THE TAXPAYERS' RESEARCH FOUNDATION LIMITED

A.C.N. 076 854 021

Unit 6, 12 Navigator Place
Hendra QLD 4011

Telephone: 07 3268 4210
Facsimile: 07 32684213

PO Box 3102
Hendra QLD 4011

Supporting the
Taxpayers Australia Group

Company Secretary : Stephen Ware

5 April 2016

Division Head
Retirement Income Policy Division
The Treasury
Langton Crescent
PARKES ACT 2600

Dear Sirs

The Taxpayers Research Foundation commissioned papers from a variety of organisations that have expertise or made contributions to the current debate on retirement incomes and the relationship of superannuation taxation concessions and the old age pension and Australia's future tax liability. The papers presented cover a range of perspectives and views.

These papers were commissioned before the announcement of the inquiry and the Foundation is making them available in the interests of furthering informed public debate on the issues.

The Foundation has also commissioned an analysis by Van Eyk, of long-term economic trends that can have a major impact on the returns to superannuation funds and therefore the viability of current arrangements in addressing our long term fiscal and retirement income issues. The issues of viability must be assessed on an uncertain future not on an historic past.

The Financial System Inquiry recommended the following primary objective:

To provide income in retirement to substitute or supplement the Age Pension.

The primary objective of superannuation must be to substitute or supplement the age pension for retirees. All citizens benefit from having their own sources of income, under their control, along with the income generating assets. There is always a great deal of uncertainty as to long-term future economic conditions, demographic changes and many other unexpected, unknowable events that could impact upon taxpayers, through the Federal government, being able to adequately finance the needs of retirees. Superannuation provides an insurance policy for the future for citizens.

Private superannuation allows individuals to make their own adjustments and decisions for savings on their own expected risk profiles and requirements in retirement. They can modify their choices away from the actuarial calculations for the average person in their category. Individuals have the incentive to do with the information for their own particular circumstances and also adjust their savings for their own risk concerns.

As noted in the paper by Collins "An objective shouldn't be to 'substitute' the Age Pension, as there will always be a need for a safety net. Superannuation Guarantee does not cover all Australians and for some that it does cover, sufficient benefit may not be able to be accumulated."

The Foundation in an occasional paper earlier this year noted that "though superannuation and age pension provision are intertwined they are rarely dealt with together in government enquiries"

Recommendation: The inquiry needs to focus on practical, achievable improvements in both superannuation and old age pension arrangements.

<u>Subsidiary objectives</u>

The inquiry also recommended that the following subsidiary objectives be considered in the analysis. The Foundation makes the following comments and recommendations based upon an analysis of the papers commissioned by us.

<u>Facilitate consumption smoothing over the course of an individual's life</u>

The current superannuation system is failing in consumption smoothing as outlined in the paper by Gilligan and Craig for a large proportion of workers earning below median incomes. Alternatives are canvassed in their paper on alternative means of delivering income smoothing through taxation, pensions and alternative superannuation funding arrangements and structures.

The paper by Dennis also outlines the failures of the current superannuation arrangements to encourage income smoothing for most lower income workers and its active use by higher income workers for tax and estate planning. As Cowan noted in his paper "maturation of the Superannuation system will reduce the total value of pension spending by only 6%" provides empirical evidence that the current superannuation system is not facilitating consumption smoothing.

Recommendation: that this enquiry undertake or commission the research to determine appropriate methodologies for consumption smoothing over the lifetime of individuals.

<u>Be fully funded from savings</u>

Ideally it would be much more desirable for a funded system rather than an unfunded system to be better able to cope with any risks or changes in economic circumstances. As noted in the papers presented in the journal it is unlikely that a fully funded scheme can be achieved but appropriate arrangements and incentives can reduce the call on taxpayer funds in the future.

Cowan in his paper noted that because of factors such as the government fiscal situation and an ageing population, old-age pensioners "cannot bank on taxpayers underwriting living standards".
Dennis recommended change to the taxation arrangements for superannuation "so they better fit the purpose of encouraging Australians to rely more on their savings in retirement and less on the taxpayer"

Recommendation: That the current system is neither designed to nor providing consumption smoothing for individuals and contributors must be provided with a thorough analysis of alternatives to achieve the objectives by financial service firms and superannuation funds .

<u>Help people manage financial risks in retirement</u>

There is no doubt that risk management is crucial for retirees. Cowan notes that for many pensioners a motivating factor "is aversion to risk and debt, with particular concern about the perceived riskiness of reverse mortgages". He is noting the failure of commercial products to become widely taken up.

Collins in his paper notes that retirees "face not only investment risk but also longevity risk". He notes there are some improvements in the provision of investment risk products but states "there are really no satisfactory products yet which minimise longevity risk". The market has failed to deliver products that meet the needs of consumers as evidenced by the low take up rates.

Dennis recommended change to the taxation arrangements for superannuation "so they better fit the purpose of encouraging Australians to rely more on their savings in retirement and less on the taxpayer".

Recommendation: That there be a thorough analysis and consideration of any alternatives, including government interventions, to minimise the perceived and actual risks of longevity for superannuants.

Be invested in the best interests of superannuation fund members

The analysis provided in the paper by Gilligan and Craig gives the current superannuation arrangements a mark of a 'bad fail' in having the incentives in place to look after the best interests of superannuation fund members or a better term contributors. There are conflicts of interest, myriad structures inhibiting efficiency and an incredible cost growth in the funds, diminishing the returns to contributors. Their benchmarking shows that Australia's industry and finance sector superannuation funds are a major vested interest that is not delivering an efficient, low-cost retirement income program.

Collins also provides details of failings in the current arrangements for superannuation, especially for costs where he asks the question "how is it that the Super industry has made billionaires of some fund managers and multi-millionaires of some financial planners?" and notes that it is the members of the superannuation fund who are taking all the risk. Many of the rewards appear to be going elsewhere in the superannuation system.

Recommendation: That Superannuation funds be regulated to ensure full transparency in management and investment operations and that choice of funds is the sole responsibility of the individual worker and not their employer or union.

A more efficient legislative/regulatory arrangement for superannuation

To ensure efficiency of understanding of the requirements of the legislation and advice to current and potential users of superannuation products, all requirements should be in the one piece of legislation. This will facilitate greater understanding and advice to be provided by advisers using the legislation rather than the current arrangements of investigating superannuation, taxation and government benefit arrangements.

Recommendation: That all aspects of retirement incomes be incorporated into the one act of legislation. If not possible, that all information be publicly available from the one source document/website even if covering multiple pieces of legislation.

Our comments on the multiplicity of problems and potential solutions in superannuation arrangements and retirement incomes are documented in the papers provided to this enquiry.

The Foundation does not accept the premise in the questions for consultation that only marginal changes should be made. Our arguments for consideration of major changes are based upon the information supplied by multiple organisations and the analysis and information behind the papers they have provided.

Yours faithfully

Stephen Ware.

Stephen Ware
Secretary