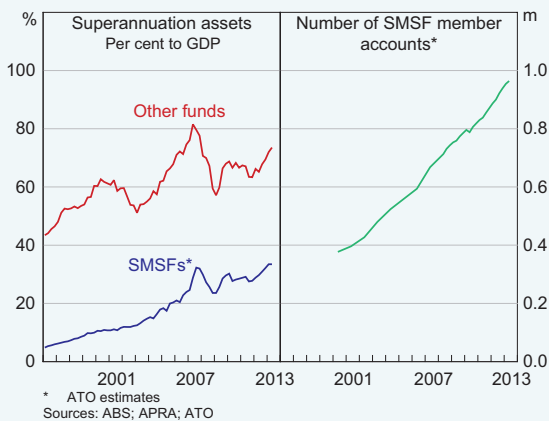


## Box D

# Self-managed Superannuation Funds

Self-managed superannuation funds (SMSFs) are the fastest-growing segment of the Australian superannuation industry. In June 2013, SMSFs held around \$500 billion in assets, accounting for almost one-third of the \$1.6 trillion in total Australian superannuation industry assets, up from 9 per cent in 1995; this is equivalent to a little over 30 per cent relative to GDP (Graph D1). The number of SMSF member accounts has also increased rapidly, having doubled over the past decade.

**Graph D1**  
**Self-managed Superannuation Funds'**  
**Assets and Members**



A range of legislative changes has supported the strong growth in superannuation, particularly in the SMSF sector, over the past decade.

- The 'Choice of Fund' legislation introduced in July 2005 allows individuals to choose which superannuation fund, including an SMSF, their employer's superannuation guarantee contributions are paid into.
- The 'Simplified Superannuation' legislation that came into effect in July 2007 eliminated

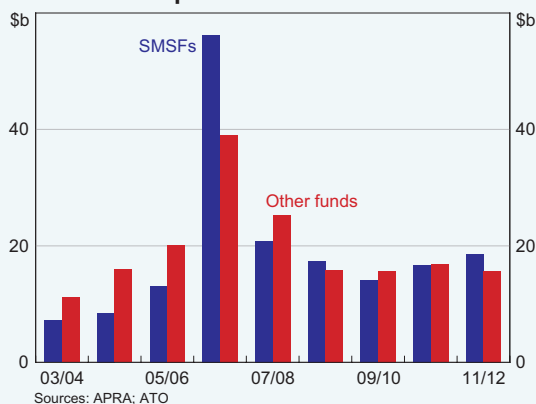
the tax payable on retirement benefits from superannuation funds for members aged 60 years and over. The legislation also introduced a cap on after-tax superannuation contributions (set at \$150 000, above which contributions are taxed at the top marginal tax rate), though in a transitional period, between May 2006 and July 2007, individuals were allowed to make up to \$1 million in after-tax contributions. Accordingly, there was a sharp increase in member contributions to SMSFs in 2006/07, and an associated shift of assets into the sector (Graph D2).

- Legislative changes have increased the accessibility and attractiveness of property investment via an SMSF (discussed in more detail below), which may have encouraged some, particularly younger, individuals to set up SMSFs. A 2013 survey by research company Investment Trends found that younger and newer members of SMSFs were more likely than other members to cite investing in real property and borrowing within superannuation as reasons for establishing an SMSF.<sup>1</sup> More recently, there has also been increased promotion of SMSFs, including of their use for geared property investment.

More generally, a desire for more control over investments has motivated many individuals to set up SMSFs. This is likely to have been even more important since the global financial crisis; the Investment Trends survey noted that concerns about the performance of existing funds and cost savings were frequently cited as reasons for the establishment of SMSFs in recent years.

<sup>1</sup> Investment Trends April 2013 *SMSF Investor Report*, based on a survey of 1927 SMSF trustees.

**Graph D2**  
**Member Contributions to Superannuation Funds**



The profile of SMSF members is quite different from that of members of other funds: SMSF members are on average older, and have significantly higher incomes and larger superannuation balances (Table D1). This is likely due in part to the fixed costs involved in setting up and managing an SMSF, which become relatively less important as the fund balance increases. However, the profile of SMSF members has

changed considerably, at least over the short period for which data are available, with younger individuals increasingly setting up SMSFs (Graph D3).

The allocation of SMSFs' assets is, on average, markedly different from that of other superannuation funds (Graph D4). As is the case for other fund types, domestic equities are the most popular investment choice for SMSFs, accounting for around one-third of their assets. However, SMSFs hold a much smaller share of their assets in foreign equities; their direct holdings of foreign equities are negligible and their total exposure to the asset class (mainly through managed funds) is also likely to be quite small compared with other funds. SMSFs also hold less debt securities, instead holding a much higher share of their assets in cash (including deposits). The asset allocation of SMSFs appears partly reflective of the high percentage of members who are in, or near, retirement. It also likely reflects the ease for an individual of investing in cash and term deposits over debt securities; this factor also probably contributes to the low allocation towards foreign

**Table D1: Characteristics of Superannuation Funds**

	Share of industry assets <sup>(a)</sup>	Average account balance <sup>(b)</sup>	Share of members aged 50 and over <sup>(c)</sup>	Taxable income of members <sup>(d)</sup>	
				Median (\$'000)	Average (\$'000)
	Per cent	\$'000	Per cent		
SMSFs	31	486.6	76	50.7	98.5
Other funds	69 <sup>(e)</sup>	29.6	26	43.5	54.0
Corporate	4	101.8	26	–	–
Industry	20	22.9	19	–	–
Public Sector	16	66.1	42	–	–
Retail	26	24.1	28	–	–

(a) As at 30 June 2013; APRA and ATO estimates

(b) As at 30 June 2012

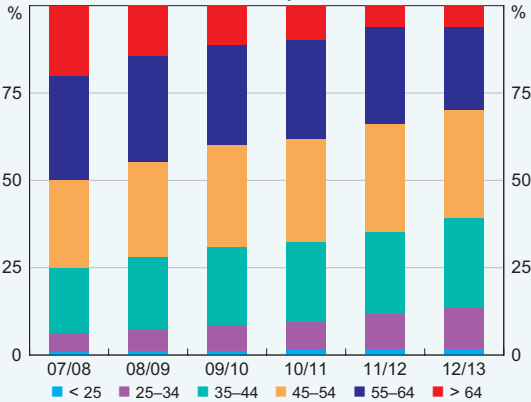
(c) SMSFs as at 30 June 2011; other funds as at 30 June 2012

(d) ATO estimates as at 30 June 2012, based on 2011 SMSF annual returns and member contribution statements for other funds

(e) Includes small APRA funds and balance of life office statutory funds

Sources: APRA; ATO

**Graph D3**  
**Age Distribution of Members\***  
 Share of members of newly established SMSFs

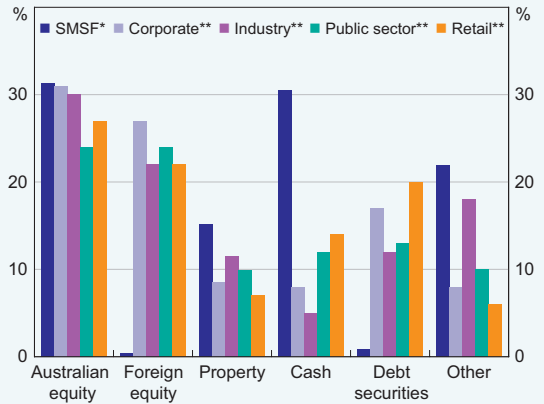


\* Estimates for 2011/12 and 2012/13 based on reported quarterly data  
 Source: ATO

equities. More recently, there are tentative signs that SMSFs are moving some of their assets out of cash and into higher-yielding assets. For example, most of the \$18 billion in hybrid issuance between November 2011 and June 2013 was bought by retail investors, mainly SMSFs, according to research by Investment Trends.<sup>2</sup>

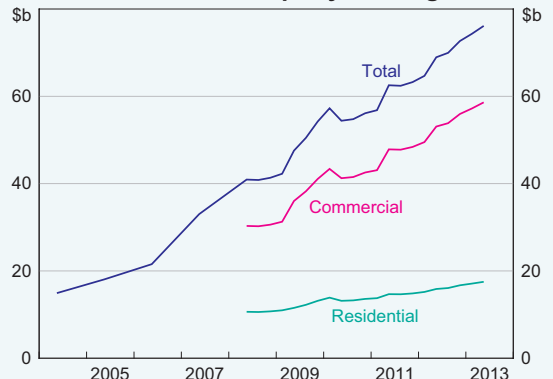
SMSFs also hold a relatively large share of their assets in property. Direct property holdings account for around 15 per cent of SMSF assets and SMSFs are also likely to have a small share of indirect property holdings through trusts and managed funds (represented by the 'Other' category in Graph D4). The bulk of these holdings are in commercial property (77 per cent), likely due to a range of incentives for small businesses to hold property through an SMSF (Graph D5). In particular, a small business owner is able to transfer their business property (and other business assets) into their SMSF and receive a capital gains tax exemption up to a lifetime limit of \$0.5 million. Once the property is in the fund, the fund can lease the property to the business owner at a commercial rate and the rent paid by the business owner can be claimed as a business expense, reducing the taxable profit of

**Graph D4**  
**Superannuation Assets by Fund Type**  
 Share of assets by value



\* ATO estimates as at June 2013; direct holdings only except for the 'Other' category, which is predominantly in listed and unlisted trusts and other managed investments; likely to exclude purchases under limited recourse arrangements for some assets  
 \*\* Allocation of default strategies as at June 2012; direct and indirect holdings  
 Sources: APRA; ATO

**Graph D5**  
**SMSF Direct Property Holdings\***



\* ATO estimates; likely to exclude some property purchased under limited recourse arrangements  
 Source: ATO

the business. By contrast, SMSFs' direct holdings of residential property are relatively small (23 per cent of their total direct property holdings).

The share of property assets held by SMSFs has increased over the past six years, partly driven by changes to superannuation legislation that have made direct property investment both more appealing and more accessible to SMSFs.

<sup>2</sup> Investment Trends November 2012 *Investor Product Needs Report*.

- The ‘Simplified Superannuation’ legislation increased the relative appeal of directing property investment through an SMSF (and also added to the incentives for some small businesses to shift their business property into a fund), because any property-related retirement benefits would be tax free for members over 60 years of age.<sup>3</sup>
- In September 2007, changes to the superannuation legislation allowed funds to borrow money to purchase assets under limited recourse conditions (that is, in the event of borrower default, the lender only has the right to recover losses from these assets). Prior to this, superannuation funds were not permitted to borrow money for investment, which limited the ability of SMSFs to directly invest in property.
- In July 2010, the rules around limited recourse borrowing were clarified. Protection of other assets in the fund was also strengthened: each loan was restricted to a ‘single acquirable asset’, and the rules explicitly ensured that SMSF members who give personal guarantees on the loan (a frequent requirement imposed by lenders) cannot recover losses out of the fund’s other assets if the guarantee is invoked.

These legislative factors, and the growing number of individuals setting up SMSFs as a vehicle to invest in property, are contributing to the momentum in geared property investment through SMSFs. ✎

<sup>3</sup> Property-related retirement benefits include: proceeds from the sale of property; the transfer of property to a member as a non-cash benefit; and rent earned from a property that remains in the fund.

