Understanding superannuation

Client Fact Sheet - September 2015

Superannuation is an investment vehicle designed to assist Australians save for retirement. The Federal Government encourages saving through superannuation by providing generous tax incentives for contributions, during investment, and in retirement.

How much is enough to retire

According to the March 2015 Westpac ASFA Retirement Standard, a couple needs at least $33,799 per annum (p.a.) in order to maintain a 'modest' retirement while a single person needs at least $23,438 p.a. By contrast, for a couple to maintain a 'comfortable' retirement, they need at least $58,444 p.a. while a single person needs at least $42,569 p.a. It's worth noting, too, that these figures do not include the cost of renting a home or paying a mortgage.

A modest retirement essentially means that a retiree can expect to live a little more comfortably than someone on the age pension alone, though they will still only be able to afford the most basic of leisure and recreational activities. A comfortable retirement, on the other hand, means that a retiree can enjoy a broader range of activities and will generally have a good standard of living, including the ability to travel, buy goods and services, and maintain private health insurance.

Currently, the maximum age pension for couples is $33,717 p.a. (or $1,297 per fortnight). The maximum age pension for singles is $22,365 p.a. (or $860.20 per fortnight). As a result, those retirees depending on the age pension alone will have a less-than-modest retirement in terms of spending power.

According to the Association of Superannuation Funds of Australia (ASFA), the average Australian male currently retires with $198,325 while the average Australian woman retires with $112,632.

(Source: ABS 2010

The next table provides an indication of just how much superannuation we would need in order to provide different levels of retirement income to life expectancy.

Age	Income in retirement	Required retirement savings (approx.)
40	$30,000	140,000
	$40,000	355,000
	$50,000	565,000
45	$30,000	160,000
	$40,000	405,000
	$50,000	640,000
50	$30,000	190,000
	$40,000	460,000
	$50,000	720,000
55	$30,000	230,000
	$40,000	520,000
	$50,000	815,000

Contributing to super

You can contribute to superannuation in the following circumstances:

- If you are under age 65 you may contribute to superannuation on your own behalf.
- If your spouse is under 65 years of age you may contribute to superannuation on behalf of your spouse.
- If you are 65-69 years of age you may contribute to superannuation if you have worked for at least 40 hours in 30 consecutive days in the current financial year. Your spouse may contribute on your behalf if you meet these criteria.
- If you are 70-74 years of age, you may contribute to superannuation if you have worked for at least 40 hours in 30 consecutive days in the current financial year. Your spouse may not contribute on your behalf.
- If you are under 75 your employer may also be required to or may choose to contribute to superannuation on your behalf.

If you are over age 75 you are no longer eligible to contribute into superannuation, regardless of your working status. The cut off date for contributions is the 28th day of the month following your 75th birthday. However, employer contributions may be accepted in limited circumstances.

Concessional contributions

Concessional contributions are tax deductible superannuation contributions and include:

- Contributions made by employers on behalf of employees
- Salary sacrifice contributions
- Contributions made by eligible persons including self employed and those with no employment income (eg, retirees, those earning passive income).

Tax deductible contributions can only be made to superannuation funds which comply with Government regulations.

If eligible, concessional contributions are generally used to reduce income tax payable or to offset a capital gains tax liability.

Generally, concessional contributions are subject to 15%[1] contributions tax, payable by the superannuation fund. Contributions tax paid by low income earners may be offset by the low income super rebate.

The Government limits the amount of concessional contributions which can be made for individuals by an employer, or by an eligible person for themselves, in any one financial year without penalty. The limit for the 2015/16 financial year is $30,000 per annum. A $35,000 concessional limit applies for those age 49 or older on 30 June 2015.

[1]Contributions tax of 30% applies to individuals earning income greater than $300,000.

Employer superannuation contributions

Employers are required to make superannuation contributions on behalf of their employees under the Superannuation Guarantee (SG) scheme. They may also offer employees the opportunity to sacrifice a portion of their pre-tax income in exchange for increased concessional superannuation contributions. This is known as “salary sacrifice”.

There is no limit to the amount of concessional contributions allowed to be contributed to superannuation; however, contributions over the specified limits will be refunded and taxed at marginal tax rates plus Medicare. A penalty interest charge will also apply. Additionally, any excess will count towards the non-concessional contributions limit (explained later).

Superannuation guarantee

The SG system was introduced during the early 1990s. The SG payable by all employers is 9.5% of their employees' earnings and must be paid quarterly. Employers are required to contribute only up to a maximum of $19,308 per annum for the 2015/16 financial year (9.5%[2] of $203,240 known as the maximum contribution base). In addition, an employer is not required to make superannuation contributions for employees who earn less than $450 per month. Superannuation contributions can be paid above these amounts, however, the employer is not legally obliged to do so.

It is important to note that SG contributions count towards the concessional contribution limit.

[2]The SG rate will progressively increase to 12% by 2025.

Salary sacrifice

Salary sacrifice is the portion of pre-tax salary that an employee gives up in exchange for additional contributions being made to superannuation for the employee by the employer.

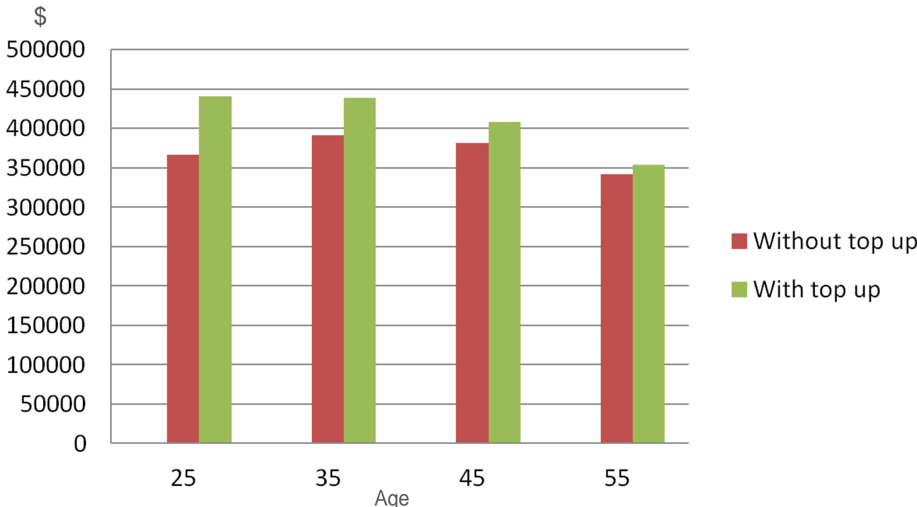
Salary sacrificed superannuation contributions are taxed at 15%[3] on entry to the fund. This is generally a much lower rate than the individual's marginal tax rate. Through salary sacrifice you can therefore reduce your tax liability while building wealth for your retirement.

It is important to note that salary sacrifice contributions count towards the concessional contribution limit.

[3]Contributions tax of 30% applies to individuals earning income greater than $300,000.

Example - salary sacrifice

If you had an initial super balance of $10,000 and salary of $40,000, when you were 25 years old and left it alone until you were 65, you would have a total of $366,317*. But if you started with the same $10,000 balance and salary sacrificed an additional $20 per week, then you would have $440,615*. That's a difference of $74,298. And consider also that the sooner you start making additional contributions to your super fund, the better off you will be over the longer term.



*Figures based on gross annual returns of 7.20% p.a. reinvested. No allowances have been made for fees, expenses or negative investment returns. Results are expressed in current dollars.
At age 25, the individual earns $40,000 per annum and has $10,000 in super.
At age 35, the individual earns $60,000 per annum and has $30,000 in super.
At age 45, the individual earns $80,000 per annum and has $75,000 in super.
At age 55, the individual earns $100,000 per annum and has $150,000 in super.

Superannuation contributions by self-employed/eligible persons

If you are an "eligible person", the Government offers generous tax concessions to encourage you to save for your own retirement. Eligible persons generally do not receive employer contributions under the Superannuation Guarantee scheme, and are not required to make superannuation contributions on their own behalf.

A person who is self-employed or substantially self-employed is eligible for these concessions. For substantially self-employed people, the concessions apply if less than 10% of the assessable income they receive relates to employment as an employee. Income from an employer includes the value of grossed up fringe benefits and reportable employer super contributions (eg salary sacrifice and voluntary employer super contributions).

To determine your eligibility to make a concessional contribution, consult with your financial adviser or tax professional. Eligible persons are able to make concessional contributions and to claim a deduction for these contributions up to age 75. However, please also note that the contribution must be made before 28 days following the month after you reach age 75. Withdrawals/ rollovers will impact the maximum amount of contributions that can be claimed as a tax deduction.

Non-concessional contributions

Non-concessional contributions are personal contributions to your superannuation that you do not claim a tax deduction for. These contributions can attract benefits such as:

- Government co-contributions,
- Spouse contributions tax offset, and/or
- Tax concessions in retirement.

For the 2015/16 financial year, the maximum non-concessional contribution you can make without penalty is $180,000. For those under age 65, the bring forward provision allows total contributions of $540,000 over three years. For persons aged 65 to 75, a contribution limit of $180,000 per annum is allowed, providing they work at least 40 hours in 30 consecutive days in the financial year of contribution. The annual entitlement will operate on a "use it or lose it" basis; that is, if the limit is not fully used in any year, then the unused amount cannot be credited to a future year.

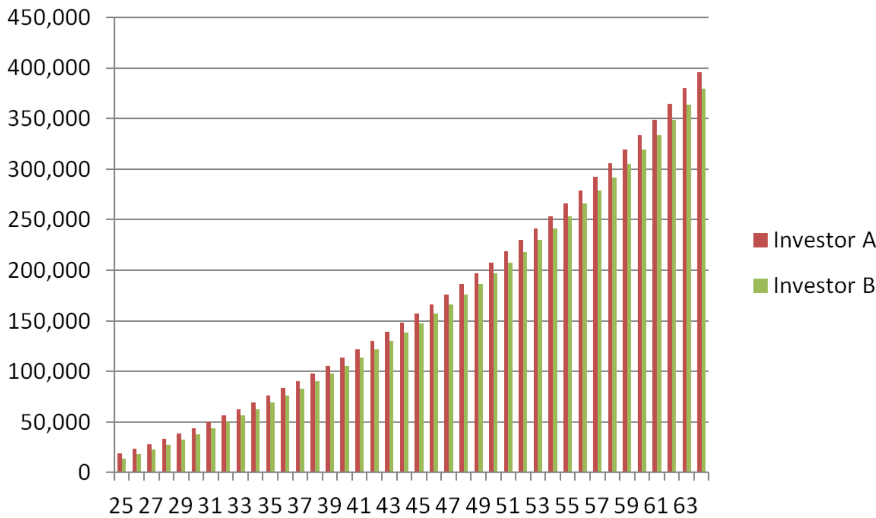
The table below shows various combinations of how the limit may be applied:

	Example 1 Maximum annual contribution	Example 2 Maximum annual contribution using averaging	Example 3 Maximum annual contribution using averaging
2014 – 2015	$180,000	$540,000	$340,000
2015 – 2016	$180,000	$0	$0
2016 – 2017	$180,000	$0	$200,000
2017 – 2018	$180,000	$180,000	$540,000

Please note this is not taking into consideration any indexation of the contribution limits.

Example - one off after-tax contribution

Investors A and B are both 25 years old and each has a super balance of $10,000 and salary of $45,000. Concerned that she might not have enough money for her retirement, investor A decides to make a non-concessional contribution of $5,000 to her super fund. Investor B does not. Over 40 years, investor A's super balance would be $532,355# compared to investor B's balance of $510,186#. That's a difference of $22,169 over the period based on just one additional contribution.



#Figures based on gross annual returns of 7.20% p.a. reinvested. No allowances have been made for fees, expenses or negative investment returns. Both investors retire at age 65. Results are expressed in current dollars.

Government co-contributions

If you make a non-concessional superannuation contribution of $1,000, the government may contribute up to $500 (2015/16) into your super account. You are eligible to receive the government co-contribution, providing you:

- have assessable income, reportable fringe benefits and reportable employer super contributions (RESC) in the income year less than the upper income threshold (i.e. $50,454)
- have made a personal superannuation contribution
- have earned at least 10% of your assessable income, reportable fringe benefits and RESC from employment or business income
- are not the holder of an eligible temporary resident visa

- are less than 71 years old at the end of the income year and
- have lodged a tax return.

The government co-contribution is available to you if you are self employed providing you earn 10% or more of your income from carrying on a business, eligible employment, or a combination of both.

Once eligible, the income test determines the amount of co-contribution you may receive. If your earnings (assessable income, reportable fringe benefits and reportable employer super contributions) are less than $35,454 in the year you make a personal contribution, the Government will contribute 50 cents for every $1 you contribute up to a maximum of $500. For earnings between $35,454 and $50,454, the $500 maximum is reduced by 0.03333 cents for every dollar earned over $35,454 until it cuts out altogether at $50,454. This means that for every $1 of personal contributions, the Government will contribute up to 50 cents, up to the maximum contribution amount available for your income level.

Government co-contributions are not tax-deductible and are not taxed when the superannuation fund receives them. You do not need to apply for the Government co-contribution. The ATO automatically calculates whether you are entitled to it, using information from your superannuation fund and your tax return. The Government co-contribution is paid as a non-concessional contribution and it is paid directly into the same superannuation fund to which you made your personal contribution. However, the Government co-contribution does not count towards the non-concessional contribution limit.

Spouse contribution

A superannuation member may make non-concessional contributions into superannuation on behalf of his/her spouse as long as the spouse is under age 70. From the ages of 65 – 70 the receiving spouse must work at least 40 hours in 30 consecutive days in the financial year of contribution. The non-concessional contributions limit applies to the receiving spouse.

Once spouse contributions are put into superannuation, they are “preserved”. This means they can’t be withdrawn until the receiving spouse meets a condition of release (eg. turning 65 or retiring between 55 and 65).

If you make a contribution to superannuation on behalf of your low-income earning spouse, you may be eligible for a tax offset within certain limits. ‘Low-income earning’ for purposes of the offset is where your spouse has assessable income, reportable fringe benefits, and reprtable employer super contributions (RESC) of less than $13,800 per annum.

A spouse is defined as either a legal or a de facto husband or wife, although they need to be living together for the contributing spouse to claim the rebate.

The maximum rebate is 18% of the eligible spouse contributions, up to a maximum of $3,000 in contributions (i.e. the maximum rebate is $540). The maximum rebate applies where the recipient spouse has a total income of less than $10,800 per annum. Total income in excess of this amount reduces the maximum rebate at the rate of 18 cents for every $1 in excess of total income above $10,800 up to the $13,800 limit.

Further conditions for the rebate to apply are that both partners must be Australian residents at the time of contribution and the contributing spouse may not claim the contribution as a tax deduction.

Spouse contributions are treated as non-concessional contributions and are preserved.

Preservation

While superannuation is extremely important in your overall retirement planning, you must remember that Government legislation preserves superannuation and restricts your access to superannuation (including non-concessional contributions) until you meet one of the conditions of release. These conditions include:

- age 65
- retirement from the workforce after reaching preservation age
- transition to retirement after reaching preservation age
- ceasing an employment arrangement after age 60
- death
- temporary disablement
- total and permanent disablement
- terminal medical condition
- permanent departure from Australia for eligible temporary residents
- severe financial hardship
- compassionate grounds.

Preservation is designed to ensure that superannuation benefits are used only for retirement.

Preservation age

Date of Birth	Preservation Age
Before 1 July 1960	55 years
1 July 1960 – 30 June 1961	56 years
1 July 1961 – 30 June 1962	57 years
1 July 1962 – 30 June 1963	58 years
1 July 1963 – 30 June 1964	59 years
After 30 June 1964	60 years

Accessing your superannuation benefits

Once you have met a condition of release, you may retain your funds in superannuation, withdraw them from the superannuation environment, or commence a retirement income stream. The tax and social security implications of these options differ significantly.

Transition to retirement option

"Transition to retirement" is a Government initiative aimed at encouraging people to participate in the workforce longer by offering incentives to older workers.

Under this scheme it is possible for you to reach your superannuation preservation age and access benefits in the form of a non-cashable income stream before you permanently retire.

For further information on transition to retirement income streams, see "Understanding Account-Based Pensions" or speak with your financial adviser.

Taking your superannuation as a lump sum

The tax-free component of a superannuation benefit is generally made up of your non-concessional contributions. The taxable component of a superannuation benefit is the total value of the superannuation benefit less the tax-free component. The taxable component is generally made up of your concessional contributions as well as earnings.

When you withdraw your funds, the following taxation implications apply for 2015/16:

Component	Below preservation age	Preservation age to age 59	Age 60 and over
Tax free component	Tax free	Tax free	Tax free
Taxable component	20% plus Medicare	First $195,000 tax free >$195,000 15% plus Medicare	Tax free

Superannuation income streams

The main type of superannuation income stream is an account-based pension. Account-based pensions provide a flexible and tax-effective method of generating income in retirement.

Earnings and capital gains within an account-based pension are tax free. Pension payments may be taxable when you receive them (unless the recipient is at least 60 years of age); however, subject to individual circumstances, if you are under age 60, you may be eligible to claim a tax-free amount, as well as a 15% tax rebate on the taxable portion of the payment.

Death benefits and taxation implications

The tax payable on death benefits depends on your age when you die, and/or whether your beneficiary is a dependant (as defined under tax legislation).

The following table shows the tax consequences of a superannuation death benefit (please note that the tax-free component is received tax free in all circumstances):

Tax implications for death benefits			
Beneficiary	Death benefit taken as a lump sum	Death benefit taken as an income stream	
		Deceased and/or dependent is at least age 60	Deceased and dependent both under 60
Tax-dependant*	Tax free	Tax free	Assessable income (15% tax rebate applies to taxable income) A tax-free amount may also apply
Non-tax dependant	Taxed up to 30% plus Medicare	Non-dependants are not entitled to an income stream death benefit	

* A tax dependant is a current or former spouse, child under 18, financial dependant or someone who was in an interdependency relationship with you prior to your death.

Advantages of superannuation

Superannuation has many tax advantages making it a preferred investment strategy.

- Superannuation fund earnings are taxed at a maximum rate of 15% (10% for crystallised capital gains on assets held for at least 12 months). Additionally, income tax of 15% may be offset by imputation credits derived from Australian equity-based investments within the fund. You can also reduce the tax payable by paying insurance premiums from superannuation money.
- You may be able to claim a tax deduction for contributions, a tax offset or co-contribution.
- There are no personal income tax implications from the returns earned by superannuation funds as no income is distributed.
- By rolling over superannuation funds rather than cashing out, the payment of lump sum tax can be deferred and possibly eliminated.
- If you are age 60 or over, you can withdraw from superannuation, either as income or a lump sum tax free.
- If you are under age 60, you can receive income from a superannuation retirement income stream and receive concessional tax treatment possibly including a tax-free amount and a 15% tax offset on the taxable income.
- Superannuation in the accumulation phase does not count under the Centrelink assets test or income test for persons under age pension age.

Insurance

Many super funds provide you with a range of personal insurance options designed to protect you in the event of serious injury, if you can no longer work or if you die. One of the key benefits of buying insurance through your super fund is that it's usually much cheaper than if you organised it on your own.

What insurance do you need?

Most financial experts agree that insurances such as income protection, life insurance, trauma cover and total and permanent disability (TPD) are fundamental to any good financial plan.

Insurance	What it does
Life	Pays your beneficiaries a lump sum when you die
TPD[4]	Pays you a lump sum if you are unlikely to work again due to a total and permanent disability
Trauma[4]	Pays you a lump sum if you suffer a specified and serious illness
Income protection	Replaces around 75% of your income if you are sick or injured and can't work

[4]Since 1 July 2014, new TPD own occupation and trauma policies are no longer offered within super.

Speak to your financial adviser about whether you should hold insurance inside or outside super.

Important note
The information contained in this newsletter is current as at September 2015 but may be subject to change. It is general information only and has been prepared without taking into account your individual objectives, financial situation or needs. Before acting on this information you should consider the appropriateness of the information, having regard to your objectives, financial situation and needs.
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