

Payments on redundancy



If you are facing redundancy...

...you have some very important decisions to make.

Do you look for another job, start your own business or perhaps retire? Everyone is different and you'll need to think carefully about your options.

Another key decision is what to do with the payments you receive from your employer. The choices you make can have a big impact on your financial position.

The aim of this guide is to provide you with general information about the types of payments you may receive and the potential tax implications.

Once you've read this guide, you should consider obtaining advice from a qualified financial adviser. They can help you make the right financial decisions by taking into account your goals and personal situation.

To find out more about the financial planning services available to you, contact a Plum Member Services Consultant on **1300 55 7586**.

What payments may you receive?

The types of payments you may receive from your employer can be grouped into three main categories – each with different tax implications. These include:

- a tax-free redundancy payment;
- an employment termination payment; and
- other termination payments.

Each of these categories are discussed in more detail throughout this guide.

Tax-free redundancy payments

If you are leaving your employer as a result of a bona fide redundancy, some (or all) of your payment will be tax-free and must be received as cash.

The maximum tax-free redundancy payment you can receive in the 2009-2010 financial year is \$7,732, plus \$3,867 for each completed year of service. These thresholds are indexed (increased) on 1 July each year.

As a general rule, a **bona fide redundancy** occurs if you are under age 65 and are not replaced by another employee (i.e. the job or role is being made redundant).

Employment termination payments

On leaving your employer, you may be entitled to an employment termination payment (ETP). Examples can include a redundancy payment exceeding the tax-free amount (see page 3), accrued sick leave or an ex-gratia payment.

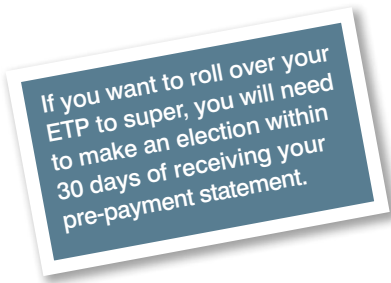
The options available to you, and the tax treatment, will depend on whether the payment amount (or a formula for determining your entitlement) was specified in your employment contract, or workplace agreement, at 9 May 2006. If it was, transitional rules will apply to ETPs received between 1 July 2007 and 30 June 2012.

Your employer will be able to confirm whether the transitional rules apply to you.

If you are eligible for the transitional rules

You can elect to roll over (transfer) your ETP into a super fund or receive the money as cash. While cashing out your ETP could be suitable, rolling over to super could be a better option if you want to maximise your retirement savings. This is because the initial tax bill will generally be less (see the table on the opposite page). As a result, rolling over to super can enable you to make a larger after-tax investment.

Also, while the money is in super, investment earnings are taxed at a maximum rate of 15 per cent. Conversely, if you cash out your ETP and invest outside super, earnings are taxed at your marginal rate, which could be up to 46.5 per cent.¹



If you want to roll over your ETP to super, you will need to make an election within 30 days of receiving your pre-payment statement.

¹ Includes a Medicare levy of 1.5 per cent.

Tax payable on ETPs in 2009/2010 – transitional rules

The table below summarises the tax treatment of ETPs in the 2009/2010 financial year, assuming you are eligible for the transitional rules.

As you can see, regardless of your age, less tax will **generally** be payable on the taxable component if you roll over your ETP, rather than receive the payment as cash.

	When ETP is received as cash	When ETP is rolled over to super
Tax free component	Nil	Nil
Taxable component		
If under 55	First \$1 million ² taxed at 31.5 per cent ³ and excess taxed at 46.5 per cent ³	Taxed at 15 per cent with excess above \$1 million ² counting towards the concessional contribution cap ⁵
If 55 or over	First \$150,000 ⁴ taxed at 16.5 per cent, ³ between \$150,000 and \$1 million ² taxed at 31.5 per cent ³ and excess taxed at 46.5 per cent ³	As above

2 This threshold is reduced by any transitional employment termination payments (ETPs) received.

3 Includes a Medicare levy of 1.5 per cent.

4 Indexed periodically in increments of \$5,000. This threshold applies to all transitional termination payments received during the transitional period.

5 The concessional cap is \$25,000 p.a. (indexed) or, if you're aged 50 or over \$50,000 p.a. (not indexed) until 30 June 2012 and \$25,000 p.a. (indexed) thereafter. If the cap is exceeded, excess contributions will be taxed at a penalty rate of 31.5 per cent, in addition to the 15 per cent tax payable when contributed to super.

Employment termination payments

continued

Case study – transitional rules

Brendan, aged 40, has been made redundant after 10 full years of service with his employer.

He is entitled to a bona fide tax-free redundancy payment of \$46,402 that will be paid as cash (see page 3). He plans to use this money to meet his living expenses and other immediate needs while he looks for a new job.

He is also entitled to an ETP of \$60,000 (consisting entirely of the taxable component) and wants to invest this money for his retirement. Because he is eligible for the transitional rules (see page 4), he is considering two options:

1. taking the ETP as cash and investing outside super; and
2. rolling over the ETP into super.

After tax is taken into account, rolling over the ETP will enable Brendan to invest an additional **\$9,900**.

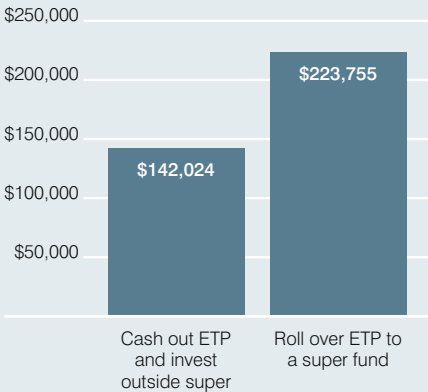
	Cash out ETP and invest outside super	Roll over ETP to a super fund
ETP amount	\$60,000	\$60,000
Less tax payable on cash lump sum at 31.5 per cent ⁶	(\$18,900)	N/A
Less tax payable when rolling over at 15 per cent	N/A	(\$9,000)
Net amount to invest	\$41,100	\$51,000

⁶ Includes a Medicare levy of 1.5 per cent.

Let's now assume Brendan maintains these investments for 20 years until he retires at age 60. In this example, the super investment will be worth an extra **\$81,731**.

This is because, in addition to making a larger initial investment, earnings in the super fund are taxed at a maximum rate of 15 per cent, not his marginal rate which we have assumed will be 41.5 per cent.⁷

Benefits of rolling over to super over 20 years



Other assumptions 20 year comparison. Total before-tax return from both the super and non-super investment is 8 per cent p.a. (split 3 per cent income and 5 per cent growth). All income is re-invested. The overall franking level on investment income is 25 per cent. Both investments are cashed out at the end of the 20 year period. All figures are after income tax (at 41.5 per cent for non-super and 15 per cent for super) and capital gains tax (including discounting). These rates are assumed to remain constant over the investment period. No lump sum tax was payable when Brendan cashed out his super, as he was aged 60 or over. These assumptions are for demonstration purposes. Investment performance may go up and down over time and the assumptions may vary.

⁷ Includes a Medicare levy of 1.5 per cent.

Employment termination payments continued

If you are **not** eligible for the transitional rules

You don't have the option of rolling over to a super fund and must receive your ETP as cash after any applicable taxes are deducted (see table below).

You could, however, invest the after-tax proceeds in super as a personal after-tax contribution⁸ should you wish to take advantage of the maximum tax rate of 15 per cent on investment earnings in super.

Tax payable on ETPs in 2009/2010 – non-transitional rules

The table below summarises the tax treatment of ETPs in the 2009/2010 financial year, assuming you are **not** eligible for the transitional rules.

When ETP is received as cash

Tax free component	Nil
Taxable component	
If under 55	First \$150,000 ⁹ taxed at 31.5 per cent ¹⁰ and excess taxed at 46.5 per cent ¹⁰
If 55 or over	First \$150,000 ⁹ taxed at 16.5 per cent ¹⁰ and excess taxed at 46.5 per cent ¹⁰

⁸ Personal after-tax super contributions and certain other amounts are subject to a non-concessional contribution cap. From 1 July 2009, this cap is \$150,000 a year (or \$450,000 in one year if you're under age 65 in that year and don't make further contributions in the following two years). If the cap is exceeded, excess contributions will be taxed at a penalty rate of 46.5 per cent.

⁹ Indexed periodically in increments of \$5,000. This is an annual limit that applies to all non-transitional termination payments received in a financial year (or related to that year).

¹⁰ Includes a Medicare levy of 1.5 per cent.

Case study – non-transitional rules

Susie, aged 42, has been made redundant after eight full years with her employer.

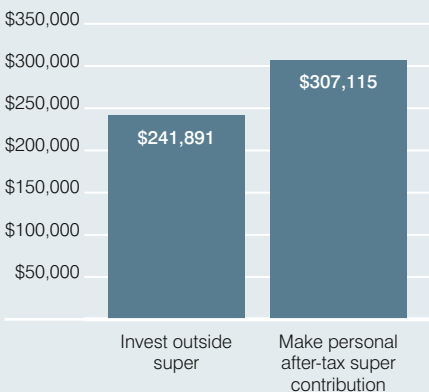
She is not eligible for the transitional rules (see page 4). She will receive a total bona fide redundancy payment of \$100,000 as cash. This amount includes both a tax-free redundancy payment (see page 3) and an ETP after-tax is deducted.

Susie will keep \$30,000 to meet her living expenses and other needs while she looks for new employment. With the remaining \$70,000, she is considering two options:

1. investing outside super; and
2. making a personal after-tax contribution into her super.

If Susie maintains these investments for 20 years until she retires at age 62, the super investment will be worth an extra **\$65,224**. This is because earnings in the super fund are taxed at a maximum rate of 15 per cent, not her marginal rate which we have assumed will be 41.5 per cent.¹¹

Benefits of making a personal after-tax super contribution over 20 years



Other assumptions 20 year comparison. Total before-tax return from both the super and non-super investment is 8 per cent pa (split 3 per cent income and 5 per cent growth). All income is re-invested. The overall franking level on investment income is 25 per cent. Both investments are cashed out at the end of the 20 year period. All figures are after income tax (at 41.5 per cent for non-super and 15 per cent for super) and capital gains tax (including discounting). These rates are assumed to remain constant over the investment period. No lump sum tax was payable when Susie cashed out her super, as she was aged 60 or over. Investment performance may go up and down over time and the assumptions may vary.

¹¹ Includes a Medicare levy of 1.5 per cent.

Other termination payments

On termination of employment, you may also be eligible to receive a range of other payments that must be taken as cash. The table below outlines the main examples and how they are taxed in the 2009/2010 financial year in the event of a bona fide redundancy (see page 3).

These payments could be used to meet your immediate needs or invested in super as a personal after-tax contribution to build your retirement savings.

Payment	Tax treatment in the event of a bona fide redundancy	When tax is paid
Accrued annual leave	100 per cent taxed at a maximum rate of 31.5 per cent ¹²	Deducted by your employer
Accrued long service leave		
Pre 16 August 1978 service	5 per cent taxed at your marginal rate	When you file your tax return
Post 15 August 1978 service	100 per cent taxed at a maximum rate of 31.5 per cent ¹²	Deducted by your employer
Final pay	Taxed at your marginal rate	Deducted by your employer

The tax treatments outlined above also apply in the event of invalidity or approved early retirement. If you are leaving your employer in other circumstances (e.g. upon resignation), different tax rates may apply to accrued annual leave and long service leave payments.

¹² Includes a Medicare levy of 1.5 per cent.

Where to from here?



In thinking about your next steps, you may want to consider:

How much money should you set aside for your living expenses or other immediate needs?

When making this assessment, you should consider whether you're eligible for the Newstart Allowance or other social security benefits.

Do you have a home loan or other personal debts?

If yes, using some (or all) of your redundancy payments to pay them off could be a sensible strategy.

Have you considered investing in super?

Rolling over or investing some of your redundancy payments in super can help you maximise your retirement savings. It could also help you qualify for (or increase your entitlement to) social security benefits. But remember, super can't be accessed until you reach a minimum age of 55 and permanently retire (or meet another 'condition of release').

Do you need to replace or top-up your insurances?

Because insurances provided by an employer usually cease when you leave, you should review your needs and make sure you are adequately covered.



Seek advice

Once you've considered the questions above, you should make an appointment with a financial adviser. A financial adviser can explain the complex financial issues surrounding redundancy in more detail and help you make the most of your opportunities. They can also recommend a range of other strategies to help you achieve your lifestyle and financial goals – now and in the future.

To find out more about the financial planning service available to you, contact a Plum Member Services Consultant on **1300 55 7586**.



Did you know...

As a member of the Plum Superannuation Fund you can access the services of financial advisers through *Momentum Financial Advice*. This service provides general advice over the phone – at no cost to you, in addition to personal face-to-face advice if you require more in-depth advice about your personal financial circumstances.

If you would like more information about *Momentum Financial Advice* or would like to access this service, contact a Plum Member Services Consultant on **1300 55 7586**.

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www.plum.com.au or



Speak with a Plum Member Services Consultant on **1300 55 7586**.

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