Tackling the retirement challenge

Strategies to secure your future
Tackling the retirement challenge

When planning for your retirement there are many questions you need to ask:
What financial challenges might I face in retirement? Which strategies can I implement to ensure I meet both my short-term and long-term objectives? Which product solutions will deliver the best result for me?

And for retirees facing high market volatility, the threat of inflation, and the risk of outliving retirement savings, mean the need for quality advice has never been greater than it is today.

At Challenger*, we want to help you secure your financial future. In this booklet, you will find investment concepts and strategies, as well as product solutions, which may help you to make the most of your retirement savings.

Use it with your financial adviser to tailor your plan, and tackle the retirement challenge with confidence.

*Challenger is Australia’s leading annuity provider. Challenger Life, the provider of the annuities, was named the latest Annuity Provider of the Year by both AFA (Association of Financial Advisers) and Plan for Life Actuaries and Researchers. Our annuities offer guaranteed capital and income, giving you peace of mind in retirement.

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How to use this brochure

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What are my challenges in retirement?

If you rely on investment returns and superannuation money to meet your living expenses in retirement, they need to be regular and dependable. There are a number of manageable risks which can impact whether your investments meet your needs. These include:

**LONGEVITY RISK**

Australians are living longer due to improvements in medical care and living standards. The average life expectancy has risen substantially in recent years and continues to increase, particularly for people over the age of 65.

Challenger estimates that an Australian male aged 65 in 2010 could expect to live to 90, while a woman aged 65 could expect to live to 92. For a couple aged 65, there is a 50% chance that at least one partner will almost live to 98. This is shown in the following chart.

Longer life expectancy means we may have to make our money last much longer in retirement.

![Longevity risk over time](chart)

The life expectancies shown above are based on Challenger estimates of mortality while taking into account future mortality improvements. The differences in life expectancy values from the Australian Life Table (ALT) estimates are driven by ALT life expectancy calculations not including a provision for future mortality improvements.

**INFLATION RISK**

Over time, inflation can erode the value of the income you receive from your investments, which means you face a decline in living standards over time.

According to estimates, a retired couple who own their own home requires an income of $31,767 p.a. to enjoy a modest lifestyle. In 10 years’ time, that would increase to $42,692 assuming an inflation rate of 3% p.a.

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2. ASFA Retirement Standard September 2011 quarter estimates. This benchmarks the annual budget needed by Australians to fund either a comfortable or modest standard of living in the post-work years. It is updated quarterly to reflect inflation and provides a detailed budget of what singles and couples would need to spend to support their chosen lifestyle.
The following chart shows the impact of inflation over time on items that cost $1,000 today using a 3% annual and 4% annual inflation rate.

Inflation will increase the cost of living over time

This example uses constant inflation figures of 3% p.a. and 4% p.a. The dollar values provided show the future cost of $1,000 in today's terms after 40 years. It is for illustrative purposes only and is not a prediction of future inflation rates.

MARKET RISK

Many people have seen significant volatility in the value of their retirement savings in recent years. If you have experienced volatility, but are many years away from retirement, you have the benefit of time to allow your savings to grow back if markets recover.

However, if you have reached, or are approaching, retirement, you usually do not have that luxury. At this stage, you have the most to lose from negative returns since this is the time that you generally have the most money invested. You also face the prospect of having to sell assets that have fallen in value to fund your income needs, which could adversely impact the growth potential of your investment portfolio. Retirees who no longer earn a wage may also find it difficult to replace lost savings following negative market movements.

The following chart demonstrates the volatility of different asset classes over the last 20 years. You can see that Australian and global shares have historically been more volatile than Australian and global fixed interest.

All returns are calculated in Australian dollars. Past performance is not an indicator of future performance.
Retirement product options

Annuities and account-based pensions are two popular types of retirement products. They can be used to help manage the investment challenges you face in retirement, and to provide you with an ongoing income.

**ANNUITIES**

An annuity is a simple, secure financial product that provides a series of payments, for a fixed term or for life, in return for an upfront capital investment. Your capital can be returned at the end of the agreed term or gradually during the term of the annuity as part of the regular payments.

Annuities can be bought with either superannuation or non-superannuation money. Your income is set at the outset, and this applies for the length of the annuity, regardless of share market movements or interest rate fluctuations. Annuities provide the peace of mind of a pre-agreed, secured income stream for a specific period of time or for life. They can also be indexed to increase in line with the inflation rate.

In Australia, annuities can only be issued by life insurance companies. They are strictly regulated by the Australian Prudential Regulation Authority (APRA), which also regulates or supervises banks and superannuation funds.

**ACCOUNT-BASED PENSIONS**

An account-based pension is an account in which you can invest your lump sum superannuation benefit and draw a regular income. With an account-based pension, you can generally choose from a range of investments and select the income you draw subject to minimum payment requirements set by the Government.

Account-based pensions are generally market-linked. This means that the capital value is linked to the performance of the underlying investments, which can in turn impact the level of your pension payments.

**FEATURES OF ANNUITIES AND ACCOUNT-BASED PENSIONS**

Investing in a combination of annuities and account-based pensions allows you to invest in growth assets while helping you manage the longevity, inflation and market risks described earlier.

The table on the following page highlights the key differences between annuities and account-based pensions.

Challenger offers a range of annuity products. See page 31 for more information.
## Features of Annuities and Account-Based Pensions

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<thead>
<tr>
<th>Feature</th>
<th>Annuities</th>
<th>Account-based pensions</th>
</tr>
</thead>
<tbody>
<tr>
<td>What income will I receive?</td>
<td>The income from an annuity is determined upfront by the issuer and may be indexed in line with the costs of living. The income level cannot be varied from what is agreed at the outset.</td>
<td>With an account-based pension you can choose and vary the level of income you receive subject to a minimum income requirement each year, based on your age and account balance. In some cases, a maximum income will also apply.</td>
</tr>
<tr>
<td>Is the income guaranteed?</td>
<td>Challenger Life has a contractual obligation under the terms of the applicable annuity to make income payments. Challenger’s ability to meet these obligations is dependent on the assets it holds from time to time to support these obligations and on capital support in accordance with APRA’s capital adequacy standard.</td>
<td>Generally not. In most circumstances your account balance will fluctuate with movements in the value of the underlying investments you choose. The income is dependent on you having sufficient assets in your account to fund the income payments.</td>
</tr>
<tr>
<td>How long will my income payments last?</td>
<td>The income can be paid for life or for an agreed term.</td>
<td>This will generally depend on a number of variables including the income and the investment return received.</td>
</tr>
<tr>
<td>How can I purchase it?</td>
<td>Either superannuation or non-superannuation money.</td>
<td>Superannuation money.</td>
</tr>
<tr>
<td>How are my income payments taxed?</td>
<td>When purchased with superannuation money, income payments from an annuity will attract a 15% pension offset between age 55 and 59 and will be fully tax free when you reach age 60. When purchased with non-superannuation money, the taxable component of regular income payments is taxed at your marginal rate.</td>
<td>As per annuities purchased with superannuation money.</td>
</tr>
<tr>
<td>How are my income payments treated for Centrelink purposes?</td>
<td>Part of the income payments from your annuity may be exempt from the Income Test. This amount is known as the deductible amount (see page 16 for an explanation).</td>
<td>Part of the income payments from your pension is exempt from the Income Test. This amount is known as the deductible amount and is calculated by dividing the amount you invest by your life expectancy.</td>
</tr>
<tr>
<td>Does the product offer investment choice?</td>
<td>No. Annuities offer a fixed rate of return that is fixed at commencement.</td>
<td>Yes. You generally have the opportunity to invest in a range of assets including growth assets such as shares and property.</td>
</tr>
<tr>
<td>Who carries the investment risk?</td>
<td>The life insurance company that issues the annuity.</td>
<td>You.</td>
</tr>
<tr>
<td>Can I make lump sum withdrawals?</td>
<td>Yes, although there is a cost for withdrawing prior to the end of the agreed term. In addition, withdrawals from lifetime annuities are only available within the withdrawal benefit period.</td>
<td>You can generally make lump sum withdrawals at any time.</td>
</tr>
<tr>
<td>Are there any management fees?</td>
<td>Annuities do not have any ongoing management fees or administration charges. In declaring the earnings rates for annuities, the life insurance company has already taken into consideration all expenses required to administer the investment.</td>
<td>Yes. An ongoing management fee is generally deducted from your account.</td>
</tr>
</tbody>
</table>
# Retirement product options

## ANNUITIES SUMMARY

<table>
<thead>
<tr>
<th>Benefits</th>
<th>Risks</th>
</tr>
</thead>
<tbody>
<tr>
<td>Guaranteed income and capital. In contrast to shares and other growth assets, annuities provide a fixed income regardless of market movements. When you buy your annuity you know exactly what income you’ll receive for the duration of the term. This makes planning your finances much easier as you don’t have to worry about market volatility affecting the income you receive from an annuity.</td>
<td>Fixed term annuities are locked in for a set period of time. If you withdraw before the end of the term, you may get back an amount less than the amount you invested, even after taking into account the payments that may have already been made to you.</td>
</tr>
<tr>
<td>No management fees. Unlike most retirement income products, annuities have no management fees. Broadly speaking, the life insurance company that offers the annuity derives income from the return on its investment portfolio minus the earnings rate paid to the investor. The ability to derive this return is taken into account when setting the applicable earnings rate. This means the return that is offered is what you get.</td>
<td>The real value of income payments may reduce over time as a result of inflation unless the annuity is indexed to CPI.</td>
</tr>
<tr>
<td>Attractive returns. Annuities have historically offered competitive earnings rates when compared to many other fixed income investments. However, past performance is not a reliable indicator of future performance.</td>
<td>There is a risk that the assets backing the underlying annuities are insufficient to meet investors’ payments. However, please note that the way Challenger Life manages the underlying investments underpinning annuities is governed by rules and regulations set by APRA to ensure that the payments can be met.</td>
</tr>
<tr>
<td>Flexible terms and payments. With annuities you can choose your investment term. It can be as short as one year, as long as 50 years or your lifetime. You can generally elect to receive your payments monthly, quarterly, half-yearly or annually.</td>
<td>Investing in an annuity may affect your eligibility for Centrelink benefits. You should seek your own professional advice about this before investing to ensure the annuity meets your personal financial and taxation needs (see page 16).</td>
</tr>
<tr>
<td>Inflation protection. With some annuities, you can elect to index your payments so they move in line with inflation (CPI) or at a fixed indexation rate. This way you won’t need to worry about the impact of inflation on your future payments.</td>
<td>Once your annuity commences, you cannot change the frequency of payments or the amount of income payments, even if your needs or circumstances change.</td>
</tr>
<tr>
<td>Tax effectiveness. If you are 60 or over and invest in an annuity using superannuation money, payments from the annuity are tax free. If you are aged 55-59, the taxable portion of your income is taxed at your marginal tax rate, but eligible for a 15% tax offset.</td>
<td>For lifetime annuities there is a risk of you dying before receiving back all your investment. To reduce the impact of this risk, they have a Withdrawal Guarantee within the first 15 years of the annuity.</td>
</tr>
<tr>
<td>Option for lifetime income. In the case of a lifetime annuity you can enjoy a secure, regular income for the rest of your life.</td>
<td></td>
</tr>
<tr>
<td>Part of the income from your annuity may be exempt from the Centrelink Income Test (see page 16).</td>
<td></td>
</tr>
</tbody>
</table>
ACCOUNT-BASED PENSIONS SUMMARY

Benefits

- Account-based pensions allow you to control your retirement income by varying the amount (subject to minimum pension payment requirements) and frequency of income paid.
- You can draw a lump sum if and when you need it.
- You can choose how your money is invested by your chosen provider. Fund managers offer different investment options to suit your investment strategies.
- You don’t pay tax on your income from age 60.
- If you are aged 55-59, the taxable portion of your account-based pension will be taxed at your marginal tax rate. However, the tax payable will receive a 15% offset.
- Part of the income from the pension is exempt from the Centrelink Income Test.

Risks

- Your investment returns (and your account balance) will fluctuate in line with market performance and the rate at which you make withdrawals.
- You will need to regularly review your income needs as you may outlive your money. Generally, there is no certainty that your super will last as long as you do.

FIXED RATE MANAGED FUNDS VERSUS REGULAR MANAGED FUNDS

Managed funds that invest in annuities issued by a life company can provide security of income and capital. When combined with managed funds investing in growth assets, such as shares or property, this strategy can be used to provide the defensive portion of your investment portfolio, giving your growth assets time to grow in value.

The Challenger Guaranteed Income Fund and Guaranteed Pension Fund are wholesale managed funds that invest in annuities issued by Challenger Life. These funds are available to investors via certain investment administration services (also known as platforms). Speak to your financial adviser for more information.

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<tr>
<th></th>
<th>Fixed rate managed funds</th>
<th>Managed fund with fixed income assets</th>
</tr>
</thead>
<tbody>
<tr>
<td>Earnings rate</td>
<td>Fixed at the time of investment.</td>
<td>Variable – dependent on the returns derived from underlying assets.</td>
</tr>
<tr>
<td>Income</td>
<td>Fixed at the time of investment.</td>
<td>Variable – dependent on the income derived from underlying assets.</td>
</tr>
<tr>
<td>Maturity value</td>
<td>Fixed at the time of investment.</td>
<td>Variable – generally does not have a maturity date and no future unit prices are known.</td>
</tr>
<tr>
<td>Management fees</td>
<td>No management fee is charged in the Fund.</td>
<td>A management fee will generally apply to a managed investment.</td>
</tr>
<tr>
<td>Security of assets</td>
<td>The Fund invests primarily in annuities issued by an APRA-regulated life company.</td>
<td>Variable – mostly market-linked assets.</td>
</tr>
</tbody>
</table>
## Strategy summary

**USE THE TABLE BELOW TO CONSIDER YOUR STRATEGY***

<table>
<thead>
<tr>
<th>Strategy</th>
<th>May be suitable for</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Secure a regular, dependable income in retirement</td>
<td>Those seeking an investment that provides a fixed income to meet living expenses.</td>
</tr>
<tr>
<td>2. Secure the defensive portion of my investment portfolio</td>
<td>Those investing via an investment platform and seeking a fixed income investment that provides certainty regarding income and capital.</td>
</tr>
<tr>
<td>3. Secure my self-managed superannuation fund pension payments</td>
<td>Those with a pension in their SMSF who want to secure income payments and protect their investment portfolio from short-term volatility.</td>
</tr>
<tr>
<td>4. Maximise my Age Pension entitlements</td>
<td>Those of Age Pension age whose pension entitlement is determined by the Income Test.</td>
</tr>
<tr>
<td>5. Reduce my aged care fees</td>
<td>Anyone in, or about to enter, an aged care facility such as a nursing home or hostel.</td>
</tr>
<tr>
<td>6. Transfer my SMSF complying pension to an annuity and maintain my Centrelink benefits</td>
<td>Those with an SMSF complying pension who fail the annual actuarial test or prefer a simpler income stream product.</td>
</tr>
<tr>
<td>7. Establish a short-term, tax-efficient investment as a non-resident</td>
<td>Non-residents seeking a short-term, secure income that is not subject to withholding tax in Australia.</td>
</tr>
<tr>
<td>8. An investment solution that offers estate planning certainty</td>
<td>Anyone seeking certainty over the transfer of their wealth upon their death.</td>
</tr>
</tbody>
</table>

*The strategies outlined in the table are general information only rather than advice. The information is based on our understanding of the current law and its interpretation at the time of writing, and may change at a future date. It has been prepared without taking account of any person’s objectives, financial situation or needs. Because of that, each person should, before acting on any such information, consider its appropriateness, having regard to their objectives, financial situation and needs. You should obtain a copy of the product disclosure statement for the relevant product and consider it before making any decision to acquire a product.
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<th>Possible outcomes</th>
<th>Helps protect against</th>
<th>See page</th>
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</thead>
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<tr>
<td>• Helps you to meet your income needs with certainty</td>
<td>• Longevity risk</td>
<td>10</td>
</tr>
<tr>
<td>• Can provide a tax-effective income as well as Centrelink benefits</td>
<td>• Inflation risk</td>
<td></td>
</tr>
<tr>
<td>• Provides an agreed level of income and fixed value at maturity regardless of market movements</td>
<td>• Market risk</td>
<td>12</td>
</tr>
<tr>
<td>• Provides an alternative to fixed income investments</td>
<td>• Longevity risk</td>
<td></td>
</tr>
<tr>
<td>• Can offset the volatility of growth assets in an investment portfolio</td>
<td>• Inflation risk</td>
<td></td>
</tr>
<tr>
<td>• Provides a fixed income return to meet income payments in the short term</td>
<td>• Market risk</td>
<td>14</td>
</tr>
<tr>
<td>• Allows growth assets to remain invested for longer</td>
<td>• Longevity risk</td>
<td></td>
</tr>
<tr>
<td>• Maximise your Age Pension payments</td>
<td>• Inflation risk</td>
<td>16</td>
</tr>
<tr>
<td>• Minimise the income counted under the Centrelink Income Test</td>
<td>• Market risk</td>
<td></td>
</tr>
<tr>
<td>• Reduce aged care fees</td>
<td>• Longevity risk</td>
<td></td>
</tr>
<tr>
<td>• Minimise the income counted under the aged care Income Test</td>
<td>• Inflation risk</td>
<td>18</td>
</tr>
<tr>
<td>• Transfer to a simpler income stream with a fixed income return</td>
<td>• Market risk</td>
<td></td>
</tr>
<tr>
<td>• May help to retain an existing Centrelink Assets Test exemption</td>
<td>• Inflation risk</td>
<td>20</td>
</tr>
<tr>
<td>• Provides a secure income at competitive rates</td>
<td>• Market risk</td>
<td></td>
</tr>
<tr>
<td>• Income is generally not subject to withholding tax in Australia</td>
<td>• Longevity risk</td>
<td>22</td>
</tr>
<tr>
<td>• Provides a certain and efficient transfer of wealth to beneficiaries</td>
<td>• Inflation risk</td>
<td>24</td>
</tr>
<tr>
<td>• Can help a surviving spouse to retain Centrelink benefits</td>
<td>• Market risk</td>
<td></td>
</tr>
</tbody>
</table>
Secure a regular, dependable income in retirement

An annuity is one of the simplest ways of securing regular income in your retirement.

When you buy an annuity you know exactly what income you’ll receive for the duration of the term or for life. This makes planning your finances much easier, since you don’t have to worry about market volatility affecting the income you receive from an annuity.

If you rely on the Age Pension to meet a part of your basic living expenses, you may be able to use an annuity to secure the remainder of your income needs with any remaining capital being invested for growth.

**CASE STUDY**

Jim and Sarah are 66 and 65, and are retiring soon. They each have $200,000 in superannuation to invest and $20,000 in a joint term deposit. They own a home which is mortgage free and have $10,000 in contents. They require income of around $32,000 per year to maintain a modest lifestyle.

In order to ensure security of income in retirement, their financial adviser has advised them to roll over $80,000 each from their superannuation accounts into a lifetime annuity with monthly payments indexed in line with inflation. This, along with their Age Pension entitlement, will deliver them a regular and dependable income regardless of movements in investment markets.

Their adviser also recommends that they each roll over the remaining $120,000 from their superannuation accounts into an account-based pension which will be almost entirely invested in growth assets.

Their cash flows in year one will be as follows:

<table>
<thead>
<tr>
<th></th>
<th>Jim</th>
<th>Sarah</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Age Pension</td>
<td>$11,460</td>
<td>$11,460</td>
<td>$22,920</td>
</tr>
<tr>
<td>Lifetime annuity</td>
<td>$4,032</td>
<td>$4,000</td>
<td>$8,032</td>
</tr>
<tr>
<td>Term deposit interest</td>
<td>$560</td>
<td>$560</td>
<td>$1,120</td>
</tr>
<tr>
<td>Total secure income</td>
<td>$16,052</td>
<td>$16,020</td>
<td>$32,072</td>
</tr>
<tr>
<td>Account-based pension</td>
<td>$6,000</td>
<td>$6,000</td>
<td>$12,000</td>
</tr>
<tr>
<td>(minimum drawdown)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total income</td>
<td>$22,052</td>
<td>$22,020</td>
<td>$44,072</td>
</tr>
</tbody>
</table>

Helps protect against
- Longevity risk
- Inflation risk
- Market risk

1. Jim and Sarah are 66 and 65, and are retiring soon. They each have $200,000 in superannuation to invest and $20,000 in a joint term deposit. They own a home which is mortgage free and have $10,000 in contents. They require income of around $32,000 per year to maintain a modest lifestyle.

In order to ensure security of income in retirement, their financial adviser has advised them to roll over $80,000 each from their superannuation accounts into a lifetime annuity with monthly payments indexed in line with inflation. This, along with their Age Pension entitlement, will deliver them a regular and dependable income regardless of movements in investment markets.

Their adviser also recommends that they each roll over the remaining $120,000 from their superannuation accounts into an account-based pension which will be almost entirely invested in growth assets.

Their cash flows in year one will be as follows:
BENEFITS

- The payments from the annuity, term deposit and Age Pension will total $32,072 in the first year, meeting Jim and Sarah’s annual expenditure requirements. Receipt of this income is not dependent on investment markets or the economy.

- The individual lifetime annuities will be paid for the remainder of Jim and Sarah’s lives and will be indexed to inflation.

- Income from superannuation annuities and account-based pensions is tax free if you are aged 60 or above. As Jim and Sarah have reached age 60, the income paid from their annuities and account-based pensions is all tax free.

- Jim and Sarah can meet any further expenditure requirements with payments from their account-based pensions.

- The annuity strategy has effectively removed the market, inflation and longevity risks from 38% of their portfolio (i.e. $160,000 invested in annuities, divided by the total portfolio value of $420,000) and ensured a minimum level of income well into their twilight years. Had Jim and Sarah followed an alternative strategy of rolling their entire superannuation balance into an account-based pension, they would have run the very real risk of their money running out before they die. Jim and Sarah can still benefit from any strong market returns via the investments in their account-based pensions.

- Lifetime annuities and account-based pensions receive favourable Centrelink Income Test treatment which may increase Age Pension entitlements and/or reduce aged care fees – see strategies 4 and 5.

OTHER CONSIDERATIONS

- A fixed term annuity may provide higher payment than a lifetime annuity; however, these payments will cease at the end of the term.

- A Challenger lifetime annuity has no commutation (withdrawal) value after 15 years. If you choose to commute in the first 15 years, you may get back an amount less than the amount you invested, even after taking into account the payments that have already been made to you.

- Age Pension entitlements are subject to the Centrelink Assets Test and Income Test. In high growth markets, the asset value of the account-based pension or the level of income you must draw may affect the amount of Age Pension you qualify for.

Notes

1. The table represents the payments received in the first year only. This may vary in future years. The examples used are for illustrative purposes only and should not be relied upon by individuals when making investment decisions.

2. Based on Centrelink Age Pension rates applicable from 20 September 2011 to 31 December 2011.


4. Assumes term deposit interest rate of 5.6%.

5. The minimum annual payment for an account-based pension is 5% of the account balance at commencement and each 1 July for a person aged 65-74, reduced to 3.75% for 2011/12. Payments are required to be made regardless of investments or the amounts of income generated.
Secure the defensive portion of my investment portfolio

A diversified investment portfolio reduces the risk of being overly exposed to one investment asset class, especially volatile assets such as international or Australian shares. Holding annuities as part of your investment portfolio can be used as a risk reduction strategy since they offer a fixed rate of return.

You can also benefit from the security provided by annuities when you invest in a fund such as the Challenger Guaranteed Income Fund.

The Guaranteed Income Fund is a wholesale managed fund that invests in annuities issued by Challenger Life. It is available to investors who invest via certain investment administration services (also known as platforms). These platforms allow you to acquire and hold a broad range of assets and provide consolidated reporting. They make it easy for you to combine an investment in the Guaranteed Income Fund with growth assets such as shares or property. Investors can generally access account-based pensions via a platform.

The Guaranteed Income Fund can provide the defensive portion of your investment portfolio, while the growth assets fluctuate with market movements. In the superannuation environment, it can provide a secure return when saving for retirement and secure your cash flow when drawing pension income.

The Guaranteed Income Fund has a number of advantages over traditional fixed income funds as detailed on page 7.

CASE STUDY

Barnaby is 60 and is retiring with $500,000 in superannuation within a platform.

Barnaby’s financial adviser recommends that he roll over his superannuation to an account-based pension within his current platform, with a long-term allocation of 55% growth assets, 30% defensive assets and 15% cash drawdown.

The growth assets are invested in a diversified mix of Australian and international shares and property funds.

Rather than use traditional fixed income funds for the defensive component of the investment portfolio, his adviser recommends that he invests $150,000 in the Guaranteed Income Fund which matures in five years time.

Barnaby’s investment portfolio would appear as follows:

- 55% Australian shares, international shares, property (growth)
- 30% Cash
- 15% Challenger Guaranteed Income Fund (defensive)
BENEFITS

• This strategy provides Barnaby with certainty over the earnings rate, timing and amount of income payments, and maturity value, for the defensive part of his portfolio.

• It also helps provide cash flow to help meet Barnaby’s minimum pension payments so he shouldn’t need to sell any growth assets involuntarily over this period.

• The Guaranteed Income Fund also offers peace of mind when it comes to the security of Barnaby’s investment. It invests primarily in annuities issued by Challenger Life Company (which is regulated by APRA).

• The Guaranteed Income Fund allows Barnaby to remove the market risk from 45% of his investment portfolio (cash and defensive assets) and secure regular, dependable cash flow to fund his income needs.

• Income from account-based pensions is tax free if you are aged 60 or above.

• Account-based pensions receive favourable Centrelink Income Test treatment which may increase your Age Pension entitlement and/or reduce aged care fees.

OTHER CONSIDERATIONS

• An investment administration platform generally charges an administration fee for all assets that are administered in the service including an investment in the Guaranteed Income Fund.

• The Guaranteed Income Fund can be purchased with either non-superannuation money or with superannuation money.

• You should continually monitor your asset allocation and make necessary adjustments as your investment in the Guaranteed Income Fund approaches the maturity date.

• If you withdraw before the maturity date of the Guaranteed Income Fund, you may receive back substantially less than if you remained invested until maturity.
Secure my self-managed superannuation fund pension payments

Many Australians choose to hold their retirement savings in self-managed superannuation funds (SMSFs) due to the flexibility and control that they can offer when accumulating superannuation benefits in retirement.

A diversified investment portfolio in your SMSF is important in minimising the exposure to any one asset class, and the potential impact of a fall in investment markets.

If your investment portfolio has fallen in value and you are many years away from retirement, you have time to allow it to recover before you retire. However, if you have reached, or are approaching, retirement you may need to sell assets that have fallen in value, to fund your income needs.

You can avoid this situation by including an annuity in your investment portfolio. The annuity can provide the cash flow needed to meet your regular income payments for the short to medium term, with the remaining assets invested in more growth-oriented assets over a longer timeframe.

CASE STUDY

Monique is aged 65 and retiring. She has accumulated $400,000 in her SMSF. She wants to draw a regular monthly income from her fund.

Monique’s financial adviser recommends she commence an account-based pension with a long-term allocation of 70% growth assets and 30% defensive assets. Monique is required to draw a minimum annual pension payment of 5% of the account balance in the first year which equals $20,000.1

To avoid selling the growth assets in the first five years, she allocates $100,000 of the account-based pension assets to a five year annuity with annual payments indexed in line with inflation and no residual capital value (RCV).

The payments will increase over the annuity term in line with inflation as set out in the following table:

<table>
<thead>
<tr>
<th>Year</th>
<th>Annuity income</th>
<th>Minimum account-based pension payment</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>$22,147</td>
<td>$20,000</td>
</tr>
<tr>
<td>2.</td>
<td>$22,811</td>
<td>$19,983</td>
</tr>
<tr>
<td>3.</td>
<td>$23,495</td>
<td>$20,210</td>
</tr>
<tr>
<td>4.</td>
<td>$24,200</td>
<td>$20,423</td>
</tr>
<tr>
<td>5.</td>
<td>$24,926</td>
<td>$20,611</td>
</tr>
</tbody>
</table>
**BENEFITS**

- The first year's annuity payment is $22,147\textsuperscript{1} p.a. which covers Monique's required minimum annual pension payment of $20,000 in year one.
- The annuity can be used to replace a portion of the fixed interest component with the fund's remaining assets invested in growth assets.
- Income from account-based pensions is tax free if you are aged 60 or over.
- Account-based pensions receive favourable Centrelink Income Test treatment which may increase your Age Pension entitlement and/or reduce aged care fees.
- If your SMSF uses an investment platform to invest, you can access the benefits of annuities by investing in the Guaranteed Income Fund – see strategy 2.

**OTHER CONSIDERATIONS**

- Monique may need to draw on growth assets if the minimum pension payment is higher than expected due to investment returns above the assumed rate.
- If you choose to commute (withdraw) the annuity prior to maturity, you may get back an amount less than the amount you invested, even after taking into account the payments that have already been made to you.
- You should continually monitor your asset allocation and make necessary adjustments in line with the SMSF’s investment strategy.
- You are able to select a shorter or longer term for the annuity depending on how long you would like to secure your income payments from your SMSF.

**Notes**

1. The minimum income payment for an account-based pension is 5% (3.75% in 2011/12) of the account balance at commencement and each 1 July for a person aged 65-74.
2. Challenger Guaranteed Annuity quote 26 September 2011. Five years, nil RCV, monthly payments indexed CPI (assumed 3% p.a.).
3. The account-based pension is assumed to earn (after fees) 6.9% on growth assets, 4.2% on defensive assets, and the commutation value of the annuity is used to calculate the account balance at the end of each financial year.
Maximise my Age Pension entitlements

Financial investments, including term deposits, shares and managed funds, are assessed by Centrelink under one simple set of rules known as deeming. The Centrelink Income Test ‘deems’ your financial investments to be earning a certain rate of income, no matter what they are actually earning.

Lifetime annuities and fixed term annuities with a term of six years or more receive more generous Income Test treatment in the form of a deductible amount. Centrelink considers this deductible amount the return of capital included in the annuity payment.

This deductible amount is calculated by dividing the amount you invest in the annuity by the term (or your life expectancy for lifetime annuities). Only the difference between the annuity payments and the deductible amount is included under the Centrelink Income Test.

**CASE STUDY**

Alison and Peter are 65 and 66 and are about to retire. They need $40,000 p.a. to meet their living expenses in retirement. They each have $50,000 in superannuation and $150,000 in a joint term deposit which has just matured. They own their home which is mortgage free and have $10,000 in contents.

Their financial adviser recommends that they use the proceeds of the term deposit to contribute $75,000 to each of their superannuation accounts as a non-concessional contribution. This brings their superannuation balances up to $125,000 each. Of these funds, $25,000 will be invested into a lifetime annuity with monthly payments indexed in line with inflation and $100,000 will be invested into an account-based pension for each of them. The results are shown in the following tables.

<table>
<thead>
<tr>
<th></th>
<th>Alison</th>
<th>Peter</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Age Pension if they retained their existing investments</td>
<td>$27,7191 p.a.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Age Pension post strategy</td>
<td>$29,3541 p.a.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Increase in Age Pension</td>
<td>$1,635 p.a.</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Cash flow (in year one)</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Lifetime annuity</td>
<td>$1,2502</td>
<td>$1,2502</td>
<td>$2,500</td>
</tr>
<tr>
<td>Account-based pension (5% income)</td>
<td>$5,0003</td>
<td>$5,0003</td>
<td>$10,000</td>
</tr>
<tr>
<td>Age Pension</td>
<td>$14,6771</td>
<td>$14,6771</td>
<td>$29,354</td>
</tr>
<tr>
<td>Total income</td>
<td>$20,927</td>
<td>$20,927</td>
<td>$41,854</td>
</tr>
</tbody>
</table>

Helps protect against

- Longevity risk
- Inflation risk
- Market risk

Strategy 4
BENEFITS

• The lifetime annuity and account-based pension receive a more favourable Income Test treatment than the term deposit and superannuation accounts. This enables Alison and Peter to qualify for more Age Pension.

• Alison and Peter are able to meet their income requirement.

• Income from account-based pensions and superannuation annuities is tax free if you are aged 60 or over.

• The individual lifetime annuities will be paid for the remainder of Alison and Peter’s lives and will be indexed to inflation.

• Alison and Peter are able to benefit from any good market returns through investments in their account-based pensions.

• A lifetime annuity is no longer assessable under the Centrelink Assets Test once you reach your life expectancy.

OTHER CONSIDERATIONS

• Age Pension entitlements are also subject to the Centrelink Assets Test. The Income and Assets Test are applied separately and the test that results in the lowest pension amount is used to determine your entitlement.

• If you are over age 65, you are only eligible to make superannuation contributions if you meet a work test. Personal after-tax superannuation contributions are subject to the non-concessional contributions cap after which tax penalties generally apply.

• Annuities with a term of five years or less are subject to deeming rates under the Centrelink Income Test (unless your life expectancy is less than six years and the term is equivalent to your life expectancy rounded up).

• Annuities with a residual capital value payable at the end of the term may not have a deductible amount, as the formula for calculating the deductible amount is: 

\[
\text{Purchase price} - \text{residual capital value} \over \text{Term of annuity}
\]

• A Challenger lifetime annuity has no commutation (withdrawal) value after 15 years. If you choose to commute in the first 15 years you may get back an amount less than the amount you invested, even after taking into account the payments that have already been made to you.

• You should continually monitor your asset allocation and make necessary adjustments.

Notes

1. Based on Centrelink Age Pension rates applicable from 20 September 2011 to 31 December 2011.
2. Challenger Guaranteed Annuity (Liquid Lifetime) quote 27 September 2011, monthly payments, CPI indexed.
3. The minimum payment for an account-based pension is 5% (3.75% for 2011/12) of the account balance at commencement and each 1 July for a person aged 65-74.
Reduce my aged care fees

The costs associated with aged care facilities such as nursing homes and hostels are very complex and can vary significantly depending on a person’s level of income and assets. Although there are many rules and regulations surrounding the costs, there may be the opportunity to reduce aged care fees and maximise Centrelink benefits with the use of an annuity.

The main fees payable by residents are accommodation payments, basic daily fees and an income tested fee.

It is the income tested fee that may be reduced by the use of an annuity.

The amount of income tested fee payable is based on your level of income and capped at an amount set by the Department of Health and Ageing. It is calculated using the following formula:

\[
\left( \text{Total fortnightly assessable income} - \text{total fortnightly assessable income free area} \right) \times \frac{5}{12}
\]

Where:

- Total assessable income includes income as assessed by Centrelink plus any Government income support payment (such as the Age or Service Pension) or income support supplement.
- Total assessable income free area is an amount provided by the Department of Health and Ageing and is determined by adding the basic age pension rate, the pension supplement and the income test free threshold together.

The same rules as for the Centrelink Income Test are used to determine the income tested fee. This means that the favourable Income Test treatment for annuities can help increase your Age Pension entitlement and reduce the income tested fee payable to an aged care facility.

**CASE STUDY**

Betty is 82, a non-homeowner and single and has recently entered a hostel facility. She paid an accommodation bond of $200,000 and is left with $250,000 in financial investments. She is currently receiving an Age Pension of $16,128 annually based on the Income Test. Her annual aged care fees are $16,390 (including the basic daily fee and the income tested fee).

Betty’s family decides to see a financial adviser who recommends allocating 30% of her portfolio to an annuity. She invests $75,000 into a six year annuity with monthly payments indexed in line with inflation and no residual capital value.

The income in the first year is $13,635. The deductible amount of the annuity is $12,500 ($75,000 divided by six years) which means that only $1,135 is assessed as income in the first year.

The results are shown on the following table.

<table>
<thead>
<tr>
<th>Benefit</th>
<th>Without the annuity</th>
<th>With the annuity</th>
<th>Benefit</th>
</tr>
</thead>
<tbody>
<tr>
<td>Age Pension</td>
<td>$16,128(^1)</td>
<td>$17,248(^1)</td>
<td>$1,120</td>
</tr>
<tr>
<td>Aged care fees</td>
<td>$16,390(^2)</td>
<td>$15,474(^2)</td>
<td>$916</td>
</tr>
</tbody>
</table>

Helps protect against
- Inflation risk
- Market risk
**BENEFITS**

- As a result of purchasing the annuity, Betty is able to increase her Age Pension and reduce her aged care fees in year one. This represents a saving of $2,036 in the first year alone.
- Annuities with a term of six years or more receive favourable Centrelink Income Test treatment compared to other financial investments, which may increase your Age Pension entitlement and/or reduce aged care fees – see strategy 4.

**OTHER CONSIDERATIONS**

- Annuities with a term of five years or less are subject to deeming rates under the Centrelink Income Test (unless your life expectancy is less than six years and the term is equivalent to the life expectancy rounded up).
- Annuities with a residual capital value payable at the end of the term may not have a deductible amount.
- If you choose to commute (withdraw) prior to maturity, you may get back an amount less than the amount you invested, even after taking into account the payments that have already been made to you.
- You should continually monitor your asset allocation and make necessary adjustments in line with your investment strategy.
- Age Pension entitlements are also subject to the Centrelink Assets Test. The Income Test and Assets Test are applied separately and the test that results in the lower pension amount is used to determine your entitlement.
- Whilst this strategy may not be applicable to you at this time, it may be relevant for a parent, close relative or family friend.
- It is important to take into account your health, or that of the person in the facility when considering an appropriate strategy.

**Notes**

1. Based on Centrelink Age Pension rates applicable from 20 September 2011 to 31 December 2011.
2. Based on the Department of Health and Ageing aged care fees applicable from 20 September 2011 to 31 December 2011.
3. Challenger Guaranteed Annuity quote 27 September 2011, six years nil RCV, monthly payments, CPI indexed (assumed 3%).
4. The table represents the payments received in the first year only. This may vary in future years. The examples used are for illustrative purposes only and should not be relied upon by individuals when making investment decisions.
Transfer my SMSF complying pension to an annuity and maintain my Centrelink benefits

Prior to 1 January 2006, self-managed superannuation funds (SMSFs) were allowed to commence complying pensions which could be fully or partially Assets Test exempt (ATE) for Centrelink purposes.

There are some circumstances in which these pensions can be transferred to a complying annuity where you can keep the ATE status and avoid incurring Centrelink penalties. These circumstances include the death of a member, where the administrative responsibilities of the SMSF have become too onerous due to the age or incapacity of a Trustee, or where the pension does not meet the actuarial requirements.

Transferring these to a complying annuity allows you to benefit from the certainty and simplicity of an annuity (as detailed in the table below), while retaining your ATE status.

<table>
<thead>
<tr>
<th>SMSF complying pension</th>
<th>Complying annuities</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Investment choice</strong></td>
<td><strong>Yes. You generally have the opportunity to invest in a range of assets including growth assets such as shares and property.</strong></td>
</tr>
<tr>
<td><strong>Who carries the investment risk?</strong></td>
<td><strong>You.</strong></td>
</tr>
<tr>
<td><strong>Management fees</strong></td>
<td><strong>Yes. A periodic management fee is generally deducted from your account. In addition you need to pay for an annual actuarial review of the pension.</strong></td>
</tr>
<tr>
<td><strong>Income</strong></td>
<td><strong>The income is determined upfront by a qualified actuary and can only vary in line with a predetermined indexation rate.</strong></td>
</tr>
<tr>
<td><strong>Access to capital</strong></td>
<td><strong>You cannot make withdrawals except in very limited circumstances.</strong></td>
</tr>
</tbody>
</table>

**Helps protect against**

- Inflation risk
- Market risk
CASE STUDY

John is 72 and has a SMSF complying pension which commenced in September 2004 and is 100% exempt from the Assets Test. The pension was set up with $300,000 for a 15 year term. The monthly payments are currently $2,158 indexed to CPI +1%.

John is married and has $400,000 in financial assets. He owns his home which is mortgage free and has $30,000 in cars and contents. John and his wife currently receive $21,3951 p.a. in Age Pension.

Due to poor performance of the assets backing the complying pension, the actuary’s certificate states that the complying pension assets are not sufficient to ensure a high probability that the assets will meet the pension liabilities. If the pension continues to be paid after 12 weeks from the certificate being issued, John’s pension will become Asset Tested based on the purchase price less any capital received to date2, i.e. $300,000 – [(300,000–0) ÷ 15) x 7)] = $160,000. This will result in a reduction to the Age Pension from $21,3951 p.a. to $16,6791 p.a. In addition to this, Centrelink will treat the complying pension as if it never had Assets Test exempt status and may raise a debt for the last five years against John.

In order to keep the Assets Test exemption and avoid the clawback debt provisions, John rolls over the balance from his complying pension, $181,521, into a 14 year annuity with monthly payments indexed in line with inflation and no residual capital value (RCV).

BENEFITS

• The income in the first year is $15,7743. The deductible amount of the annuity is $12,966 ($181,521 ÷ 14), which means that only $2,808 is assessed as income in the first year. As a result their Age Pension will increase from $21,3951 to $22,9191.

• Income from annuities is tax free if you are aged 60 or over, so John continues to pay no tax on his annuity income.

• Both SMSF complying pensions and complying annuities receive favourable Centrelink Income Test treatment which may increase your Age Pension entitlement and/or reduce aged care fees – see strategies 4 and 5.

OTHER CONSIDERATIONS

• You should continually monitor your asset allocation and make necessary adjustments.

• You should consider whether retaining the SMSF is still appropriate after the transfer of the complying pension.

• In order to be complying, you must purchase a lifetime annuity or a fixed term annuity with a term ranging between your life expectancy rounded up and the number of years until you turn 100.

Notes
1. Based on Centrelink Age Pension rates applicable from 20 September 2011 to 31 December 2011.
2. The formula used by Centrelink to determine the asset value of an annuity is: Purchase price – (purchase price ÷ term) x term elapsed
3. Challenger Guaranteed Complying Annuity quote 28 September 2011, 14 years, nil RCV, monthly payments, CPI indexed (assumed 3%).
Establish a short-term, tax-efficient investment as a non-resident

If you are a non-resident looking for a secure short-term investment, short-term annuities may be a suitable investment for you. Annuities offer a guaranteed income at competitive rates with no tax payable in Australia in many cases.

Non-residents are generally taxed in Australia on all Australian-sourced income. This includes Australian-sourced pensions or annuities unless an exemption is available under a double tax agreement (DTA) with the country of residence.

Australia has a DTA with more than 40 countries and this generally means that individuals who are residents of these countries will not pay Australian tax on any annuity income they receive.

These DTAs provide an opportunity for non-residents to receive guaranteed, tax-free income in Australia, though they may need to declare the income in their own country of residence.

In contrast, investing the funds in an Australian term deposit or cash management trust will generally result in non-resident withholding tax of 10% on the interest income.

COUNTRIES THAT HAVE A DTA WITH AUSTRALIA

We have listed a few of the countries that have a DTA with Australia where annuity income would not be taxed in Australia under the current agreement. The full list of countries that have a DTA with Australia is listed on the Australian Taxation Office website www.ato.gov.au.

<table>
<thead>
<tr>
<th>Country</th>
<th>Country</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fiji</td>
<td>Singapore</td>
</tr>
<tr>
<td>France</td>
<td>South Africa</td>
</tr>
<tr>
<td>India</td>
<td>Spain</td>
</tr>
<tr>
<td>Italy</td>
<td>Taipei</td>
</tr>
<tr>
<td>Japan</td>
<td>Thailand</td>
</tr>
<tr>
<td>Malaysia</td>
<td>United Kingdom</td>
</tr>
<tr>
<td>New Zealand</td>
<td>United States</td>
</tr>
<tr>
<td>Philippines</td>
<td>Vietnam</td>
</tr>
</tbody>
</table>
CASE STUDY

The below comparison highlights the different options available to non-residents with a DTA should they choose to invest in an annuity or term deposit.

The table displays the payments after 10% withholding tax and assumes $100,000 is invested for two years. Both the annuity and term deposit are paying 5.35% (interest paid annually).

<table>
<thead>
<tr>
<th></th>
<th>Annuity</th>
<th>Term deposit</th>
</tr>
</thead>
<tbody>
<tr>
<td>Gross payment</td>
<td>$10,700</td>
<td>$10,700</td>
</tr>
<tr>
<td>Withholding tax</td>
<td>$0</td>
<td>$1,070</td>
</tr>
<tr>
<td>Net payment</td>
<td>$10,700</td>
<td>$9,630</td>
</tr>
</tbody>
</table>

BENEFITS

- Non-residents may find annuity rates more competitive than in their own country of residence.
- Can be suitable for non-residents who require an income stream.
- Annuities can be indexed in accordance to inflation, which is not available in most term deposits.

OTHER CONSIDERATIONS

- If Australia does not have a DTA with the country of which you are a resident, or the DTA does not contain the relevant exemption, the annuity income may be taxable in Australia at non-resident tax rates.
- Challenger can only accept applications from a current Challenger product disclosure statement (PDS) that have been completed and signed in Australia.
- The annuity income must be paid into an accessible account with an Australian bank or other financial institution.
- If you choose to commute (withdraw) prior to maturity, you may get back an amount less than the amount you invested, even after taking into account the payments that have already been made to you.
- If you are considering this strategy, please seek independent taxation advice.
An investment solution that offers estate planning certainty

Estate planning can help you ensure that your wealth is transferred to your beneficiaries upon your death in line with your preferences. It can also help you ensure that the transfer happens efficiently and in a tax-effective manner.

Assets including cash, real estate, shares and managed funds generally form part of your estate and are usually dealt with under the terms of your will. Other assets such as jointly held assets, superannuation and annuities do not form part of your estate and are therefore generally dealt with separately.

If you invest non-superannuation money in an annuity and nominate a beneficiary to receive any of the proceeds upon your death, the annuity must be paid directly to that beneficiary rather than your estate.

For couples receiving the Age Pension it can help transfer wealth to other beneficiaries, such as children, without impacting the Age Pension entitlement of the surviving spouse.

CASE STUDY

Carl and Amanda are 75 and 70 and have a joint term deposit of $300,000. Carl also has $100,000 in a fixed income managed fund. They own their home which is mortgage free and have $10,000 in contents.

They have one adult child and two grandchildren.

They currently receive the Age Pension of $23,6991 p.a. and as Carl is currently in poor health he is concerned about ensuring that his family is provided for in the event of his death.

His current will leaves his entire estate to Amanda with the plan for Amanda to then distribute some of the wealth to their child and grandchildren.

If Carl was to die, the term deposit would automatically pass to Amanda as it is a joint asset and the managed fund would form part of his estate.

If all the assets ended up in Amanda’s name, her Age Pension would reduce to $10,7621 p.a. Any attempt to pass assets to their child or grandchildren will be caught by the Centrelink gifting rules which apply to any gifts that exceed $10,000 in a financial year or $30,000 over a five year rolling period. Gifts in excess of these limits are counted as an asset and subject to deeming rates for five years from the date of gifting.

Carl instead invests the proceeds of the managed fund in an annuity and nominates his child as the beneficiary. The following table shows the scenario if Carl passes away.
### Current will and assets vs Investing into an annuity

<table>
<thead>
<tr>
<th>Current will and assets</th>
<th>Investing into an annuity with the child as beneficiary instead of the fixed income managed fund</th>
</tr>
</thead>
<tbody>
<tr>
<td>Term deposit</td>
<td>$300,000 term deposit would pass to Amanda</td>
</tr>
<tr>
<td>Managed fund (fixed income)</td>
<td>$100,000 fund would become part of the estate that will be paid to Amanda</td>
</tr>
<tr>
<td>Annuity</td>
<td>N/A</td>
</tr>
<tr>
<td>Amanda's assets</td>
<td>$300,000 term deposit&lt;br&gt;$100,000 managed fund (Fixed Income)&lt;br&gt;$10,000 home contents (Home)</td>
</tr>
<tr>
<td>Gifting rules for passing asset to the child</td>
<td>Gift – if estate assets are passed from Amanda to the child</td>
</tr>
<tr>
<td>Age Pension payments</td>
<td>$10,762¹ p.a.</td>
</tr>
</tbody>
</table>

### BENEFITS

- Any death benefits from the annuity would be paid directly to Carl and Amanda’s child rather than via Carl’s estate, and any payment will not affect Amanda’s Age Pension.

- Amanda would be entitled to an Age Pension of $14,662¹ as opposed to $10,762.

### OTHER CONSIDERATIONS

- Estate planning law is very complex and therefore you need to seek professional advice with regard to your specific circumstances.

- Challenger superannuation annuities allow for a beneficiary nomination that is not binding on the trustee of the fund. The trustee may pay any death benefits to a dependant as defined by superannuation law or your estate.

- Challenger lifetime annuities may be established with a reversionary beneficiary who will receive income payments if they survive the primary annuitant. Otherwise any death benefit will be paid to the estate.

- On death, a beneficiary may be given the option to continue to receive the income payments from an annuity, otherwise they will receive a lump sum commutation value.

- If you choose to commute (withdraw) prior to maturity, you may get back an amount less than the amount you invested, even after taking into account the payments that have already been made to you.

### Notes

1. Based on Centrelink Age Pension rates available from 20 September 2011 to 31 December 2011. We assume they have assets of $410,000 when Carl dies.
Glossary

ACCOUNT-BASED PENSION
An account in which you can invest your lump sum superannuation benefit and draw a regular income. With an account-based pension, you can generally choose from a range of investments and select the income you draw subject to minimum payment requirements. For the 2011/12 financial year, the reduced minimum of 3.75% applies for the minimum percentage factor. In the 2011 Federal Budget, the Government legislated this 25% reduction in the minimum annual payment for the 2011/12 financial year. It has also been proposed that the reduced minimum will be in effect for the 2012/13 financial year.

ANNUITY
A life insurance policy in which you can invest a lump sum in return for a predetermined regular income. An annuity can be purchased with either superannuation or non-superannuation money.

ASSETS TEST
A test applied by Centrelink to determine your entitlement to Centrelink benefits. The value of your assets is tested against a threshold which depends on your marital status and whether you own your home. Your entitlement is also subject to an Income Test.

ASSETS TEST EXEMPTION (ATE)
This is a concession that applies to certain assets including complying income streams purchased before a certain date. It means that the value of this asset is not included in the assessable assets when determining entitlements to Centrelink benefits under the Assets Test.

COMMUTATION
The process of converting some or all of your future annuity income payments into a lump sum.

COMPLYING ANNUITY
An annuity that meets specific conditions and may entitle investors to certain tax or Centrelink concessions.

COMPLYING PENSION
A long-term pension or annuity that met specific conditions under previous legislation that enabled it to be eligible for an Assets Test exemption or other tax concessions.

CONSUMER PRICE INDEX (CPI)
A measure of inflation that is determined by measuring the change in the cost of a fixed basket of products and services.

DEDUCTIBLE AMOUNT (CENTRELINK)
The portion of the payments received from a pension or annuity that is not assessed as income for Centrelink purposes each year.

DEFENSIVE ASSETS
Investments such as fixed interest and cash. Defensive assets are expected to deliver lower returns than growth assets over the long term; however, with a more stable capital value.

EARNINGS RATES
The earnings rate (or rate) refers to the interest paid by a fixed term annuity. For example, an investor taking out a $100,000 three year annuity with a 100% residual capital value, offering an earnings rate of 6.46% p.a. and annual income payments, would receive interest of $6,460 each year. The earnings rate provided at the time of the investment applies for the term of the annuity.

FIXED TERM ANNUITIES
Fixed term annuities have a fixed start date and end date as chosen by the investor. The term can be as short as one year or as long as 50 years. Income payments are made for the duration of the term.

GROWTH ASSETS
Assets such as shares and property that have the potential to increase in value in line with movements in investment markets.

INCOME PAYMENTS
Income payments can generally be made monthly, quarterly, half-yearly or annually from an annuity. The amount of income paid can be fixed at the outset, indexed by a set percentage or indexed to inflation. For a lifetime annuity, payments can be fixed or indexed to inflation. Indexing against the impact of inflation may be particularly relevant for long-term annuities as it provides protection against increases in the cost of living.
INCOME TEST
A test applied by Centrelink to determine your entitlement to Centrelink benefits. Your assessable income is tested against an income test threshold to determine your entitlement. The relevant threshold depends on factors such as your marital status. Your entitlement is also subject to an Assets Test.

INFLATION
The rise in the general level of prices of goods and services over a period of time. This can be measured by the Consumer Price Index.

INFLATION RISK
The risk that over time inflation will increase the cost of living. This means the income received from your investments must also increase in line with inflation to maintain your spending power and standard of living. In constructing retirement portfolios, managing inflation risk by including assets that do provide inflation protection is important.

LIFE EXPECTANCY
The expected number of years of life remaining at a given age based on statistics. Life expectancies used in calculating deductible amounts are determined using the relevant Australian Life Table at the investment date.

LIFE INSURANCE COMPANY
A company that is registered under the Life Insurance Act and is regulated by the Australian Prudential Regulation Authority (APRA).

LIFETIME ANNUITIES
An annuity where the income payments will continue to be paid for the remainder of your life and if selected, another person’s life.

LONGEVITY RISK
The risk of living longer than expected, resulting in retirement funds being insufficient to finance an individual’s income needs for their whole life.

MARKET RISK
The impact of volatility of investment returns on the value of your investment.

NON-CONCESSIONAL CONTRIBUTION
A contribution to a superannuation account made with after-tax income for which no tax deduction is claimed.

PLATFORM
An administration system for your investments. Platforms offer a broad range of investments, enabling you to consolidate your portfolio in the one location.

TERM
The length of an annuity policy. Fixed term annuities are generally available for fixed terms of between one and 50 years. The investor selects the term most appropriate to them. The term of a lifetime annuity is the rest of the investor’s life – income payments continue until they die.

RESIDUAL CAPITAL VALUE (RCV)
Any capital left at the end of an annuity term is known as the ‘residual capital value’. The residual capital value, or RCV, is set by the investor at the start of the annuity. It can be 100% of the capital invested, 0% of the capital invested, or generally somewhere in between. If an RCV of 50% is set, then 50% of the initial capital is paid out through income payments and 50% is repaid to the investor at the end of the term.

SUPERANNUATION ANNUITY
An annuity that is purchased with superannuation money.

WITHDRAWAL GUARANTEE
For lifetime annuities, there is a commutation (withdrawal) option within the first 15 years. You can choose to commute your lifetime annuity at any time in this period provided the no commutation option is not chosen.
Frequently asked questions

ARE ANNUITIES A SAFE INVESTMENT?

In Australia, annuities can only be issued by life insurance companies. The way in which life insurance companies are managed is regulated by the Life Insurance Act and overseen by the Australian Prudential Regulation Authority (APRA).

APRA specifies certain prudential standards, including capital adequacy standards that apply to life insurance companies. Broadly speaking, these capital adequacy requirements are designed to ensure the solvency and financial soundness of the life insurance company and to provide a high level of certainty that life insurance companies can meet their obligations to investors and creditors on an ongoing basis.

CAN I TAKE MY MONEY OUT OF AN ANNUITY BEFORE THE END OF THE TERM?

For both the Challenger Guaranteed Annuity and Guaranteed Income Plan, you generally can. It’s known as a ‘commutation’. If you commute your annuity before the end of the term you may receive back significantly less than the amount you originally invested, even after taking into account any payments you’ve already received.

Challenger Liquid Lifetime annuities allow you to commute (withdraw) your investment within the first 15 years of the investment provided you have not chosen to remove this option. The withdrawal value at the end of 15 years is set out in the following table:

<table>
<thead>
<tr>
<th>Age at commencement</th>
<th>Withdrawal guarantee* (as a percentage of amount invested)</th>
<th>Single lifetime</th>
<th>Joint lifetime</th>
<th>Single lifetime with a reversionary annuitant</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>Male</td>
<td>Female</td>
<td>Male</td>
</tr>
<tr>
<td>Less than 66</td>
<td></td>
<td>85%</td>
<td>100%</td>
<td>100%</td>
</tr>
<tr>
<td>66-70</td>
<td></td>
<td>70%</td>
<td>90%</td>
<td>100%</td>
</tr>
<tr>
<td>71-75</td>
<td></td>
<td>40%</td>
<td>50%</td>
<td>80%</td>
</tr>
<tr>
<td>76-80</td>
<td></td>
<td>20%</td>
<td>30%</td>
<td>50%</td>
</tr>
<tr>
<td>81 and above</td>
<td></td>
<td>10%</td>
<td>15%</td>
<td>20%</td>
</tr>
</tbody>
</table>

* At the end of the Withdrawal Benefit Period. For a joint lifetime or single lifetime with a reversionary annuitant, the percentage is based on the older life.

WHAT HAPPENS TO MY ANNUITY INVESTMENT IF I DIE BEFORE THE TERM IS UP?

For a fixed term annuity, the investor’s estate or beneficiary generally have the option of either continuing to receive payments until the end of the term or commuting (terminating) the annuity and having it paid as a lump sum. The commutation value may be significantly less than the original amount invested, even after taking into account any payments already received. However, the commutation calculation upon death is generally more generous than a voluntary commutation.

With Challenger’s Liquid Lifetime annuity, a commutation (withdrawal) value is only available within the first 15 years of the annuity term.

HOW ARE ANNUITIES ASSESSED FOR TAX?

If you are over 60 and buy an annuity with superannuation money then all regular payments are tax free. If the annuity is purchased outside superannuation (i.e. with non-superannuation money) then the income component of regular payments is considered to be assessable income and may be subject to tax.

HOW DO ANNUITIES AFFECT CENTRELINK BENEFITS?

Annuities are assessed under both the Income Test and Assets Test for Centrelink purposes.

The purchase price (investment amount) of an annuity is assessed under the Assets Test. If you choose to receive all of the capital at the end of the selected term, the assessed asset value does not change. If you choose to have some of the capital returned as part of the regular payments, the asset value is recalculated every six or 12 months and reduced by the amount of capital returned up to that time.

The amount of income assessed depends on factors including the term of the annuity, your life expectancy and the residual capital value. A financial adviser can provide you with more detailed information on how your investment choices can affect your Centrelink entitlements.
HOW DO I BUY AN ANNUITY?
We recommend you seek financial advice from a qualified financial adviser to determine whether an annuity is right for your circumstances. A financial adviser can help you understand how an annuity could fit within your investment portfolio and how to select the appropriate investment amount, term and residual capital value.

If you do not have a financial adviser, call Challenger on 13 35 66 to be referred to a financial adviser in your area or to obtain more information about the features of Challenger’s annuities. While we are happy to refer you to a financial adviser, we provide no endorsement or recommendation of any financial adviser. A copy of the product disclosure statement for any of our annuities is also available on our website www.challenger.com.au and should be considered before making any investment decision.

HOW DO I INVEST IN THE GUARANTEED INCOME FUND?
The Guaranteed Income Fund is only available through investment platforms. We recommend you seek financial advice from a qualified adviser to determine whether it is right for your circumstances. In order to invest in the fund you must apply anytime during the application open period. You cannot invest 12 months before the maturity date.

If you do not have a financial adviser, call Challenger on 13 35 66 to be referred to one in your area or to obtain more information on the fund’s features. While we are happy to refer you to a financial adviser, we provide no endorsement or recommendation of any financial adviser. The product disclosure statement is available on our website www.challenger.com.au and should be considered before making any investment decision.
About Challenger

Established in 1985, Challenger Limited is a large Australian financial institution listed on the Australian Securities Exchange. Our business is dedicated to providing safe, reliable and high-performing fixed income products to a wide range of institutional, superannuation and retail clients.

Challenger’s annuity and annuity-like offerings are protected by the capital and income guarantee of our prudentially-regulated life company, yet also offer attractive rates of return that usually exceed those offered by bank term deposits and investment-grade bond funds.

Challenger’s annuities are commonly used by institutions, retail customers and financial advisers to:

- Provide stable, regular retirement income that is payable yearly, half-yearly, quarterly or monthly.
- Invest cash securely for the medium to long term (up to 50 years).
- Diversify from other secure investments such as bank term deposits.

ABOUT CHALLENGER LIFE

Challenger’s life company (Challenger Life) is Australia’s leading annuity provider. It is contractually obliged to make the annuity payments and any residual capital value provided under these annuities contracts. Challenger Life is a life company registered under the Life Insurance Act 1995 (Cth) (‘Act’) and regulated by APRA.

Challenger Life invests the funds it raises in a range of instruments across four main asset classes. As at 30 September 2011, Challenger Life’s assets under management were invested as follows:

Challenger Life asset allocation split

18%
18%
73%
6%
3%

- Property
- Debt investments, cash and receivables
- Infrastructure assets
- Equity and other assets

REGULATORY ENVIRONMENT

APRA receives regular reporting on the capital position of the company and conducts regular reviews of the company’s policies, processes and procedures.

Under the Act, annuities are required to be held within statutory funds. Statutory funds, while not being trusts, have a number of ‘trust-like’ aspects. Assets of the statutory fund are used to ensure policy holders receive their promised payments.

In addition, the Act requires that, in the investment, administration and management of the assets of a statutory fund, a life company must give priority to the interests of owners and prospective owners of policies referable to that statutory fund.

CAPITAL POSITION

The Act, together with APRA prudential standards, determines the minimum amount of statutory capital Challenger Life is required to hold. This capital is required to be continuously maintained even as market conditions change. The capital adequacy standard is designed to ensure that there are always sufficient assets to meet policy holder obligations. As part of calculating the amount of capital to be held, Challenger Life looks at both the current value of its assets and liabilities as well as the value under certain adverse ‘shock’ scenarios. In addition, the standards set out certain maximum exposure limits that apply to investments funded using policy holder monies.

Challenger Life Board-approved policies determine the amount of ‘target surplus’ Challenger Life holds above the required statutory capital amount. In effect this acts as a buffer to ensure that Challenger Life does not breach its regulatory requirements. As at 30 June 2011, Challenger Life had more than $675 million of excess capital above its regulatory minimum.

LIQUIDITY MANAGEMENT

Challenger Life has in place a Board-approved Liquidity Management Policy that aims to ensure Challenger Life has sufficient cash resources to meet its liquidity requirements as a going concern as well as under adverse market conditions. In particular, Challenger Life projects the cash flows arising from its assets, allowing for adverse movements, and compares them with the cash flows due under its liabilities, again allowing for adverse movements.

Challenger Life then ensures that it maintains a buffer between the adverse asset cash flows and adverse liability cash flows. Challenger Life’s liquidity position is continuously monitored by the company and is subject to APRA supervision.
## Challenger – Product solutions

<table>
<thead>
<tr>
<th>Product type</th>
<th>Product</th>
<th>Issued by</th>
<th>Features</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fixed term annuities</td>
<td>Guaranteed Annuity</td>
<td>Challenger Life Company Limited</td>
<td>Standard fixed term annuity</td>
</tr>
<tr>
<td></td>
<td>Guaranteed Income Plan</td>
<td>Challenger Life Company Limited</td>
<td>Fixed term annuity with inbuilt adviser remuneration</td>
</tr>
<tr>
<td></td>
<td>Guaranteed Annuity – Complying</td>
<td>Challenger Life Company Limited</td>
<td>Assets test exempt</td>
</tr>
<tr>
<td></td>
<td>Guaranteed Income Plan – Complying Annuity</td>
<td>Challenger Life Company Limited</td>
<td>Assets test exempt with inbuilt adviser remuneration</td>
</tr>
<tr>
<td>Lifetime annuities</td>
<td>Guaranteed Annuity – Liquid Lifetime</td>
<td>Challenger Life Company Limited</td>
<td>Standard lifetime annuity</td>
</tr>
<tr>
<td></td>
<td>Guaranteed Income Plan – Liquid Lifetime</td>
<td>Challenger Life Company Limited</td>
<td>Lifetime annuity with inbuilt adviser remuneration</td>
</tr>
<tr>
<td>Fixed rate managed investment</td>
<td>Guaranteed Income Fund</td>
<td>Challenger Retirement and Investment Services Limited</td>
<td>Managed fund investing in annuities</td>
</tr>
<tr>
<td></td>
<td>Guaranteed Pension Fund</td>
<td>Challenger Retirement and Investment Services Limited</td>
<td>Managed fund investing in annuities, nil RCV</td>
</tr>
<tr>
<td>Superannuation</td>
<td>Guaranteed Personal Superannuation</td>
<td>Challenger Retirement and Investment Services Limited</td>
<td>Super fund</td>
</tr>
<tr>
<td>Pension</td>
<td>Guaranteed Allocated Pension</td>
<td>Challenger Retirement and Investment Services Limited</td>
<td>Allocated pension</td>
</tr>
</tbody>
</table>

For more information or to request a product disclosure statement, speak to your financial adviser, visit www.challenger.com.au or call 13 35 66. You should consider the product disclosure statement for the relevant product before deciding to acquire the product.

### A gold medal winner

Challenger is the largest annuity provider in Australia, managing over $8 billion of assets to secure the benefits of around 60,000 annuity investors as at 30 September 2011. For years we have provided retirement incomes to people who want certainty of returns and a guaranteed retirement income.

In 2011, Challenger was again named winner of the AFA/Plan for Life ‘Annuity Provider of the Year’, further reinforcing our strength in the annuity market.
Key contacts

AUSTRALIAN TAXATION OFFICE (ATO)
The ATO is a statutory agency responsible for the administration of Australia’s taxation system.
www.ato.gov.au

AUSTRALIAN PRUDENTIAL REGULATION AUTHORITY (APRA)
APRA is the prudential regulator of banks, insurance companies and superannuation funds, credit unions, building societies and friendly societies.
www.apra.gov.au

AUSTRALIAN SECURITIES AND INVESTMENTS COMMISSION (ASIC)
ASIC is responsible for enforcing company and financial services laws to protect consumers, investors and creditors.
www.asic.gov.au

CENTRELINK
The Federal Government agency which delivers a range of payments and services for retirees, the unemployed, families, carers, parents, people with disabilities, Indigenous Australians, and people from diverse cultural and linguistic backgrounds, and provides services at times of major change.
www.centrelink.gov.au

FINANCIAL PLANNING ASSOCIATION (FPA)
The FPA is one of the peak bodies for Australia’s financial planners.
www.fpa.asn.au

NATIONAL SENIORS AUSTRALIA
National Seniors Australia is a non-profit organisation that gives voice to issues that affect older Australians. It also assists the over 50s community by providing economic and social benefits and making donations to charitable institutions.
www.nationalseniors.com.au