Superannuation

Superannuation is a tax advantaged way of saving for retirement and makes up two of the three "pillars" of the Government's retirement income policy. The three pillars are:

- A Government funded means-tested age pension
- Compulsory superannuation contribution (i.e. the Superannuation Guarantee)
- Voluntary superannuation contributions

Superannuation is often simply referred to in everyday conversation as "super". The Australian superannuation sector has grown to become one of the largest private pension funding arrangement in the world with assets exceeding $2.75 trillion as at December 2019.

Superannuation consists of two distinct components:

Compulsory Superannuation

If you work in Australia, your employer may have to contribute to a superannuation fund for you under the Superannuation Guarantee system if you:

- Are paid a salary or wages of $450 or more in a calendar month;
- Are over 18 years of age, working on a full-time, part-time or casual basis; or
- If under 18 years of age, you are employed for more than 30 hours per week.

In certain limited situations, and industrial award or workplace agreement may impose additional superannuation obligations of an employer.

Superannuation payments are paid by your employer in addition to the salary or wages you receive. If you are eligible for superannuation, your employer will pay your superannuation directly into a superannuation fund.

Voluntary Superannuation

In addition to compulsory superannuation contributions, individuals may make their own personal and tax deductible contributions and employers may make additional contributions for an employee, generally structured under a "salary sacrifice" arrangement. Salary sacrificed contributions are made from an employee's pre-tax salary

Types of Funds

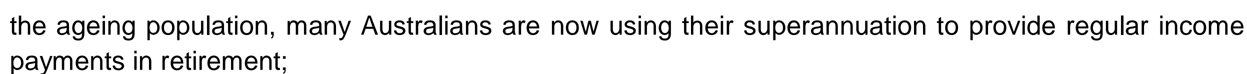
There are a number of different types of superannuation funds. Knowing the different types of fund will make it easier for you to choose a fund that is appropriate for your purposes. Superannuation funds can be grouped into a number of categories. Features differ in each category.

Retail Funds

These are usually run by banks or investment companies, their general characteristic are as follows:

- Anyone can join;
- They often have a large number of investment options, sometimes in the hundreds;

- They are usually used by financial advisers who may receive a fee or commission; they offer both accumulation and pension fund options most Australians have their superannuation in an accumulation fund. They are called 'accumulation' funds because your money grows or 'accumulates' over time, but with



the ageing population, many Australians are now using their superannuation to provide regular income payments in retirement;

- Most retail funds range from mid to high cost, but some are now offering a low cost alternative;
- The company that owns the fund aims to retain some profit.

Industry Superannuation Fund

Larger industry superannuation funds are open for anyone to join. Some others are restricted to employees in a particular industry. The main features of an industry fund are:

- They usually have a range of investment options, which will meet most people's needs;
- They are generally low to mid cost funds although some have high fees;
- They are 'not for profit' funds which means all profits are put back into the fund for the benefit of all members.

Public Sector Funds

Public sector funds were created for employees of Federal and State government departments. Most are only open to government employees. The main features are:

- Some employers contribute more than the 9% minimum;
- A modest range of investment choices that will meet most people's needs;
- Many long-term members have defined benefits, newer members are usually in an accumulation fund;
- They generally have very low fees;
- Profits are put back into the fund for the benefit of all members.

Corporate Superannuation Funds

A corporate fund is arranged by an employer, for its employees.

Some larger corporate funds are 'employer sponsored' funds where the employer also operates the fund under a board of trustees appointed by the employer and employees.

Other corporate funds will be operated by a large retail or industry superannuation fund (especially for small and medium-sized employers).

Features of these funds include:

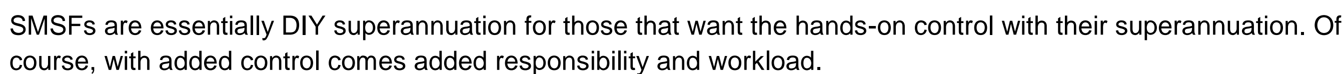
- Funds run by the employer or an industry fund will return all profits to members. Corporate funds run by retail companies will retain some profits;
- If it is managed by a retail or industry fund it may offer a wide range of investment options;
- They are generally low to mid cost funds for large employers but may be high cost for small employers;
- Some older corporate funds have defined benefit members, most others are accumulation funds.

Eligible Rollover Fund

An Eligible Rollover Fund (ERF) is a holding account for lost members or inactive members with low account balances. These funds often have low investment returns and may charge high fees.

Your money is likely to grow faster if you consolidate your ERF with your active superannuation fund.

Self-Managed Superannuation Fund (SMSF)



SMSFs are essentially DIY superannuation for those that want the hands-on control with their superannuation. Of course, with added control comes added responsibility and workload.

SMSFs can be suitable for people with significant superannuation savings and skills in financial and legal matters. You must be prepared to research and track your superannuation investments regularly if you want to manage them yourself.

You can set up your own private superannuation fund and manage it yourself, but only under strict rules regulated by the Australian Taxation Office (ATO).

A SMSF can have one to four members. Each member is a trustee (or director if there is a corporate trustee).

Running your own fund is complex so think carefully before setting one up. If you set up a SMSF you must:

- Carry out the role of trustee or director, which imposes important legal duties on you;
- Use the money only to provide retirement benefits;
- Set and follow an investment strategy that ensures the fund is likely to meet your retirement needs;
- Keep comprehensive records and arrange an annual audit by an approved SMSF auditor.

If you're running a SMSF, you will typically need:

- A large amount of money in the fund to make set up and yearly running costs worthwhile - usually at least $500,000;
- To budget for ongoing expenses such as professional accounting, tax, audit, legal and financial advice;
- Plenty of time and energy to manage the fund;
- Financial experience and skills so you are more likely to make sound investment decisions;
- Separate life insurance, including income protection and total and permanent disability cover.

You can pay an adviser a fee to do the administration or help with the investment decisions for your SMSF. However, you cannot pass on the responsibility of being a trustee or director.

Types of Contributions

When money is paid into a superannuation fund, it is referred to as a contribution. There are two types of contributions; concessional contributions and non-concessional contributions. Concessional contributions include contributions made by an employer, personal contributions that will be subject to a personal tax deduction, and any other contributions that are not a non-concessional contribution.

A non-concessional contribution is one that is made by an individual on their own behalf, or for their spouse, or children under 18 years of age.

Investing Money within Superannuation

Most superannuation funds will provide their members with some flexibility in deciding how they would like their superannuation savings invested. The range of investment options will vary between funds with some funds offering only a small number of options, through to other offering hundreds of different investment options.

Unless you are an experienced investor, it would be prudent to seek specialist advice from a licensed financial planner before deciding where your superannuation savings are to be invested.

Components of a Superannuation Benefit

Accumulated superannuation benefits may be classed as a taxable component and/or a tax-free component.

For those people with an accumulation account, the tax-free component will generally be made up of any non-concessional contributions they have made to the fund. The taxable component comprises of concessional contributions, and investment earnings that accrue of both concessional and non-concessional contributions.

When a person commences to draw an income stream from their superannuation fund, the taxable and tax-free components are crystallised at the time the pension commences. Future investment earnings are apportioned between the taxable and tax-free components.

When withdrawing money from superannuation, benefits are apportioned between the taxable and tax-free components in proportion. It is not possible to select that a partial withdrawal or income stream payment be tax from one component only.

Taxation of Superannuation

Superannuation is concessionally taxed but is not necessarily tax free, except in certain situations.

- Non-concessional contributions are not taxed in the hands of the superannuation fund. However, non-concessional contributions that exceed the non-concessional contribution cap, are taxable in the hands of the person for whom the contributions are made.
- Concessional contributions are taxed as income to the superannuation fund to which they are made. The rate of tax is 15%, however contributions for a person with an adjusted taxable income of more than $250,000 per annum, are taxed at a rate of 30%. This is referred to as Division 293 tax.
- Income received by a superannuation fund on its investments is generally taxed at a rate of 15%. Where the superannuation fund is paying an income stream to a member or members, the income derived from the investments being used to support the income payments is generally not taxed within the superannuation fund. The tax exemption on earnings does not apply to pensions being paid under transition to retirement rules.
- Capital gains made by a superannuation fund, subject to meeting certain taxation conditions, are taxed as income to the fund (accumulation account interests) however they may be subject to a 33.33% discount. Capital gains derived from the disposal of pension or income stream assets are generally tax free to the superannuation fund.
- Lump sum benefits paid by a superannuation fund to it members are tax free to the extent the benefit is derived from a members' tax-free component. Benefits that comprise of a taxable component are tax free if paid after the member reaches age 60. If aged under 60, the tax-free component of a benefit payment will be taxed on a sliding scale, depending on the age of the member at the time of withdrawing their benefit.
- Where a benefit is paid in the form of an income stream or pension, the benefit will be tax-free once the member reaches age 60. When an income stream is paid to a person under age 60, the income may be

taxable depending on the components of the benefit, and the age of the member at the time the benefit is paid.
- For those who are members of older style public sector superannuation funds, and constitutionally protected funds are subject to taxation treatment that differs from that mentioned above.

Getting Money Out of Superannuation

Most superannuation benefits are preserved, meaning that they cannot be accessed until such time as a “condition of release” has been met.

The most common conditions of release include:

- Attaining age 65;
- Retirement on or after reaching preservation age;
- Death;
- Diagnosis of a terminal illness;
- Permanent incapacity;
- Temporary incapacity;
- Reaching preservation age and not retiring;
- Severe financial hardship;
- Compassionate grounds.

Specific restrictions apply to the release of superannuation benefits on grounds of temporary incapacity, reaching preservation age but not having retired, and in cases of severe financial hardship and compassionate grounds.

Preservation age is 55 for people, born before 1 July 1960. For those born after that date, preservation age is progressively increasing to 60 years of age, as set out in the following table:

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

Your benefits can be paid as a lump sum or an income stream, depending on your circumstances and the fund.

Lump Sum

Lump sum withdrawals are usually tax-free if you are over 60. If you’re aged between your preservation and 59, or a public servant with untaxed super, you’ll probably pay tax.

Some of the benefits from withdrawing a lump sum are:

- Clear debts, or pay other necessary expenses, which will save you money in the long run;
- Invest outside of superannuation and put it in a simple savings or investment product, such as a low-fee savings account or term deposit, or another investment that suits your needs. This may help ensure you have some cash for short to medium-term needs;
- You might be able to pay for something that wasn’t affordable before, such as travel, home improvements or a car.

The drawbacks however are as follows;

- You may be tempted to overspend or live beyond your means until the money runs out;
- Spending now will reduce your retirement income in the future;
- Tax may apply to investment earnings outside super. Investments can grow tax-free in a retirement income stream.

Income Stream

An income stream is paid when you commence to draw a pension from your superannuation fund or account.

The benefits from an income stream are:

- Pay less tax. By keeping your money in the superannuation system your investment earnings are tax-free, and for most people over 60, income payments are also tax-free;
- Your money can be invested in a time frame that suits your needs;
- Your money may last longer if you withdraw it in stages as an income stream, rather than all at once.

The Government has set minimum amounts that must be withdrawn from your income stream each year. The minimum level of income you must draw is based on the balance of your superannuation fund at the beginning of the financial year, and a percentage factor based on your age. If you commence a pension part way through a financial year, the minimum income you must draw is pro-rated.

There is no statutory maximum to the amount of income you draw in a financial year unless your income stream is being paid under the “transition to retirement” rules. Where you commence a pension at any time between your preservation age and age 65, and you have not retired, the maximum amount of income you can draw each year is limited to 10% of your pension account balance.

The following table shows the minimum income payment that must be made on an annual basis:

Age	Income Factor - Standard	Income Factor - 2019-2020 & 2020-2021
Under 65	4%	2%
65 – 74	5%	2.5%
75 – 79	6%	3%
80 – 84	7%	3.5%
85 – 89	9%	4.5%
90 – 94	11%	5.5%
95 and over	14%	7%

A Non-concessional Contribution (NCC) is a personal contribution made to a superannuation fund by an individual for their own benefit or for the benefit of their spouse or children under 18 years of age.

NCCs are generally made from after-tax income, from savings, and from the sale of other investments and assets. NCCs may also be made from inheritances, gifts and windfalls.

Where a tax deduction will be claimed for personal contributions, they are treated as a concessional contribution.

NCC Limits

The annual limit or ‘cap’ that applies to NCCs is $100,000 per annum, however up to three years contributions may be made in a single year in certain circumstances.

A NCC can only be made for an individual where they have a ‘total superannuation balance’ of less than $1.6m.

The total superannuation balance is the sum of all amounts a person has in superannuation at the previous 30 June. This includes amounts held in both accumulation accounts and accounts paying a pension for income stream. Where a person is a member of a defined benefit or constitutionally protected fund, special rules apply to determine their total superannuation balance.

Three year bring forward rule

Provided a person was under the age of 65 at the start of the financial year in which they intend to make a NCC, they may be able to bring forward up to three years contributions. The three year bring forward rule is triggered when NCCs in a financial year exceed $100,000. When this occurs, the maximum that may then be contributed over the course of the next two financial years is $300,000, less NCCs made in years 1 (and 2).

People aged from 65 to 74 are unable to make contributions under the three year bring forward rule unless they triggered it before turning 67. If triggered in a previous year, the remaining balance of the three year cap may be contributed, subject to meeting the rules relating to contributions (e.g. meeting the ‘work test’).

Where a person has a total superannuation balance of $1.4m or more, the amount that can be contributed under the three year bring forward rule is scaled back as shown in the following table:

Total superannuation balance	Maximum NCC
Less than $1,400,000	$100,000 + 2 years = $300,000
$1,400.000 to $1,499,999	$100,000 + 1 year = $200,000
$1,500,000 to $1,599,999	$100,000
$1,600,000 or more	$0

Taxation of NCC’s

When a NCC is made to a superannuation fund it is not taxable in the fund. 100% of the contribution, less any entry fee charged by the fund (if applicable) is invested for the benefit of the person for whom the contribution is made.

NCC form part of an individual’s tax-free component within super. When the tax-free component is paid as either a lump sum or as an income stream, the benefit is tax-free in the hands of the recipient.

Investment earnings that accrue on the tax-free component of a benefit are added to the taxable component where the fund is in the accumulation phase, and is apportioned between an individual’s taxable and tax-free components when the fund is paying an income stream.

Exceeding the NCC cap

If NCCs exceed the allowable cap, the Australian Taxation Office will issue an excess NCC determination. Provided an election is made to withdraw the excess NCCs together with associated earnings, which are taxed at an individual’s marginal tax rate, no other penalty is applied. A 15% tax offset is provided to compensate for the tax paid by the superannuation fund on the associated earnings.

Where an election is not made within the prescribed time (within 60 days of the date the determination was issued), the Australian Taxation Office will tax the excess NCCs at a rate of 47%. The Australian Taxation Office

has the power to order the compulsory release of excess NCCs from a superannuation, where the election is not made by the member of the fund.

Benefits of NCC's

Making NCCs to superannuation can assist increasing retirement savings and by adding a member's tax-free component.

This may result in a member receiving tax-free lump sum and income stream benefits from their fund. Where member of a superannuation passes away, the tax-free portion of their accumulated savings is tax-free when paid to their legal personal representative (i.e. their Estate) or directly to other beneficiaries.

People making NCCs may be eligible to receive a Government co-contribution and/or the spouse contribution tax offset.