld at appropriate rates and taking into account possible tax offsets.

Tax on income from an immediate annuity may be reduced by tax offsets (rebates) or deductible amounts depending on the annuity type. Non-superannuation annuities with an RCV less than 100% have a deductible amount, calculated by subtracting the RCV from the purchase price and dividing the result by the term of the annuity or the longer life expectancy of the owner or reversionary beneficiary.

From 1 July 2007 payments from superannuation immediate annuities are tax exempt for people aged over 60 years. When paid between preservation age and age 60 years or prior to preservation age as a disability benefit, the 'taxable' component proportional to the fund, is taxed at the member's Marginal Tax Rate (MTR) and a 15% tax offset applies.

Government Income Support

Assets test: Immediate annuities purchased after 19 September 2007 are assessable assets with the asset values readjusted each 6 months.

Immediate annuities purchased before 20 September 2007 which complied with applicable rules remain Assets Test Exempt (ATE) or 50% ATE as applicable.

Income test: For an immediate annuity with a term of more than five years (including life time and life expectancy annuities), the income received less a deductible amount is assessed as income. Immediate annuities with a term of five years or less are treated as financial assets (investments) and are assessed under the deeming provisions.

Security and Risk

An immediate annuity is a contract with a provider. The income from the annuity and the residual capital value are guaranteed by that company. The guarantee is only as good as the company providing it.

What is detailed in the contract should be precisely what is received. The income and duration of the annuity are both guaranteed by the company and are not affected by poor investment returns. The company bears the investment risk.

Investing with Safety

It is prudent to get at least three quotes (with identical options) from different providers before purchasing an annuity. Be aware that quotes obtained are only valid for a limited time (usually 7 days).

All immediate annuity contracts offer a cooling off period. Use this opportunity to carefully check the contract and fully understand it. This may avoid problems before they occur and provides time to cancel the annuity, without penalty, if you decide not to proceed.

Immediate annuities are inflexible once commenced. If using them it is prudent to diversify with other income stream products and investments of varying duration.

Immediate annuities should not be the only investment held. If possible have money available elsewhere that is readily accessible as a cash reserve.