

WHAT IS

A defined benefit pension?

JULY 2026

If you're a member of a defined benefit superannuation fund, you may be able to commence a pension or elect to access an immediate lump sum in lieu of a pension. Carefully compare your options before proceeding.

How does it work?

A defined benefit superannuation fund is an older style of superannuation fund that was common in public sector and local government workplaces until the 1990's.

Some defined benefit schemes provide its member retirement benefits in the form of a pension payable throughout their lifetime and/or the lifetime of a reversionary beneficiary. You can generally commence a pension when you retire or meet one of the conditions of release of the scheme.

Typically pension payments from a defined benefit pension are indexed each year to keep up with inflation; however, where that does not apply, the real value of the pension payments will reduce over time.

How much you'll receive as a pension payment is typically based on a formula that considers factors like your time with your employer, your salary and your age. For example, an employer might offer a plan that pays 1.5% of your average salary for the previous five years, multiplied by the number of years you were employed. So, if you worked for that employer for 20 years, then you might receive pension payments equivalent to 30% of your average salary over the five years preceding your retirement.

It's important to note that there is no single method used by defined benefit funds to calculate a pension. You'll need to contact your scheme operator to request an estimate of your potential pension entitlement.

If you are eligible for a defined benefit, be sure to check how your benefit is calculated.

What is a reversionary beneficiary?

A reversionary beneficiary is a spouse nominated to automatically continue receiving pension payments when you pass away. Some schemes will continue to pay your reversionary 100% of the amount that was payable whilst you were alive, but others may pay a lower amount than this.

For example, the pension payments received by a reversionary may only be a percentage of your pension, e.g., your reversionary might only receive two-thirds (or even less) of the full pension.

You'll need to enquire directly with your defined benefit superannuation fund to confirm if this feature is available, and how much, if anything, the pension payments will be reduced by.

Lump sum option

Most defined benefit schemes provide members the option to access an immediate lump sum, in lieu of a defined benefit pension, when they retire. This can be in the form of cash, or a rollover benefit to another complying superannuation fund.

If you elect to take part or all of your entitlement as a lump sum, you'll be foregoing some or all of your entitlement to receive a lifetime pension. Some schemes impose a time restriction for members to make an election should they wish to take a lump sum payment, for example, this could be three months from final date of service, although the timeframe can vary from fund to fund. If you do not nominate a lump sum within this period, you will be required to take the full pension option. Please make sure you are familiar with your scheme's deadline (if any).

When deciding whether to commence a pension or convert it into a lump sum, use caution as the total pension payments received over a lifetime could potentially outweigh the lump sum amount paid upfront.

As the decision you make regarding your pension is permanent, please refer to the product disclosure statement of your defined benefit or speak to a financial adviser before proceeding.

Social security treatment

When calculating the payment rate of the Centrelink Age Pension or Department of Veterans' Affairs Service Pension, there is an income and assets test. Whichever test produces the lowest rate determines your payment.

For the assets test, a defined benefit pension is not assessed.

For the income test, the assessable income from a defined benefit pension is equal to the gross annual payment less a deductible amount.

The deductible amount of a defined benefit pension is equal to the tax-free component, capped at 10% of the gross annual payment. This means if the pension has a tax-free component greater than 10% of the gross income, the deductible amount is capped at 10%.

The following defined benefit funds are exempt from this cap:

- Defence Force Retirement & Death Benefits Scheme (DFRDB)
- Military Superannuation & Benefits Scheme (MilitarySuper), and
- Defence Force Retirement Benefits Scheme (DFRB).

If you choose to convert your pension into a lump sum, the amount you receive is assessed for social security depending on how it is invested, e.g., savings in the bank are assessed under the assets test and deemed for the income test.

Taxation

How your retirement benefit is taxed depends on the super components of your retirement benefit, your age and whether it is paid as a pension or lump sum. From 1 July 2007, superannuation components for taxation purposes were replaced with two categories: "tax free" and "taxable".

The tax free component represents:

- the pre July 1983 proportion (if any) of your actuarially determined benefit as at 30/06/2007, plus
- the total of your post tax contributions paid to the fund.

The taxable component attracts various tax rates according to your age at date of payment, and the amount paid.

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When you commence a defined benefit pension, your transfer balance cap will be credited with an amount equal to your first payment (as an annualised amount) multiplied by a special factor of 16.

Currently, the general transfer balance cap is $2.1 million (for 2026/27). Where the defined benefit pension exceeds the transfer balance cap, the taxation of the pension payments will change. Pension payment (income) above what is known as the "capped defined benefit income cap" is subject to different taxation rates compared to amounts within the cap. In 2026/27, the general capped defined benefit income cap is $131,250.

The following tax treatment applies to a pension:

Taxable component (taxed element)

Age of recipient	Pension amount below $131,250*	Pension amount above $131,250
60 years or more	Not assessable, not exempt income	50% of amount above cap added to assessable income and taxed at marginal tax rate
Under preservation age	Taxed at marginal tax rates, with no tax offset – Tax offset of 15% is available if a disability super benefit	Taxed at marginal tax rate

Taxable component (untaxed element)

Age of recipient	Pension amount below $131,250*	Pension amount above $131,250
Age 60 years or more	Taxed at marginal rates, with a 10% tax offset	Taxed at marginal rates
Under preservation age	Taxed at marginal rates, with no tax offset	Taxed at marginal tax rates

*A general cap applies in 2026/27. Please note that the defined benefit income cap may be reduced in certain circumstances.

Medicare levy applies in addition to the rates shown. If your pension contains a tax-free component, that portion is not taxed. The Pension scheme operator is required to withhold tax from your benefit in accordance with requirements specified in Tax Acts and regulations administered by the Australian Taxation office.

For information on the lump sum treatment of super, please refer to '**What are the superannuation withdrawal rules?**' fact sheet.

Things you should know before commencing a defined benefit pension

- To commence a pension, you generally must have retired.
- When you commence a defined benefit pension, you may pay additional tax based on your transfer balance cap and the capped defined benefit income cap.
- Your defined benefit pension will not form part of your estate as the pension will cease in the event you and/or your reversionary beneficiary pass away.

For more information, refer to '**What are the limits on super contributions?**' fact sheet. You can also visit the ATO website at www.ato.gov.au and search 'Contributions to a defined benefit fund'.

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Defined benefit pension advantages

- Retirement benefits are guaranteed, offering the security of a regular pension in retirement without the employee having to make regular contributions.
- Payments are not affected by market fluctuations – no matter how the underlying investments perform, your pension payment is not affected.
- Potential for spousal support – you may nominate a spouse as a reversionary beneficiary to continue receiving guaranteed payments after you pass away.

Defined benefit pension disadvantages

- No investment choice – you have no say in how your retirement benefits are invested e.g., socially responsible companies.
- It takes time to accrue – if a company requires an employee stay for five years to be eligible for a defined benefit pension and the employee leaves after two, any accrued earnings stay with the defined benefit fund and may not be transferred.
- Non-commutable – once you commenced your defined benefit pension you will not be able to make lump sum withdrawals from the pension under any circumstances.
- Lack of portability – Once you commence your defined benefit pension, you will not be able to transfer your pension to a different pension provider.
- Less chance to increase your benefit – some defined benefit funds use a set formula to calculate your pension. This means you will not be able to participate in future investment growth or interest rate rises.
- Pension will cease upon the death of both you and your reversionary beneficiary and nothing will be left to your estate.

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