Australia's Future Tax System

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A submission on the retirement income system

Consultation questions

The following questions are posed to stimulate community input to the Panel's consideration of issues relating to retirement incomes.

The retirement income system

Q1.1 In considering the future of Australia's retirement income system, which objectives are relevant in setting retirement income policy? Does the current system of the Age Pension and compulsory and voluntary savings meet these objectives? If not, how should the system be changed to meet these objectives?

The three pillar system appears to only work effectively for those with continuous work and higher incomes.

For low income workers and people with broken work patterns, the "voluntary savings" pillar has minimal incentives, tax concessions and provides no flexibility for contingencies. Hence any extra savings are placed outside super.

The "compulsory savings" pillar provides no tax advantage to low income workers, but does to higher income workers.

Some ideas on changes

<u>Super Guaranteed</u>

- Remove tax concession for 9% super guaranteed contributions.
- The savings made should be used to increase incentives for voluntary savings. E.g. co-contribution
- Remains preserved

<u>Voluntary Savings</u>

Increasing the co-contribution at the expense of the tax concession on the 9% SG, would likely increase voluntary savings above those currently experienced.

- Convert First Home Savings Account (FHSA) to a voluntary savings account
- Allow access to voluntary savings.

The FHSA account should be changed to provide:

- Increased contribution incentives
    - Allow Co-contribution payments
    - Increase co-contribution rate from tax concession savings made on SG
    - Co-contribution for all tax payers at a flat rate

- Access – Pay back co-contribution when withdrawing money.
- Continue with housing deposit scheme – with a cap for a deposit.
- Allow account to continue until retirement.
- Allow to invest in growth assets.
- The contributions limit may need to be changed.

The First Home Saver Account (FSHA) could serve this purpose for voluntary savings. It could be converted to a medium term savings account that runs in parallel with the superannuation system. This ensures that the existing superannuation system of SG and preservation is protected and continues without change.

The design of the FHSA would allow a highly flexible voluntary savings account. It provides higher co-contributions combined with the ability to access your own contributions, but at the expense of paying back the co-contribution.

The increased co-contribution and access to savings, makes it more attractive than paying of your home loan faster. The FHSA also acts as a redraw facility earning a higher rate of return and co-contribution than placing extra repayments into a lower rate of return home loan.

A broad and adequate retirement income system

Q2.1 As the SG system matures, it will become a greater part of an employee's retirement income. What are the implications for individuals partially or fully excluded from the mature SG system (the self-employed, individuals with broken work patterns such as carers, women and migrants), and how can the retirement income system best accommodate these groups?

For carers, a payment to superannuation of an equivalent 9% of a minimum nurse wage. This equates to about $2,500 per year. ($28,276 x 0.09 = $2,544). Source: NSW Nurses Association, 8 July 2008.

As discussed in Q1.1, workers with low income and broken work patterns have lower SG savings, and thus need higher voluntary savings to compensate. These people need the flexibility to access their limited savings, but also need a tax effective savings vehicle when they can.

Changes to FHSA could provide flexibility and tax benefits for these people.

Q2.2 Noting that the adequacy of the Age Pension is being considered by the Pension Review, what is an appropriate concept of adequacy for the retirement income system? Should it be to ensure there is a minimum level of income in retirement, to replace a proportion of income earned prior to retirement, or some other alternative?

Nil

Q2.3 What should the role of the government be in assisting individuals to meet their retirement income expectations in relation to the support provided by the Age Pension, the level of compulsory savings and incentives to make additional savings? Should the role of government change as an individual's income increases over their working life?

Projections:

- Government should regulate projections.
- Projections should be given in terms of income per year, and not lump sum. *($300,000 sounds a lot, but $15,000 per year does not*)
- Projections should not include the age pension. *(Thus highlighting a smaller final income at retirement, and thus increasing the likelihood that the person will take action to increase voluntary savings).*

Voluntary Savings

- As discussed, making changes to the FHSA provides a flexible voluntary savings vehicle that is separate to preserved SG.
- Providing a higher co-contribution to the FHSA, but is paid back if savings are accessed before retirement.
- The higher co-contribution is funded from removal of the contribution tax concession on the SG.

An acceptable retirement income system

Q3.1 Do the settings of the retirement income system, such as the level of SG and access to concessions, adequately consider the needs and preferences of individuals both before and after retirement?

Nil

Q3.2 Is the current level of superannuation income tax concessions appropriate and sustainable into the future? Are the current concessions properly targeted, and if not, how should they be reformed?

Current tax concessions for the 9% SG only benefit middle to high income earners. The cost of this limits the ability to use tax concessions for voluntary savings for low to middle income earners. It also impacts the sustainability of the system.

As discussed, remove SG contribution tax concession, and use this saving to increase co-contribution payments to increase voluntary savings. i.e. where behavior can be influenced.

A robust retirement income system

Q4.1 At what age should an individual be able to access their superannuation and at what age should they become eligible for the Age Pension?

Voluntary savings should be accessible before retirement age, but only at marginal tax rates.

For many younger people, accessing money at age 65 or even 70 is many decades away. And the thought that we could work continuously full time until that age, seems unrealistic. Many people will want to drop back to part time or casual work. Doing this allows people to extend their working life without burn out. To support this work\life balance some partial drawdown on savings or use of income from investments could help.

Converting the FHSA, would serve the purpose to provide drawdown of “voluntary only savings” before age 65.

Q4.2 What is the role of individuals in dealing with investment and longevity risk in accumulating and drawing down their retirement income? Do financial markets provide the means to deal with these risks? If not, is there a role for government to address these shortcomings?

Nil

A simple and approachable retirement income system

Q5.1 In what ways does the retirement income system impose undue complexity and cost on retirees and workers? How could this complexity be reduced?

Nil

A sustainable retirement income system

Q6.1 The Age Pension serves two roles, as a safety-net for individuals who are unable to sufficiently save for their retirement and as an income supplement for many individuals who do save. What should be the role for the Age Pension and means testing in a future retirement income system and what impact does this have on its sustainability into the future?

In the future, number of retirees will double, but the number of taxpayers will plateau. Hence either taxes are increased or pensions are reduced. Therefore all assets including house and land should be utilised to support retirement income.

In calculating the CPI, land is not included as it is classified as an investment.
Land holds the greatest wealth in our country, yet it’s not fully assessed for the pension.

Q6.2 In what ways does retirement income policy affect workforce participation decisions and what, if any, changes might reduce disincentives to work? Does the sustainability and cost of the retirement income system affect the workforce decisions of younger generations of workers?

Nil

Q6.3 What impact could financial intermediation have on the effectiveness of retirement income policy?

Nil