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To whom it may concern

Submission to the Retirement Income Covenant consultation

National Seniors Australia welcomes the opportunity to make a submission to the Treasury Retirement Income Covenant Position Paper consultation.

National Seniors is the peak consumer body for older Australians. We draw on high quality research and other engagement activities to understand the needs and views of older Australians. We use this information to promote policies beneficial to all older Australians.

National Seniors agrees with the general approach taken with the retirement income covenant position paper. We support a principles-based approach that does not rely on compulsion or default arrangements but encourages superannuation trustees to offer products which address the needs of individual members and for superannuation members to choose options which meet their needs and are in their best interests.

National Seniors research has demonstrated older people value stable and secure income, and value products like defined benefit schemes as reducing worry in retirement. While this means there is likely to be support from older Australians for the approach taken in the covenant, it is important to recognise that retirement objectives and goals depend on the specific circumstances of individual fund members.

Our research has shown, there is a need to tailor retirement income strategies to the specific circumstances of individual retirees. While retirees who can afford personal financial advice will be able to tailor their retirement income strategies to their needs, there are many that cannot because they have limited superannuation balances, particularly women.

They will rely heavily on trustees and government to help guide their decision making, which is negatively impacted by poor financial literacy and system complexity.

We believe trustees must have the flexibility to respond to specific circumstances of members who cannot engage with costly personal financial advice.

In this regard, trustees should be required to engage with their members. They could also be required to offer members (who cannot afford personal advice) a choice of retirement income options that meet individual objectives. This should include protection from taking up products that are not in their best interests.

The success of these reforms will rely on the capacity of members to make informed choices. More attention must also be paid to the simplifying the retirement income system and to improving the financial literacy of older Australians.

Government should also ensure independent and trustworthy online tools are available to enable retirees to compare retirement income products and options.

Further detail supporting this submission is outlined in the attached sections, including a summary of National Seniors research relevant to retirement income planning.

Should you require further information please contact Dr Brendon Radford, Manager of Policy and Advocacy b.radford@nationalseniors.com.au.

Yours Sincerely



Ian Henschke
Chief Advocate

Appendix 1: Detailed response to the retirement income covenant position paper

Timeframe

National Seniors questions whether the timeframe set out in the position paper is realistic. Given the legislation has not yet been drafted, let alone passed, it would appear the current implementation date of 1 July 2022 is unrealistic. Trustees must have ample time to understand the needs of members in order to develop a comprehensive and valuable retirement income strategy or strategies.

Principles based approach

National Seniors supports the principles-based approach put forward within the position paper. This is in line with the existing covenants in the Superannuation Industry (Supervision) Act 1993 (SIS Act) and will ensure trustees have flexibility to be responsive to the needs of their members.

In this regard, we are pleased the position paper does not seek to impose certain retirement products on members. National Seniors does not support moves to compel older Australians to purchase specific retirement income products. This would not be in the interests of all members.

We agree members should not be defaulted into “particular products” or “forms of advice”. This would be contrary to the interests of members.

Informed choice

Members should be free to choose products which meet their specific needs. It is important the legislative environment promotes informed choice with adequate safeguards. This will help members tailor their retirement plans to meet their needs.

Government has an important role to play. It must assist consumers to easily understand and compare product offerings. This can be achieved by providing simplified online tools to compare product outcomes, as is done for example with comparison rates for home loans or with the Energy Made Easy comparison site for electricity and gas.

Ultimately, our hope is the covenant places pressure on the financial services sector to develop high quality products that account for differences in the circumstances and needs of retirees. A one-size-fits-all approach to retirement income planning will not improve outcomes for retirees.

The uptake of new and innovative retirement income products will depend on the ability of retirees to make informed choices. Unless members have adequate financial literacy, there is risk they will not take up products.

Uptake of innovative retirement income products will also depend on trust. Older Australians will not take up retirement income products unless they have confidence in the financial services sector. In this regard, there

is still a long way to go before the full implementation of the Hayne Royal Commission and Future of Financial Advice (FOFA) reforms.

It is imperative trustees be obliged to provide information and advice commensurate with the financial resources and needs of members by simply communicating the costs and benefits of different retirement income products.

Personal financial advice

National Seniors research on retirement comfort reinforces the importance of individual advice.

It found that benchmark approaches used to estimate retirement comfort (the ASFA Retirement Standard) provides only a general guide to planning for a financially comfortable retirement and argued there is need to understand the specific needs and preferences of older people when developing a retirement strategy to achieve a comfortable retirement¹.

While the proposed covenant requires trustees to make develop a general retirement income strategy, including the option of making specific cohort specific strategies, positive retirement income outcomes for members will depend on the capacity of trustees to tailor solutions to the needs of individuals.

While the position paper laments “most people do not seek financial advice at retirement” to help navigate the complexity of the retirement income system, this ignores the fact that many members have low superannuation balances and may rationally see little benefit in paying for costly individual advice.

Wealthier retirees will likely see the value in paying for personal financial advice tailored to their specific needs, but a significant proportion of superannuation members are not in this privileged position.

Analysis of ATO data conducted by the Association of Superannuation Funds of Australia (ASFA) has shown that median superannuation balances are still relatively low. Fifty per cent of men had a balance which was less than \$178,326 and 50% of women had a balance less than \$171,679 in the 65-69 age group in 2017-18.² A proportion of them will have balances approaching zero and will have no interest or need for longevity products.

While the Retirement Income Review final report estimated a higher proportion of retirees will have larger balances in the future, this remains to be seen. It will depend on a range of factors, not least the trajectory of house prices (real mortgage debt of the over 55s jumped 600% between 1987 and 2015)³. This may

¹ Hosking, D., Minney, A. and McCallum J., 2020. Retirement comfort: Personalised versus standard plans. Canberra: National Seniors Australia and Challenger: 28/10/2020 <https://nationalseniors.com.au/uploads/V11-clean-Comfort-categories-report.pdf>

² Clare, R. 2021. *Superannuation balances prior to death: Superannuation balances of older Australians* ASFA: March 2021 <https://www.superannuation.asn.au/ArticleDocuments/359/2103-Super-balances-just-before-death-Paper.pdf.aspx?Embed=Y>

³ Ong, R., Wood, G., Cigdem-Bayram, M. and Salazar, S. 2019. *Mortgage stress and precarious home ownership: implications for older Australians*, AHURI Final Report 319, Australian Housing and Urban Research Institute Limited:

undermine superannuation balances as retirees increasingly use their superannuation to pay off outstanding mortgages upon reaching retirement.

As such, it is important the needs of retirees with low balances are accommodated. This group will be heavily reliant on product information being communicated in simple ways that are easily understood without the impost of costly advice.

Supporting low balance retirees

While we do not support compulsion, trustees should be required to support members, unable pay for complex advice, to make informed choices about their retirement income options.

Trustees could do this by providing members (who don't engage with individual advice) with a series of retirement income options based on different retirement income outcomes.

A member could select their preferred outcome from a list of options. This might mean choosing either an option that balances the three objectives outlined in the position paper and options that achieve a greater emphasis on one or more of the three objectives.

The trustee would then recommend which of the options best meets their desired outcome. This would be similar in some respects to the way that superannuation works in the accumulation phase, but without using a default option.

For this to be effective there would need to be an obligation on trustees to demonstrate they have done more to engage members who do not take up individual advice.

Simplifying the retirement income system

To achieve this, government will need to make further legislative changes to simplify to the retirement income system.

In our submission to the Retirement Income Review in 2020, National Seniors argued the system was overly complex. Older Australians find the current rules and regulations governing the retirement income system, including the complicated means testing arrangements, as a barrier to decision making

The interplay between superannuation, other private investment, the Age Pension and the taxation system must be made simpler to make planning for retirement easier, particularly for those with limited resources and financial literacy.

Melbourne. https://www.ahuri.edu.au/_data/assets/pdf_file/0026/44954/Mortgage-stress-and-precarious-home-ownership-implications-for-older-Australians-Executive-Summary.pdf

As noted earlier, there will continue to be a large proportion of older Australians with limited savings in superannuation for the foreseeable future. The needs of these retirees, the majority who are women, should not be ignored.

It is not enough to simply expect balances will increase in the distant future. Nor is it acceptable to expect all retirees will pay for personal financial advice – which may not be in their best interests.

Unless further simplification of the retirement income system occurs, retirees will continue to find it difficult to plan for their retirement leading to sub-optimal decision making. For example, National Seniors regularly hears from retirees who chose to place significant sums of money in low return savings options, such as term deposits, because it is viewed as the simplest and safest way to invest.

Retirement income objectives

We support in principle the idea that trustees balance the following three objectives developing a retirement income strategy under the covenant:

- maximise retirement income
- manage risks to the sustainability and stability of their retirement income; and
- have some flexible access to savings during retirement.

However, these objectives will not be equally important across the retiree population. As such, we are wary of attempts to “lock-in” these objectives for individual retirees.

While maximizing retirement income is a universally appealing objective, retirees may view the sustainability and stability of retirement income differently based on their personal circumstances. As such, they are not likely to have equal importance and therefore should not be treated as such, otherwise there may be negative outcomes for some retirees.

For example, encouraging a member with limited savings and/or limited life expectancy to purchase an annuity to manage life expectancy may not be in their best interests.

Superannuation fund members need to be protected against taking up products not in their interests. As it was argued in Rice Warner’s submission to the previous retirement income covenant position paper, members with balances of less than \$150,000 would not see any benefit in adopting products which provide protection against longevity risks because of the Age Pension⁴.

While we agree there is a need to increase the availability of better retirement income products, this will only achieve better outcomes if the products meet members specific needs and there is sufficient trust in these products.

⁴ Rice Warner 2018. *Retirement Income Covenant Position Paper: Submission* <https://www.ricewarner.com/wp-content/uploads/2018/06/Ltr-Retirement-Income-Covenant-Position-Paper-The-Treasury-190618375894.8u.pdf>

This requires sufficient financial literacy on the part of the retiree. It also requires significant transparency and regulatory oversight of retirement income products. Neither of these at present are in strong supply.

Longevity risk

The issue of income sustainability is of significant interest to older Australians.

Research conducted into older people's worries about having enough retirement income, consistently shows many worry they will outlive their savings and investments.

Unsurprisingly, people with a defined benefit scheme or annuity were the least worried about outliving their savings.^{5,6} As it was argued in our 2019 research:

“Retirees with a defined benefit pension report experiencing a sense of comfort and security about their future. This confirms the importance of policy solutions to provide comparable options in retirement for those who are not in a defined benefit scheme.”

Earlier research conducted by National Seniors into older people's perceptions about retirement income has shown “an income that lasts a lifetime” and “a desire for regular and constant income” are some of the most important financial goals of older people.^{7,8}

Our most recent research has shown a high proportion of retirees (85%) are also aware of increasing life expectancy. It found roughly 50% of retirees have made plans to address longevity risks. The research also showed that around 50% of retirees supported the idea of superannuation funds offering a form of longevity insurance, with a similar proportion supporting the idea of putting aside a proportion (10%) of superannuation funds to provide an income for life.⁹

It would appear beneficial for the market to offer retirement income products to address longevity risks and for income sustainability and longevity risk be included as objectives in the covenant. However, there are two caveats to consider.

⁵ McCallum, J, Hosking, D. & Rahn, A. 2019. *Feeling financially comfortable? What retirees say*. Brisbane: National Seniors. <https://nationalseniors.com.au/uploads/ChallengerReport-FeelingFinComfortable-Web.pdf>

⁶ National Seniors and Challenger 2020. *Retirement income worry: Who worries and why?* Canberra: National Seniors <https://nationalseniors.com.au/uploads/0120203573PAR-RetirementIncomeWorry-ChallengerRpt-FNREV.pdf>

⁷ National Seniors and Challenger 2018. *Once bitten twice shy: GFC concerns linger for Australian seniors*. Brisbane: National Seniors. https://nationalseniors.com.au/uploads/07183036PAR_OnceBittenTwiceShy_Web_0.pdf

⁸ National Seniors Australia and Challenger 2017. *Seniors more savvy about retirement income*. October 2017 https://nationalseniors.com.au/uploads/09172675CRP_ChallengerReport_RetirementIncome_FN_0.pdf

⁹ McCallum, J., Maccora, J., & Rees, K. 2018. *Hope for the best, plan for the worst? Insights into our planning for longer life*. Brisbane: National Seniors. https://nationalseniors.com.au/uploads/01182863PAR_HopeForTheBest_Report_FN.pdf

The first is that our research into retirement income worry found worry was higher among people with lower levels of savings, including those expecting their main source of income would be the Age Pension.^{10,11} In our later research into longevity risk, we also found that those more likely to be supportive of longevity risk products, were less likely to be able to fund these at the time of retirement¹².

This does not bode well for the take up of products like annuities, because the use of lifetime income stream products by those with low superannuation balances may not be in their best interests (as noted earlier).

There is also a question about how best to deal with longevity risk when balances are limited, as this creates additional complications for members and trustees.

For example, it may be more beneficial for a member to hold onto their limited savings so they can use it for larger, unexpected, health and aged care costs, rather than converting this into an annuity. Given both approaches deal with longevity risks but in different ways, superannuation trustees will need to think carefully about how they assist low balance members and consider which course of action is more prudent.

In this regard, it is also entirely rational for low balance retirees, who suspect they will have a lower life expectancy, to avoid purchasing an annuity product, especially when the Age Pension already exists to address longevity risk (without any loss of capital).

The second caveat to consider regarding longevity risk is the issue of ‘present’ versus ‘future’ orientation. As our research into longevity risk found, older Australians appear to be more inclined to be ‘present’ orientated in terms of retirement spending. They are inclined to be focused on spending earlier in life for leisure activities than saving for later life unknown’s, like aged care.¹³

While this might be negative in terms of longevity risk and undermines the likelihood that members take up products to deal with longevity risk, on the other hand, it could be positive because it contradicts fears, such as those in the recent Retirement Income Review final report, that older people are maintaining their capital rather than spending for a better retirement.

The obligation on trustees to ensure a longevity risk is addressed as part of their retirement income strategy raises several questions about the practical application of this requirement.

Will a fund have an obligation to offer a product/s dealing with longevity risk to meet the objective to manage risks to the sustainability and stability of members income?

¹⁰ McCallum, J, Hosking, D. & Rahn, A. 2019. *Feeling financially comfortable? What retirees say*. Brisbane: National Seniors <https://nationalseniors.com.au/uploads/ChallengerReport-FeelingFinComfortable-Web.pdf>

¹¹ National Seniors and Challenger 2020. *Retirement income worry: Who worries and why?* Canberra: National Seniors <https://nationalseniors.com.au/uploads/0120203573PAR-RetirementIncomeWorry-ChallengerRpt-FNREV.pdf>

¹² McCallum, J., Maccora, J., & Rees, K. 2018. *Hope for the best, plan for the worst? Insights into our planning for longer life*. Brisbane: National Seniors https://nationalseniors.com.au/uploads/01182863PAR_HopeForTheBest_Report_FN.pdf

¹³ McCallum, J., Maccora, J., & Rees, K. 2018. *Hope for the best, plan for the worst? Insights into our planning for longer life*. Brisbane: National Seniors https://nationalseniors.com.au/uploads/01182863PAR_HopeForTheBest_Report_FN.pdf

Will a fund meet the objective to manage risks to the sustainability and stability of members income if it provides an option or options to address concerns about longevity even if only a limited number of members take up such a product?

If a trustee is obliged to offer products that manage longevity risk and only a limited number of members take up this product – raising the costs for members, does this undermine the first goal of maximising member returns?

Appendix 2: National Seniors Australia Research Papers

National Seniors Australia, with assistance from Challenger, has undertaken ongoing surveys of older Australians to elicit insights on retirement income. These have been produced in a range of research reports.

The findings are summarized below and provide valuable insights into the challenges in planning for retirement. Many of these insights are relevant for considerations of the Retirement Income Covenant.

Retirement Comfort: Personalised versus standards plans, October 2020¹⁴

This report compared spending patterns across retirement comfort lifestyle markers with an objective measure of retirees' wealth - the Association of Superannuation Funds of Australia (ASFA) Retirement Standard.

It found that benchmark approaches used to estimate retirement comfort provide only a general guide to planning for a financially comfortable retirement.

While the research found retirees with higher wealth and income were generally more comfortable in their spending than those with lower wealth and income and higher dependence on the Age Pension, this was not entirely consistent.

"The inconsistencies shown in retiree spending decisions according to their objective wealth levels suggests using a general set of lifestyle spending markers alone does not effectively capture how retirees view comfort. Being comfortable is more nuanced and likely defined according to personal characteristics."

Another important finding was the strong relationship between worrying about outliving savings and investments and spending. Having 'enough to last' and preserving capital were important in defining comfort. Those that were unworried about outliving their savings were more likely to be comfortable in their spending.

"Personal preferences, together with lifestyle and care priorities need to be identified and finessed by using a tailored approach to plan an effective strategy for future retirement comfort."

"A retirement plan that is tailored to individuals' lifestyle preferences, is flexible and provides strategies for long-term security is more likely to be successful."

There is need, therefore, to understand the specific needs and preferences of older people when developing a retirement strategy to achieve a comfortable retirement.

¹⁴ Hosking, D., Minney, A. and McCallum J., 2020. *Retirement comfort: Personalised versus standard plans*. Canberra: National Seniors Australia and Challenger <https://nationalseniors.com.au/uploads/V11-clean-Comfort-categories-report.pdf>

Hope for the best, plan for the worst? Insights into our planning for a longer life, February 2018¹⁵

This research examined whether retirees were aware of and planning for increased life expectancy, whether their plans cover the higher costs of later life and whether they support savings options to address longevity.

The report found that an overriding majority of retirees (85%) are aware of increasing life expectancy and half (50%) had financial plans to accommodate longer lifespan but with 22% having made no plans at all.

The research found of those planning ahead only 3% planned to spend more in later life, 61% planned to spend the same throughout and 36% planned to spend more in the early years of retirement. In this regard there appears to be a competition between spending on leisure activities (such as travel) in the early years of retirement with spending on care in later life.

It argues people are more inclined to be present orientated and focused on spending earlier in life than for unknown's in later life. It acknowledges one of the barriers to planning for later life and aged care needs is a fear and distrust of the aged care sector.

The research also asked respondents if superannuation funds should include an insurance option to keep paying an income if they lived longer than 85. 55.7% answered yes and 35% answered no.

It asked a further question about whether people would put aside 10% of their of their savings to receive an income for life after age 85. It found 57% would consider this option, with 32.4% responding they would be unlikely and 10.8% saying no because they wouldn't live that long.

However, it was found those more likely to support these options were less likely to be able to fund these at the time of retirement

¹⁵ McCallum, J., Maccora, J., & Rees, K. 2018. *Hope for the best, plan for the worst? Insights into our planning for longer life*. Brisbane: National Seniors https://nationalseniors.com.au/uploads/01182863PAR_HopeForTheBest_Report_FN.pdf

Retirement income worry Who worries and why? January 2020¹⁶

This research investigates people’s worry about having enough retirement income.

As shown in Figure 1, just over 50% of older people worry they will outlive their savings and investments. Unsurprisingly, people with a defined benefit scheme or annuity were the least worried about outliving their savings.

It showed worry is higher among people not already retired. It argues this anticipatory worry could be dealt with by better planning and saving and that superannuation trustees have an important role to play here.

It also showed worry was higher among people with lower levels of savings, which is understandable.

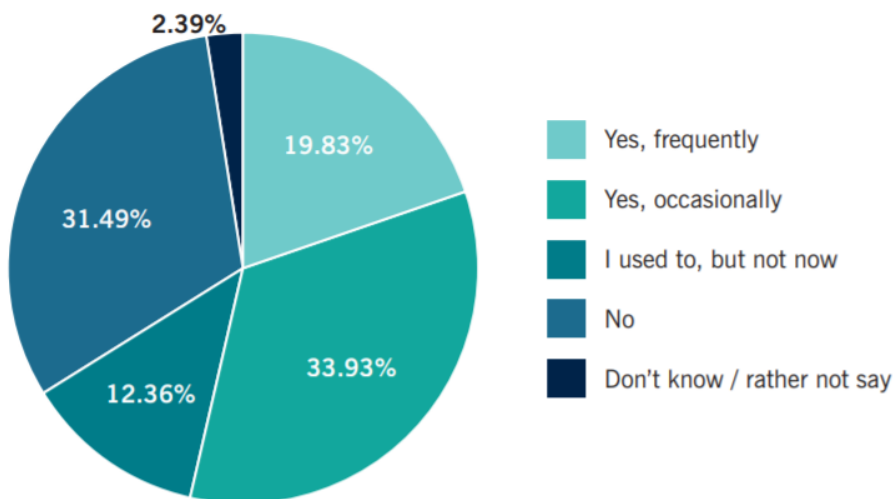
People expecting their main source of income will be the Age Pension also worry more.

Worry is higher among women, likely as result of expectation of caring roles and risk of outliving a partner.

An interesting finding is worry about running out of money is no different between those who received some form of financial advice and those who didn’t.

However, those that received advice from a financial adviser were more satisfied than other sources of advice.

Figure 1: Do you worry that you might outlive your savings and investments?¹⁷



¹⁶ National Seniors and Challenger 2020. *Retirement income worry: Who worries and why?* Canberra: National Seniors <https://nationalseniors.com.au/uploads/0120203573PAR-RetirementIncomeWorry-ChallengerRpt-FNREV.pdf>

¹⁷ National Seniors and Challenger 2020. *Retirement income worry: Who worries and why?* Canberra: National Seniors <https://nationalseniors.com.au/uploads/0120203573PAR-RetirementIncomeWorry-ChallengerRpt-FNREV.pdf>

Feeling financially comfortable? What retirees say March 2019¹⁸

This report documents the consumer experience of different comfort levels in retirement for those with private assets and how different financial situations affect a retiree's sense of comfort.

Over half of respondents worried about outliving their savings and investments. The incidence of worry was higher among women, those in poor health and with less savings.

Despite having low tolerance of loss many continue to invest in the market.

Those with defined benefit schemes reported peace of mind and security.

Having 'enough to last' and preserving capital are strong focal points for achieving comfort.

"Retirees with a defined benefit pension report experiencing a sense of comfort and security about their future. This confirms the importance of policy solutions to provide comparable options in retirement for those who are not in a defined benefit scheme."

Once bitten twice shy: GFC concerns linger for Australian seniors July 2018¹⁹

This report examines older Australians' understanding of retirement income issues through their experiences of the global financial crisis (GFC).

Older Australians remain wary of market turmoil and appear intolerant of enduring losses if a future economic crisis were to occur. Despite this they continue to hold a proportion of their savings in market-linked investments.

One third of respondents over 80 had already run out of money in retirement with a quarter of respondents aged between 75 and 79 running out.

Having income that lasts a lifetime and a desire for regular and constant income were seen as the most important financial goals.

Just over half of respondents had made a financial plan for living longer.

A majority of respondents were happy to be retired and had chosen to retire, with those retiring younger being happier in retirement and more regrets among retirees who chose to retire at an older age.

The GFC has resulted in retirees tending to be more conservative in their retirement income strategies.

¹⁸ McCallum, J, Hosking, D. & Rahn, A. 2019. *Feeling financially comfortable? What retirees say*. Brisbane: National Seniors <https://nationalseniors.com.au/uploads/ChallengerReport-FeelingFinComfortable-Web.pdf>

¹⁹ National Seniors and Challenger 2018. *Once bitten twice shy: GFC concerns linger for Australian seniors*. Brisbane: National Seniors https://nationalseniors.com.au/uploads/07183036PAR_OnceBittenTwiceShy_Web_0.pdf

Seniors more savvy about retirement income October 2017²⁰

Having a regular, constant income that met essential spending needs was found to be most important in terms of retirement finances.

Three quarters of respondents were aware and planning for the possibility of living longer.

Conserving capital for the next generation is no longer a key consideration with as many as 50% indicating they will spend all or most of their savings.

A majority said they used a financial adviser to get information about retirement

In general, it found retirees had conservative investment plans with a focus on retirement income as a stable wage.

Over 50s: still not confident about their retirement income²¹

Older retirees (over 80) are either reliant on the Age Pension or have savings in non-super financial assets to support themselves in retirement. Super was not available to everyone in this cohort and the survey confirms only a small proportion of older retirees are generating income from super.

Even though older Australians expect super will be their income source in retirement, less than half of them are confident it will be adequate.

A majority of respondents under the age of 80 had recently consulted a financial advisor and a majority of all respondents use a budget to manage their finances.

It was found that retirees have a range of favored strategies for controlling expenses, suggesting a bias towards preserving capital.

Reasons for preserving savings was to meet unexpected expenses, with the unpredictability of retirement years feeding this behaviour.

Uncertainty about changing family, health and living arrangement situations appears to be a critical source of insecurity for older Australians when thinking about their retirement income.

²⁰ National Seniors Australia and Challenger 2017. *Seniors more savvy about retirement income*. October 2017
https://nationalseniors.com.au/uploads/09172675CRP_ChallengerReport_RetirementIncome_FN_0.pdf

²¹ National Seniors Australia and Challenger 2016. *Over 50s: still not confident about their retirement income* National Seniors Australia: Melbourne
https://nationalseniors.com.au/uploads/05161796CRP_ChallengerReport_REV070716.pdf