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# Is an SMSF right for you?

If you're reading this book, you're probably wondering whether a self managed super fund (SMSF) can offer you benefits your current super fund can't. You may have heard about the growth of the SMSF sector and be wondering why so many Australians have a self managed super fund. But how do you know if an SMSF is right for you?

## What is an SMSF?

An SMSF is a special entity that holds your superannuation savings. Compared with other super funds, an SMSF is a small super fund that you run yourself. You can have up to three other people in the fund with you and, together, the four of you look after your own retirement savings.

## What are the benefits of self managed super?

An SMSF offers many benefits. By offering unparalleled investment choice, control, transparency and flexibility, SMSFs can provide a big boost to your retirement savings.

### *More investment options*

As the name suggests, with an SMSF you manage your own investments, and the options are nearly endless. You choose your cash accounts, select the individual shares you want to invest in or purchase the investment property you want. You take control of the investment strategy for your super.

In an industry fund, you might be limited to 10 to 15 options, ranging from investing in 100 per cent cash to a highly aggressive option, with higher risk, like 100 per cent shares. Retail funds offer a similar range of investment types to industry funds, but significantly more options within that scope. In either type you simply choose an investment option by ticking a box on a form. Although you may know broadly what you are invested in, such as 100 per cent shares, you have no say over the underlying investments, such as what companies the money is invested in, or whether the money is invested directly in shares or through managed funds. Your self managed fund will give you this transparency and control.

## *Investment control*

The control offered by an SMSF has many advantages. You're able to adapt your investment strategy to suit your circumstances and your preferences.

If market conditions change, you will be able to quickly make investment decisions in response. You can change your SMSF's share portfolio immediately by selling or buying shares on the stock exchange. The additional administrative requirements of other funds mean this process may take much longer and may expose you to a greater amount of risk as the market moves.

If you need to free up some cash in your SMSF for tax or investment purposes, you will be able to select the most appropriate assets to sell. You can defer selling investments until a time when it may be more tax effective, such as after starting a pension in retirement. Working out the long-term potential of each investment is still very important. Considering the tax implications will help you with investment decisions.

Retail or industry super funds generally don't give you this flexibility. The underlying investments in their investment options are usually pooled together so you don't have the scope to select specific investments and manage your tax liabilities in this way.

### *Fee transparency*

Transparency is also evident in the fees. You will know exactly what your SMSF administrator or accountant charges to prepare the fund's tax return and financial statements. If you get help with investment advice, you will know what the brokerage costs or your adviser's annual fees are. You won't have to search through account statements or call up your fund to work out all the hidden costs. Your fund doesn't have to be subject to fees based on the size of your super balance. You can pay set fees, even if your balance grows.

### *General flexibility*

Self managed funds are flexible. You're able to quickly amend your fund's trust deed if the government changes the superannuation rules. Larger funds find it more cumbersome to change and adapt their procedures.

How about insurance? Why be limited to the one insurer and one fee structure offered through your existing fund? Within your SMSF, you can compare premiums and types of cover across all insurers in the marketplace and choose the best option for you (see chapter 8).

> **Did you know?**
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> Life insurance is commonly held inside an SMSF as the premiums are tax deductible (see chapter 8 for a more detailed discussion).

Once you reach pension age the benefits of an SMSF only get better. Starting a pension account is generally very tax effective. What if you need to start another pension account? And then another shortly after? With other types of funds, this can mean selling and re-buying assets several times. You will need new account numbers, and there may be countless forms to fill in. It could take weeks to finalise each pension account. For an SMSF, this involves some simple paperwork that can be completed very quickly.

The whole family can benefit from an SMSF. Your children can be members. You may also find they become more interested in super or investing due to their involvement. Passing your wealth to your loved ones in the most tax-effective way and other estate planning strategies can also be easily managed.

These are just some of the benefits of self managed super, and we'll explore them in more detail throughout this book.

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## Why I have an SMSF

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The more you learn about investing the more you realise that it's not a one-size-fits-all proposition. Every investor has a different set of requirements and these are not constant.

With an SMSF you are in control and you have a responsive investment vehicle. You can adjust your investing strategies according to your own changing circumstances.

You can access and adjust your portfolio at any time. No other form of superannuation can match these advantages.

***Max Walsh***
*Leading business, economics and political commentator*
*Deputy Chairman of Dixon Advisory*

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## Do you need to be a superannuation expert to run an SMSF?

This is one of the most commonly asked questions. The simple answer is 'No'. Look at the numbers. According to APRA, in January 2011 about 32 per cent of Australia's total superannuation assets were held in SMSFs, which now represent the largest sector of the market. In June 2011, the ATO reported that the number of self managed super funds grew by 7.7 per cent during 2010–11, and SMSFs have more than 867 000 members. Would you expect all of these people to be super experts? It's unlikely.

Becoming the controller, or trustee, of an SMSF brings additional roles and responsibilities. In an industry or retail fund, a board of trustees generally controls the fund. They are responsible for monitoring investment decisions, ensuring legal compliance, meeting reporting requirements and the general operations of the fund. In your SMSF, you become that board, on a smaller scale. It's your responsibility as a trustee to take on these roles and comply with all the requirements of running a superannuation fund.

So how can so many people handle this level of responsibility?

Some try to go it alone, but most people who run SMSFs rely on professional assistance. Some of the service providers available to help you run an SMSF include accountants, dedicated self managed super administration firms, and financial and investment advisers.

Identifying the services you need and paying only for these is the key to good management. Perhaps you have the knowledge and skills to manage your fund's investment portfolio, but you need help to complete the paperwork and end-of-year tax return. Maybe you don't have the time to run your own SMSF, and want an administrator to take care of all the details for you.

Is there extra work involved? Yes, but the real question is how much extra work is involved. And that depends on who is helping you.

Only a handful of Australians would have self managed super funds if they had to draw up all the legal documents, complete the end-of-year tax return and financial statements, make all the investment decisions and implement all the tax-planning strategies on their own.

That's where your choice of service provider can make a real difference. No matter which provider you use or what level of assistance you receive, you will still be involved in the decisions in all these matters and that will generally give you greater overall control of your super than you would have with an industry or retail fund.

For most people, superannuation is the largest, or second largest asset, behind the family home. So if you're attracted by the possible benefits of an SMSF, the extra work may be worth it.

## How do SMSFs compare with other funds on fees?

Comparing fees within the superannuation industry is not an easy matter. Administration fees, contribution fees, management expense ratios, adviser commissions and entry/exit fees are some of the expenses that may be difficult to identify, let alone compare.

> **Tip**
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> Phone your existing super funds and ask them to list all the fees that apply to your account. The member statements you receive are unlikely to outline all the fees you are currently paying.

### *What are the other funds charging?*

Industry funds boast a simple fee structure. They're able to keep their fees low by limiting their investment options, reducing reporting facilities and streamlining a lot of their processes. You will probably be looking at a fee range of between 0.5 per cent and 1 per cent of your total balance each year, depending on the investment option you choose.

Understanding retail fund fees is generally more difficult. There may be underlying commissions, costs in switching between investment options and performance fees. But you usually have extra benefits in a retail fund over an industry fund, including more diversity of investment options, better reporting facilities, potentially greater access to insurance options and the support of a financial adviser. The fees will generally be significantly higher than an industry fund for these added benefits. You might be looking at an annual fee range of 1 per cent to 2.5 per cent of your super balance. Your investment option will again be a significant factor.

Employer-sponsored funds sit between industry and retail funds. They're generally set up by organisations that want to help their employees manage their superannuation while improving the efficiency of their internal payroll processes. They can offer the advantages of a retail fund at a cost similar to an industry fund, as they're usually established by an agreement between the employer and a large fund operator. That's until the employee leaves the company, and then the fund operator's normal fees and options will usually apply.

Defined benefit funds, which are less common and mostly closed to new members, were set up by governments or large organisations, and generally have low in-built fees. Fees are not easily comparable because the employee's benefit is calculated using a set formula rather than being based on contributions and earnings. If you have defined benefit super, it's unlikely you would be better off changing funds. However, if you want to salary sacrifice and start pensions, it may be worthwhile considering an SMSF in addition to your defined benefit fund to assist you with these strategies.

## *How do SMSFs compare?*

Answering this question depends on the size of your super balance and what services you need from SMSF professionals.

It's generally advisable to have a minimum balance of between \$150 000 and \$200 000 to start a self managed super fund. If you're paying a set fee for professional services, your overall costs as a percentage will reduce as your super balance grows. Say you are being charged $5000 by a service provider to administer your fund. If your balance was $500 000 this would represent a 1 per cent fee. If your balance increased to $625 000, your fee as a percentage of your balance would reduce to 0.8 per cent. This often makes SMSFs more favourable than other types of funds that charge fees on the basis of a percentage of assets managed.

But it's not the only factor to consider. Self managed super funds can have up to four members. Your overall fees may be reduced significantly if you're pooling your family's super balances. You may also save on insurance fees by being able to choose from a range of providers. Depending on your knowledge and expertise, you may also be able to reduce the level of professional assistance you need. Alternatively, the benefits to your returns of using expert advisers may actually outweigh the higher annual cost. We will discuss these issues at length later on.

## Is it worth swapping your current super solution for an SMSF?

You don't need to have a complicated financial situation to benefit from self managed super. Even people with the simplest financial affairs can benefit from an SMSF.

Consider a common strategy of investing either a proportion or the entire balance of your super in cash. An SMSF will allow you to do this with greater choice and flexibility. You can select the highest yielding term deposit or at-call cash account you can find, and you will know exactly what it will earn. This return is likely to be much higher than you would get on the cash option chosen for you by an industry or retail fund. As a test, compare the cash return of your current fund over the past year with term deposit rates over the same time period.

Perhaps you're living off a small to medium-sized pension from your super fund as well as a partial Age Pension. Managing your super fund withdrawals and your partner's situation within an SMSF in a strategic way can help you increase your fortnightly government benefit. We will look at this further in chapter 7.

You may feel comfortable in your current superannuation fund and not see the need to change. Just because your current super choice is familiar or appears cost-effective, don't discount other alternatives that may provide a better result. A benefit of a self managed super fund is the many tax-saving strategies available. It's possible you're missing out on these.

Are you over pension age, making additional contributions to super or wanting to protect your wealth for beneficiaries? If you fall into any or all of these categories, your current super solution may not be working hard enough for you, and an SMSF may offer you strategies that will improve your situation.

## Does an SMSF suit your stage in life?

Your age and working status are significant in reaping the benefits of a self managed super fund.

Superannuation should form an important part of your overall financial objectives in your 40s and 50s. An SMSF at this age offers you the opportunity to take greater control of your super and start investing for the long term. If you want to invest in direct shares or property to be held for the next 10 to 20 years, you can do this within the tax-effective super environment. If protecting yourself against death or disability is important, a self managed fund offers you a choice of insurers and policy options. You will feel more secure in meeting your retirement goals the earlier you take an interest in, and take control of, your super.

The advantages of an SMSF increase once you reach pension age. If you're still working but want the tax benefits of starting pension accounts (see chapter 7), a self managed fund is the easiest way to achieve this. Say you salary sacrifice wages to your fund and then draw a pension payment to assist with your cash flow. You won't have to sell any investments because the cash that goes into the fund can come straight back out. You can easily start multiple pensions when your account balance grows, which will save your fund tax on earnings. While you will need to keep appropriate records, you don't have to fill in complex forms or wait extended periods for the super fund to process your request. Pension drawings are as simple as writing a cheque or electronically transferring money from your SMSF bank account.

If you have reached age 60, all your super withdrawals are tax-free. Although you may think there are no further tax savings to be made, in fact there are significant opportunities to reduce the amount of tax paid by your beneficiaries who will receive any remaining super after your death. The ability to manage several pension accounts and super withdrawals easily can lead to larger tax savings. Using your SMSF for strategies such as withdrawing and re-contributing funds or allocating excess pension drawings in the most tax-effective way (see chapter 7), could save your beneficiaries thousands of dollars in tax.

## You think an SMSF might be for you?

So you're interested in the flexibility and control offered by self managed super. Over the coming chapters you will get a clear picture of what's involved in setting up and managing an SMSF, and read some testimonials from real people in a broad range of situations who are successfully controlling their own super.

Find out as much as you can about your current super fund(s). By being informed about the fees, strategies and options in your current fund(s), you will be in a much better position to determine if an SMSF is more suitable for your situation.

Rushing the setup of your SMSF is not recommended. Asking the right questions and knowing the rules will be critical to the long-term success of your fund. Chapter 2 explores other important characteristics of SMSFs, and I have included a handy checklist to ensure you cover all the bases before taking the first steps towards managing your own super.

## In summary

→ A self managed super fund (SMSF) is a special entity for holding your superannuation savings that you run yourself.

→ SMSFs offer unparalleled investment choice, control over your super, transparent fees and more flexibility than other super funds.

→ SMSF providers are available to help with all aspects of your fund's administration, accounting and compliance.

→ It is advisable to start an SMSF with a minimum balance of between $150 000 and $200 000.

→ SMSFs can have up to four members and give you the chance to pool super funds with other family members — and reduce overall fees.

→ Set administration fees can make SMSFs more favourable than other super funds that charge a straight percentage fee.

→ If you are in your 40s or 50s and want to invest in direct shares or property to be held for the next 10 to 20 years, an SMSF will give you a tax-effective environment for those investments.

→ The advantages of having self managed super, especially the tax benefits, increase when you reach pension age.