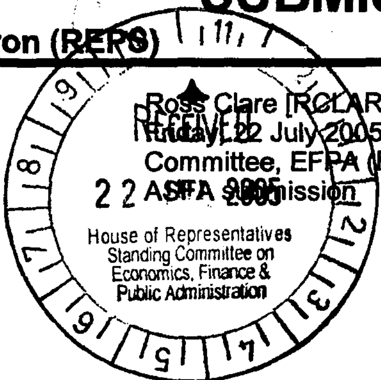
SUBMISSION 16

Bryant, Sharon (REPS)



From: Ross Clare [RCLARE@superannuation.asn.au]
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House of representatives Standing Committee on Economics. Finance and Public Administration

Submission No: 16

Date Received: 22/7/05

Secretary: SB

200511 Under 40 July 2005.doc ...

I have pleasure in forwarding the submission of the Association of Superannuation Funds of Australia in regard to the Committee's current investigation into improving the superannuation savings of people aged under 40.

Ross Clare
Principal Researcher
ASFA

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ASFA 2005 National Conference & Super Expo
9th-11th November 2005 Melbourne <http://www.superannuation.asn.au>

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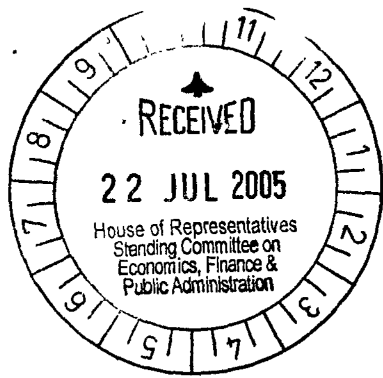

SUBMISSION 16

House of representatives Standing Committee on Economics, Finance and Public Administration

Submission No: 16

Date Received: 22/7/05

Secretary: [illegible]

Submission to

House of Representatives Standing Committee on Economics, Finance and Public Administration

Inquiry into

Improving the superannuation savings of people under 40

by

The Association of Superannuation Funds of Australia Ltd

July 2005

Recommendations

Recommendation 1: ASFA recommends that, in order to better meet retirement income needs and expectations, contributions be increased in effect to an amount equivalent to 15% of wages through a combination of compulsory contributions, voluntary contributions and tax relief.

Recommendation 2: The parameters of the superannuation co-contribution be changed from 2006-07 onwards so that it is extended to individuals on low/middle incomes of up to $60,000 per year, and that the phase-out rate for the co-contribution be adjusted so as to provide a greater incentive for middle income earners in particular.

Recommendation 3: That the current standard 15% rate of tax applying to contributions be abolished, either in one year or progressively over five years, with effect from 2006-07 onwards.

Recommendation 4: That the $450 a month earnings threshold for Superannuation Guarantee payments be abolished.

Recommendation 5: That the current age based contributions limits currently applying to those aged under 40 be abolished or be significantly modified to allow for greater flexibility in the pattern of employer contributions to superannuation over a working life.

Recommendation 6: ASFA recommends that the Government pursue reforms that would permit superannuation funds to provide benefit projections to individual members on a standardised basis as part of their annual reporting to members.

1. Introduction

ASFA is a non-profit, non-party political national organisation whose mission is to protect, promote and advance the interests of Australia's superannuation funds, their trustees and their members. As such it is the "Voice of Super". ASFA is distinctive amongst industry organisations in that it has a strong focus on the interests of consumers. These interests range from improving consumer protection to enhancing the financial security and retirement income of all Australians.

ASFA's 375 or so constituent member funds have been estimated to be responsible for over 80 per cent of the total superannuation assets held in funds other than Self Managed Superannuation Funds (SMSFs). ASFA member funds are responsible for the vast majority of assets and members in each of the retail, public sector, corporate and industry fund sectors. ASFA also has a strong representative function for the 20 per cent or so of assets held by SMSFs given that many of the major advisory firms for SMSFs are members of ASFA. ASFA member funds in aggregate represent over 80 per cent of Australians with superannuation, and the bulk of the $710 billion in superannuation assets as at March 2005.

Given this wide coverage of both funds and fund members ASFA is uniquely placed to present both industry and community views on the issues of adequacy of both retirement savings and retirement income. In doing so it is able to draw on the experience of member funds, and a significant body of research. Most ASFA member funds have extensive experience in the design of retirement benefit arrangements and/or have had considerable exposure to fund member expectations in regard to retirement living standards. The research undertaken by ASFA includes both modelling of projected retirement incomes and needs in retirement, and public opinion polling (of both those aged under 40 and those over 40) in regard to community perceptions of adequacy and what individuals and government can do to improve adequacy of retirement incomes.

2. What we know about Australians aged under 40

2.1 The broad demographic characteristics of the population aged under 40

Those aged under 40 are by definition younger than the rest of the population, but they demonstrate both similarities and differences to the rest of the population. Some of the differences come from being at a different stage of the life course than the rest of the population, but some differences will remain (and others will emerge) as this group in the population ages.

People aged under 40 are fortunate in being able to escape being characterised as "babyboomers". While definitions can differ slightly between different researchers, babyboomers are generally regarded as the large numbers of people born in the post-World War 2 demographic of 1946 to 1964 (Kelly et al, 2002). They are now aged at least 40, and can be as old as 59.

Those aged under 40 are generally tagged as Generation X and Generation Y. Again, definitions differ between various pop-demographers, but Generation X are not infrequently regarded as the group currently aged between 30 and 40, while Generation Y is the group currently aged between 20 and 30. Beyond that the alphabet starts to run out, with Generation Z sometimes being regarded as those currently aged under 20.

Clearly those aged under 40 differ from those aged over 40 because they are younger, but whether this is a fundamental difference or merely being at a different stage of the life course is a matter for conjecture. Those aged under 40 are only a part way through their life course, with the younger under 40s only a very small part of the way through. They will have their dreams about their future life (perhaps even about their standard of living in retirement), but the challenge will be to put in place the means for achieving those dreams. For many of the younger members of this age cohort completion of formal full-time education and getting the first real job in terms of paid employment is still to happen. Table 1 below provides further detail on various indicators of economic and social outcomes for different age cohorts.

Table 1: Characteristics of individuals within various birth cohorts, 1998-99

	Gen X and Y	Baby Boomers	55-64 years olds	Retired
	%	%	%	%
Employment Status				
Employee - full time	**44**	47.3	22	1
Employee - part time	**19.3**	16.5	10.5	2.4
Self employed	**5.2**	11.6	11.9	2.8
Unemployed	**8**	4.7	2.3	-
Not in the labour force	**23.4**	19.8	53.3	93.8
Occupation				
Managers/ administrators	**2.4**	6.7	5.6	1.6
Professionals	**11.2**	15.7	6.6	1.2
Associate Professionals	**6.4**	10.3	4.3	0.7
Tradespersons	**10.8**	9.2	5.3	0.6
Marital status				
Never married	**58.7**	8.8	4.3	3.7
Widowed	**0.2**	1	6.5	28.6
Divorced	**1.2**	7	8.7	4.7
Separated	**1.5**	4.1	3.8	1.3
Married	**28.1**	73.7	74.4	61.1
De facto	**10.2**	5.4	2.2	0.5

Note: Retired refers to those aged 65+
Source: ABS 1998-99 Household Expenditure Survey, unit record data, as reported in Kelly et al 2002.

Household formation and purchasing a home has not happened for a significant proportion of the adult population aged under 40, and would not show any dramatic increase if the table was updated to 2005. In particular, there are indicators that the average age of first marriage and average age for purchasing the first home have increased over the last decade or more. Significant proportions of both Generation X and particularly Generation Y are still comfortably in place in the family home (ABS 2005). However, this may well indicate delay in achieving these stages of the life course, rather than any evidence of a decline in the eventual rates of family formation and house purchase. As well, the low rate of divorce amongst Generations X and Y rather than evidence of relationship stability is more an outcome of only a small proportion of them being either married at all or married long enough for marital discord to take hold.

2.2 Life expectancy and years in retirement for those currently aged under 40

Projections of life expectancy and average years in retirement are very relevant matters to take into account when considering the adequacy of current contributions to superannuation by those aged under 40, and the extent to which contributions should be increased to generate the retirement incomes Australians of that age cohort expect and deserve.

There are some interesting projections bandied about from time to time. For instance, some commentators have suggested that a baby girl born this year can expect to live into her nineties, and hence will have forty or so years in retirement. This statistic or projection is certainly interesting, but it would be news to most demographers. In Australia, life expectancy at birth (as traditionally calculated) currently is 76 years for men and 82 years for women. Average life expectancy could increase to something in the nineties, but it would require yet-to-be-discovered medical breakthroughs and/or the passage of a lot of time. Equally, some nasty new virus affecting humans could emerge, or Australians could become victims of their own affluence with a higher incidence of obesity, increasing the rate of premature death. Whether life expectancy will continue to increase and at what rate is essentially unknowable. Policies should be designed to cope with uncertainty, rather than assuming one possibility is a certainty.

2.2.1 A possible central case for population projections

According to information published by the Australian Government Actuary, currently about one in ten men die by age 60 and one in ten women die by age 65. These ages have increased by around 10 years over the last two decades, with medical treatment and improved health outcomes particularly effective in reducing the incidence of premature death. These ages are expected to increase further to around 64 and 69 respectively for persons born around now (who will be retiring in about sixty years).

For those retiring over the next few decades who necessarily have a life expectancy that is already more or less determined, **it is likely that around 40% of the population will spend up to 25 years in retirement, around 40% will spend up to 35 years in retirement and around 10% will spend more than 35 years in retirement. A significant minority of individuals will spend more time in retirement than they did in the labour force.**

3. The distribution of superannuation amongst the population aged under 40

The current superannuation entitlements of those aged under 40 largely reflect their involvement in the paid labour force. Very young people do not have any superannuation. Measures such as the provisions allowing the establishment of superannuation accounts for children which were in place for a short time prior to June 2004 were not at all popular. In June 2004 there were only 3 children's accounts out of 9 million accounts in total in industry, corporate and public sector funds. Changes to the contribution rules for superannuation that have applied since 30 June 2004 have made it possible for any person with legal capacity to open a superannuation account and make contributions, but there is nothing to indicate that at this stage these changes have led to significant new contributions by those who are relatively young and/or are not in paid employment.

However, persons aged under 40 make up a large proportion of the members of superannuation funds. Data collected by the Australian Prudential Regulatory Authority (APRA 2005) indicates that those aged under 35 amount to 39% of the membership of corporate funds, 52% of the members of industry funds, 31% of the members of public sector funds, and 44% of the members of retail funds. The proportion of the assets of those funds associated with these members is much lower than those percentages, reflecting their lower average account balances.

As indicated by the figures in bold type in Table 2, a large majority of males and females aged under 25 have a current superannuation balance of less than $5,000, with over 40% having no superannuation at all. For those aged between 25 and 34, around half of men have balances between $10,000 and $50,000, while around half of women have a superannuation balance between $1,000 and $20,000. For those aged 35 to 44 around half of men have balances between $20,000 and $100,000, while for women around half have balances between $5,000 and $50,000.

Table 2: Distribution of Superannuation Balances by Age and Gender

	Superannuation Balances - Males								
	No Super	$1 - $1000	$1000 - $4999	$5000 - $9999	$10000 - $19999	$20000 - $49999	$50000 - $100000	> $100000	Total
15 - 24	**7.5%**	**3.7%**	**4.2%**	1.8%	.8%	.3%	.1%	.1%	18.4%
25 - 34	1.5%	.6%	2.8%	2.8%	**4.9%**	**4.3%**	1.5%	1.0%	19.3%
35 - 44	1.6%	.4%	1.4%	1.6%	2.7%	**5.6%**	**2.8%**	3.1%	19.3%
45 - 54	2.3%	.2%	.8%	.7%	1.5%	3.2%	2.6%	6.1%	17.3%
55 - 64	3.9%	.2%	.4%	.2%	.7%	1.4%	1.4%	4.4%	12.6%
65+	9.6%	.1%	.1%	.1%	.2%	.5%	.5%	1.9%	13.1%
Total	26.4%	5.2%	9.7%	7.3%	10.7%	15.2%	8.8%	16.6%	100.0%
	Superannuation Balances - Females								
15 - 24	**7.8%**	**4.0%**	**3.3%**	1.1%	.8%	.3%	.1%	.0%	17.4%
25 - 34	3.4%	1.1%	**3.7%**	**3.0%**	**4.0%**	2.7%	1.1%	.4%	19.2%
35 - 44	4.1%	.8%	2.9%	2.0%	**3.1%**	**3.0%**	1.5%	1.3%	18.7%
45 - 54	4.0%	.4%	1.7%	1.4%	2.3%	3.2%	1.7%	2.6%	17.2%
55 - 64	5.7%	.4%	.5%	.5%	.6%	1.3%	1.1%	2.1%	12.2%
65+	13.4%	.1%	.1%	.1%	.2%	.4%	.3%	.8%	15.3%
Total	38.2%	6.8%	12.2%	8.0%	11.0%	10.9%	5.7%	7.2%	100.0%

Source: Unit record file of the 2002 data collection of the Household, Income and Labour Dynamics in Australia (HILDA) Survey.

Along with differences in superannuation balances related to the age of individuals, there also are differences related to income (and gender). Women tend to have lower superannuation balances than men due to segmentation of the workforce, with women tending to be clustered in low paying occupations, and women also tending to have more breaks from the paid workforce due to family responsibilities. For example, women in full-time jobs on average earn 92% of the average hourly rate earned by men (ABS 2005), and women on average are in the paid labour force for the equivalent of around 20 full-time working years, compared to around 37 years for men (Clare 2001). Table 3 provides details of the subsequent differences in superannuation balances.

Table 3: Superannuation Balances by Age Group, Gender and Level of Income**

		Average Superannuation Balance ($)		
	Age Group	*Low Income*	*Medium Income*	*High Income*
Men	15 - 24	500	10,000	8,000
	25 - 34	**9,000**	**20,100**	**39,400**
	35 - 44	**13,600**	**40,500**	**93,400**
	45 - 54	34,500	70,700	164,700
	55 - 64	55,500	104,200	252,000
	65+	16,200	78,000	196,000
	Total	17,000	46,600	122,500
Women	15 - 24	600	6,200	6,600
	25 - 34	**7,900**	**14,900**	**49,800**
	35 - 44	**10,400**	**26,800**	**82,300**
	45 - 54	18,000	40,300	156,300
	55 - 64	22,900	74,800	127,000
	65+	6,500	39,200	77,600
	Total	9,400	29,700	100,000

** Low Income = Gross income of less than $15,000 in the last financial year
Medium Income = Gross income of $15,000 - $49,999 in the last financial year
High Income = Gross income of $50,000 + in the last financial year

Source: Unit record file of the 2002 data collection of the Household, Income and Labour Dynamics in Australia (HILDA) Survey.

3.1 Prospective superannuation balances for the population currently aged under 40

Individuals currently aged 40 and under will generally end up with higher superannuation savings than indicated in the tables above as most will still have many years in the paid labour force remaining. Table 4 sets out projections of eventual retirement savings for different income levels based on some reasonably arbitrary (but not unrealistic) starting points. For individuals currently aged 40 and under the preservation age for accessing superannuation for retirement purposes is age 60, rather than between 55 and 60 for those aged over 40.

Table 4: Projections of lump sum superannuation benefits based on current age and past receipt of the Superannuation Guarantee(a)

Wage		**$30,000**	**$40,000**	**$60,000**	**$80,000**	**$90,000**	**$100,000**
Starting balance		*$18,000*	*$24,000*	*$36,000*	*$48,000*	*$54,000*	*$60,000*
Age	**Retiring at**						
25(b)	**60**	142 000	190 000	285 000	380 000	**427 000**	**475 000**
	65	178 000	238 000	357 000	**476 000**	**535 000**	**594 000**
30	**60**	156 000	207 000	311 000	**415 000**	**467 000**	**519 000**
	65	194 000	258 000	388 000	**517 000**	**581 000**	**646 000**
35	**60**	123 000	164 000	246 000	328 000	369 000	410 000
	65	156 000	207 000	311 000	415 000	467 000	519 000
40	**60**	95 000	126 000	190 000	253 000	285 000	316 000
	65	123 000	164 000	246 000	328 000	369 000	410 000

Source: ASFA Research Centre projections.

(a) The projections are in current dollar terms using a 3.75% AWE deflator, and assumed nominal fund earnings of 7% after taxes and fees per year, with contributions at the SG rate of 9%.

(b) No prior superannuation savings are assumed for those aged 25. For ages above these, the start balance assumed takes into account the phased introduction of the Superannuation Guarantee. While examples of salary levels in excess of $80,000 a year are given for age 25 on the grounds of completeness, it is unlikely that there would be many such cases.

As the table indicates, an individual needs a substantial number of years of contributions together with a substantial annual salary in order to generate retirement savings of the order of $500,000 or more, which is the amount needed to generate sufficient income in retirement to support a comfortable lifestyle for a couple retiring at age 65, assuming that both will have eligibility for a full or part Age Pension during the course of their retirement.

ASFA has undertaken research into what expenditure is objectively required to sustain a comfortable standard of living in retirement. The level of the Age Pension tells you what people can survive on, but most Australians want and need more than the Age Pension. This will be particularly the case for those currently aged under 40.

The research results, based on a comprehensive research project and report conducted by the Social Policy Research Centre at the University of New South Wales (SPRC 2004), provides detailed budgets of what singles and couples would need to spend to be able to have a comfortable lifestyle in retirement, enabling an older, healthy retiree to be involved in a broad range of leisure and recreational activities and to have a good standard of living through purchase of such things as household goods, private health insurance, a reasonable car, good clothes, a range of electronic equipment, and domestic, and occasionally international, holiday travel. These budgets are known as the Westpac-ASFA Retirement Living Standard. They are very commonly used by individuals planning for retirement, and by advisers to such persons. Government agencies such as the Treasury have also made use of the budgets in their modelling work on adequacy levels (for example see Rothman and Bingham 2004).

The comfortable budget allows for entertaining at home (a family roast) once a fortnight, seven glasses of wine a week, eating out at a RSL Club restaurant 3 times a week or a more expensive restaurant once a week. It allows for the maintenance of a second hand car – a 4-year-old Camry rather than 8-year-old car. It allows for the bathroom or kitchen to be replaced during retirement rather than those items being left untouched for 20 years or more. The comfortable budget also makes provision for the maintenance of a personal computer, mobile phone, and a digital camera – items that allow Australian retirees to participate in a modern society and which are also very much used by those currently aged under 40. It allows for a budget overseas holiday every 5 years. The budgets are updated every three months in line with movements in relevant prices. The current annual levels of expenditure for a comfortable lifestyle are $34,000 (single) and $44,500 (couple). Detailed budgets and the underlying research report can be downloaded from the ASFA website (www.superannuation.asn.au).

Such lifestyles in retirement would not be regarded as lavish by those currently aged under 40 given the typical lifestyles and expectations of such individuals. However, for many individuals achieving the retirement savings required to fund such a lifestyle may prove difficult. As shown by Table 5, career breaks and periods of low earnings, not unusual events for many women and an increasing number of men, lead to relatively modest retirement savings even after a period of 35 years or so. For those women who manage to achieve a high income towards the end of their working life, the combined effect of the delay in achieving a significant income and years out of the workforce is considerable.

Table 5: Impact of breaks from paid labour force

Scenarios (based on SG contributions)	Lump Sum
Starting at $20,000 for 10 years. A break for 7 years then $45,000 for 17 years	$115 365
Starting at $40,000 for 10 years. A break for 7 years then $40,000 for 17 years	$140 090
On $40,000 for 34 years, no breaks	$181,000
Starting at $40,000 for 10 years. A break for 7 years then $80,000 for 17 years	$212 601
On $60,000 for 34 years, no breaks	$271,700

Source: ASFA Research Centre projections.

Finally, Table 6 provides an indication of the gap between what the Superannuation Guarantee will deliver, and what would be required to be contributed in order to generate retirement incomes of the order wanted or expected by many individuals currently aged under 40. As the table clearly indicates, even leaving the task of additional savings until 20 years before retirement (say age 40 or 45) leads to a very substantial additional savings task. If additional savings were made over the entire period of superannuation contributions then the task becomes more manageable.

Table 6: Percentage of income over and above the 9% Superannuation Guarantee required to be saved to achieve 60% of pre-retirement income(a)

	Final income (Retirement income sought)		
Years to retirement	**$35000 ($21000)**	**$50000 ($30000)**	**$75000 ($45000)**
20	13%	22%	28%
25	7%	14%	19%
30	3%	9%	12%
35	1%	5%	8%
40		2%	4%

(a) Projections based on fund net (after tax and fees) earning rate of 7% nominal and growth in average earnings of 3.75% with contributions being made by the employer and subject to 15% tax. The first figure in the top row of the columns is the annual wage, with the figure in brackets the retirement income sought at that income level.

Accordingly, ASFA considers that the current rate of the Superannuation Guarantee will not in itself be sufficient to generate the retirement savings and retirement incomes that those currently aged under 40 need.

ASFA recommends that, in order to better meet retirement income needs and expectations, contributions be increased in effect to an amount equivalent to 15% of wages through a combination of compulsory contributions, voluntary contributions and tax relief.

For instance, this could be achieved by increasing the total amount of compulsory and voluntary contributions to 12% of wages and salaries and by the government assisting by removing the tax on contributions (value approximately 3% of wages). The combined effect would be similar to a 15% contribution under current superannuation tax arrangements.

4. Survey evidence on attitudes, needs and intentions of those aged under 40

ASFA has on a regular basis commissioned surveys of the public in order to gain a better understanding of the views of the Australian population in regard to superannuation. The 2004 exercise by the professional polling organisation ANOP involved a telephone survey of 755 Australians aged 30 to 69 years, and was conducted in late May/early June 2004. Amongst other things, the survey provides an inter-generational analysis (Generation X vs Baby Boomers) and compares the views and expectations of those retired with the experiences of retirees in the 30 to 69 age band. While some of the differences between those aged under 40 and the rest of the population come from being at a different stage of the life course, there also are other differences that are likely to be sustained over the longer term. Those aged under 40 should not and cannot be regarded as being incomplete babyboomers.

While the main findings of the research were published in August 2004, more detailed cross-tabulations were made available to ASFA and these findings form the basis of this section of the submission.

4.1 Retirement age

Of those surveyed, men expected to retire later than women, with a mean expected retirement age of 60 for men and 59 for women. Just over 30 per cent of men expected to retire at 65 or over, compared to 22 per cent of women. Of those survey aged 30 to 39, a substantial 15% expected to retire before age 55, compared to only 6% of those aged 40 to 49. Given that the preservation age of 60 applies to those aged under 40, an intention to retire prior to age 60 implies one or more of an expectation of being able to rely on a partner or inheritance for financial support, achieving significant savings outside superannuation, or ignorance of the preservation arrangements for superannuation.

The survey data suggest that for a variety of reasons many individuals also retire before they expected to. The mean actual retirement age for those retired was 57 for men and 55 for women, with both these figures somewhat below the expected retirement ages for those not yet retired.

While future outcomes might differ from past outcomes, this suggests that many women and men will retire earlier than they anticipated. A significant proportion of both women and men will therefore not be able to rely on the employment income they were anticipating to receive after age 55 or 65 or whatever.

4.2 Attitudes to retirement

Around 40 per cent of both men and women of all ages were looking forward to retirement, with only around 5 per cent of those aged 30 to 39 not looking forward to retirement. Those in that age group were looking forward to retirement because there would be less stress, and there would be free time and time for travel. Around 60 per cent of the cohort claimed that they were preparing well financially for retirement, with 40 per cent not confident about their preparation. The not confident proportion was higher than for older respondents.

4.3 Savings for retirement

Those aged 30 to 39 indicated relatively high reliance on home ownership and compulsory superannuation as parts of their savings for retirement. Around 40 per cent identified voluntary superannuation contributions as part of their savings plans, a lower figure than for older age groups. The 30 to 39 year olds were also less prone to identify savings accounts as a savings plan and more prone to identify purchase of an investment property as a means of saving for retirement.

4.4 Income required in retirement

The mean (average) minimum annual retirement income considered to be required for the respondent and their partner for respondents currently aged 30 to 39 was around $43,000 per year. This age group generally had higher retirement income targets than older respondents. Only 21 per cent of those aged 30 to 39 considered that an income of less than $29,000 a year would be sufficient, with 34 per cent considering that $50,000 plus would be the minimum they would need.

These minimum requirements were often accompanied by doubt whether they would be achieved, with around 40 per cent of respondents indicating that their savings would be less than required to generate the income specified, or that they were unsure whether it would be achieved.

4.5 Knowledge of likely income in retirement

When pressed about how good an idea the respondent had about likely income in retirement, around 75 per cent of those aged 30 to 39 indicated that they really did not know, with only 8 per cent indicating that they had a good idea. In comparison, 34 per cent of those aged over 50 claimed they had a good idea.

4.6 Work plans in retirement

Around 50 per cent of those aged 30 to 39 expected to continue in some kind of paid work in retirement, with around 40 per cent expecting to be involved in voluntary work (with some expecting both). The actual experience of those respondents who had retired indicates there may be some disappointed expectations, with only 36 per cent of men and 21 per cent of women continuing in paid work, with 30 per cent of men and 35 per cent of women continuing in voluntary work.

However, those aged 30 to 39 did acknowledge the potential difficulty in obtaining paid work of some kind after retirement, with 87 per cent of respondents saying it would be difficult to get such work. Some of this attitude might be a little self serving, with 20 per cent of the respondents indicating that it would be hard to compete with young people. This compares to only 7 per cent of those aged 60 to 69 indicating that it is hard to compete with young people.

Over 40 per cent of women would like to work in some management or professional role in retirement, but amongst women actually retired only 7 per cent do so, with the bulk (50 per cent) employed in clerical, service or sales. On the other hand, most men in paid employment in retirement reported that they worked in a management or professional role. Both expectations and reality favoured casual work, followed by regular part-time work.

4.7 Expectations of receiving the Age Pension

Of those aged 30 to 39, a large majority (72 per cent) do not expect to receive the Age Pension. Whether this is because they do not think they will qualify, or because of doubts about it still being available is not clear. This compares to 55 per cent of those aged over 50 and not yet retired who do not expect to receive the Age Pension. In contrast, projections suggest that for a very long time to come only around 25 per cent of retirees will not receive at least a part Age Pension. However, compared to when a similar question was asked in 2001, expectations of receiving the Age Pension have increased, particularly among 30 to 39 year olds.

4.8 Adequacy of compulsory superannuation

Around 70 per cent of those aged 30 to 39 consider that more than the 9% compulsory employer superannuation contribution is needed. Around 50 per cent think that the primary responsibility for increasing superannuation contributions should be on the individual, compared to around 40 per cent considering that the government should have primary responsibility. This compares to figures of 60 per cent and 40 per cent respectively for respondents aged over 40.

4.9 Reasons for and against contributing more into superannuation

Respondents aged 30 to 39 indicated that reasons to contribute more into superannuation included it being a good way to save, it is tax effective, and a good investment. Reasons not to contribute more included cannot afford to, and prefer other investments.

4.10 Perceptions of what would be good government measures to help adequacy

Respondents aged 30 to 39 indicated that the most important measure to help adequacy would be for the government to reduce the tax on superannuation contributions, with 38 per cent of respondents indicating this. The next most identified measure was matching contributions of low and middle income earners (32 per cent). Only 11 per cent of respondents indicated that that ensuring superannuation fund fees are reasonable would be the most important measure. Only 1 per cent of respondents identified encouraging people to work until they are 70 as the most important measure.

5. Strategies to move forward

ASFA's priorities for the long term reform and further development of Australia's retirement income system remain:

- ensuring adequacy of retirement incomes;
- providing incentives for greater self reliance, with assistance particularly directed to lower and middle income groups;
- broader coverage of superannuation, especially the self employed, casual employees, and those with a limited or no link to the paid labour force;
- simplification, particularly of taxation arrangements;
- promoting confidence and security for retirement/superannuation strategies.

These priorities are applicable to both those aged under and over 40 years. They also are very relevant to the specific terms of reference of the inquiry, namely the barriers and disincentives to contributing to superannuation, current incentives in place to encourage voluntary contributions, and improving the awareness of the importance of saving early for retirement.

5.1 Options for achieving better adequacy

The level of income replacement in retirement is sensitive to a number of factors. These include the pattern of paid employment of an individual and the number of years over which the contributions are made; the level and pattern of contributions, the level of contributions and earnings taxes and the rate of investment returns within the fund that is used. Some of these factors are susceptible to changes in policy, while others basically are history and/or are driven by social and economic factors that are difficult to influence.

That said, modelling of individual outcomes clearly confirms what is technically described by researchers as "the bleeding obvious". Higher contributions for more years, lower or no contribution taxes, and higher fund earning rates all contribute to greater adequacy of retirement income. Better product disclosure has allowed consumers to identify what they are paying for, to determine whether fees charged are appropriate to the features of the product, and to select an investment product appropriate to their investment needs.

As noted at Recommendation 1 of this submission at page 12, in order to better meet retirement income needs and expectations contributions have to be increased in effect to an amount equivalent to 15% of wages through a combination of compulsory contributions, voluntary contributions and tax relief.

Accordingly, ASFA has focussed on options involving additional contributions and/or removal of contributions tax as ways of improving adequacy.

5.2 Providing an even more effective co-contribution

The public opinion research commissioned by ASFA indicates that there is a very high level of support in the community for greater self-reliance in retirement, provided the responsibility is shared with government through more incentives to save for retirement. The polling also indicates that affordability of making additional contributions is an important consideration for those aged under 40.

The Government in adopting the superannuation co-contribution has recognised Australians' widely based support for mutual obligation, in which individuals save more for their retirement in return for greater support from government. The co-contribution provides a practical mechanism to deliver support from the government which is conditional on an individual's circumstances and the size of their own contribution. ASFA strongly recommends that the current co-contribution be built upon as a strategy to increase contributions to superannuation.

The current co-contribution applying to contributions made in 2004-05 and later years provides for a maximum co-contribution of $1,500, with this available for persons with assessable income and reportable fringe benefits of less than $28,000 a year. The government co-contribution matches the personal contribution of the superannuation fund member on a $1.50 for each dollar contributed by the member basis.

The maximum co-contribution phases down with increasing income, at a rate of 5 cents in the dollar. For individuals on $58,000 per annum and above no co-contribution is available. The maximum co-contribution is also relatively modest for those with income of more than $50,000 per year. Table 7 provides further examples, together with the amount of contribution needed to attract the maximum co-contribution. Those who might have the resources to make a contribution are provided with only a very modest incentive to do so.

Table 7: Current parameters of the superannuation co-contribution

Income level (assessable income plus reportable fringe benefits) per annum	Maximum co-contribution currently applying to contributions in 2004-05 and later years	Amount of personal contribution needed to achieve maximum co-contribution
$28,000	$1,500	$1,000
$30,000	$1,400	$934
$40,000	$900	$600
$45,000	$650	$434
$50,000	$400	$267
$55,000	$150	$100
$58,000	0	

The co-contribution has been well received by the Australian population. As at 1 June 2005 the Australian Taxation Office had paid out $291 million in co-contribution payments to the superannuation accounts of around 550,000 individuals. Over 60 per cent of recipients were women, with an average payment of $570. The Treasury costing of the measure for 2004-05 was $275 million, so it was a little more successful than

anticipated in encouraging contributions. These new contributions and the effectiveness of the measure as a means of encouraging individuals to save more for retirement has been welcomed by the Assistant Treasurer, the Hon Mal Brough, in a number of speeches and media releases.

ASFA's proposal is that additional contributions be encouraged and supported as part of a process of mutual obligation. It would provide an enhanced incentive for voluntary contributions by middle income earners, one of the groups most in need of making such contributions. As noted by Treasury researchers in a recent paper (Bingham and Rothman 2005), the current co-contribution provides a good incentive for individuals on relatively low wages, while the abolition of the surcharge restores some tax advantages for those who are higher paid. It is the view of ASFA that it is the middle income earners who now deserve to be assisted.

The co-contribution already is a very useful supplement to retirement savings and an incentive for additional savings by low income earners, but ASFA considers that it should be enhanced so as to provide greater incentives for both low and middle-income earners. There is both need and scope to provide greater assistance to individuals with a taxable income between $40,000 and $60,000 a year.

Accordingly, ASFA recommends that the parameters be extended to individuals on low/middle incomes of up to $60,000 per year, and that the phase-out rate for the co-contribution be adjusted so as to provide a greater incentive for middle income earners in particular. More specifically, it is recommended that for contributions made in 2006-07 and later years the maximum co-contribution remain at $1,500, but this be available for persons with assessable income and reportable fringe benefits of less than $40,000 a year. It is also recommended that the maximum co-contribution phase down as income exceeds $40,000 a year, at a rate of 7.5 cents in the dollar.

Table 8 below illustrates the maximum co-contribution that would apply at various income levels if the ASFA proposal were adopted. The ASFA proposal would deliver benefits to those who are in need of higher retirement income savings and who have some capacity to make additional contributions themselves. The proposal is also very consistent with the views and needs of the population aged under 40.

Table 8: ASFA proposed parameters for the superannuation co-contribution

Income level (assessable income plus reportable fringe benefits) per annum	Proposed maximum co-contribution currently applying to contributions in 2006-07 and later years	Amount of personal contribution needed to achieve maximum co-contribution
$40,000	$1,500	$1,000
$45,000	$1,125	$750
$50,000	$750	$500
$55,000	$375	$250
$60,000	0	

Extending the parameters of the proposed scheme would make the co-contribution even more attractive to the electorate. In doing so the Government would make clear its

commitment to providing real support and encouragement to voluntary saving for retirement by low and middle income earners.

Over the longer term ASFA would support the extension of the maximum co-contribution to individuals who earn moderate incomes (set as indexed assessable income and reportable fringe benefits equal to Average Weekly Ordinary Time Earnings (currently $51,680)) and would propose that this be phased out at 1.5 times AWOTE (currently $77,520).

5.3 Reduce the rate of tax applying to contributions

Removing the tax on contributions to superannuation would be one of the most effective strategies available to government to improve the adequacy, equity and simplicity of superannuation for all Australians. It would have a particular impact on the retirement savings of those aged under 40 as the great bulk of such individuals will have substantial further contributions made by employers on their behalf.

The tax taken out of employer and other tax deductible contributions significantly erodes the net amount saved and invested for superannuation fund members. For instance, an individual receiving employer contributions at the standard Superannuation Guarantee rate of 9% of their applicable earnings only receives net contributions of 7.7% once the tax on contributions is taken out.

For those individuals who were subject to the superannuation surcharge, the erosion of contributions was even greater. The Government's decision to abolish the surcharge on contributions made on or after 1 July 2005 reflects, amongst other things, a recognition of such concerns and the government's interest in improving retirement income adequacy. ASFA considers that abolition or at least reduction of the standard tax on contributions is also justified. This is a measure that the polling indicates would have considerable support amongst those aged under 40 as a means of supplementing retirement savings and encouraging further contributions.

If the contributions tax were completely removed, it would reduce the retirement savings target by 2 or 3%, making it considerably easier and more achievable for individuals. So instead of having to save 15% of wages over 30 years to fund an adequate retirement income, individuals would only have to save 12% or 13% over 30 years. Removing the tax would also provide an incentive for individuals to make additional salary sacrifice contributions or at the very least would remove what many regard as a disincentive.

Managing the transition

Taxing retirement savings once at the end benefits stage is widely acknowledged throughout the world as being best, and most equitable, practice. A difficulty for Australia in moving to that best practice lies in the current reliance of government on the advance revenue stream provided by the tax levied on contributions and on fund earnings. Over $3 billion a year is currently collected from the standard 15% contributions tax on superannuation.

While it is indisputable that taxation of superannuation contributions has been important for governments, such taxation represents short-term thinking and in effect amounts to

poor long-term financial management. Large taxation collections from superannuation now mean lower retirement incomes and tax collections in future decades when demands on government will be greater due to the ageing of the population structure.

However, moving forward it should now be possible - given the current positive state of government finances - to remove the 15% tax on superannuation contributions in either one hit or over a period of three to five years. On an accruals basis, removing the tax on contributions would cost around $3.3 billion in 2005-06, while reducing it over five years would have a first year cost of $660 million, growing by $660 million or so in each of the subsequent four years.

The net cost of removing or reducing the taxation of contributions would be somewhat lower than this. Reducing the tax on contributions would subsequently boost tax collections from fund earnings given the increase in average balances that would result from such a cut. There would also be growing tax collections from the higher benefits that would be available to individuals. The impact of this would grow from some tens of millions of dollars in revenue in the early years following reduction of contributions tax to some hundreds of millions of dollars in subsequent years.

A reduction in the rate of tax paid on contributions does not imply any adjustment to the rate of tax paid at the benefit stage, and certainly not in regard to benefits attributable to contributions which have already attracted the full rate of contributions tax (and surcharge as well in some cases). A reduction in the tax rate on contributions is proposed in order to improve the adequacy of retirement, not to shift the time of payment of taxation.

Recommendation: That the current standard 15% rate of tax applying to contributions be abolished, either in one year or progressively over five years, with effect from 2006-07 onwards.

5.4 Remove the $450 a month earnings threshold for Superannuation Guarantee contributions

When the Superannuation Guarantee was first introduced in 1992 a threshold of employee earnings of $450 a month was set. If an employer paid an employee less than this amount in a calendar month, no SG liability arose. This was the case even if an individual had more than one employer, and their total earnings were more than $450 in a month.

The basic rationale for this provision was to save employers from having to make relatively small superannuation contributions, and to reduce the incidence of accounts being opened with relatively small sums before becoming inactive. Such arguments had considerable force when the Superannuation Guarantee was only 3% of wages, many people did not have superannuation accounts, and choice of fund did not apply, limiting the extent to which employees could direct their contributions to one fund.

The environment now is quite different. The SG has risen to 9% of wages, almost all employees will have one or more superannuation account, and choice of fund (which took effect on 1 July 2005) will permit employees in most instances to direct contributions from a casual or part-time job to a viable superannuation account of the

employee's choosing. Increased use of electronic payment facilities has reduced the cost of making payments. The portability rules have been further amended (with effect from 1 July 2005) making it easier for employees to combine superannuation accounts.

There also has been a substantial increase in the number of casual employees, with 26% of employees casual in 2003, compared to 22% in 1993, leading to an increase in casual jobs from 1.3 million to 1.9 million (ABS 2005). A significant proportion of these job holders achieve the equivalent of full-time employment through the combination of two or more jobs.

Removing the $450 threshold would be of particular benefit to women, given that women have a higher incidence of casual and part-time jobs. Many women (and men) also hold multiple jobs, for example, doing cleaning work for a number of different employers. It also would be particularly relevant to young people, as recent Australian Bureau of Statistics figures indicate that 40 per cent of casual employees are aged 15 to 24 years.

If there were a concern about the administrative burden to employers of making very small SG contributions, then it could be possible in conjunction with the removal of the $450 threshold to specify that an employer is not required to make a SG contribution in regard to an employee if the amount during the relevant SG contribution period is less than, say, $10.

Recommendation: That the $450 a month earnings threshold for Superannuation Guarantee payments be abolished.

5.5 Abolishing or modifying the age based contribution limits

One of the very few specific provisions in superannuation and taxation law relating to those aged under 40 is the cap on the deductibility of contributions related to the age of the member. For those under 35 the cap is $14,603 in 2005-06, and for those 35 to 49 it is $40,560.

Essentially the rationale for this measure, which was introduced in 1994, is to limit the amount of savings that receive concessional taxation treatment, particularly contributions made on behalf of those who are relatively young. Apparently there was government concern that the Reasonable Benefit Limits (RBL) on final benefits received were not effective in capping concessional tax treatment available for some individuals. However, there has never been any clear official statement or explanation of exactly what the age based limits achieve.

In particular, while the pattern of age based limits is compatible with those fortunate enough to have career paths of continuous employment in more or less the same type of work, the limits can impose severe restrictions on those who bloom early or late. The limit for those aged under 35 is not supportive for individuals who seek high paid employment early in their life and then withdraw from the labour force for family or other reasons. It is also contrary to other messages being delivered about the virtues of saving for retirement, and in particular to start early.

It also would be fair to say the limits have a number of arbitrary elements. For instance, the limit on deductible contributions for those aged under 35 is relatively low. While the limit is sufficient to allow contributions to be made consistent with Superannuation Guarantee obligations up to the maximum earnings base for SG purposes, there is relatively little leeway.

The maximum SG obligation for the higher paid takes up around 85 per cent of the deductible contribution limit for those aged under 35. Employers need to be careful about the timing of contributions in regard to their more highly paid employees.

For those who are older there is considerably more flexibility. An annual deductible contribution of more than $100,000 for those aged over 50 clearly is far greater than required by the SG legislation or by the normal contribution rates of standard employer sponsored schemes. Only a very small number of individuals would have a remuneration package to support, or inclination to have, employer contributions of such an amount made on their behalf. The main advantage of such a relatively high annual amount is that it allows individuals to catch up with salary sacrifice contributions in cases where only relatively modest contributions were made at an earlier age.

Age based contribution limits have a number of technical and design limitations. For instance, the limits have little or no effect apart from a demonstration effect when the employer is not a taxable entity. This is the case for a significant number of employees of Commonwealth and State government entities and not-for-profit employers. The limits also apply to each employer of an individual, so if an employee has multiple jobs within a year or more than one employer they can have deductible contributions which are a multiple of the standard limits.

While the limits can be relatively generous or have no impact at all for some individuals, for others they can be relatively harsh. The limits are based on annual contributions rather than the amount and duration of savings or the eventual level of benefits at retirement. That they are a very blunt policy instrument is highlighted by the major differences in allowable deductions brought about by an increase in age from 34 to 35 and from age 49 to 50.

It could be argued that the limits are unduly restrictive under age 35, relatively generous over age 50, and that the transition between the various age limits is too sharp. It is not clear why it is permitted to catch-up when aged over 50, but it is not permitted to make adequate provision for retirement early in a working career. Given family and other responsibilities it could be argued that either pattern of work and saving for retirement should both be permitted and encouraged. The more fundamental question is why both age based contribution limits and Reasonable Benefit Limits are needed.

Recommendation: That the current age based contributions limits currently applying to those aged under 40 be abolished or be significantly modified to allow for greater flexibility in the pattern of employer contributions to superannuation over a working life.

5.6 Providing members with additional information on future benefits

The terms of reference of the inquiry refer to improving the awareness of those aged under 40 of the importance of saving early for their retirement. In this regard, a concern raised by the OECD in its recent report *Ageing and Employment Policies: Australia* was the "general lack of information about the size of future superannuation entitlements" (p. 29). This is consistent with the survey findings reported in section 4.5 of this submission which indicate that when pressed about how good an idea the respondent had about likely income in retirement, around 75 per cent of those aged 30 to 39 indicated that they really did not know, with only 8 per cent indicating that they had a good idea. Providing information about future superannuation entitlements based on current behaviours may assist in better informed decision-making by people under 40 and encourage those individuals to make additional contributions now, thus addressing future adequacy.

The OECD suggested Australia consider adopting the "orange envelopes" currently used in Sweden. In Sweden, employer contributions to both social security and funded individual retirement accounts are made to a central Government agency, the Premium Pension Agency (PPM), which then distributes the latter contributions to funds chosen by the individual.

Using this data, the PPM issues the "orange envelopes" annually to every participating Swedish citizen. This notice contains information about both their present benefits and future benefits as projected using a set of standardised assumptions. These projections are done using a number of scenarios for the individual (for example with different income growth, real returns and retirement ages) and indicate the likely income the individual would receive as a result. As noted in the OECD report "(t)he main reason for these projections is to increase the knowledge among people about the size of their future entitlements, how their pensions are determined and what is affecting them" (p. 91).

This type of centralised, individualised projection would be difficult in the Australian context. However, the concept could be applied if superannuation funds were given greater capacity to provide benefit projections to members.

In the United Kingdom there is actually an obligation on funds to provide such projections to members on an annual basis. From 6 April 2003, an annual illustration (Statutory Money Purchase Illustration in the parlance of the UK legislation) must be given to scheme members of most approved pension schemes providing benefits on a money purchase basis (the equivalent of our accumulation schemes). The supporting legislation is the Occupational and Personal Pension Schemes (Disclosure of Information) Amendment Regulations 2002.

The main principle behind the legislation is to help individuals plan for their retirement and to encourage long term savings.

The calculation basis is defined in a technical memorandum which was prepared after consultation with the Faculty of Actuaries. In particular, the pension illustration must be prepared in "real terms", allowing a direct comparison of the projected outcome with

the member's present day income and cost of living. Most elements of the calculation are prescribed, but there is some scope to allow for the individual's personal circumstances. Investment returns may be adjusted to reflect the scheme's investment strategy, but are subject to a cap of 7 per cent per annum.

An example of such an illustration based on the United Kingdom approach is set out in the box below.

Mr Person under 40 superannuation fund statement

This statement is a guide to the amount of superannuation that you might get when you retire. In this statement we refer to this as an "illustration". It is shown in today's prices and is not a promise or guarantee that your superannuation will be the amount shown. This is because it is based on a number of assumptions.

Please read the notes on the back of the statement. They explain more about the way your illustration has been calculated, the assumptions that we have made and what will decide how much your final superannuation benefit will be.

Your name: Mr Person under 40
Your date of birth: 1 March 1970
The name of your superannuation scheme: The really beaut super fund
The date you joined the scheme: 10 September 1995
The effective date of this illustration: 1 July 2005

Contributions paid into your super in the year ended 30 June 2005: $5,400
The value of your superannuation so far: $36,000

Your future superannuation balance

To illustrate your possible future superannuation balance we have assumed that:
your retirement date is 30 June 2035
you will continue to have employer contributions at the compulsory rate of 9% until your retirement date

The estimated superannuation balance when you retire is: $311,000

In the United Kingdom the benefit illustration includes a projection of the annuity income stream that the accumulation superannuation balance would generate. This reflects the fact that in the United Kingdom retirement benefits are generally taken in the form of an annuity. There are good grounds for focussing on the ongoing income in retirement from superannuation savings rather than the lump sum achieved at the time of retirement. Accordingly there would be a case for the development of standard assumptions and approaches in Australia which would facilitate the calculation of projections of income in retirement which could be used in such illustrations.

Limitations imposed by Australian law and ASIC views

Currently, ASIC Policy Statement 170 places strong restrictions on the use of prospective financial information. Combined with concerns over future legal action by disgruntled members, benefit projections are rare.

The Government should consider enabling superannuation funds, if they so choose, to project future benefits to members on a standardised basis. A standardised projection

would be useful for a number of reasons. It would enable consistent information to be provided. The provision of a number of scenarios would also further protect both the Government and funds from claims of making an implicit promise.

Recommendation: ASFA recommends that the Government pursue reforms that would permit superannuation funds to provide benefit projections to individual members on a standardised basis as part of their annual reporting to members.

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