SMSF
Owners'
Alliance
Limited ABN 96 161 052 464
Not-for-profit public company

11 May 2015

Hon Josh Frydenberg MP
Assistant Treasurer
Parliament House
CANBERRA ACT 2600

Attention: Martin Codina

Dear Minister

Reducing minimum superannuation pensions

The reduction of the official cash rate to 2% will further erode the earnings of superannuation funds from their cash assets.

In particular, the earnings of self-managed superannuation funds will be impacted as SMSFs tend to hold a larger proportion of their assets in cash than the mainstream funds. The ATO's statistics on SMSFs show that the average allocation to cash/term deposits is 28%. Low balance funds generally hold a higher proportion of their assets in cash. For example, funds with $150-200k in assets hold 45% in cash/term deposits (see Table 2 below).

Over time the cumulative reductions in interest rates have a significant impact.

On the latest ATO annual statistics (2012-13) for SMSFs, the median value of assets held in self managed funds was $486,602.

On the ATO figures, a fund of that size typically would hold 36.5% of its assets in cash amounting to S177,609. A fund with $175,000 in cash that was enjoying interest of 5% a year ago, delivering income of $8,750 will now be earning only $4,375 at 2.5% - a drop in income of 50%. This is not taking inflation into account.

SMSF members pay heavily as interest rates are lowered.

With earnings from deposits so low, funds are in the position where the fixed minimum withdrawal rates for account based pensions are requiring people on super to sell down more of their capital. For example, self-funded retirees in their early 70s must now withdraw 6% of their fund assets each year as a pension. With term deposit rates now below 3%, funds with relatively high holdings in cash may find the minimum pension exceeding the fund's earnings by a greater margin and depleting capital faster than it should.

For such pensioners’ superannuation to last their lifetime, it is important that their capital not be distributed and paid out too early. If so, there is an increased risk that it will run out and the superannuants will have to revert to the Age Pension.

It was never the intention when the minimum withdrawal rates were set that in times of especially low interest rates superannuants would be obliged to spend more of their capital.

While it may be argued that running down the capital value of superannuation funds is consistent with the objectives of superannuation, older Australians are worried about how long their superannuation savings will last and some may wish to reduce their current year drawings in favour of making their funds last. As the Intergenerational Report showed, Australians are living longer and, of course, many will live longer than the average.

Older Australians are concerned not only about whether they will have enough to live on and stay off the age pension but also whether they will have a buffer in their superannuation funds to take care of unexpected events in their lives, high medical expenses and the cost of aged care.

As the Governor of the Reserve Bank has pointed out, retirees who seek returns higher than cash must take on riskier investments. Many older people are reluctant to do so.

The solution is to reduce the minimum superannuation pension rates as occurred during the Global Financial Crisis when the minimum pension withdrawal rates were reduced by 50% for three years and then by 25% for one year.

Lowering the minimum pension rate would have no effect on the Federal Budget. It would be well received by self-funded retirees concerned about conserving their retirement savings as long as possible. And it would not prevent people taking more than the minimum pension if they need to do so.

We would be pleased to work with your advisers and with Treasury on a more appropriate regime for minimum pension withdrawals while interest rates remain very low.

Looking past the immediate issue, we believe the concept of minimum withdrawals needs to be re-examined and we will be providing some observations on this in our submission to the Taxation White Paper.

Yours sincerely

Bruce E Foy
Chairman
SMSF Owners’ Alliance

Table 1: Minimum pension withdrawal as percentage of fund assets (GFC adjustments 2008-13)

Age	Minimum pension	GFC level 2008-2011	GFC level 2012-2013
55-64	4%	2%	3%
65-74	5%	2.5%	3.75%
75-79	6%	3%	4.5%
80 -84	7%	3.5%	5.25%
85-89	9%	4.5%	6.75%
90 - 94	11%	5.5%	8.25%
+ 95	14%	7%	10.5%

Table 2: Asset value range of funds – cash/term deposits (as percentage of fund assets)

$1-50k	$50-100k	$100-150k	$150-200k	$200-500k	$500-1m	$1m-$2m	$2m-5m	$5m-10m	$10m+
57.07	51.34	48.27	45.08	37.95	35.37	33.74	30.48	26.76	23.61

Source – Australian Taxation Office Self-managed Superannuation Fund Statistical Report 2013

Table 3: Effect of 0.25% reduction in interest on cash investments from common Big 4 SMSF rate of 2.6% at 6 May 2015

Cash component of fund	Income earned at 2.6% interest	Income earned at 2.35% interest	$ reduction in interest income	% reduction in interest income
$50,000	$1,300	$1,175	$125	9.6
$150,000	$3,900	$3,525	$375	9.6
$250,000	$6,500	$5,875	$625	9.6
$500,000	$13,000	$11,750	$1,250	9.6