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When is it Time to Stop Investing in Super?

Theo Marinis discusses turning 50 and concludes it's never too early to plan for retirement but it can sometimes be too late.

By Theo Marinis

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As you pack the recycling with the empty bottles of Jansz and Penfold’s 389 and reflect on turning 50 perhaps it’s also time to get real about how much superannuation you have. If you and your partner want a dream old age, you should be thinking about an accumulated $1.7 million. Each.

A combined total of $3.4 million in retirement savings will deliver annual tax-exempt income of $170,000, increasing with inflation over time. This figure is based on the Account Based Pension (ABP) ‘minimum’ income level of 5 per cent for the age range 65 – 75, as per the ABP ‘glide’ plane set by the Government Actuary.

This 5 per cent is also conservative and well below the ASX All Ord’s average return of 8.9 per cent per annum over the 30 years to 30 June 2020 – a period which includes the GFC and the COVID-19 collapse, but not the unbelievable recovery (thus far) in 2021. It goes without saying but I will say it anyway – “Past performance does not guarantee future performance”.

It should also go without saying that when in income drawdown phase your retirement savings would generally not, or should not, be 100 per cent invested in Australian shares or in some other combination of growth assets.

When considering a portfolio to produce retirement income, diversification across asset classes, with further diversification within each asset class in line with your individual risk profile, is vital precisely because past performance is no guarantee of future performance.

So, while your $3.4 million in combined ABP funds will return less than 8.9 per cent per annum over the long term, it will still be a financial magic pudding.

But what if you are like most of us and you've put the mortgage and the kids' education, a nice car and the odd "look at me" holiday in Europe ahead of saving for the future?

Then it really is time for a reality check, and time to resist the urge to buy a holiday house or the latest Range Rover. According to the Association of Superannuation Funds of Australia, the average Australian male aged 50 – 54 has a superannuation balance of $242,000. The average Australian woman aged 50 – 54 has $159,000.

Paying off the family home is smart. Don't dawdle, particularly with interest rates around 2.5 per cent per annum. Pay it off quickly even if this might mean in some instances having a chat with your partner about going back to work or increasing paid work hours.

In the meantime, increase your personal super contributions and, if possible, those of your partner to the current maximum Concessional Contribution (CC) cap of $27,500 pa, (noting that this cap is inclusive of your employer's Super Guarantee and/or your salary sacrifice contributions).

What may surprise many people with taxable incomes above $45,000, is that additional Concessional Contributions are very tax effective when compared against a personal tax rate of 34.5 per cent and the 15 per cent contributions tax payable by your super fund.

The tax savings are even greater when your annual taxable income is over $120,000, or above $180,000 (based on personal tax rates of 39 per cent and 47 per cent respectively).

That said, there are still immediate tax advantages for taxable income above $18,200 and up to $45,000, as the personal tax rate (inclusive of Medicare Levy) is 21 per cent versus 15 per cent in super. However, the higher the income (and the higher the tax rate) the greater the benefits.

The exception to this general rule is when ‘Division 293 income’ exceeds $250,000. Division 293 adds back several items into taxable income (e.g., negative gearing property losses, among others). The result is the application of Division 293 tax in the form of an additional 15 per cent on CCs, (or 30 per cent in total).

The increased tax rate is designed to bring the concession for higher-than-average income earners back to an amount in line with the average concession – effectively reducing the tax concession for individuals whose combined income and contributions are greater than the current Division 293 threshold of $250,000.

For those unfortunate (or, maybe, fortunate) to be in this position, paying super tax at 30 per cent on your CC is still better than a personal tax rate (Medicare Levy inclusive) of 47 per cent.

If you have money invested outside of superannuation and a home which is paid off, it is worth remembering that you can top up to $110,000 per year in Non-Concessional Contributions (NCCs).

Bear in mind that there is a cap of $330,000 in any one year via the “Three Year NCC Bring Forward rules”. Within your medium-term planning, keep an eye also on the 2021 budget-day announcement which, if legislated, will allow downsizers over 60 to each contribute an additional $300,000 to their super, (effectively a $600,000 limit for couples). This amount is over and above the normal NCC limits.

While NCCs do not provide any immediate tax saving benefit, the earnings inside the fund will only be taxed at a maximum 15 per cent (zero once you can start your ABP) and you could be boosting your super balance close to the magic $1.7 million figure, for each of you.

Based on the scenarios above, many will be thinking: “great ideas, but I don’t have the extra cash to top up our super.” Don’t forget that you are in an age-group where you are also likely to inherit. If you do, my best general advice would be to address the mortgage first (as the home is Capital Gains Tax free) then put any extra into super, subject to the contribution caps which apply.

Buying a boat or upgrading the car should not be considered without first addressing these priorities.

There is, however, an associated balancing act to consider here. Once your cash is in super, it can be very difficult to get it out until you've retired and reached your preservation age (currently 59 for those born 1 July 1963 to 30 June 1964) unless you are in exceptionally difficult circumstances, and even then only in very small amounts. Consider having a cash reserve for emergencies.

Bear in mind too that at around age 50 we also may also enter the "career death" phase. Speaking bluntly, if we become too expensive – sometimes our IT skills and energy levels are far below the younger generation – we can become obsolete. Very few well paid executives/senior managers remain in these positions until retirement age – let alone super preservation age, which will be age 60 from next financial year.

A further harsh reality is that around this age, via the circumstances of friends and acquaintances, we become increasingly aware not only of our mortality, but our morbidity. Protecting the family financial base by having appropriate insurance in place should be an integral part of our retirement planning considerations.

And speaking of your family financial base, if you have children, you would also be aware that they will not really become financially independent until at least age 25. This can be due to the comfort of home and the increasing pressure to have a master's degree, combined with a certain level of job insecurity while they are under 30.

Now, at this point, it is easy to throw our hands in the air and declare that $3.4 million just won't happen, and that is true for most Australians. Bear in mind, however, that $2.4 million in super is far better than $1.4 million, which is much better than $400,000.

The starting point is to be realistic about your situation. Involve your partner, who also has a profound interest in the outcome, and who may just not have thought about the impact a small super balance will have on their retirement lifestyle.

A 'one page' assets and liability sheet, so that you both know where you really are financially, can help you to start the discussion about what retirement might look like for you both. Had you considered life 'post-kids' or moving back home to the country?

The next step is to meet with a financial planner who can help you organise your finances and realistically assess where you want to be and help to guide you there.

To my retirement savings mantra "put away as much as you can, as soon as you can – for as long as you can" I would also add "don't procrastinate, be realistic and get help; it is rarely too late to benefit from professional guidance".

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