Self Managed Super Fund Association

ACCURIUM

SMSF Retirement Insights

Are trustees prepared for retirement?

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Our research shows how lower investment returns and proposed superannuation changes affect SMSF trustees heading into retirement.

For SMSF practitioner use only

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Executive summary

The SMSF Association and Accurium have come together to present this extensive study of over 65,000 SMSFs looking at how retirement wealth of Australia's SMSF trustees has changed over the 2015 financial year. Based on Accurium's extensive database, it provides the first detailed figures to be released for the 2015 financial year and considers how well prepared SMSF trustees are for retirement.

The research also includes analysis of the impact of key superannuation measures proposed in the 2016-17 Federal Budget on SMSF trustees.

Retirement adequacy

- The median SMSF balance increased by 3.0% over the 2015 financial year, based on a median investment return of 4.2%. This is lower than the average return over the previous 5 years of 6.2% p.a.
- The current lower return environment means retirees need more in savings to achieve their retirement goals. Accurium's estimate of the amount a 65-year-old couple need in retirement savings to be reasonably confident[1] of affording a comfortable retirement[2] has increased to $702,000. Around 30% of SMSF couples have insufficient balances in their SMSFs to afford this lifestyle, up from 25% last year.
- 65 year-old SMSF couples with aspirations of a higher standard of living will need $1,886,000 in savings to be reasonably confident of affording $100,000 p.a. in retirement. The proportion of 65 year-old SMSF couples with sufficient assets in their SMSFs to support this lifestyle has fallen from 34% to 29% over the year.
- An analysis of the detailed retirement spending plans of SMSF households shows that the median desired spending level is $75,000 p.a. Around 30% of SMSF households plan to spend $100,000 p.a. or more in retirement.
- Helping to dispel the myth that SMSFs are commonly used as estate planning tools, our study found that fewer than one in five SMSF households included an explicit desire to leave a bequest in their retirement plans.
- Based on actual spending plans and household wealth, our study found that two in five SMSF households can't be confident that their retirement plans are sustainable. Only a third can be very confident that their desired spending levels will not see them outlive their savings.
- Our analysis revealed a clear correlation between the sustainability of SMSF households' retirement plans and their level of wealth, suggesting that the SMSF trustees in our study may not be adjusting their spending levels to match their means. This presents a real opportunity for SMSF practitioners to help their clients optimise their retirement plans.

Impact of 2016-17 Federal Budget changes

- Our study found that almost one in five SMSF trustees over the age of 65 have balances of over $1.6 million meaning they are likely to be impacted by the proposed retirement balance transfer cap. Around 8% of two member SMSFs have both members with balances in excess of the cap. Even so, for most SMSF trustees, keeping the excess over $1.6 million in accumulation is likely to be more beneficial than withdrawing it from superannuation altogether.
- Nearly a third of the SMSF trustees in our study made concessional contributions in excess of the proposed $25,000 cap. Of those trustees contributing more than $25,000, 70% already have balances in excess of $500,000 meaning that they cannot take advantage of the proposed 5 year 'look back' rule.
- Over 48% of the SMSF trustees in our study would have been affected detrimentally by one or more of the proposed superannuation changes, had they been in place for the 2015 financial year. With their higher average balances, SMSF trustees are likely to be most affected by the Budget changes.

1 'Reasonably confident' is defined as requiring an 80% probability of the required retirement spending level being sustainable for life, allowing for tax and Age Pension entitlements. To be 'very confident' of their retirement plans being sustainable, we assume SMSF retirees would want a 95% probability of not outliving their savings. See Appendix 2 for detailed methodology and assumptions.

2 As defined by the ASFA Retirement Standards.

Background

About Accurium

Established in 1980 and now part of the Challenger Limited group, Accurium provides a range of services to self-managed superannuation funds (SMSFs) in, or transitioning to, retirement with the help of accountants and other SMSF practitioners.

Accurium leads the SMSF market for actuarial certificates, placing it in a unique position to provide analysis on SMSFs in the retirement phase. Accurium supports more than 65,000 SMSFs which are paying pensions and thus require an actuarial certificate, giving Accurium access to an unrivalled amount of information on which to undertake research to assist accountants and SMSF practitioners provide quality service to their clients.

As experts in SMSF retirement, we're committed to passing on the essential tools and information you need for success including our pioneering retirement health**check** service which assists in making sure that your clients are on track to meet their retirement goals.

About SMSF Association

The SMSF Association is the leading and authoritative voice for the SMSF sector, established to improve the quality of advisors, the knowledge of trustees and the credibility and health of a vibrant SMSF community. The Association's core beliefs embrace every Australian having the right to a good quality of life in retirement and having the right to control their own destiny. Representing professionals providing a range of strategic advice and services across various professional disciplines in the complex area of SMSFs, the Association also engages directly with trustees to assist them to become better educated and informed. The SMSF Association is an advocate for the highest professional standards to ensure SMSF trustees always receive the best advice and to continue to build the integrity of the SMSF sector as a major source for our nation's prosperity for today and our future.

Introduction

Accurium and the SMSF Association have come together to bring this thought-provoking research to SMSF practitioners and their clients.

Changes in SMSF balances

Over the year to 30 June 2015, the median balance of two member SMSFs in Accurium's database increased by 3.0% to $1,124,000. This increase reflects a median imputed investment return of 4.2% over the year.

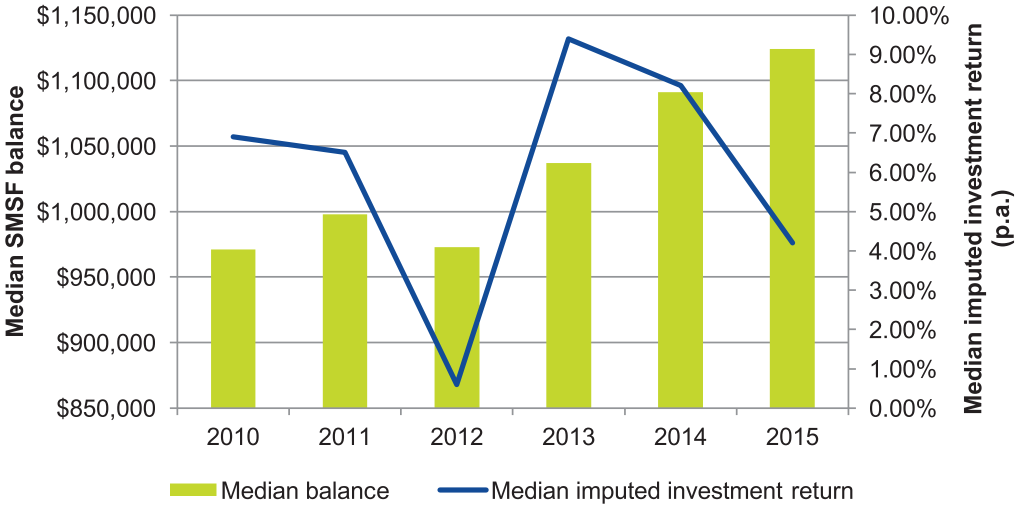
Table 1: Median SMSF balances and investment returns as at 30 June

Year ended	30 June 2010	30 June 2011	30 June 2012	30 June 2013	30 June 2014	30 June 2015
Median balance for two member SMSFs	$971,000	$998,000	$973,000	$1,037,000	$1,091,000	$1,124,000
Median imputed investment return	6.9%	6.5%	0.6%	9.4%	8.2%	4.2%

Note: Imputed investment returns are calculated net of administration expenses and gross of income tax (for further details on the methodology for calculating returns see Appendix 2). These imputed investment returns should not be used in comparisons, particularly with other superannuation sectors.

The returns, and other data in this report, are representative of SMSF trustees in or transitioning to retirement rather than the SMSF sector as a whole. These trustees may have a more conservative asset allocation to preserve capital and maintain liquidity to make pension payments, reducing their returns relative to SMSFs in accumulation phase. Additionally, the incentive of fully franked dividends paid from Australian companies creates a bias for SMSF trustees to invest in listed Australian companies. Accordingly, the imputed investment return reflects the modest performance of Australian equities as an asset class through 2015. (See Chart 11 over the page).

Chart 1: Median SMSF balances and investment returns as at 30 June



The imputed investment returns of the top 25% (i.e. upper quartile) returning SMSFs was over 7.2%. Conversely, the imputed investment returns of the bottom 25% (i.e. lower quartile) returning SMSFs was below 1.6%.

Consistent with ATO data, there is a strong correlation between SMSF balance and net investment returns, with those funds with a higher balance achieving higher returns on average. This is highlighted by the fact that the average balance of the top 25% ($2,105,000) returning SMSFs was 3.4 times higher than the bottom 25% ($624,000). This is likely to be reflective of the higher cost ratios for lower balance funds, often accentuated by set-up fees for new funds. To the extent that fund set-up and advice fees are included in the data, this is likely to understate investment returns.

How well placed are SMSF trustees for retirement?

Using the model underlying Accurium's retirement health**check**, we have estimated the levels of savings required to afford given lifestyles in retirement with differing levels of confidence. We model 2,000 economic and demographic scenarios allowing for retirees' entitlements to the Age Pension and taxes.

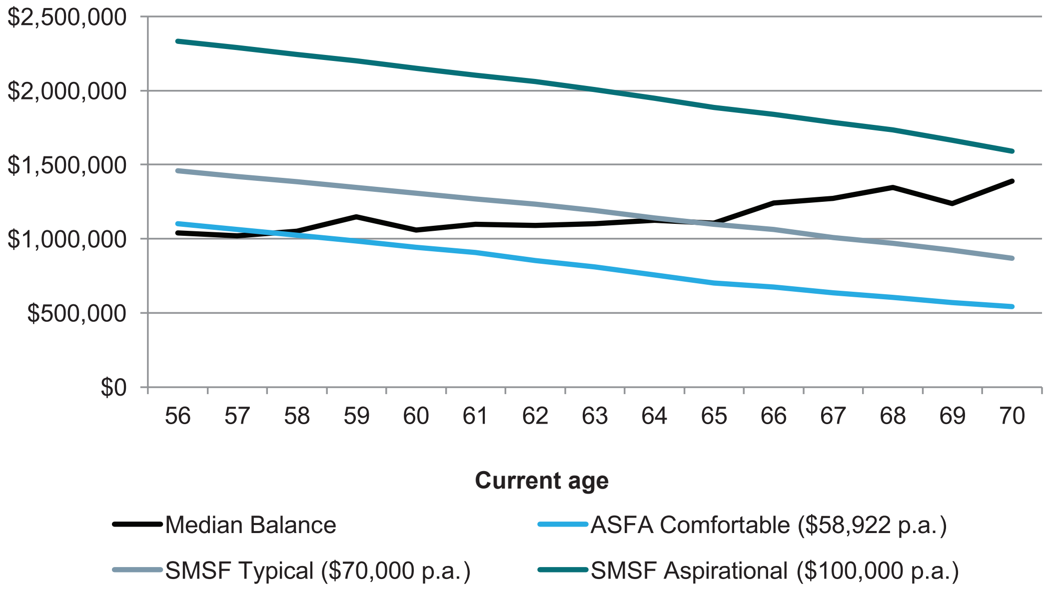
We use this modelling to calculate the levels of savings an SMSF couple would need in order to retire at different ages on the following lifestyles at both 80% and 95% confidence levels:

- the ASFA Comfortable Retirement Standard of $58,922 p.a.
- a higher standard of living more "typical" of retired SMSF couples of $70,000 p.a.
- a more "aspirational" lifestyle for SMSF couples of $100,000 p.a.

Spending levels are assumed to keep pace with inflation, and allow for changing circumstances as retirees age. Specifically, spending is assumed to reduce by 10% once retirees reach age 85 and to drop by 30% once one spouse passes away. These changing spending patterns are broadly consistent with those found in the ASFA Retirement Standards which show discretionary spending on travel and leisure reducing with age, perhaps reflecting increasing conservatism towards longevity risks. See Appendix 2 for further details on the assumptions and methodology behind this modelling.

The results are compared to the median balances as at 30 June 2015 in the two member SMSFs in Accurium's actuarial certificate database and shown in the chart below[3].

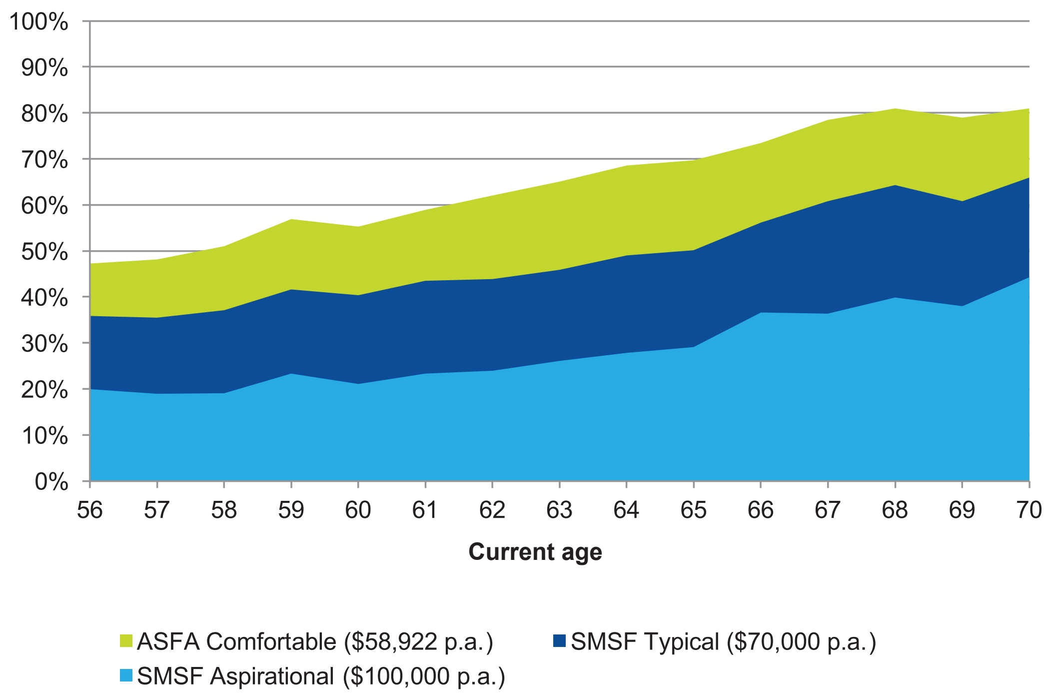
Chart 2: Savings required for different spending levels with 80% confidence vs. median SMSF balance



SMSF couples over age 57 with the median balance can be reasonably confident (80%) of affording the ASFA Comfortable Standard for life. Couples with the median balance would need to wait until age 65 before being reasonably confident of retiring on the SMSF Typical lifestyle. However, our study shows that median balances are not sufficient to support SMSF Aspirational lifestyle of $100,000 p.a., regardless of age.

The chart below shows the proportion of SMSF couples in Accurium's database with sufficient assets in their SMSFs to support these benchmark spending levels in retirement with 80% confidence.

Chart 3: Proportion of SMSF couples reasonably confident (80%) of affording different spending levels in their retirement



3 Tables containing figures in this chart are included in Appendix 1.

The results show that the majority of SMSF couples can be reasonably confident of affording a comfortable retirement, as defined by ASFA. The median balance of 65 year-old SMSF couples of $1,104,000, is significantly higher than the $702,000 in savings needed to afford the ASFA Comfortable standard for life with 80% confidence.

However, the proportion of SMSF couples who aren't in this fortunate position has increased compared to our analysis last year. The proportion of 65 year-old SMSF couples unable to afford the ASFA Comfortable standard with an 80% confidence level has increased from 25% to 30% over the year.

While ASFA's annual budget for a comfortable retirement has increased slightly over the year, changes in the market scenarios used in our modelling have had a bigger impact on the savings required. The deterioration in the global economic outlook has, on average, led to lower investment returns across the forecasts in our 2,000 market scenarios. More capital is needed today with lower expected returns to support the same level of spending over retirement.

For those with aspirations of a higher standard of living, our estimate of the amount needed to be reasonably confident of affording $100,000 p.a. in retirement from age 65 has increased to $1,886,000 from $1,769,000 last year. This means that the proportion of 65 year-old SMSF couples with sufficient assets in their SMSFs to support this lifestyle has fallen from 34% to 29%.

This reinforces the need for SMSF trustees approaching retirement to constantly evaluate their retirement plans and investment strategy to meet their desired level of income in retirement.

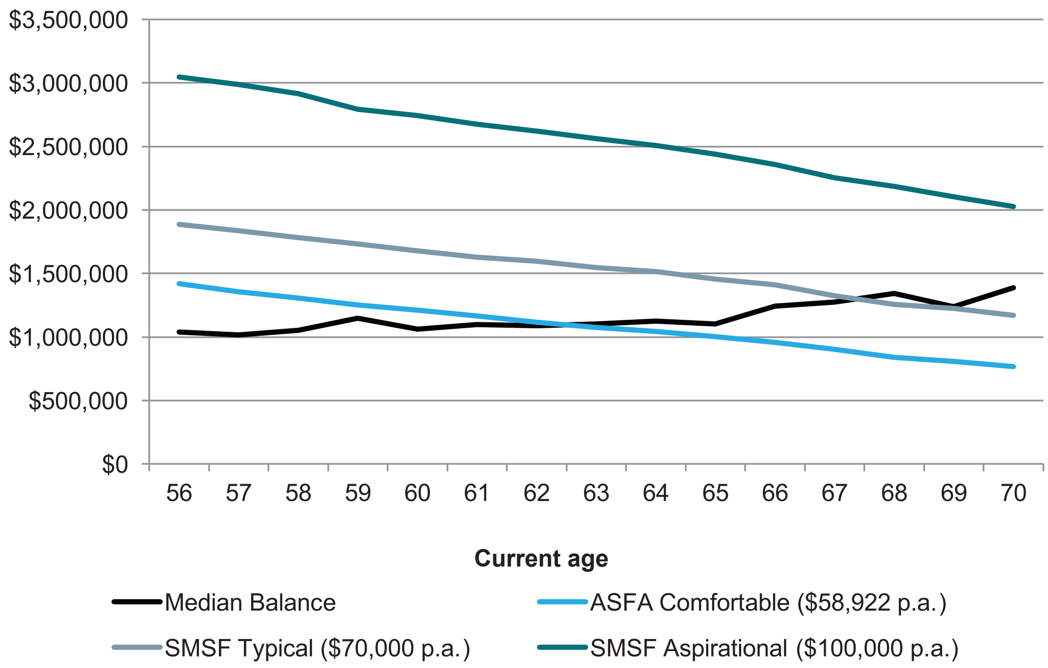
Achieving greater confidence in retirement outcomes

An 80% confidence level still leaves retirees with a one in five chance of outliving their SMSF savings. Many will want a greater degree of certainty in their retirement plans in order to achieve a real peace of mind.

The chart below shows the savings needed to achieve the same spending levels in retirement with 95% confidence. That is, the risk of running out of money is reduced to a one in twenty chance. A 65 year-old SMSF couple would need $1,002,000 in their SMSF in order to be confident of affording a comfortable retirement. The "typical" and "aspirational" SMSF lifestyles of $70,000 p.a. and $100,000 p.a. in retirement would require $1,454,000 and $2,441,000, respectively, at the same higher confidence level.

These figures show that the $1.6 million cap on assets in the retirement phase proposed in the 2016-17 Federal Budget is unlikely to have a significant impact on SMSF couples seeking a "typical" or "aspirational" lifestyle. However, it does emphasise the importance of ensuring that people have adequate opportunities, especially later in life, to contribute and build their retirement savings to these levels.

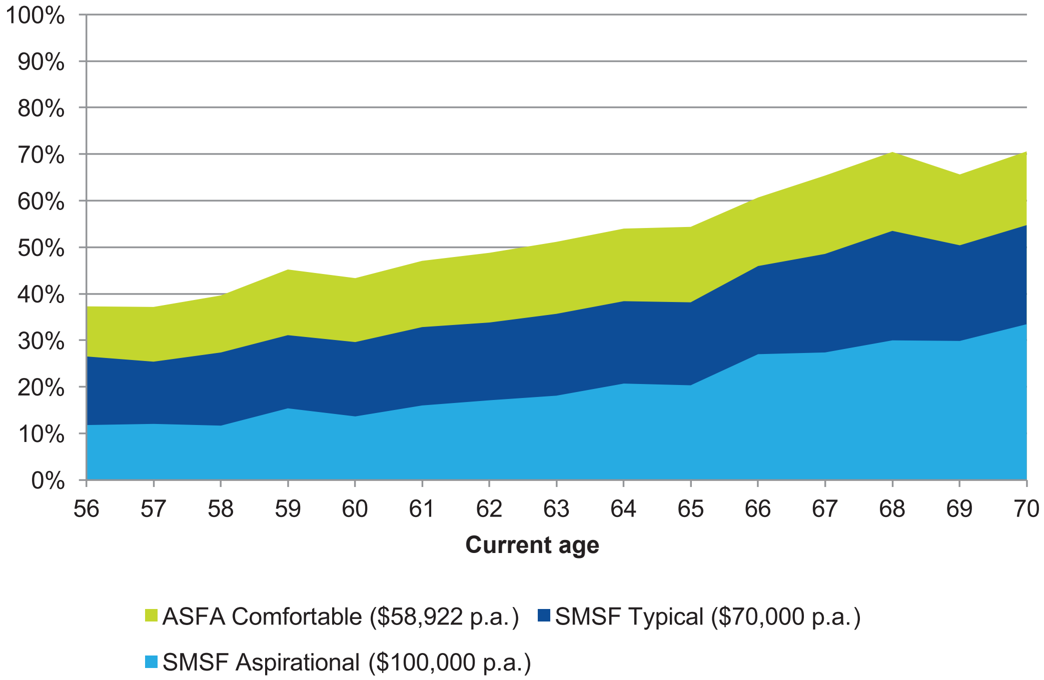
Chart 4: Savings required for different spending levels with 95% confidence vs. median SMSF balance



Clearly, greater confidence comes at a price and fewer SMSF couples have enough in their funds to provide this greater level of certainty. 54% of 65 year-old SMSF couples have sufficient balances to be able to afford a comfortable retirement with 95% confidence. 38% of 65 year-old couples can be confident of sustaining a $70,000 p.a. lifestyle and only 20% can spend $100,000 p.a. with 95% confidence.

The proportion of SMSF couples in Accurium's database with sufficient assets in their SMSFs to support these retirement lifestyles with a high level of confidence is shown in the chart below.

Chart 5: Proportion of SMSF couples very confident (95%) of affording different spending levels in their retirement



It is worth noting that the analysis above considers SMSF couples' ability to afford different benchmark lifestyles using only their SMSF balances. Many SMSF households will have significant assets outside their SMSF available to support their retirement. The analysis below looks at the full financial picture for SMSF households and whether they have the means to support their retirement plans.

What lifestyles do SMSF trustees aspire to in retirement?

So far, we have looked at SMSF trustees' ability to afford three benchmark lifestyles in retirement funded by their retirement savings. However, this does not consider SMSF households' actual retirement plans and whether they have the means to support these aspirations. For that information, we are able to analyse anonymous data collected from users of Accurium's retirement health**check**, an online tool used by SMSF practitioners to assist with retirement planning.

The following analysis considers the retirement plans and household wealth, including assets outside the SMSF, of over 1,500 SMSF households.

Desired annual spending levels

Analysis of Accurium's retirement health**check** database shows a range of desired spending levels for SMSF households in retirement. Of around 1,500 health**checks** completed to date:

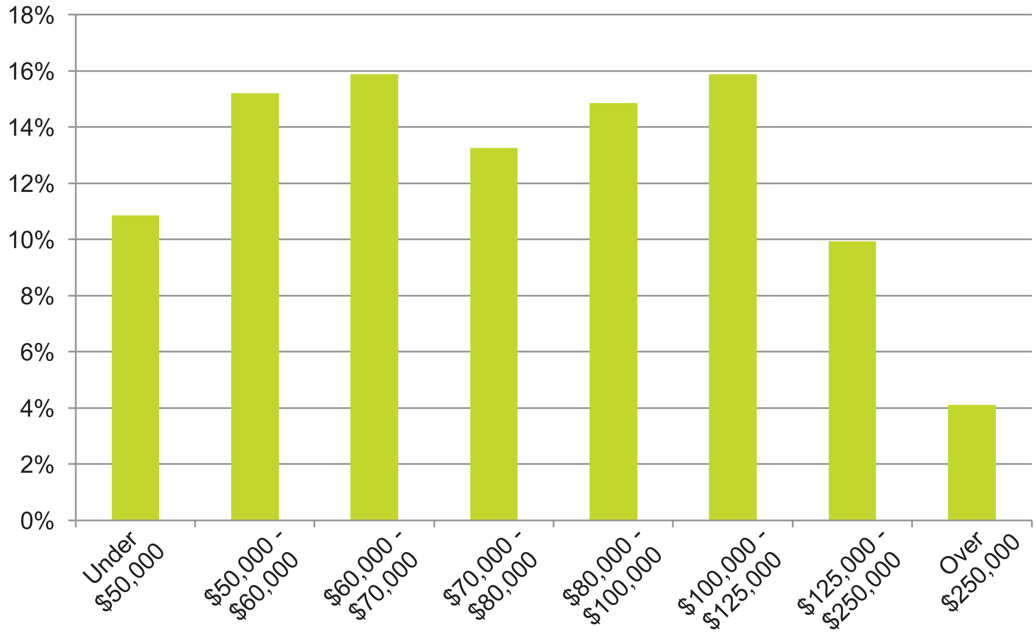
– The average desired level of spending is $92,000 p.a.

– The median desired level of spending is $75,000 p.a.

– 30% of SMSF households plan to spend over $100,000 p.a. in retirement

The median and average desired spending levels are similar to the SMSF Typical ($70,000 p.a.) and SMSF Aspirational ($100,000 p.a.) retirement benchmarks considered earlier. These could form the basis of retirement benchmarks for future analysis. The chart below shows the range of desired spending levels for retired SMSF households in our current study.

Chart 6: Desired annual spending levels of retired SMSF households



Bequests

Much has been made of wealthy retirees using their SMSFs as an estate planning tool, using the tax concessions superannuation offers to maximise the amount they can pass on to their heirs. An analysis of the actual retirement plans of SMSF households shows that:

– Only 20% of SMSF households included an explicit desire to leave an inheritance in their retirement plans.

– Of those SMSF households that did plan to leave an inheritance, the average bequest was close to $750,000.

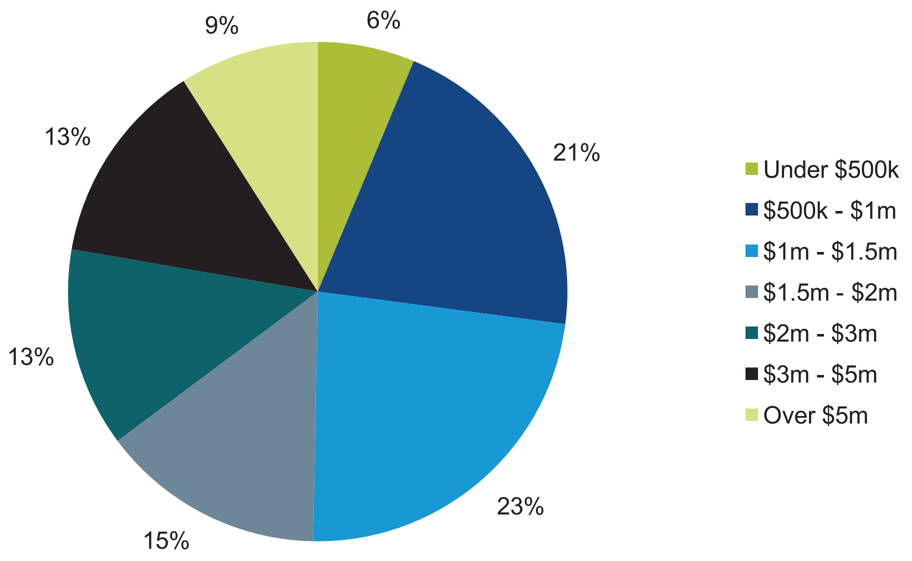
– SMSF households with total wealth of over $2m are twice as likely to wish to leave a bequest compared to those with less than $2m.

Note that these desired bequests could be paid from any household assets, not the SMSF. Changes proposed in the 2016-17 Federal Budget, such as the $1.6 million cap on assets in retirement phase and the new limit on non-concessional contributions, are likely to curb the ability of future retirees to make significant bequests through superannuation.

Total SMSF household wealth

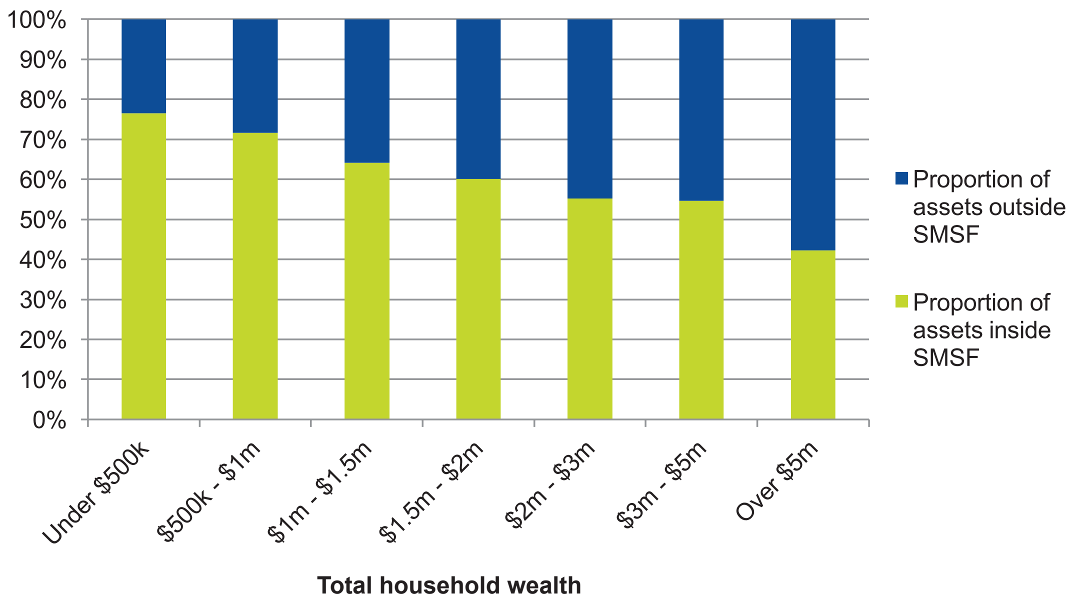
The chart below shows the distribution of total household wealth of retired SMSF households. Overall, the average total wealth of SMSF households in our study was $2.47 million and median total wealth was $1.49 million.

Chart 7: Distribution of total wealth of retired SMSF households (excluding the family home)



For many SMSF households, the savings in their SMSF are only part of their total wealth. In fact, our analysis shows that, on average, retired SMSF households have over 40% of the wealth (excluding the value of their home) outside of the SMSF. The chart below shows that, on average, the wealthier a household is, the more of their wealth they hold outside their SMSF. This suggests that the restrictions on contributions to superannuation have stopped wealthier SMSF households from transferring a higher proportion of their wealth into the low tax superannuation environment.

Chart 8: Proportion of assets inside and outside the SMSF, by total wealth



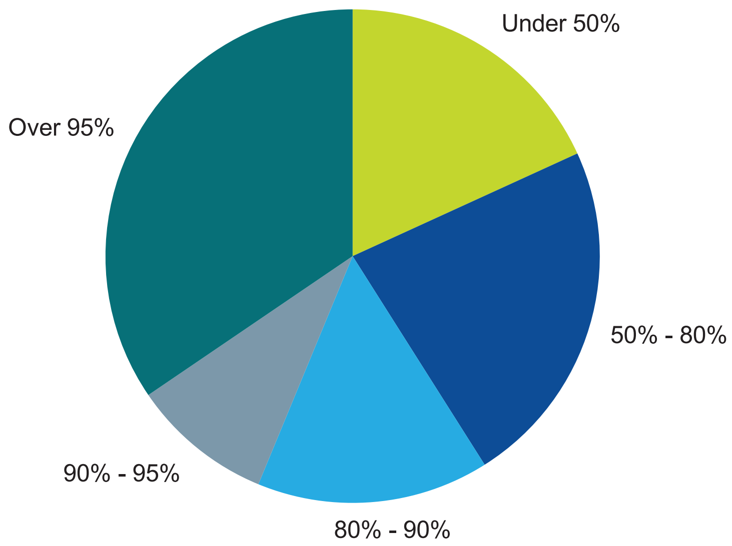
Sustainability of SMSF trustees' retirement plans

Accurium's retirement health**check** uses detailed actuarial modelling techniques to assess how sustainable SMSF retirees' actual spending plans are, given the resources at their disposal. These resources include the assets in their SMSF, investments outside the SMSF and any entitlements to the Age Pension. The result is a probability of being able to achieve their desired spending for life without outliving their savings and falling back solely on the Age Pension.

As outlined above, for retirees to be reasonably confident of sustaining their desired lifestyle in retirement we consider that they will need at least an 80% probability of not outliving their savings. To be very confident they would need at least a 95% probability of not spending all their savings and falling back on the Age Pension. Our study shows that two in five SMSF households can't be confident of achieving their desired lifestyle in retirement. On the flip side, over a third can be very confident that they won't outlive their savings.

The chart below shows the distribution of sustainability scores for SMSF households in our study.

Chart 9: Sustainability of retired SMSF households' desired spending levels (confidence in achieving desired retirement lifestyle)



Our study also found a clear correlation between wealth and sustainability. It may seem intuitive that those with more wealth are more likely to be able to sustain their desired level of spending in retirement. However, it also shows that SMSF retirees do not automatically increase their spending in line with higher levels of wealth.

The higher sustainability levels found for wealthier SMSF retirees suggests some might be able to enjoy a higher standard of living than they are currently planning, without introducing a significant risk of outliving their savings. This is perhaps reflective of the conservative nature of retirees, who may be overly conservative in their spending habits relative to their savings and income levels.

The table below shows the sustainability of SMSF households' retirement spending plans broken down by total wealth (excluding the home).

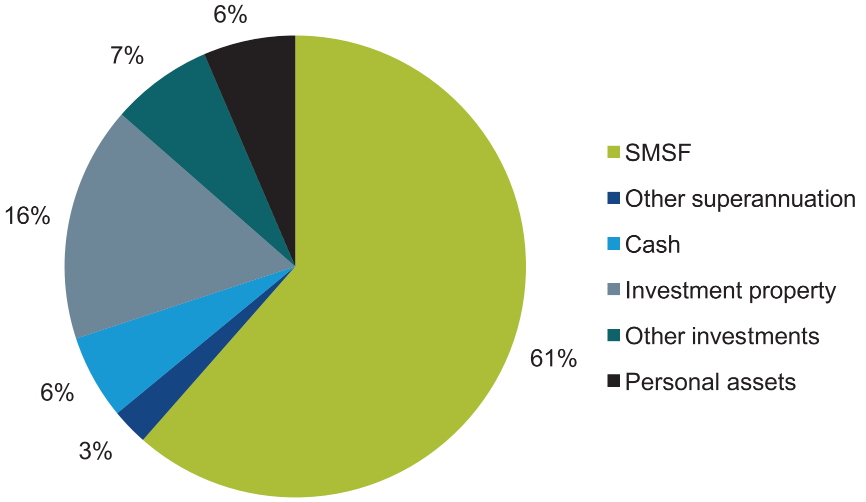
Table 2: Sustainability of spending levels by total wealth

Total wealth of SMSF household	Average probability that retirement plans will be sustainable
Under $500k	51%
$500k - $1m	66%
$1m - $1.5m	70%
$1.5m - $2m	78%
$2m - $3m	85%
$3m - $5m	85%
Over $5m	95%

SMSF household asset allocation

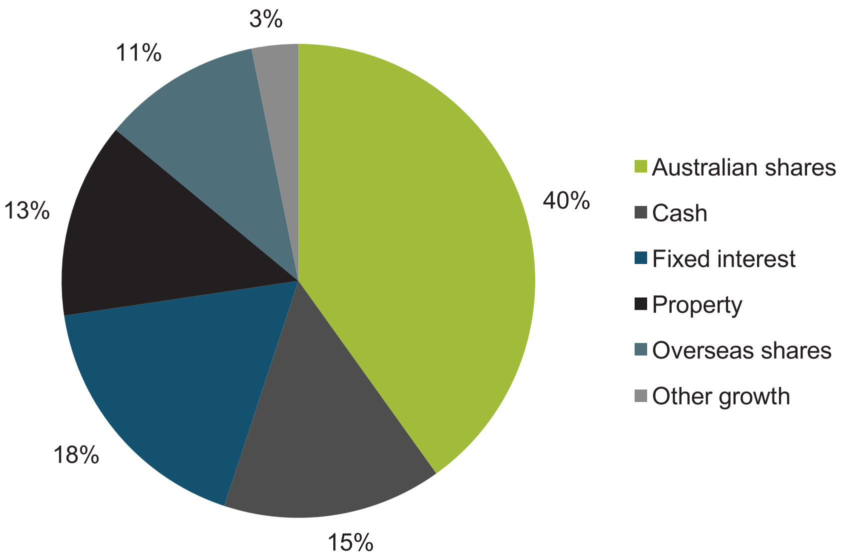
The asset allocation for overall wealth of SMSF households is shown below. It shows that property is by far the largest asset class for these households outside their SMSF, with nearly half of non-superannuation assets invested in property (excluding the family home).

Chart 10: Overall asset allocation retired SMSF households (excluding the family home)



The chart below looks at the average asset allocation within the SMSF, as provided by retirement health**check** users.

Chart 11: Average SMSF asset allocation



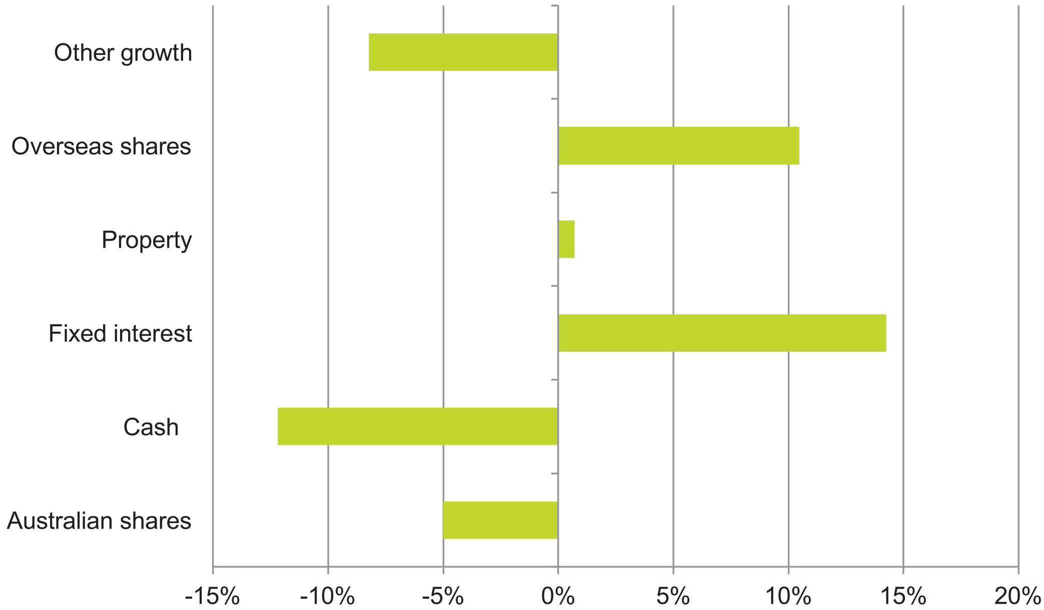
As shown above, our study confirms the preference for Australian equities found in other surveys and in ATO data[4], with 40% of assets held in this asset class.

4 ATO: Self-managed super funds: A statistical overview 2013-14.Table 16: Asset allocations by fund phase (2014), pension phase.

ATO statistics have generally shown SMSFs have a high allocation to cash, with minimal investment in bonds. However, the cohort of retirees in our study has a significantly lower allocation to cash and a correspondingly higher allocation to fixed interest assets. One possible reason for this difference is that a higher proportion of SMSF trustees in this study take financial advice on their investments. Financial planners typically include some allocation to fixed interest in their model portfolios.

Another notable difference between ATO data and the findings of this study is the allocation to international equites, which is also significantly higher in our study. This might be a reflection of how SMSF investors access international equities and how the ATO classifies these investments. Investments in international equities made via managed funds or exchange-traded funds (ETFs) are not classed as international equities in the ATO data.

Chart 12: Difference between asset allocation in Accurium database and ATO pension phase average[5]



5 Compares asset allocation of SMSFs in Accurium's database with those found in the ATO's statisitics, Self-managed super funds: A statistical overview 2013-14.Table 16: Asset allocations by fund phase (2014), pension phase.

Proposed changes in 2016-17 Budget

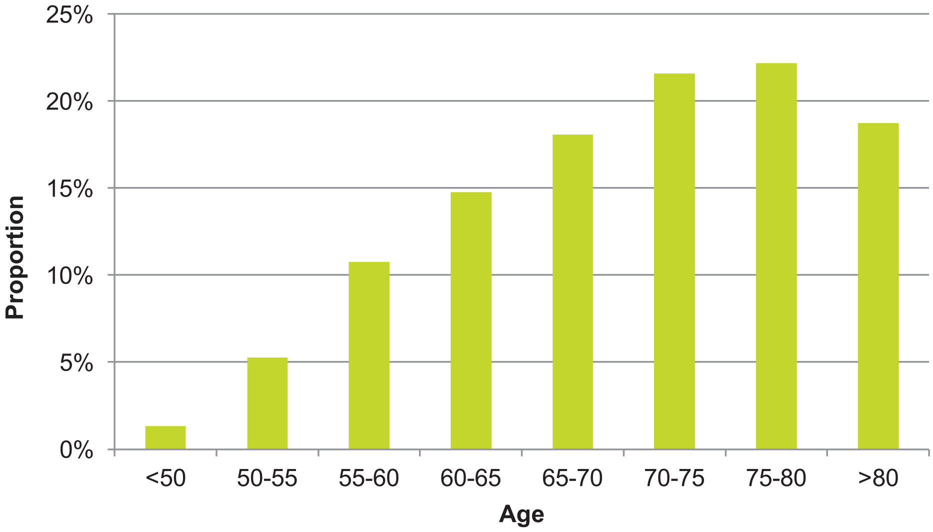
The 2016-17 Federal Budget proposed far-reaching changes to the superannuation system designed to make the system 'fairer' and reduce tax concessions for wealthier superannuants. Below we have analysed some of the key measures and their likely impact on SMSF trustees.

$1.6m retirement transfer balance cap

The Government has proposed a limit of $1.6 million on the amount that can be transferred to the tax-free retirement phase.

The analysis below shows the proportion of SMSF trustees in Accurium's database of over 110,000 members who currently have balances over $1.6m and are likely to be affected by these proposals.

Chart 13: Proportion of SMSF trustees with balances greater than $1.6m



Overall, 19% of SMSF trustees over age 65 in Accurium's database had total balances in excess of $1.6 million as at 30 June 2015. Should the transfer cap be legislated, many of these retirees will be faced with the choice of rolling back a proportion of their pension accounts to accumulation and paying tax on the earnings or withdrawing the excess from their funds altogether.

The retirement adequacy analysis in section 4 considers SMSF couples, whereas the proposed transfer cap applies at an individual level. Between them, a couple can start tax-free pensions with a combined balance of up to $3.2 million. This allows couples as young as age 56 with the required $3.0m to retire on $100,000 p.a. with a high level of confidence without breaching the cap, provided their savings can be balanced across their accounts. It is worth noting, however, that the reduced contribution caps also proposed in the budget may make equalising balances between couples more difficult.

Around 8% of two member SMSFs in the Accurium database have both members with balances over the $1.6 million cap. Of those funds with one member over the cap, the average balance of the second member is around $820,000, leaving room for re-balancing if the proposed rules around contributions caps will allow.

The following case study highlights the potential impact of the proposed transfer cap on retirement adequacy:

Case study 1	
Age	65
Sex	Single Male
SMSF balance	$2,500,000
Asset allocation in SMSF	In line with ATO average for SMSFs in pension phase
Assets outside SMSF (excluding family home)	$1,000,000
Asset allocation outside SMSF	50% growth, 50% defensive

Using Accurium's retirement health**check**, we have estimated the impact of the transfer cap on the above retirees' retirement spending plans.

	Current rules	With $1.6 million transfer cap (assuming excess is withdrawn and invested outside super)	With $1.6 million transfer cap (assuming excess remains in SMSF and earnings taxed at 15%)
Spending affordable for life with 80% confidence	$177,000 pa	$166,000 pa	$173,000 pa
Spending affordable for life with 95% confidence	$136,000 pa	$128,000 pa	$132,000 pa

In the above example, keeping the excess over $1.6 million in accumulation phase in the SMSF is likely to prove more beneficial than withdrawing it from superannuation altogether and being taxed at marginal rates. Indeed, in this example, the retirees' sustainable spending level in retirement only fell by 2-3%.

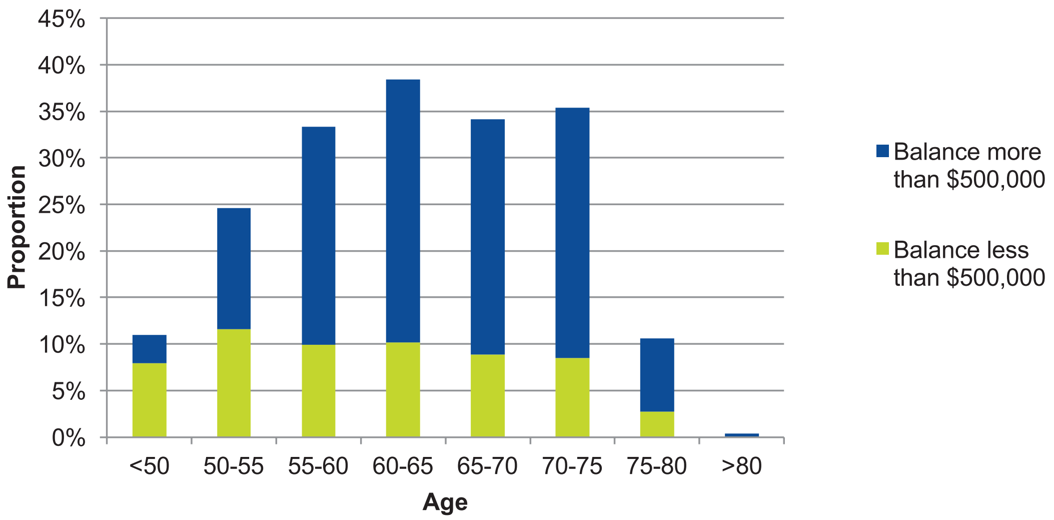
This suggests that SMSFs will remain an attractive vehicle for retirement savings even for Australians with significant retirement savings.

Concessional contributions cap reduced to $25,000
The Budget proposed reducing the concessional contributions cap to $25,000 a year for all ages up to 75 from 1 July 2017. Currently, the caps are $30,000 a year for those under 50 and $35,000 a year for those over 50. The proposals will also allow the use of unutilised caps from the previous five years for those with balances under $500,000.

Accurium's database shows that 57% of SMSF trustees made concessional contributions to their fund in 2015, with 31% contributing more than $25,000. Of those making contributions over $25,000, over 70% already had balances above $500,000 and therefore wouldn't be able to make use of the 5-year 'look back' rule if introduced.

The chart below shows the proportion of SMSF trustees in Accurium's database making concessional contributions in excess of $25,000 in 2015 by age. It also highlights the proportion with balances in their SMSFs in excess of $500,000.

Chart 14: Proportion of SMSF trustees making more than $25,000 in concessional contributions in 2015



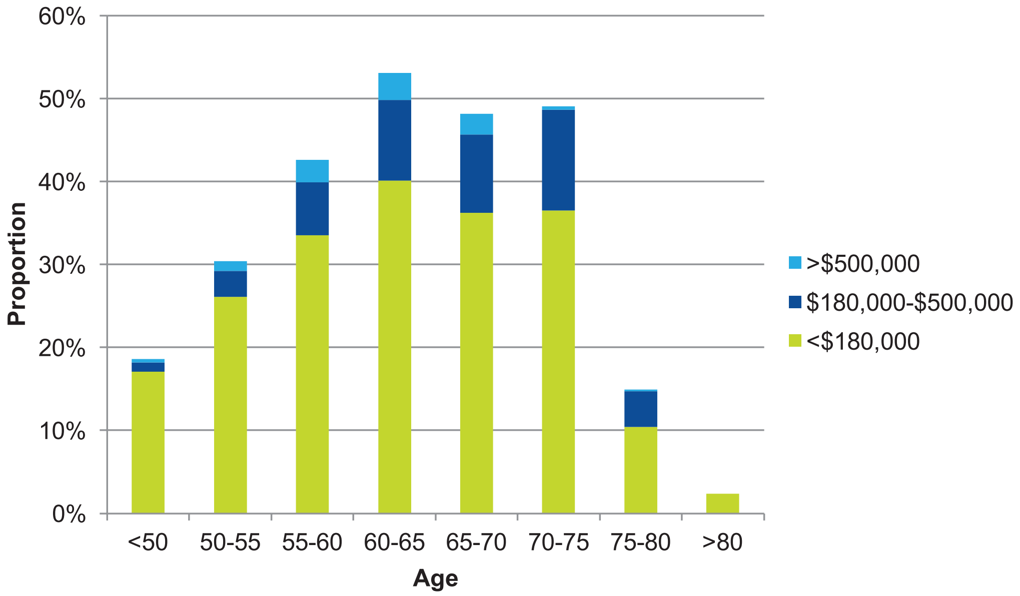
Non-concessional lifetime cap of $500,000

Another pillar of the 2016-17 Budget's superannuation reforms is imposing a lifetime cap on non-concessional contributions of $500,000. The cap is proposed to take effect from 3 May 2016 once implemented and will include all non-concessional contributions made since 1 July 2007. Individuals who have already exceeded the $500,000 lifetime cap will not be penalised, however, they will be unable to make additional non-concessional contributions.

Analysis of Accurium's database can be used as a proxy for the proportion of SMSF trustees likely to be impacted by the cap. However, without records going back to 2007 for all trustees, it is difficult to do so accurately.

The chart below shows the proportion of trustees making different levels of non-concessional contributions at different ages. Overall, 43% of trustees made a non-concessional contribution in the 2015 financial year. Around 10% of trustees made use of the three-year 'bring forward' rule to make contributions in excess of the current annual $180,000 cap. Very few made contributions in excess of $500,000 in a single year.

Chart 15: Proportion of SMSF trustees making non-concessional contributions in 2015



Removal of tax exemption on transition to retirement (TTR) pensions

TTR pensions allow those over their preservation age who have not otherwise met a condition of release (e.g. retiring) to access their superannuation in the form of an income stream. Currently, earnings on the assets supporting TTR pensions and withdrawals for those aged 60 and over are tax free. TTR pensions have proved very popular with SMSF trustees looking to maximise their superannuation balances as they move towards retirement.

The 2016-17 Budget proposed removing the tax exemption on earnings on TTR pensions with effect from 1 July 2017. Our analysis suggests that around 25% of the SMSF trustees in Accurium's database were using TTR pensions[6] in 2015. However, Accurium's database has a higher proportion of SMSF trustees in the TTR pension age range than the SMSF population as a whole.

The Government has suggested that around 80,000 SMSF trustees are currently using TTR pensions and are likely to be impacted by the proposed changes. Our analysis broadly agrees with this figure.

However, it is worth noting that the legislated increases in preservation ages over the next 8 years will, over time, result in fewer people being eligible for TTR pensions. The preservation age for 2014-2015 was 55 and increased to 56 for 2015-2016. It is legislated to increase to age 60 on 1 July 2024.

6 Note: Accurium's database does not include details on account-based pension types. This analysis is based on SMSF trustees receiving pensions and also making concessional contributions to their fund during the year.

Conclusions

Our research shows that most SMSF trustees remain well placed for a comfortable retirement, despite lower than average returns in 2015 and a less favourable economic outlook. In fact, many can be confident of spending more in their old age.

However, our research suggests that they may not be able to afford the higher levels of retirement spending they are hoping for. We have found that a significant proportion of SMSF households' retirement spending plans are unlikely to be sustainable. This presents a real opportunity for those advising SMSF trustees to help them before and during retirement. Decisions around how much to spend each in year in retirement, how essential expenditure will be met and how to adjust asset allocations in response to potentially lower yielding markets are the most important part of any retirement plan. It is in this area where SMSF practitioners can provide real value to their retiring and retired clients..

Our analysis also shows that SMSF trustees are likely to bear the brunt of the government's proposed changes to superannuation. While the government has estimated that only 4% of the population will be impacted by the changes, a very significant proportion of these will be SMSF trustees. Indeed, were the policies in place in 2015, over 48% of the SMSF trustees in Accurium's database would have been impacted by at least one of the changes.

However, even with these changes, our view is that superannuation remains the best vehicle for saving for and providing income in retirement. We firmly believe that for those looking to take control of their superannuation, SMSFs will continue to be a popular option.

Appendix 1 – Data tables

The figures behind many of the charts presented in this paper are provided below for reference.

Table 3: Savings needed to support ASFA Comfortable ($58,922 p.a.) in retirement with differing levels of confidence vs. median balance

Couple's age	Median balances for two member SMSFs ($)	Savings needed with 80% confidence	Savings needed with 95% confidence
56	1,039,000	1,100,000	1,419,000
57	1,018,000	1,063,000	1,357,000
58	1,051,000	1,023,000	1,306,000
59	1,148,000	986,000	1,253,000
60	1,060,000	944,000	1,210,000
61	1,099,000	906,000	1,166,000
62	1,088,000	852,000	1,117,000
63	1,103,000	809,000	1,074,000
64	1,125,000	754,000	1,042,000
65	1,104,000	702,000	1,002,000
66	1,242,000	676,000	956,000
67	1,273,000	635,000	903,000
68	1,345,000	606,000	840,000
69	1,239,000	570,000	809,000
70	1,390,000	543,000	766,000

Table 4: Savings needed to support SMSF Typical ($70,000 p.a.) in retirement with differing levels of confidence vs. median balance

Couple's age	Median balances for two member SMSFs ($)	Savings needed with 80% confidence	Savings needed with 95% confidence
56	1,039,000	1,460,000	1,886,000
57	1,018,000	1,421,000	1,837,000
58	1,051,000	1,386,000	1,784,000
59	1,148,000	1,346,000	1,734,000
60	1,060,000	1,309,000	1,680,000
61	1,099,000	1,270,000	1,630,000
62	1,088,000	1,232,000	1,596,000
63	1,103,000	1,190,000	1,545,000
64	1,125,000	1,140,000	1,515,000
65	1,104,000	1,099,000	1,454,000
66	1,242,000	1,064,000	1,410,000
67	1,273,000	1,009,000	1,325,000
68	1,345,000	971,000	1,256,000
69	1,239,000	924,000	1,224,000
70	1,390,000	868,000	1,170,000

Table 5: Savings needed to support the SMSF Aspirational retirement benchmark of $100,000 p.a.

Couple's age	Median balances for two member SMSFs ($)	Savings needed with 80% confidence	Savings needed with 95% confidence
56	1,039,000	2,332,000	3,045,000
57	1,018,000	2,290,000	2,989,000
58	1,051,000	2,242,000	2,916,000
59	1,148,000	2,200,000	2,792,000
60	1,060,000	2,149,000	2,744,000
61	1,099,000	2,104,000	2,674,000
62	1,088,000	2,062,000	2,619,000
63	1,103,000	2,007,000	2,562,000
64	1,125,000	1,949,000	2,505,000
65	1,104,000	1,886,000	2,441,000
66	1,242,000	1,839,000	2,358,000
67	1,273,000	1,785,000	2,254,000
68	1,345,000	1,734,000	2,186,000
69	1,239,000	1,665,000	2,106,000
70	1,390,000	1,591,000	2,027,000

Appendix 2 – Methodology and assumptions

Imputed investment return methodology

Imputed SMSF investment returns presented in this paper are based on financial information provided to Accurium with the application for an actuarial certificate. As such, the imputed investment return is calculated net of fund expenses, but before allowance for any income tax that may be payable (or tax refunds such as imputation credits). Member cash flows are allowed for in the return calculations to the extent that they have been included in the data provided to us. Fund expenses include administration costs and levies, professional fees and may also include life insurance premiums paid by the fund (which would not ordinarily be regarded as reducing investment returns). This means that the median imputed investment return might by very slightly lower than the actual investment return.

There are two other factors that should be taken into account in drawing conclusions from the imputed investment returns in this paper:

- the dataset of funds is restricted to SMSFs that need an actuarial certificate. This means they are partially in the retirement phase and might have a different asset allocation from a typical accumulation fund; and
- after-tax returns might actually be higher for SMSFs receiving substantial franking credits.

Note that care must be taken when using these imputed investment returns, particularly when making comparisons with other investment return data, particularly from other superannuation sectors. For example, both the data collected and the methodology used are different from that used by APRA to estimate returns on assets for APRA-regulated superannuation funds. Appendix 2 to the ATO's *'Self-managed super funds: A statistical overview 2013-2014'* explains a number of the data limitations and differences in methodologies that affect comparisons of SMSFs with non-SMSF sectors.

It should also be noted that the 2013 financial year was the first year in which SMSFs were required to value all assets at market value in their accounts.[7] It is not known to what extent this will have affected SMSF balances in that year.[8]

7 Regulation 8.02B of the Superannuation Industry (Supervision) Regulations 1994.
8 For a more comprehensive discussion of the differences in investment performance reporting across the industry, see Appendix 1 to the 2010 report by Industry Super Network (now ISA) entitled: 'Towards full and transparent reporting of investment returns in super'.
9 Investment Trends: 2014 Retirement Income Report.

Modelling methodology

Accurium provides actuarial services for over 65,000 SMSFs. This uniquely positions us to develop insights into how well prepared SMSF trustees are for retirement.

The analysis is based on the outputs of Accurium's Retirement Adequacy Model, which uses stochastic modelling, instead of a deterministic modelling approach often used in retirement financial planning. Deterministic modelling is convenient and relatively simple because it assigns assumed, fixed values to random variables like expected share market returns and individual life expectancy. Deterministic models often employ mean or median values as 'averages' for reasons of intuitive appeal. However, this approach is inherently flawed, because by definition, the majority of outcomes will not reflect these assumptions. Surveys show[9] that retirees are left with understandable concerns around outliving their savings.

Stochastic (or probabilistic) modelling doesn't assume fixed values for key unknown variables. Instead, it accepts uncertainty and computes thousands of possible scenarios using a range of values for each variable, and in doing so can ascribe probabilities or confidence intervals to each outcome. Where a deterministic model will posit an 'average' output based on 'average' inputs, a stochastic model can calculate the probability of achieving a given output and therefore allows retirees to make informed decisions that take into account risk.

Accurium's Retirement Adequacy Model incorporates variables in investment returns, inflation rates, Age Pension payments and retiree lifespans. We have forecast typical SMSF trustee couples through 2,000 'what if' scenarios for each of these variables. Each scenario demonstrates a different series of possible market returns, inflation rates and lifespans. For the calculations in this paper, the assumed investment mix used is based on the average for SMSFs in pension phase published by the ATO.

Modelling assumptions

Some of the key things to note about the calculations underlying the tables in this paper are:

- Spending is assumed to increase with inflation each year in retirement except:
  - When retirees reach age 85 spending is assumed to reduce by 10%. This reduction is in line with that found in the ASFA Retirement Standards that show that spending on travel and leisure reduces with age, partially offset by an increase in medical costs.
  - When the first spouse in the couple passes away spending is assumed to reduce by 30% to reflect lower living costs for single people.
- No explicit allowance is made for aged care costs. However, it is assumed that retirees do not sell or downsize their home. Anecdotally, the family home is often relied upon for meeting significant residential aged care costs that can sometimes arise in later life.
- When calculating the probability of being able to sustain a particular standard of living for life, we assume that all capital is available to be used to support that level of spending (there is no minimum bequest requirement).
- The statistics used to generate longevity scenarios are based on the 2010-12 Australian Life Tables published by the Australian Government Actuary. We also allow for the 25-year mortality improvement rates from the same publication.
- On the death of one spouse, all assets and superannuation are assumed to transfer to the surviving spouse.
- The investment returns and rates of inflation used to calculate the statistics have been generated by Willis Towers Watson using their Global Asset Model.
- The assumed investment mix is based on the average for SMSFs as published by the ATO. We assume the SMSF investment mix is regularly rebalanced throughout retirement and an allowance is made for fund expenses.
- Tax on non-superannuation investment returns is modelled; including the senior Australians tax offset (SATO) rules and Medicare Levy.
- The Age Pension is allowed for using Centrelink means testing rules i.e. we assume the person is eligible based on residency rules. On 22 June 2015, legislation was passed that alters the Age Pension assets test with effect from 1 January 2017. Our projections allow for these new rules to apply from 1 January 2017.

Other, more detailed, points to note include:

- The Minimum Pension Standards, as required under the Superannuation Industry (Supervision) Regulations, are allowed for. If the minimum pension payment in any particular year exceeds the household's spending, then this is added to the household's non-superannuation assets.
- SMSF pensions are assumed to be subject to the Centrelink deeming rules, rather than grandfathering rules (i.e. they are assumed to have commenced on or after 1 January 2015).
- All tax and Centrelink rates, bands and thresholds used are those current as at 1 June 2016. All future payment rates, bands and thresholds are assumed to change in line with inflation each year.
- We have allowed for the following asset mix in line with the ATO average for SMSFs in pension phase:
  - Cash 27.2%
  - Fixed interest 2.1%
  - Property 13.9%
  - Australian shares 45.0%
  - Overseas shares 0.4%
  - Other growth 11.4%
- We have allowed for the following fees and charges:
  - SMSF administrative fees of $2,500 per annum
  - Investment management charges within the SMSF of:
    - Cash 0% p.a.
    - Fixed interest 0.5% p.a.
    - Property 0.8% p.a.
    - Australian shares 0.5% p.a.
    - Overseas shares 1.0% p.a.
    - Other growth 0.5% p.a.
  - Investment management charges on non-superannuation assets of:
    - Cash 0% p.a.
    - Other assets 0.5% p.a.

Notes

Notes

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