

What is the best way to save for retirement?

For most people, superannuation is the most tax effective way to save for retirement. And, just as importantly, it is the most tax effective way to generate a retirement income.

What are the tax advantages of super?

Let's say you decide to invest \$10,000 of your salary. If you invest it via your super fund, from your pre-tax salary, this is how your contribution will be taxed (assuming it is part of a salary sacrifice arrangement):

- Firstly you won't have to pay PAYG tax on the \$10,000 of salary.
- But once in your super fund, tax of 15% will be levied, leaving you with \$8,500 invested.

Compare that to investing your \$10,000 outside of super. In that case, you'll have to pay PAYG tax, leaving you with just \$6,300 (assuming your marginal tax rate is 37%) for investment wherever you like.

The earnings generated by the investments outside of super will be taxed at 37%.

However, earnings generated by investments in your super fund will be taxed at only 15%.

Case study

The tax differential between investing in super and non-super adds up over time.

Let's say Bob is on a tax rate of 37%, can afford to invest \$10,000 p.a., and his salary and investment contribution is indexed at 3% p.a.

If he invests that money in superannuation as part of a salary sacrifice arrangement (i.e. \$8,500 after contributions tax) and the fund earns 8% p.a. gross, he would accumulate \$153,141 after 10 years, and \$549,649 after 20 years, as shown in Chart 1.

However, if Bob chooses to not use superannuation, he'll have only \$6,300 p.a. (indexed) to invest after paying PAYG tax.

And he will be paying tax on investment income of 37% (compared to 15% in super). As a result, after 10 years he'll accumulate only \$104,391, and after 20 years \$356,122, assuming an 8% p.a. gross return.*

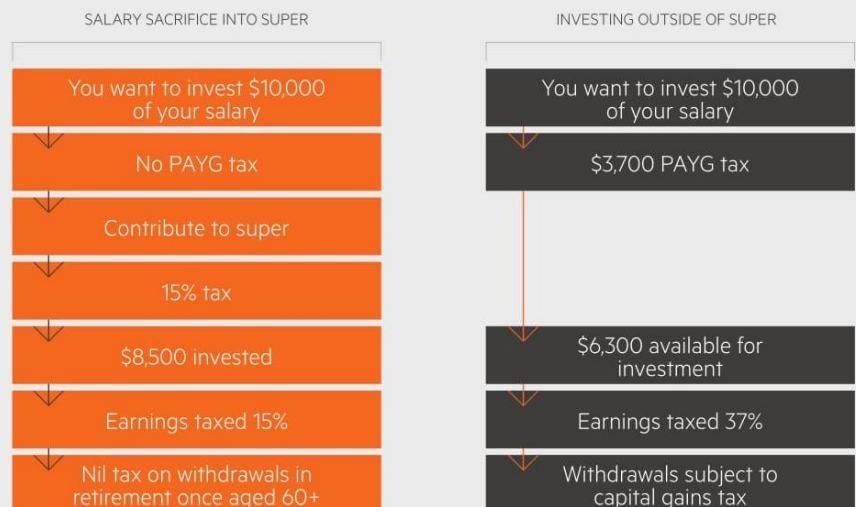
The sole reason for the difference is the preferential tax treatment of superannuation.

How much can you invest in super on a tax-effective basis?

Because super is tax advantaged, there is a limit on how much you can invest in super and qualify for a tax deduction. This limit is shown below, and it includes your employer's super guarantee contributions.

Concessional contribution cap (2017/18):
\$25,000

Super means you can have more invested*



*Assumes MTR 37% based on 2017/18 tax rates

No tax on super withdrawals for retirees aged 60+

For most retirees over age 60, there is no tax payable on withdrawals from super, and no tax on income paid from or withdrawals made from retirement phase pensions. Additionally, if you are invested in a retirement phase pension, there will be no tax on fund earnings (including on capital gains), however the amount a person can invest in a retirement phase pension is limited by transfer balance caps. Currently, the limit is \$1.6 million.



Superannuation Pros:

- Low tax on contributions
- Low tax on earnings in the fund
- Little or no tax on retirement income (if finances properly arranged)

Superannuation Cons:

- Generally you can't withdraw money until you are 56+ and retired (but you may be able to start a pension from your super money after age 56 even if you are still working)
- Rules are complex and subject to change

Chart 1: An improvement of \$193,527 for retirement*



*Assumes MTR 37% and an investment return of 8% p.a. gross

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