

Your money Your future



Financial Planning newsletter



The Super Guarantee turns 20

This year marks the twentieth birthday of the Superannuation Guarantee, Australia's unique system of compulsory retirement savings funded by employers. What was once a privilege extended to professionals and public servants is now the right of all employees who earn more than \$450 a month.

As a result, Australians now have more than \$1.2 trillion invested in super, up from \$230 billion in 1995¹. In the process, the Superannuation Guarantee, or SG as it is known, has changed the investment landscape in ways that few people could have imagined back in 1991.

For many individuals, super is their largest financial asset outside the family home and this provides a compelling incentive to take more interest in their investments. At a national level, the SG is designed to create a financial buffer to support our rapidly ageing population in retirement.

But the SG has turned super into more than just a retirement savings vehicle. During the 2008/09 financial crisis, Australia's superannuation system provided a pool of money to help cushion the economy from the worst of the financial shocks². Super funds have invested about \$50 billion in new infrastructure projects, and provided up to half of new capital raised by Australian companies to repay debts³.

The Three Pillars

Governments in many countries, including our own, are grappling with the social and financial challenges of increasing longevity. Most developed nations have some form of government age pension supplemented by private pension schemes.

Australia has developed a 'Three Pillars' retirement income system which relies on a combination of government age pension, employer-funded superannuation, and private savings.

Like Australia, countries such as the Netherlands and Sweden, widely regarded as having excellent pension systems, have some form of compulsory private pension, whereas private pensions in the US and UK – although widespread – are voluntary.

A global comparison of retirement income systems in 14 developed nations ranks Australia fourth behind the Netherlands, Switzerland and Sweden. The verdict of the Melbourne Mercer Global Pension Index⁴ is that Australia is doing well, but could do better. Suggested improvements are increasing the SG to 12 per cent, reducing the costs of super, increasing the workforce participation of people aged over 55, and making it compulsory for people to take at least part of their super payout as a pension. Some of these reforms are already in the pipeline.

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1 ATO.

2 The Weekend Australian, 17-18 September, 2011.

3 ASFA, The Allen Consulting Group, Better living standards and a stronger economy: the role of superannuation in Australia, September 2009.

4 Melbourne Mercer Global Pension Index 2010.

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redefining ✓
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The Super Guarantee turns 20 continued

Building Australia's super scheme

The SG was originally set at 3 per cent of pre-tax income, rising to 9 per cent by 2002. In last year's budget the Federal Government announced a proposal to increase it from 9 to 12 per cent by July 2019. It also plans to raise the age limit for eligibility to 75 by July 2013⁵. At the same time, eligibility for the age pension is being lifted gradually from 65 to age 67 in 2024.

During your working years you and/or your employer contribute money into super. If you are aged between 18 and 70, earn more than \$450 a month, and are regarded as an employee for tax purposes, then your employer must make contributions to your super fund on your behalf⁶. However, you cannot access that money until you satisfy a condition of release or reach age 65.

The reward for locking your money away for 40 years or more is two-fold: investment earnings inside super are taxed at concessional rates, and withdrawals from your savings are tax free after age 60⁷.

The restrictions placed around access to your super savings may be strict, but they provide a rare win-win for government and investors. The longer you leave your money invested

in super, the longer compound interest has to weave its magic and create a substantial nest egg for your retirement. Therefore, the government needs to spend less money on the age pension and other welfare benefits in the future.

A brighter future

The compulsory nature of these employer-funded payments takes the pain out of saving for many Australians, but there is no cause for complacency.

The average super payout in 2009/10 was \$198,000 for men and just \$112,600 for women. The current generation of retirees has had the benefit of the SG for only 20 years and many women have had time out of the workforce. But as the superannuation system matures, retirement benefits should increase substantially.

For example, someone on a modest income of \$50,000 with 40 years in the workforce could expect to retire with a lump sum of around \$466,000 based on 9 per cent SG and no voluntary contributions. This would provide annual retirement income of around \$30,000, which is better than the pension but would only afford a modest lifestyle⁸.



If you would like to discuss ways to boost your retirement savings, perhaps with an increase in voluntary contributions to super, then call us so we can help you realise your goals.

5 ATO.

6 ASFA, The Allen Consulting Group, Better living standards and a stronger economy: the role of superannuation in Australia, September 2009.

7 Assuming retirement is at age 60, note super payments between 55 and 59 may not be tax free.

8 ASFA, The Allen Consulting Group, Better living standards and a stronger economy: the role of superannuation in Australia, September 2009.

Women and money

Against a backdrop of global debt woes and financial market uncertainty, Australian women are more worried than men about their financial wellbeing and less optimistic about the economic outlook.

According to recent surveys by Million Dollar Woman, only 30 per cent of working women are confident that Australia will avoid an economic downturn, compared with 47 per cent of men¹. What's more, nearly twice as many women (18 per cent) are pessimistic about the economy's future than men (10 per cent)².

It is not clear from the research why women are more concerned about their finances than men, but there are a number of possible reasons.

In most families, women have primary responsibility for household shopping so they may be more sensitive to rises in the cost of living.

Debt could also be an issue. Research by Million Dollar Woman found that women owe \$2.60 for every \$1 they earn, compared to \$2.10 for men³. Debt can be good when it is used to build wealth, but it causes problems when it is used for everyday spending and not managed wisely. The less income you

have, the more difficult it is to support a significant amount of debt.

Not only do women earn less than men on average, they are more likely to take time out of the workforce to raise children, leaving them with less money saved for retirement. The average superannuation balance in 2009/10 was just \$40,475 for women compared with \$71,654 for men⁴.

Knowledge is power

There is another possible explanation for women's lack of optimism; perhaps they are just more realistic than men. The most famous study of gender differences in investing, by academics at the University of California, found that male investors tend to be overconfident and this leads them to trade their share investments more often than women and take greater risks⁵. But men were no more skilful or successful than women. Could it be that women are more willing to own up to the fact that they do not know everything?

While women may have good reasons to be less optimistic than men, it does not mean they are powerless to act.

The best way for women – and men – to take control of their financial destiny is to increase their knowledge.



Your financial adviser can help keep your finances on track but the more you learn about investment and sound money management the brighter your future will be.

1 Million Dollar Woman, Australia's financial outlook 'worries' women, 19 August, 2011

2 Allianz Future Optimism Index, 23 August, 2011

3 Million Dollar Woman, *ibid.*

4 ASFA, based on ABS Survey of Income and Housing 2009/10 (released 19 September 11)

5 Brad Barber and Terrance Odean, 'Boys will be boys: Gender, overconfidence and Common Stock Investment', Quarterly Journal of Economics, February 2001.

Taking care of the children

Most families run a tight ship when it comes to finances. There's money for the mortgage, the utilities, the school fees, child care, general living expenses and perhaps a holiday most years. But what happens if the ship hits some stormy weather?

That storm can be triggered not only by losing your job or becoming sick, but also if someone in your family requires extensive medical care.

In a perfect world, no child would be ill but sadly that is not the case. For instance, each year approximately 600 Australian children are diagnosed with cancer¹. Each year there are also around 1,000 spinal cord injuries to children, 544,000 children are admitted to casualty, and 200,000 children become critically ill².

Figures from the Australian Bureau of Statistics (ABS) indicate that 8 per cent of children aged 15 or under will suffer some type of disability³. The ABS defines this as the presence of any limitation, restriction or impairment which has lasted for at least six months and restricts everyday activities.

Additional financial burden

Sick children need a lot of care and attention, and the family may be placed under additional financial pressures. This can prove difficult to deal with, especially if you have other children to care for. Aside from the emotional turmoil and feelings of helplessness, you still need to find time to look after the rest of the family.

Let's take Tom, aged 9, who developed childhood leukaemia resulting in long stays in hospital. Mum Sally found it impossible to keep up with her part-time job and look after Tom as well, which resulted in the family losing an income.

Even though she now had the time to spend at the hospital, her other two children, Lucy, 5, and Ben, 7, still needed to be cared for both before and after school. This was not previously an issue as Sally was working from 10 am to 2 pm, and she was there for the children when they were not at school.

Medical costs also need to be taken into account.

At least the family lived in a major capital city, but if they had lived in regional Australia they may have had to add the costs of accommodation and travel to seek treatment from specialists at the city hospital.



Thankfully, after discussions with their financial adviser, Sally and her husband Rick had the foresight to take out trauma insurance for themselves and had opted to buy extra cover for their children.

Child trauma protection

Most insurance providers offer children's trauma insurance as an adjunct to the adult trauma policy, and its importance cannot be underestimated.

The insurance usually covers children aged from 2 to 16 years old, although this can vary and the premiums are significantly lower than those for an adult. Sums insured can be as high as \$200,000.

With this cover, Sally and Rick received a lump sum payment which covered all the associated expenses of Tom's illness.

Had his illness been different, for example if he became wheelchair-bound, there would have also been money available to pay for modifications to their home.

Most trauma insurance policies cover such events as blindness, cancer, major head trauma and severe burns. Many policies offer a continuation option, so that once the child becomes a young adult, they can convert it to their own contract.

As with all insurance policies, it is important that you choose one that best suits the individual needs of your family. Every policy is different, with different inclusions and exclusions. Consequently, it is wise to get advice to help you navigate your way around all the policies and options available.

It is also possible for grandparents to cover their grandchildren through their stand-alone life/trauma policy. Of course, many people in their 60s and 70s may no longer have life insurance if dependent children and having a mortgage are things of the past. Nevertheless, the option is there.

Insurance – whether life, income protection or trauma – is all about taking care of your family should you lose your ability to earn an income. It may be time to review your insurance needs with your adviser, to revisit trauma insurance, and the different options available. Including your children in the cover is worth considering as your ability to work may be impeded should they suffer a significant illness or injury.

1 Australian Cancer Research Foundation

2 Cominsure Statistics, 2007

3 ABS, 4446.0 – Disability, Australia, 2009

Capping to the max

When there is a chance to cut the tax bill, most of us want to take a closer look. By increasing your superannuation contributions now you may have a chance to build your retirement benefit and possibly cut your current and future tax bills.

Why? Because once you have turned 60, your super pension is tax-free, this allows you to put as much as possible into super while you still can.

If you already have more than \$500,000 in your super and are over 50, this financial year will be your last chance to contribute up to \$50,000. From 1 July 2012, it is proposed that the concessional contribution cap for those aged over 50 with more than \$500,000 in super will be halved from \$50,000 to \$25,000, the same cap applying to the under 50s.

However, if you are over 50 with less than \$500,000 in your super – one of 275,000 Australians according to government estimates¹ – the cap will stay at \$50,000.

But always remember, if you breach your cap you may be liable to pay the top marginal tax rate of 46.5 per cent on the excess contribution.

Tax-free earnings

Super becomes more attractive once you are in the pension phase, as all money earned within the fund is tax-free. That is an instant saving of 15 per cent tax on interest earned or dividends paid on your retirement investments.

Once you turn 60, both your pension income and all your drawdowns are tax-free.

There are also potential tax savings from salary sacrificing. Even if you are not in pension phase, you will only pay 15 per cent contributions tax rather than your full marginal tax rate which may be up to 46.5 per cent².

Transition to retirement

The tax break on salary sacrificing into super is one of the key reasons why a transition to retirement (TTR) strategy is recommended for over 55s. Under a TTR strategy, you can draw money from your superannuation fund while salary sacrificing up to your concessional cap at the same time. The result may be a reduction in tax payable.



For many people, it is well worth seeking advice in relation to TTR since the tax benefits may be significant.

Given the tax-friendly super environment, you should consider increasing your contributions to super while you still have the opportunity.

- [1 http://www.futuretax.gov.au/content/Content.aspx?doc=FactSheets/concessional_contributions_caps.htm](http://www.futuretax.gov.au/content/Content.aspx?doc=FactSheets/concessional_contributions_caps.htm)
- [2 http://www.ato.gov.au/super/content.aspx?doc=/content/38172.htm%20](http://www.ato.gov.au/super/content.aspx?doc=/content/38172.htm%20)

Christmas, what does it mean to you?

One of life's paradoxes is that the events we most look forward to often cause us the most stress.



The festive season and Christmas cheer, presents and parties – they all seem to begin earlier each year. This joyful time can become overwhelming and create unrealistic expectations personally and financially.

To avoid some of the pressure, we can try to think differently about Christmas this year.

What does Christmas mean to you and your loved ones? Peace – of mind or in the world; beliefs – in a religious or magical sense; or joy – whether it comes from loved ones or gifts.

If overspending will cause financial strain, reconsider your spending plans. Be realistic about Christmas this year. It is only one day of the year and people will remember your presence more than the presents.

You can start planning for Christmas spending early and spread your expenses over the year so you are not left dreading the arrival of bills in January. And to reduce your expenses, buy items that can be shared or start a new tradition in your family such as Kris Kringle.

So this year, focus on what is important and what it means to you and your family. Enjoy the festive season and ensure you have a happy new year.

Interesting facts about Christmas:

- Australia Post estimates that 70 million cards will be sent this Christmas ensuring the tradition is as popular as ever.
- The word Christmas is derived from the Old English word 'Cristes maesse' which literally translates to Christ's Mass – although no one knows for sure the exact date of Christ's birth.
- In many households, the fun of eating Christmas pudding is in finding a trinket that predicts your fortune for the coming year. The idea of hiding something in the pudding comes from the tradition in the Middle Ages of hiding a bean in a cake that was served on Twelfth Night.
- The poinsettia is a traditional Christmas flower. In Mexico (its original birthplace), the poinsettia is known as the 'Flower of the Holy Night'.
- Leftover food can sometimes be your enemy. Spoilt leftovers are responsible for 400,000 cases of post Christmas associated illnesses.
- The first Christmas stamp was released in Canada in 1898.

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