APPENDIX 3

Source: The Alexander Consulting Group

RETIREMENT INCOME STREAM ACCOUNT (RISA)

Q1 What is RISA?
A A RISA is an arrangement for a retired person to have his money managed for him. It is hoped that widows will soon be able to utilise the facility.

Q2 How does RISA work?
A Exactly the same as an investment account. Your investment is the opening balance. The account is credited with investment income on the balance remaining from time to time. The account is debited with your drawings and with the manager's charges.

Q3 Who can issue RISAs?
A Life insurance companies and other financial institutions approved by the ISC. To be approved, a financial institution must prove experience in investment management and its suitability to manage individuals' savings for retirement.

Q4 What types of investment are available to me if I purchase a RISA?
A Most RISAs will be invested in tax-free balanced portfolios with wide discretion for the managers to invest in any kind of investment. These portfolios, with significant share and property investments at most times, are expected to have the best 'growth' features over the long term and to provide the best protection against inflation. There is no reason why capital-stable or capital-guaranteed investment mediums, or a mixture of types of investment, cannot be used provided the investment managers have tax-free facilities.

Q5 Lots of organisations will manage my money for me, including unit trusts. What is different about RISA?
The essential differences from other money arrangements are firstly, that RISA meets Government requirements for payment of a retired income and secondly, because it is part of the approved retirement income system, there are significant taxation advantages.

Q6 What are the Government requirements?
A The fundamental requirement is that you must make regular drawings of specified amounts from your account. The drawings which you must make are related to your age and to the balance remaining in your account.

Q7 Why do minimum drawings depend on age?

A The idea is to enable a RISA investor to spread his income over the rest of his life. So younger investors might not be required to draw even the income earned. Drawings are required because the purpose of the system is to provide retirement incomes.

Q8 You referred to 'younger' investors. Can anyone buy a RISA?

A At the present time, RISAs are only available to retiring members of superannuation funds. Later, it is hoped that anyone who wishes to buy an immediate retirement income stream will be able to buy a RISA in just the same way as anyone can buy an immediate annuity. However, the 'market' is expected to be

- retired persons who have lump sum superannuation money or personal savings which need to be transformed into an income stream

- widows and disabled persons who receive lump sum superannuation.

Q9 What is the scale of minimum drawings?

A The balance held 3 months before the beginning of a financial year (or the amount invested where the person made his investment after that date) is divided by a factor, as follows, to give the minimum quarterly rate of drawing during that financial year.

	Age last b'day on 1 July	Factor	Age last b'day on 1 July	Factor	Age last b'day on 1 July	Factor
Up to & incl	55	22.0	63	16.0	71	12.0
	56	19.5	64	15.5	72	11.5
	57	19.0	65	15.0	73	11.0
	58	18.5	66	14.5	74	10.5
	59	18.0	67	14.0	75	10.0
	60	17.5	68	13.5	76	9.5
	61	17.0	69	13.0	77	9.0
	62	16.5	70	12.5	78	8.5
					79 or more	8.0

Q10 How do I know how much I must draw?

A Your manager will issue you a quarterly statement. When your March statement is issued he will tell you not only the balance standing to your credit but how much you must draw from the next 1 July. He will automatically pay the minimum unless you have nominated a larger amount.

Q11 How frequently will payments be made?
A Monthly. Lump sums can be drawn at any time. Tax will be deducted from both regular drawings and lump sums.

Q12 Are there any maximum drawings?
A No, but remember that all drawings other than the return of your undeducted purchase price are taxed as income. So if you draw too much in one year, you may increase the rate of tax on all of your income, including your regular drawings. Most RISA holders will draw only what they need for regular income needs and use the lump sum facility for special capital requirements.

Conserve capital, maximise the income credited to your account and protect your old age!

Q13 You said there are taxation advantages. If drawings are taxable, what are the advantages?
A The first advantage is that your investment suffers no tax at all while it is in your RISA account. It is a significant advantage to pay tax only on what you draw and not on what you earn. This increases dramatically the 'compounding ' power of your savings.

Q14 You said that this is the first advantage. Are there others?
A The other very significant advantage concerns the undeducted purchase price.

Q15 The undeducted purchase price. What is that?
A This is the amount invested which has not qualified for a taxation deduction, ordinary savings for example. A superannuation benefit on which tax has been paid becomes 'ordinary' money and like personal savings invested in a RISA (or annuity) is an undeducted purchase price.

If a superannuation benefit is rolled over before tax, the pre 1 July 1983 component and, usually, the employee's personal contributions made on and after 1 July 1983 are an undeducted purchase price.

Q16 What then is the advantage attaching to the undeducted purchase price?
A No tax is payable on the undeducted purchase price component of drawings. All other drawings are taxed as income. The undeducted purchase price component is determined by a formula which produces relatively large tax free components early on and smaller ones later.

Q17 That should make the minimum drawings go further in the years following retirement when travel and other activity are popular. Are there any other taxation factors?

A Yes, indeed. If you roll your super over before tax, the post 30 June 1983 component earns a 15% tax rebate.

Q18 That all sounds complicated.

A It isn't really. The manager records your undeducted purchase price and tells you on each statement how much has been drawn and how much remains to be drawn. He will also tell you how much of your credit is post 30 June 1983 super money and the rebate earned.

Remember that if you paid the tax on your super and then invest in a RISA (or an annuity) you will not be entitled to a post 30 June 1983 component rebate.

Q19 What happens if I invest my money in a market linked RISA and the market crashes?

A You simply ride it out. Because you will normally draw only a very small proportion of your balance at any one time, you will ride out all the ups and downs of the market. Your credit follows the experience line of the manager. It is sure to bounce up after a decline in prices and similarly to be 'cut down to size' after a boom. Your long term drawing capacity will follow the manager's underlying trend line.

The important action to be avoided is cashing out in a downturn. The ISC will be considering whether a maximum should be imposed on lump sum drawings to stop RISA holders from 'shooting themselves in the foot' by pulling out when the market is down.

Q20 Can I top-up my RISA with additional investments?

A Not after you have commenced drawings except by adding any roll over which you may have kept in an Approved Deposit Fund. However, the final rules may authorise the payment of lump sum contributions at any time.

Q21 What are the advantages of a RISA over an annuity?

A There are several advantages

- the ability to leave one's undrawn capital to heirs (this has special significance to many people who have a lump sum option at retirement, particularly where the member or his spouse is in poor or indifferent health)

- protection against inflation through participation in a mixed trust under experienced management

- flexibility in income with the opportunity to blend into social security

- retention in a very real sense of the 'ownership' of one's savings (The ability is there to change managers but, as a general rule, this would not be a frequent occurrence.) The ability to withdraw even one's full balance is provided but is seldom exercised.

Q22 What are the advantages of a life annuity over a RISA?

A A life annuity continues at its contractual level however long the annuitant or annuitants live. A RISA could fall away and would fall away rapidly if drawings significantly exceed earnings.

It is possible to buy a fully indexed annuity at the present time. Although the income is low relative to capital, initially, this is the only means of ensuring that real income is maintained. The supply of such annuities is likely to be limited and when inflation is expected to rise they probably will not be available at all.

Q23 Speaking of income relative to capital, annuities seem to be a good deal, don't you think?

A Annuities effected in the high interest rate era provide a very good income stream. New annuities are not nearly so good. Annuities reflect for their whole life, the economic conditions prevailing at the time of purchase.

Annuities and RISA's are alternatives. It is a matter of weighing up the pros and cons of each.

The average rate of return on a RISA should be better than on an annuity because the manager is not constrained by guarantees as is the issuer or an annuity.

The long livers may do well out of annuities. Those who live a short period transfer some of their capital to the long livers.

Some people will be happy to lock-in their income through an annuity and will be content to accept that on death after expiry of the term certain (if any) there will be no residual payment available to children. The residual payment on death during the term certain declines quite rapidly.

Whilst annuities are generally unsatisfactory at the present time, RISAs present the opportunity to buy in at relatively low prices because of the depressed share and property markets.

Q24 I have only a modest lump sum. The annuity is really very small. Is a RISA any better?

A Yes. You can draw your RISA at a rate sufficient for you or live on and then move to social security. Better still, your adviser will work out a drawing plan to blend your RISA income with social security. You can 'fine tune' your program as you go along or make a major change e.g. drawing it down more rapidly or slowing the drawings to a minimum to best suit your changing circumstances. Family circumstances can change quite dramatically after retirement. Misfortune does befall some families. (Dad had a good super but he bought an annuity. We have four kiddies still at school since Tom's illness it has all been uphill and will stay that way.)

Q25 I am not 65 yet. When should I buy my RISA? I have some personal savings, my Company super and super from a previous job rolling up in an ADF.

A Your RISA commences when you retire but you can retain your ADF credits and roll them into your RISA later (but not after age 65 of course).

Q26 If I have a lot of money in my super, is there anything special to watch out for?

AS As a general rule, it is not a good idea to accumulate your super over the lump sum reasonable benefit limit (RBL) unless you can go a long way over and, hopefully, approach the pension RBL.

If you go over your lump sum RBL the choices are

- pay tax at your marginal rate on the excess

- take at least half your lump sum as what is called a complying pension. This has the effect of reducing the lump sum subject to concessional taxation treatment.

At the present time, only an indexed, non commutable life annuity is a complying pension.

Hence, if your super rubs up against your lump sum RBL it is generally a good idea to retire, transfer it to a RISA and start drawings.

It is important to consult your adviser. There are choices to be made and unfortunately it is the case that very few people can make an informed decision without guidance.

Q27 Why does switching to a RISA avoid the excess benefits problems?

A Once you are in a RISA it doesn't matter how much you earn, it will accumulate tax-free. Of course, the more you earn, the greater your drawings must be.

Q28 What happens if I die?

A The balance standing to your credit is payable. A spouse can continue to draw income under the RISA, as before but the minimum drawings are adjusted for the spouse's age.

Q29 What is the taxation position if the balance is paid as a lump sum?

A Any undrawn undeducted purchase price is payable tax free. The remainder is taxable but subject to rebate where applicable.

Q30 To whom is the balance payable?

A Typical superannuation trust provisions apply. The Trustee has a discretion to pay one or more dependants or the legal personal representative of the deceased.