The problem with pensions

NOEL WHITTAKER

There's a big move against linking the age pension to the cost of living.

AUSTRALIA has one of the most generous superannuation systems on the planet. There is just one problem – it's unsustainable. Under the current rules, a couple can have up to $1,151,500 of assets, plus a family home of unlimited value, before losing access to at least a part pension. The cut-off point for the income test is $74,818 a year.

Granted, at these levels, the pension paid is minuscule, but it's not the amount that attracts retirees. It's the ability to get the prized pensioner health card, which is available to anyone who is receiving a part age pension.

Pension eligibility is under attack from all sides. Pension increases are currently linked to average weekly earnings – about 4 per cent a year. The government wants to link increases to the cost of living instead. The full pension for a couple is now $33,717 a year. Under the existing arrangements, it would be $75,000 a year in 20 years – if the increase was reduced to the consumer price index, it would be just $55,500 in 20 years.

It's not unreasonable to think that linking the age pension to the cost of living is fair, but there is already a groundswell of feeling that this is a bridge too far. If that is so, the only viable alternative strategy will be adjusting the taper rate – this is the rate at which the pension reduces as assets or income rise.

Social Services Minister Scott Morrison is open to tightening the taper rate, the Greens are happy to consider it, and some cross-benchers like Nick Xenophon can't wait to see it happen.

But changing the taper rate is fraught with difficulties. If you make the taper too steep, pensioners are placed in the invidious position that it's not worth earning extra income because of the effect on the pension. If you make it too shallow, as it is now, you push out eligibility so far that even a person earning $74,000 a year is eligible for a part pension.

Currently, under the income test, every additional dollar earned above the threshold causes a reduction of 50¢ in pension. Under the assets test, the full pension is reduced by $1.50 per fortnight for each $1000 above the threshold. Pension eligibility is then assessed using the test that produces the lowest pension. Because of the way the numbers work, almost everybody with financial assets in excess of $350,000 is assessed under the assets test.

Those who are advocating a change in the taper rate are seeking a return to the Howard government years, when the asset test taper was $3 for each $1000 above the threshold. This might be a simple concept to toss around in the cloistered atmosphere of the cabinet room, but it's a very different matter in the real world.

Case study: Mick and Mary are aged 70, and have $450,000 in financial assets such as super, and $50,000 in lifestyle assets like a car and furniture. They own their own home and are assessed under the assets test. Their current pension is $25,390 a year. If the taper rate was changed, as foreshadowed above, their pension would drop by $8327 a year, or $160 a week. That's bad enough, but now think about their neighbours who have $720,000 in assessable assets. They would lose the entire pension and the concessions that go with it.

Do you really think either couple are going to give without a battle?

Yes, the current pension system is unsustainable – the problem is that any government who tries to change the system will be saddling up for the fight of their lives.

It's not the amount but the ability to get the prized pensioner card that attracts retirees.

Noel Whittaker is the author of *Making Money Made Simple* and numerous other books on personal finance. His advice is general in nature and readers should seek their own professional advice before making any financial decisions. Email: noelwhit@gmail.com.

Q My parents own their home and will soon move into an aged care facility. Hopefully they will live long enough to sell the house and finance the costs of their care. They won't have to sell within two years because I have been caring for them and living in their home for more than that time. If I inherit the money remaining from the proceeds of selling the house, is it taxed and if so, in what way?

A If the property was your parents' residence before they moved to aged care, it will be a CGT (capital gains tax) exempt asset, and will be deemed to have passed to you on their death at its market value then, assuming you do not rent it out for more than six years. If it is sold before their deaths, it will be CGT exempt provided it has not been rented out for more than six years. There is no death duty, but of course normal personal taxation could be payable on any investments you make with the proceeds.

Q I am 20 and earn $60,000 a year. I bought an investment property 12 months ago, and moved in six months ago to make minor renovations. The house is valued at $380,000 with a mortgage of $290,000. Am I able to claim the CGT exemption for the next six years now that I have been living in the house for over six months, even though it was initially bought as an investment? With interest rates dropping, is it better to concentrate on paying off the mortgage, or should I reduce the debt by half and buy shares or another type of investment?

A Because it was an investment property before you moved in, you are not eligible for the CGT exemption from the date you bought it. However, if you move out and don't claim any other property as your principal residence, you will be entitled to a six-year exemption from the date you moved in. I suggest you diversify into shares in a small way to get the compounding effect working at an early an age as possible.

Twenty small tips that can add up to huge savings

By **MELISSA BROWNE**

I LOVE life hacks. Those tips that seem so strange are often so sensible that you cannot believe you haven't already tried them.

Generally these life hacks are based on fitness, wellness, technology or cleaning, but what about finance and money hacks? Following are 20 of my favourite money hacks that, if adopted, could potentially save you thousands of dollars every year. None of them are rocket science but if you adopt even a few of them, you will notice a big impact on your bank account by the end of the year.

1. Take your cards out of your wallet. All of them. Instead bring cash for your lunch or your coffee. That way you cannot be tempted to buy anything else in your lunch hour because you cannot pay for it.

2. Shop your loans around. Each year, shop your loans around for a better interest rate and if you find one, take it to your bank and ask them to match it.

3. Pay yourself first. You have probably heard this one before but are you doing it? If not, set up an automatic transfer to make sure the money for your savings is the first thing that is paid.

4. Keep your savings in an offset account. If you have a mortgage, you will save more interest by keeping your money in an offset account than you will in a savings account. Plus you will not pay tax on it.

5. Pay for tax deductions on your card. That way if you lose your receipt, the bank statement is proof of the deduction.

6. Pay down debt using a zero-interest credit card. If you are not paying off your balance at the end of the month then apply for a zero interest card and transfer your debt. Then do yourself a favour and cut up both cards.

7. Buy property in a self-managed superannuation fund. When you retire, the rent may be tax-free and when you sell the property after retirement the capital gains may be tax-free. A win-win.

8. Pay down your bad debt first. Maximise your tax deduction by keeping your good debt (investment loans) as interest-only loans and pay the extra amount on to your bad debt (home mortgage).

9. Unsubscribe from online shopping sites and delete your credit card information. Nothing destroys your willpower faster than having a sale pop up in your inbox and your credit card details are saved and ready to go. Instead, start shopping on your terms.

10. Do a financial detox – 30 days with no spending. This is designed to break your subconscious spending and help you set up great saving and spending patterns. It works best if it is done twice a year.

11. Cook. I once heard a nutritionist say that more time in the kitchen means less time at the doctor, dentist and therapist. I would add that it also means more money in your bank account.

12. Shop at farmers' markets and online with a grocery list. Cut out the middle man, pay less and watch how much longer your fruit and vegetables last when you buy them directly from the farmer. Plus, shopping online with a list saves you from impulse buys.

13. Share and rent. For anything that is not going to increase in value, do not buy – share instead. There are many sites online where you can do this now and there are many ways to do it – sharing everything from holidays to clothes to cars to lawnmowers.

14. Teach your kids about money and say no. Teaching your kids great money habits now will save you money because you are not always giving in, and you are also setting them up for a great relationship with money for the long term.

15. Embrace the cloud. There are so many cheap or free sites to help you with your finances. From the free Money Smart site through to banks giving you details on your spending patterns via internet banking. If you have a business make sure you don't miss out: check out Xero, Commonwealth Bank's Albert app, or for a great, cheap, one-stop solution head to St George's My Business Connect.

16. Renegotiate monthly payments. It is the regular small monthly amounts that add up to an annual large amount. Negotiate payments where possible or cancel them completely if they are unnecessary.

17. Buy a quantity surveyor report for your rental property. If your investment property is less than 40 years old, you could be missing out on thousands of dollars every year by not organising this report.

18. Travel in the off-season. There is a reason why it is more expensive to go away at Easter and Christmas, so do not travel during peak times and if you do not have to travel during school holidays – then don't.

19. Build multiple streams of income. This does not mean a second job any more. Instead it might be share trading, properties, online businesses, consulting, blogging or importing and selling products.

20. Manage electricity costs. This is one of the biggest bills and there are so many ways to reduce it. Drop your airconditioning to 20 degrees, turn off machines not used, switch to energy-efficient light bulbs and air-dry clothes instead of using a clothes dryer.

Life hacks – they are simply creating better habits. After all, it is the small changes that are the easiest to make and, combined with others, make the biggest impact.