

**Gordon D Mackenzie CA**

*B Sc LLB (Mon) LLM (Syd)*

*Grad Dip Securities Analysis*

*F Fin CTA*

*Solicitor*

Senior Lecturer

School of Taxation and Business Law

UNSW Business School

Room 630

Quadrangle Building

UNSW Australia

Kensington NSW

Tel +61 2 99091568

Mob 0423 477 294

Email [gordon.mackenzie@unsw.edu.au](mailto:gordon.mackenzie@unsw.edu.au)

Skype [gordonmack1](#)

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**Division Head**

Retirement Income Policy Division

The Treasury

Langton Crescent

PARKES ACT 2600

By email: [superannuationobjective@tresury.gov.au](mailto:superannuationobjective@tresury.gov.au)

Dear Sir/Madam,

**Objective of Superannuation**

Discussion Paper

**Introduction and Background**

I refer to the Discussion Paper, Objective of Superannuation, and the invitation to provide feedback and comments on the issues outlined in that paper.

I very much welcome the opportunity to provide feedback and comments on the issues outlined in the Discussion Paper and applaud the Government for initiating a discussion about what is a very important question to a significant number of Australians. My feedback and comments follow below.

By way of introduction and background I am currently Lecturer in Charge of three superannuation subjects (Taxation of Superannuation, SMSF Law and

Taxation Strategies in Financial Planning), which are part of our Masters programs at the UNSW Business School.

In addition, I am Convener of the Master of Tax (Financial Planning and Tax), as well as the Master of Applied Tax (Superannuation) and I am Director of the UNSW SMSF Specialization Program for both the Chartered Accountants Australian and New Zealand (CA ANZ) and CPA Australia.

I have just completed a research project on the underlying principles for the regulation of SMSF, which involved a cross country comparison with SMSF-equivalent pension funds in USA, UK and Canada.

Full details of my academic output can be seen here  
<https://www.business.unsw.edu.au/our-people/gordonmackenzie>

In terms of superannuation industry experience, prior to becoming an academic I was Global Tax Director at AMP Ltd and prior to that was a superannuation lawyer at AMP Ltd having established the first master trust deeds for superannuation funds, drafted trust deeds for the first industry superannuation funds, as well as establishing a superannuation administration company to service that sector of the superannuation market.

In terms of industry advocacy roles, I have been at times on the tax committee of the Business Council of Australia, of the Financial Services Council, of ASFA and of the Property Council of Australia, in addition to having been chair of Taxpayer's Australia.

## **Feedback and Comments**

### **Is the Age Pension the appropriate benchmark? Are business owners considered?**

While the Discussion Paper invites responses to some or all of the three questions that are asked, it also notes that feedback and comments do not to have to be limited to the issues the subject of those three questions.

In that regard, and by way of introduction, it is apposite to make some observations about the superannuation system as a whole, some of which is in response to issues that are raised under the heading "Context" in the Discussion Paper and others directly relevant to the questions posited.

Again, the importance of having a clear understanding of the objective of superannuation is to be welcomed, however three things in particular are observed about the Discussion Paper as a whole and the putative objective recommended by the FSI.

Of those three observations the first is that referencing the objective of the system to the Age Pension (" To provide income in retirement to substitute or

supplement the Age Pension”- page 2) seems to narrow the purpose of superannuation from what is actually the case in practice. Secondly, again by referencing the objective of superannuation to the Age Pension the Discussion Paper seems to proceed in the reverse on which the three pillars of a good retirement system are founded, and, thirdly, the background and questions in the Discussion Paper omit inclusion of the retirement funding of a particular cohort of individuals, being owners of businesses.

Focusing on the Age Pension as the starting point for considering the objective of superannuation seems to ignore that the superannuation system provides payments on the occurrence of other events. That is to say that the purpose of the superannuation system, in fact and in practice, is more than just providing an income to members after retirement from the workforce.

This is most clearly seen in the legislation of the Sole Purpose test in Section 62 Superannuation Industry (Supervision) Act (“SIS Act”) which, briefly, permits payment of benefits from a superannuation fund on death of a member of the fund to their dependents, as well as the payment of benefits on a member suffering permanent disablement before retirement, both of which are additional objectives of the superannuation system to providing a benefit on retirement.

In addition to payments being permitted in these events, payments can also be made by superannuation funds in subsidiary type events such as on the member suffering a terminal illness or suffering severe financial hardship, amongst other events.

The point being, importantly, that these events when the member can be paid a benefit or, indeed, where payments can be made to the members dependents on death, from a superannuation fund, are not substitutes for the Age Pension, which is a payment solely dependent on the age of the recipient (currently age 65) but subject to income and means tests of course.

That then raises the question about whether, in that case, the Age Pension should indeed be the benchmark for determining the objective of superannuation?

It is suggested that the objective of superannuation be discerned, when taking into account the other events when payments can be made,

Secondly, as is noted in the Discussion Paper, it is generally considered that there are three pillars to a good retirement system, being compulsory superannuation, voluntary payment and the Age Pension.

However, and importantly, the role of the Age Pension as one of these pillars is that it is a “safety net” in that it is intended to prevent individuals from living in poverty in old age.

Again, the point here is that referencing the objective of the whole superannuation system to the Age Pension, the purpose of which is to keep people from living in poverty, seems to understate the importance of the

superannuation system to the majority of citizens who are highly unlikely to ever be at risk of being poor in retirement.

In that regard, it seems to approach the question of articulating the objective of superannuation from the reverse angle or, to express that another way, from the bottom-up rather than the top-down. Nevertheless, it is acknowledged that as a matter of tax equity, the system should have limits, both to prevent inappropriate wealth creation and from being a drain on public revenue.

Thirdly, what has not been addressed is the objective of the superannuation system to business owners. In that regard the term business owner is a reference to individuals who, by satisfying the relevant tax and regulation legislation, can contribute to their superannuation fund amounts from the disposal of their business assets in addition to the amount of contributions that all other individuals can make. It seems obvious that for that cohort of individuals' that a superannuation fund is not the primary source of retirement income, rather it is the value of their business assets, which, implicitly from these tax rules, is their retirement funding asset.

The design of the rules being that they can use a superannuation fund to house the proceeds from disposal of their business assets, but, again, the primary accumulation of retirement funding is from their business assets and not contributions to their superannuation fund.

### **Questions for Consultation**

#### **Do you agree with objectives recommended by the FSI? Why?**

Certainly, the primary objective recommended by the FSI is not supported for the reasons above and some alternate suggestions follow.

However, the other recommendations by the FSI are supportable in that consumption smoothing over a lifetime, managing financial risk in retirement, having a fully funded system, funds being invested for the best interest of members, alleviating fiscal pressures of the retirement income systems, and simplicity and efficiency are self-evidently valid objectives for the superannuation system.

Specifically, objectives dealing with: retirement myopia (lifetime smoothing), asset /liability management (managing longevity risks), resolving agency problems in the system caused by asymmetry of information between superannuation providers and members (best interest of members), fiscal sustainability and intergenerational equity (fiscal pressure management), participation and engagement by members (simplicity and efficiency), clearly should found the regulation of the superannuation system.

Whether it is considered appropriate to enshrine these, in effect, principles for a good superannuation system in the legislation are another issue. It is considered that, on balance probably not. It is hard to think of a precedent in any legislation

articulating the underlying principles in accordance with which the rules are formulated.

Equally it is hard to think of what value would be achieved in doing that. Would it give disgruntled individuals a right of action against the Regulator if the interpretation of the rules being by the Regulator were not considered by the disgruntled individual to be a consistent interpretation with the articulated objectives? Probably not. Would it obligate any future Government to only legislate consistently with those stated objectives or, indeed, limit future Governments to only those stated objectives? Probably not, as well.

**If you do not agree with the FSI recommendation, what do you think should be the objective of superannuation? Why? What are the implications of that objective?**

To the extent the primary objective recommendation of the FSI is not supported it is submitted that the objective of superannuation should connote that the objective of superannuation is to provide an income in retirement.

That, of course, begs the question about the amount of that income and it is noted that in the Discussion Paper about incorporating an income amount in retirement as part of the objective seemed to be considered unfavorably.

Specifically, the "Issue" under "Points to be consider for discussion" in the table on page 3, when referring to "Adequacy" in terms of a retirement income argued against using that formulation. Amongst other reasons given was that there was no consensus about what "Adequacy" means.

On the other hand, using a formulation around standard of living does seem to have some benefits. It is noted, and the Discussion Paper also says this in that it says, that such a formulation would ".....clarify that superannuation is meant to help fund a person's retirement, it is not for unlimited wealth accumulation or bequests".

Such a qualification of the objective would then be consistent with standard financial planning practice where the amount required by individuals to fund their retirement usually expressed as a percentage of their pre-retirement income. The most common formulation is that individuals need to fund an income in retirement equal to between 65% to 70% of their pre-retirement income to maintain their lifestyle.

Other metrics of income in retirement related to living standards are, for example, those published by ANU/ASFA Retirement Standards.

Indeed, measuring retirement income using the Age Pension is similar in principle to what is being suggested here, the difference being that the retirement income standard would not be based on a poverty prevention measure.

Should there be any qualification on a standard of living retirement income objective? Perhaps there should be.

While at some stages of the evolution of the Australian superannuation system individuals were permitted to fund a retirement accumulation equal to seven times their final salary on the basis that, at that point in time when interest rates were at 10%, seven times their income invested at that rate would fund a 70% pre-retirement income pension.

That had no regard for equity issues such as the wealthy funding a pension using in that formula distorting the system.

In that case and to give as much scope as possible to accommodate all the ways that the superannuation system operates it is suggested that the objective of the superannuation system, in addition to referring to an income in retirement qualify that by it being a 'reasonable' income in retirement. Use of such a general term is consistent with numerous other types of legislation, which have the effect of retaining discretion about the scope of the rules and their application.

### **In which piece of legislation should the objective be legislated and why?**

There is a precedent in superannuation law for legislative expression of the purpose or objective of certain rules. Specifically, see section 291-5 ITAA97 where the object of the excess contributions rules is said to be “...superannuation benefits that an individual receives results from contributions that have been made gradually over the course of the individuals life”, and, also, section 293-5 ITAA967 referring to extra contribution taxes being paid “.. for very high income individuals”.

However, probably more relevant in the context of an objective for superannuation than being include in the income tax laws is the equivalent to banking system role of the RBA in managing inflation and system integrity of the system.

In that case the most suitable and indeed logical legislation for the objective of superannuation to be enshrined is the SIS Act.

Yours sincerely,



Gordon D Mackenzie

