
# 4 out of 5 people are still confused about superannuation

## So lets try to clear up some of the  confusion.

### Background to superannuation.

In 1989 when I started working in the financial services industry universal Superannuation did not exist, it was not even talked about. People retired on the pension, cash at bank and possibly income from Whole of Life Policies.

So where and why did Universal Superannuation come about?

Australia's first Super funds were established in 1862. The fund was established by the Bank of New South Wales for their employees. This was followed in 1869 by the AMP who established a fund for their staff.

This was shadowed by State and Commonwealth aged pension schemes.

Today the total of Australian Superannuation assets stands at around $1.7 trillion, the asset pool is projected to grow to $4 trillion in the next 10 years and $7.6 trillion by 2030. This is without doubt the largest investment pool Australia has ever seen.

In the 1980s as part of the national wage case the federal government supported an ACTU claim for a three percent productivity payment to be paid in the form of award superannuation. Today about 95% of workers have super. A far cry from that of the middle of last century.

Demographers have long realized that we are living longer. An Australian male born in the 1880s, had a life expectancy of 47.2 years, a male born today can expect to live until age 79. Women born today can expect to live 30 more years that Australian women born in the 1880s.

It was recognized in the coming decades with Australians living longer and an anticipated increase in age pension payments this would place a financial strain on the Australian economy. Income support for seniors (mostly Age Pension) currently represents 29% of total welfare expenditure.  I recall attending a seminar and being told all payments from superannuation are currently lower than age pension outlays; however it is projected that, by 2018, age retirement benefits will exceed federal government age pension outlays.

The federal government understands the challenges facing older Australians. Many seniors have not benefited from a lifetime of superannuation, and for many the current Age Pension is simply a wage replacement.


## Introduction of Superannuation

Superannuation is a key part of Australia's retirement income system, Superannuation has become more than a financial asset, and today it is a national institution.

In 1992 the then labor government of Paul Keating recognized this fact and introduced a compulsory "**Superannuation Guarantee**" system. This formed a major part of a reform package addressing Australia's long-term retirement income policies.

Contribution levels in the 1990's started at 3% and grew to the equivalent of 9% of an employee's ordinary time earnings.

## But what is Superannuation?

Well superannuation is a trust. And a trust is an obligation imposed on a person - a trustee - to hold property or assets for the benefit of others. These others are known as beneficiaries (members).
The trustee is the legal owner of the property or assets, but is under a legal obligation to use the property and assets exclusively for the benefit of another person (the beneficiary).

In the case of a superannuation trust, the rights and obligations of the trustee and the beneficiaries ("members") are set out in a document this is called a "trust deed".

As superannuation is a trust in general terms superannuation benefits do not form part of a member's estate. The distribution of a members assets/benefits is determined by the nomination of a beneficiary of the member. In short the distribution of assets/benefits is determined by the arrangement made between the member and trustee.


## Types of Superannuation Funds

Essentially there are four types of Superannuation funds

Personal Funds
Retirement Funds
Workplace Funds
Self-Managed Super Funds (SMSF) this is today's fastest growing sector.
If you are considering a SMSF fund please make yourself familiar with the responsibilities of being a trustee

Prior to July 1 2005 the employer choose the super fund that the Super Guarantee Contributions (SGC) were paid. The introduction of Super Choices in July changed everything and the focus moved to the needs of the employee. Ultimately the employee has the choice of where to invest their funds.

Over the years I have been amazed at the disconnect between people and their superannuation.
People fail to understand superannuation contributions form part of their salary package.
The money placed into our Super funds is money earned.

**Every superannuation fund is different and they must tell you about its main features, including:**

- What benefits you can receive, <u>including any death and disability benefits and Income Protection</u>
- Who can make contributions and how to go about making the contributions.
- What fees you will pay.
- Whether you can choose your own investment strategy.
- The objectives of the investment strategy, its risks and returns
- An important issue can invests be made into direct equities. If so who owns the tax credits.
- Taxation within superannuation is a big issue and with the correct advice there is no reason that tax payable can't be greatly reduced.

Investment income earned within the fund t earnings are taxed at a maximum rate of 15%. Capital gains longer than 12 months within the fund will be taxed at 10%.

The level or amount of tax your fund will pay depends on whether the fund has any tax deductions or tax credits. A growth fund which receives franking credits may only pay 7% tax because its dividend income entitles are used as tax credits.


## Personal Protection within Superannuation

Super funds typically have three types of insurance for members:

Life Insurance – This is the benefit that is paid to your beneficiary if the insured person was to pass away. Please make sure a beneficiary is nominated.

Total and Permanent Disability (TPD) cover - You receive a benefit if you become seriously disabled and are unlikely to ever work again. Loosely called a living benefit

Most important of all is Income Protection or (IP) cover – Your ability to earn an income is your greatest asset. Continuation of income allows to maintain your lifestyle in periods of sickness or temporary disability.

It is generally though that Super is just a place to accumulate your savings until retirement or a condition of release is met. However in the event of a death or medical disaster the last thing of concern to the beneficiary is how much the fund earned last year, the question is how much life cover is there?

## Investment Risk within Superannuation.

Within any investment there is an element of risk.

This can include:

**Economic risk**, where real rates of return (above Inflation) on investments prove unsatisfactory this can be due to inflation, poor return on investment or stagnation within the economy.

Where the value of investments in an individual superannuation account may fluctuate and suffer a significant falls in value this is called **Market risk**. Equally the investor may be outside of the market during a boom period.

The collapse of an investment within the superannuation fund is referred to as **default risk**

**Legislative Risk** often over looked however there have been hundreds of changes to super since 1993

Since 1993, long-term **Growth asset** annualized returns have been 9.2 per cent (three years), 9.6 per cent (five years), and 7.0 per cent (10 years to 31 December, 2013). Using the rule of 72, your super would have doubled every 8-10 years.

At the moment, **annuities** are the only product type offering a guaranteed income stream in retirement,

While Australians have options to “better manage the financial risks they face in retirement, few have a real interest and put their faith in others. There will always be market risk, inflation risk and the greatest risk of all, they may outlive their superannuation account based pension. That is when it is good to know your Centrelink entitlements.

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## Where to from here?

Our superannuation system has already holds a strong international reputation.
The Australian system was recently ranked third in the world, behind only Denmark and the Netherlands, when looking at against the features of adequacy, sustainability and integrity

The contribution superannuation has made to national saving has risen from around ½ per cent of GDP in 1992 to about 1½ per cent of GDP currently and, over the next few decades, is estimated to rise to close to 3 per cent. That is a huge ball investments and reduces the long term dependency on Centrelink and other state benefits.

## In conclusion

Superannuation is money you have earned and for many of us is the biggest pool of money we will ever have.
It is your money.

Significant financial decisions will need to be made. It is never too early to form a bond with a local planner.  Only some of us bite.   darryl.ellis@capitalsg.com.au

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