

# **EXPLANATORY STATEMENT**

## **Select Legislative Instrument 2005 No. 56**

### **Issued by authority of the Minister for Revenue and Assistant Treasurer**

*Retirement Savings Accounts Act 1997*

*Superannuation Industry (Supervision) Act 1993*

*Retirement Savings Accounts Amendment Regulations 2005 (No. 1)*

*Superannuation Industry (Supervision) Amendment Regulations 2005 (No. 2)*

The purpose of the Regulations is to amend the *Superannuation Industry (Supervision) Regulations 1994* and the *Retirement Savings Accounts Regulations 1997* in order to implement a Government policy initiative announced in the 25 February 2004 statement 'A more flexible and adaptable retirement income system'. The announced initiative will allow people to access their superannuation benefits from their preservation age in the form of a non-commutable income stream without having to retire or leave their job.

#### ***Retirement Savings Accounts Amendment Regulations 2005 (No. 1)***

Subsection 200(1) of the *Retirement Savings Accounts Act 1997* (the RSA Act) provides in part that the Governor-General may make regulations prescribing matters required or permitted by the RSA Act to be prescribed, or necessary or convenient to be prescribed for carrying out or giving effect to that Act.

The *Retirement Savings Accounts Regulations 1997* (the RSA Regulations), among other matters, set out the cashing rules for Retirement Savings Account (RSA) providers, as well as the rules for the preservation of benefits in these accounts.

The Regulations introduce a new limited condition of release for benefits held in an RSA. The new limited condition of release allows benefits to be paid out in a specified form to an RSA holder who has attained their preservation age. The cashing restriction attaching to the limited condition of release allows benefits to be paid only in the form of a non-commutable annuity or pension, or a non-commutable allocated annuity or pension. Definitions of these terms are inserted into the Regulations for purposes of the new condition of release.

Details of the Regulations are set out in Attachment A.

The Regulations commence on 1 July 2005.

The Regulations are a legislative instrument for the purposes of the *Legislative Instruments Act 2003*.

***Superannuation Industry (Supervision) Amendment Regulations 2005 (No. 2)***

Subsection 353(1) of the *Superannuation Industry (Supervision) Act 1993* (the SIS Act) provides, in part, that the Governor-General may make regulations prescribing matters required or permitted by the SIS Act to be prescribed, or necessary or convenient to be prescribed for carrying out or giving effect to that Act.

The *Superannuation Industry (Supervision) Regulations 1994* (the SIS Regulations), among other matters, set out the cashing rules for regulated superannuation funds, as well as the rules for the preservation of superannuation benefits.

The Regulations introduce a new limited condition of release for benefits held in a regulated superannuation fund. The new limited condition of release allows benefits to be paid out in a specified form to a member who has attained their preservation age. The cashing restriction attaching to the limited condition of release allows benefits to be paid only in the form of a non-commutable annuity or pension, or a non-commutable allocated annuity or pension. Definitions of these terms are inserted into the Regulations for purposes of the new condition of release.

Details of the Regulations are set out in Attachment B.

The Regulations commence on 1 July 2005.

The Regulations are a legislative instrument for the purposes of the *Legislative Instruments Act 2003*.

The Government undertook consultation with industry and the community in relation to the policy details of this initiative. This process involved the release of a Treasury discussion paper in November 2004 canvassing a number of issues in relation to the design of the policy and inviting feedback on these. Targeted consultation with industry also took place on the draft SIS and RSA Regulations.

## **REGULATION IMPACT STATEMENT**

### **BACKGROUND/ISSUE**

To ensure that concessional taxed superannuation is used for its intended purpose of supporting retirement income, superannuation benefits are generally required to be preserved in a superannuation fund until the member's retirement, on or after attaining preservation age.

The current superannuation cashing rules require people below the age of 65 to retire before they can access their superannuation benefits. For a person who has reached 60 years of age, 'retirement' includes the termination of an arrangement under which the person was gainfully employed. These rules may lead to people deciding to retire or leave their job prematurely in order to access their superannuation benefits. The

rules also do not adequately cater for more flexible workplace arrangements where people may choose to reduce their hours of work as they approach retirement.

As part of the policy statement, *A more flexible and adaptable retirement income system* released on 25 February 2004, the Government announced that the superannuation cashing rules would be amended to allow a person who has reached their preservation age and is still in the workforce to access their superannuation benefits in the form of a non-commutable income stream. This measure commences on 1 July 2005.

The Government noted that the details of the measure, including the types of non-commutable income streams and other aspects of the policy including the need for limits on the amount of benefits that can be accessed, would be settled following a community consultation process.

This RIS focuses on the implementation details of the measure.

### **POLICY OBJECTIVE**

The purpose of allowing people to access their superannuation from their preservation age without having to retire or leave their job is to give them more flexibility to develop strategies in their transition to retirement. Providing greater flexibility in the rules for accessing superannuation benefits may encourage people to retain a connection with the workforce for a longer period.

The measure is not intended to provide people with a vehicle to dissipate their superannuation savings excessively before retirement. The design of the policy should therefore be consistent with the policy principle that savings should be drawn down in a regular and orderly way over the course of retirement.

### **IMPLEMENTATION OPTIONS**

The central feature of the policy is that people who have reached their preservation age will be able to access their superannuation in the form of a non-commutable income stream without the need to retire from the workforce.

Options for implementing the policy revolve around the types of non-commutable income streams through which benefits can be accessed before retirement, whether or not there will be a cap on the amount of benefits that can be accessed under the policy, and whether eligibility for the measure will be subject to a work test.

Under each of the options specified below, it would not be compulsory for superannuation funds to offer the transition to retirement policy to their members. Making the policy voluntary avoids imposing undue compliance costs on some (eg defined benefit) funds associated with amending fund rules and systems to allow members to both accumulate and draw down benefits at the same time.

### **Option 1**

This option involves:

- restricting access to the measure to the existing range of non-commutable complying income streams;

- capping the amount of benefits that can be accessed under the policy; and
- making eligibility for the measure subject to a work test so that only those people working part time will be able to access their benefits before retirement.

### **Option 2**

This option involves:

- allowing access to the measure through the existing range of non-commutable complying income streams, as well as through a non-commutable variant of an allocated pension;
- capping the amount of benefits that can be accessed under the policy; and
- making eligibility subject to a work test so that only those people working part time will be able to access their benefits before retirement.

### **Option 3**

This option involves:

- allowing access to the measure through the existing range of non-commutable complying income streams, as well as through a non-commutable variant of an allocated pension;
- not capping the amount of benefits that can be accessed under the policy; and
- not making eligibility subject to a work test.

## **IMPACT GROUPS**

The policy will impact on superannuation funds, their members and providers of retirement income stream products (these may be superannuation funds or life offices). The policy will impact these groups directly. Retirees will be impacted by being allowed more options for accessing their superannuation benefits after reaching preservation age. Funds and income stream providers will be impacted where they choose to release benefits under the new limited condition of release, and where they choose to pay one of the non-commutable income streams through which benefits will be accessed.

## **ANALYSIS OF IMPACTS**

### **Policy benefits**

At a broad level, the transition to retirement measure is expected to benefit employees and fund members by giving them more flexibility to develop strategies in their transition to retirement. For example, an individual might choose to continue working on a part-time basis, using part of their superannuation to supplement their employment income, instead of leaving the workforce altogether simply to access their superannuation.

Providing greater flexibility in the rules for accessing superannuation will remove a possible regulatory impediment to people retaining a connection with the workforce. Greater labour force participation by mature age workers will increase retirement incomes among this group. It will also become increasingly important to maintaining economic growth in the context of the ageing of the Australian population in the coming decades. From a broader social perspective, there is also evidence that those who participate in the workforce are healthier than those who do not.

### **Costs/benefits of implementation options**

An analysis of the impacts of the alternative options for implementing the measure is provided below.

#### Option 1

##### *Retirees*

People who wished to take advantage of the measure would be required to ‘lock away’ their superannuation benefits in a non-commutable income stream beyond the age at which they would otherwise be able to access them. This would reduce the appeal of the measure and may lead to some people retiring from the workforce altogether in order to access their benefits. Premature retirement is likely to result in a lower level of overall retirement savings relative to a situation where a person retains a connection with the workforce.

Imposing a cap would also be likely to constrain take-up of the policy by limiting the amount of income, and hence income replacement, that the non-commutable income stream could generate. People who were affected by a cap might be deterred from accessing the policy if it meant that they were unable to generate an income stream of sufficient value to compensate for the reduction in employment income associated with their transition to retirement.

Due to the nature of their employment, some people might not be able to reduce their hours of work. As a result, imposing a work test might lead to these people retiring from the workforce altogether in order to access their benefits.

Where people do have some control over their hours of work, a work test might reduce participation to the extent that people respond by reducing their hours of work where they would otherwise have worked a greater number of hours or continued to work full time.

Some people might choose to make the transition to retirement by reducing their level of responsibilities, with an associated reduction in their level of remuneration, rather than reducing their hours of work. A work test would exclude these people from the measure.

##### *Superannuation/income stream providers*

Restricting access to the measure to the existing range of complying income streams should have minimal or no impact on income stream providers, as the rules for these products would be largely the same irrespective of whether the income stream is commenced before or after retirement.

A work test would increase the complexity of the measure. To ensure its integrity, a work test would need to be applied on an ongoing (eg fortnightly or monthly) basis. This would impose ongoing costs on income stream providers through the need to monitor whether individuals continued to meet the test.

A rough guide to the nature and quantum of these costs can be found in evidence given to the Productivity Commission's Review of the Superannuation Industry (Supervision) Act 1993 in relation to the cost of administering the previous 10 hours per week work test for cashing of superannuation benefits for members over the age of 65. Evidence indicated that the work test imposed large costs on businesses through the need to regularly monitor and verify the employment status of members. The Productivity Commission received evidence from a firm administering 21,000 accounts for members aged over 65 that the annual cost of administering the work status of these members was around \$77,000 per annum.

Setting a cap on the amount of benefits that can be accessed under the measure would also increase compliance costs for superannuation funds associated with having to ensure that the cap is not exceeded. However, unlike the administration of a work test, these costs could be expected to be of a one-off rather than an on-going nature. Information is not readily available which would enable an estimate of the magnitude of the costs of imposing a cap to be made. However, it could be expected that such costs would not be as significant as the on-going costs associated with administering a work test.

### *Government*

The superannuation regulators (APRA and the ATO) may incur some minor costs associated with implementing the measure – for example, through the need to issue supporting explanatory material in relation to the changes. These costs are expected to be broadly the same under the three options.

## Option 2

### *Retirees*

Relative to Option 1, this option would provide individuals with an additional choice of accessing their benefits through a non-commutable allocated income stream.

An allocated income stream would give individuals the flexibility to vary their income payments from year to year (within the prescribed payment limits) and to commute the income stream on retirement or in order to return their benefits to the accumulation phase. This would allow a person to stop drawing down on their benefits if, for example, they choose to return to full-time work.

Allowing this additional flexibility is likely to increase the take-up of the policy relative to what would be the case under Option 1.

The impacts on retirees of the imposition of a cap and a work test are the same as for Option 1.

### *Superannuation/income stream providers*

The impacts on superannuation/income stream providers of imposing a work test and a cap on benefits are as for Option 1.

Allowing benefits to be accessed as a non-commutable allocated pension would involve some minor additional compliance costs for income stream providers. Providers would need to modify the rules for their allocated pensions to ensure that they cannot be commuted to a lump sum while the recipient is still in the workforce. Aside from this restriction, the regulatory arrangements for these products would be the same as for allocated pensions generally.

### Option 3

#### *Retirees*

The impacts on retirees of allowing benefits to be accessed through a non-commutable allocated pension are the same as for Option 2.

Compared with Options 1 and 2, not making access to the measure subject to either a benefits cap or a work test gives retirees a greater degree of flexibility to use their superannuation as part of a transition to retirement strategy.

For example, people would not be constrained in their decisions over whether, and by how much, they reduce their hours of work, or whether they make the transition to retirement by reducing their level of responsibilities as opposed to their actual hours of work.

Similarly, the absence of a cap on the amount of benefits that can be accessed under the policy means that retirees would be free to use all or part of their benefits to generate an income stream to support their transition to retirement. At the same time, the fact that benefits can only be accessed as a long term income stream protects against the excessive dissipation of savings prior to retirement.

### *Superannuation/income stream providers*

The compliance costs associated with ensuring that allocated pensions cannot be commuted to a lump sum while the recipient is still in the workforce would be the same as under Option 2. However, this option would avoid the compliance costs under Options 1 and 2 associated with having to administer a work test and ensure that a cap is not exceeded.

## **CONSULTATION**

A public consultation document on the transition to retirement measure was released on 3 November 2004. The document discussed and invited comment on a number of policy issues associated with the measure, including the nature of the income streams through which benefits would be accessed, as well as other issues such as whether there should be a cap on the amount of benefits that can be accessed and whether eligibility should be limited to those working part time. Submissions on the document were invited up to 10 December 2004.

Submissions were generally opposed to a cap on the amount of benefits that can be accessed and to making eligibility subject to a work test so as to limit the measure to part-time employees. The majority of these submissions argued that these restrictions would add to complexity and reduce the flexibility offered to individuals under the measure. To promote flexibility, submissions were also generally supportive of allowing access to the policy through a non-commutable allocated pension.

A number of submissions from industry bodies also argued that the existing range of income stream products would provide suitable vehicles for the measure, and that the creation of a totally new income stream product would add complexity and create additional compliance costs for income stream providers. The policy details of the measure have been formulated having regard to these concerns. In particular, access to benefits under the new limited condition of release will be allowed through existing income stream products (with minor modifications). The existing products are well known and understood within the industry and the retiree community.

### **CONCLUSION AND RECOMMENDED OPTION**

In comparison with Option 3, the imposition of a cap on benefits and a work test on eligibility under Options 1 and 2 would restrict the ability of retirees to develop a transition to retirement strategy which best matches their individual preferences and circumstances. Options 1 and 2 would also impose higher compliance costs on income stream providers relative to Option 3, in particular due to the need to administer an on-going work test to determine eligibility for the measure.

Option 3 provides the greatest degree of flexibility to people seeking to access the transition to retirement measure. Accordingly, this option could be expected to increase the take up of the measure relative to the other options, and to maximise the desired impact of the policy on participation among mature aged workers. By not imposing a work test on eligibility or capping the value of benefits that can be accessed, Option 3 also involves lower compliance costs on funds and income stream providers relative to the other options.

On the basis of the comparison of options, Option 3 is considered to be the preferred option.

### **IMPLEMENTATION AND REVIEW**

The recommended option will be administered by the Australian Prudential Regulation Authority (APRA) as part of its overall administration of the superannuation industry regulatory framework. As part of this process, APRA will advise the Government of any implementation issues as they arise. The changes will be reviewed as part of the Government's broader on-going monitoring of the superannuation system.

Superannuation and income stream providers will also have the opportunity to raise any implementation issues associated with the measure with the Government as part of existing regular industry consultation arrangements.

The preferred option has been chosen on the grounds that it provides retirees with an appropriate level of flexibility, while minimising additional complexity and compliance costs on business associated with the changes.

## ATTACHMENT A

***Retirement Savings Accounts Amendment Regulations 2005 (No. 1)***

**Regulation 1** specifies the name of the Regulations as the *Retirement Savings Accounts Amendment Regulations 2005 (No. 1)*.

**Regulation 2** provides that the proposed Regulations commence on 1 July 2005.

**Regulation 3** provides that Schedule 1 amends the *Retirement Savings Accounts Regulations 1997*.

**Schedule 1 – Amendments****Item 1**

The Regulations correct the reference to the *Superannuation Industry (Supervision) Regulations 1994* in the definition of *SIS Regulations* contained in subregulation 1.03 (1).

**Item 2**

The Regulations insert new definitions of non-commutable allocated pension and non-commutable pension into subregulation 4.01 (2) for the purposes of the cashing restriction attaching to the proposed new limited condition of release.

*Non-commutable allocated pension*

The Regulations define a non-commutable allocated pension as a pension which meets the standards of subregulation 1.07 (2) and which is provided under rules which in general ensure that if the pension is commuted, the resulting eligible termination payment (ETP) cannot be cashed. Exceptions to this restriction permit an ETP resulting from a commutation to be cashed where the pensioner has satisfied a condition of release of benefits with a ‘nil’ cashing restriction, or where the commutation is for certain specified purposes. These specified purposes are: to cash an unrestricted non-preserved benefit; or to pay a superannuation contributions surcharge; or to give effect to a payment split under family law (that is, the Regulations allow commutation if it is to give effect to the split of a benefit under family law or related legislation).

The restriction on commutation outlined above does not prevent commutations for purposes other than to cash the resulting ETP. For example, commutation is allowed where the resulting ETP is rolled over or transferred within the superannuation system – such as to return a benefit to the accumulation phase or to purchase another income stream. Where an ETP is rolled over or transferred, it will retain its preservation status. This means that until the pensioner has met a condition of release with a ‘nil’ cashing restriction, regulations 4.21 and 4.22 allow the benefit to be cashed only in a form permitted under Schedule 2 to the *Retirement Savings Accounts Regulations 1997*. The effect of this is that a non-commutable allocated pension can be commuted to purchase another non-commutable allocated pension, a non-commutable pension, a non-commutable allocated annuity or a non-commutable annuity.

Benefits in an income stream may consist of unrestricted non-preserved benefits, restricted non-preserved benefits and preserved benefits. Where an income stream consists of more than one of these benefit categories, in the event of a commutation the provider will need to determine the preservation components of the resulting ETP. For this purpose, the income stream provider would observe the order for cashing of benefits set down in regulation 4.29. This regulation requires benefits to be cashed in the sequence of unrestricted non-preserved benefits, restricted non-preserved benefits and preserved benefits.

Unrestricted non-preserved benefits and restricted non-preserved benefits are fixed dollar amounts which will be known at the commencement of the income stream. Payments made out of the income stream up to the time of commutation will also be known. By following the cashing order set down in regulation 4.29, an income stream provider will be able to determine the preservation components of a commutation ETP.

*Example: Commutation of a non-commutable allocated pension.*

Stephanie commences a non-commutable allocated pension from an RSA institution. The pension has an opening account balance of \$100,000 comprised of \$10,000 of unrestricted non-preserved benefits, \$10,000 of restricted non-preserved benefits and \$80,000 of preserved benefits.

After 3 years, Stephanie decides to return to full-time work and commutes the pension to roll back the account balance to the accumulation phase. At the time of the commutation, the account balance of the pension is \$85,000, with \$25,000 having been paid out in income payments. The \$85,000 represents an ETP.

To ascertain the preservation status of the commutation ETP, the allocated pension provider should observe the order for cashing of benefits set down in regulation 4.29. The \$25,000 of income payments from the pension will therefore have consisted of \$10,000 of unrestricted non-preserved benefits, \$10,000 of restricted non-preserved benefits and \$5,000 of preserved benefits. As the unrestricted non-preserved and restricted non-preserved components of the pension have been fully paid out, the ETP of \$85,000 consists entirely of preserved benefits.

Where an income stream contains benefits in more than one preservation category, it would be open to an RSA provider under regulation 4.18 to alter the benefit category as long as this does not result in an increase in the amount of unrestricted non-preserved benefits, or a decrease in the amount of preserved benefits. This regulation therefore gives income stream providers the option to reclassify unrestricted non-preserved benefits and restricted non-preserved benefits as preserved benefits. This would avoid the need for the provider to determine the preservation components of an ETP resulting from any commutation.

#### *Non-commutable pension*

The Regulations define a non-commutable pension as a pension which meets the standards of subregulation 1.07 (3A), but whose rules in general ensure that if the

pension is commuted under subparagraph 1.07 (3A) (e) (i) (the rule which allows commutation within 6 months of the pension's commencement), the resulting ETP cannot be cashed. Exceptions to this restriction allow an ETP resulting from such a commutation to be cashed where the pensioner has satisfied a condition of release of benefits with a 'nil' cashing restriction, or where the purpose of the commutation is to cash an unrestricted non-preserved benefit.

The restriction on commutation outlined above does not prevent commutations under the 6 month rule for purposes other than to cash the resulting ETP. For example, commutation under this rule is allowed where the resulting ETP is rolled over or transferred within the superannuation system – such as to return a benefit to the accumulation phase or to purchase another income stream. Where an ETP is rolled over or transferred, it will retain its preservation status. This means that until the pensioner has met a condition of release with a 'nil' cashing restriction, regulations 4.21 and 4.22 allow the benefit to be cashed only in a form permitted under Schedule 2. The effect of this, for example, is that a non-commutable pension can be commuted under the 6 month rule to purchase another non-commutable pension, a non-commutable annuity or a non-commutable allocated annuity or pension.

Under the rules set down in subregulation 1.07 (3A), commutation is allowed outside of the 6 months period for certain specified purposes. The Regulations do not affect these commutation options.

In determining the preservation components of a commutation ETP, income stream providers would follow the process described under the definition of non-commutable allocated pension.

### **Item 3**

The Regulations insert a new limited condition of release for preserved benefits and restricted non-preserved benefits into Schedule 2. The new condition of release allows a person who has reached preservation age to access his or her benefits in the form of:

- a non-commutable allocated pension; or
- a non-commutable pension; or
- a non-commutable allocated annuity or a non-commutable annuity (within the meaning of Part 6 of the SIS Regulations).

## ATTACHMENT B

*Superannuation Industry (Supervision) Amendment Regulations 2005 (No. 2)*

**Regulation 1** specifies the name of the Regulations as the *Superannuation Industry (Supervision) Amendment Regulations 2005 (No. 2)*.

**Regulation 2** provides that the proposed Regulations commence on 1 July 2005.

**Regulation 3** provides that Schedule 1 amends the *Superannuation Industry (Supervision) Regulations 1994*.

**Schedule 1 – Amendments****Item 1**

The Regulations insert new definitions of non-commutable allocated annuity, non-commutable allocated pension, non-commutable annuity and non-commutable pension into subregulation 6.01 (2) for the purposes of the cashing restriction attaching to the new limited condition of release.

*Non-commutable allocated annuity and non-commutable allocated pension*

The Regulations define non-commutable allocated annuity and non-commutable allocated pension to be annuities and pensions which meet the standards of subregulations 1.05 (4) and 1.06 (4) respectively, but whose rules in general ensure that if the annuity/pension is commuted, the resulting ETP cannot be cashed. Exceptions to this restriction permit an ETP resulting from a commutation to be cashed where the annuitant/pensioner has satisfied a condition of release with a ‘nil’ cashing restriction, or where the commutation is for certain specified purposes. These specified purposes are: to cash an unrestricted non-preserved benefit; or to pay a superannuation contributions surcharge; or to give effect to a payment split under family law (that is, the Regulations allow commutation if it is to give effect to the split of a benefit under family law or related legislation).

The restriction on commutation described above does not prevent commutations for purposes other than to cash the resulting ETP. For example, commutation is allowed where the resulting ETP is rolled over or transferred within the superannuation system – such as to return a benefit to the accumulation phase or to purchase another income stream. Where an ETP resulting from a commutation is rolled over or transferred, it will retain its preservation status. This means that until the annuitant/pensioner has met a condition of release with a ‘nil’ cashing restriction, regulations 6.18 and 6.19 allow the benefit to be cashed only in a form permitted under Schedule 1 to the *Superannuation Industry (Supervision) Regulations 1994*. The effect of this is that a non-commutable allocated annuity/pension can be commuted to purchase another non-commutable allocated annuity/pension, or a non-commutable pension or a non-commutable annuity.

Benefits in an annuity or pension may consist of unrestricted non-preserved benefits, restricted non-preserved benefits and preserved benefits. Where an income stream contains more than one category of benefits, in the event of a commutation the

provider would need to determine the preservation components of the resulting ETP. For this purpose, the income stream provider would observe the order for cashing of benefits set down in regulation 6.22A. This regulation requires benefits to be cashed in the sequence of unrestricted non-preserved benefits, restricted non-preserved benefits and preserved benefits.

Unrestricted non-preserved benefits and restricted non-preserved benefits are fixed dollar amounts which will be known at the commencement of the income stream. Payments made out of the income stream up to the time of commutation will also be known. By following the cashing order set down in regulation 6.22A, an income stream provider will be able to determine the preservation components of a commutation ETP.

*Example: Commutation of a non-commutable allocated pension.*

Alison commences a non-commutable allocated pension from a superannuation fund. The pension has an opening account balance of \$100,000 comprised of \$10,000 of unrestricted non-preserved benefits, \$20,000 of restricted non-preserved benefits and \$70,000 of preserved benefits.

After 3 years, Alison decides to return to full-time work and commutes the pension to roll back the account balance to the accumulation phase. At the time of the commutation, the account balance of the pension is \$85,000, with \$25,000 having been paid out in income payments. The \$85,000 represents an ETP.

To ascertain the preservation status of the commutation ETP, the allocated pension provider should observe the order for cashing of benefits set down in regulation 6.22A. The \$25,000 of income payments from the pension will therefore have consisted of \$10,000 of unrestricted non-preserved benefits, and \$15,000 of restricted non-preserved benefits. As the unrestricted non-preserved benefits have been fully paid out, along with \$15,000 of restricted non-preserved benefits, the ETP of \$85,000 consists of the remaining \$5,000 of restricted non-preserved benefits and \$80,000 of preserved benefits.

Where an income stream contains benefits in more than one preservation category, it would be open to an income stream provider under regulation 6.16 to alter the benefit category as long as this does not result in an increase in the amount of unrestricted non-preserved benefits or a decrease in the amount of preserved benefits. This regulation therefore gives income stream providers the option to reclassify unrestricted non-preserved benefits and restricted non-preserved benefits as preserved benefits. This would avoid the need for the provider to determine the preservation components of an ETP resulting from a commutation.

#### *Non-commutable annuity and non-commutable pension*

The Regulations define non-commutable annuity and non-commutable pension to be annuities and pensions which meet the standards of subregulations 1.05 (2), (9) or (10) and 1.06 (2), (7) or (8) respectively, but whose rules ensure that if the annuity/pension is commuted under the 6 month 'cooling-off' period which applies to

these products, the resulting ETP cannot be cashed. Exceptions to this restriction allow an ETP resulting from such a commutation to be cashed where the annuitant/pensioner has satisfied a condition of release of benefits with a 'nil' cashing restriction, or where the purpose of the commutation is to cash an unrestricted non-preserved benefit.

The restriction on commutation outlined above does not prevent commutations under the 6 month rule for purposes other than to cash the resulting ETP. For example, commutation under this rule is permitted where the resulting ETP is rolled over or transferred within the superannuation system – such as to return a benefit to the accumulation phase or to purchase another income stream. Where an ETP is rolled over or transferred, it would retain its preservation status. This means that until the annuitant/pensioner has met a condition of release with a 'nil' cashing restriction, regulations 6.18 and 6.19 allow the benefit to be cashed only in a form permitted under Schedule 1. The effect of this, for example, is that a non-commutable pension can be commuted under the 6 month rule to purchase another non-commutable pension, a non-commutable annuity or a non-commutable allocated annuity or pension.

Under the rules set down in subregulations 1.05 (2), (9) and (10) and 1.06 (2), (7) and (8), commutation is allowed outside of the 6 months period for certain specified purposes. The proposed Regulations do not affect these commutation options.

In determining the preservation components of a commutation ETP, income stream providers would have regard to the process described under the definition of non-commutable allocated annuity/pension.

Because annuity providers are not subject to the payment standards under the SIS Regulations, the Regulations include a requirement for payments of benefits under a non-commutable allocated annuity and a non-commutable annuity to be made in accordance with the standards that apply to regulated superannuation funds under SIS Regulations 6.16, 6.18, 6.19 and 6.22A. This ensures that the outcomes described above in relation to the form and the order in which benefits can be cashed, and the ability of income stream providers to alter the preservation category of benefits, apply equally to both regulated superannuation funds and annuity providers.

### **Items 2 and 3**

The Regulations insert a new limited condition of release for preserved benefits and restricted non-preserved benefits into Parts 1 and 2 of Schedule 1. The new condition of release allows a person who has reached preservation age to access his or her benefits in the form of:

- a non-commutable allocated annuity; or
- a non-commutable allocated pension; or
- a non-commutable annuity; or
- a non-commutable pension.