SUBMISSION 17

Bryant, Sharon (REPS)

From: Fiona Galbraith [Fiona_Galbraith@aas.kaz.com.au]
Sent: Friday, 22 July 2005 8:35 PM
To: Committee, EFPA (REPS)
Subject: Inquiry into Improving the Superannuation Savings of People Under 40.

Reps Committee Inquiry into Su...

Dear Sir / Madam,

Australian Administration Services ("AAS") appreciates the opportunity to make a submission to this inquiry.

By way of background, AAS is one of Australia's largest providers of administration and customer services to the industry and corporate superannuation market. We currently provide these services to over 3.5 million members and 165,000 employers.

Attached please find our submission with respect to this Inquiry.

<<Reps Committee Inquiry into Super Under 40s - Final.doc>>
Should you have any queries with respect to this, please do not hesitate to contact me.

Yours faithfully

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Standing Committee on Economics, Finance and Public Administration

Inquiry into Improving the Superannuation Savings of People Under 40

Submission by Australian Administration Services Pty Ltd

22nd July 2005

Australian Administration Services ("AAS") appreciates the opportunity to make a submission to this inquiry.

AAS is one of Australia's largest providers of administration and customer services to the industry and corporate superannuation market. We currently provide these services to over 3.5 million members and 165,000 employers.

The terms of reference of the inquiry are as follows: -

> "Inquiry into improving the superannuation savings of people under 40 with particular reference to:
> - Barriers and \ or disincentives to contribute to superannuation
> - Current incentives in place to encourage voluntary superannuation contributions
> - Improving their awareness of the importance of saving early for their retirement".

1. Barriers and \ or disincentives to contribute to superannuation

The most obvious disincentive to contribute to superannuation is compulsory "preservation" – the fact that a person generally cannot have access to their superannuation benefit until they have reached their "preservation age", currently between ages 55 and 60 depending on their date of birth.

Given the policy objective of individuals being able to accrue sufficient amounts such that they are able to reduce, or even eliminate, their reliance on the Age Pension by becoming "self-funded" in retirement, and the concessional tax treatment afforded superannuation to assist that outcome, it is important that preservation be retained as one of the underlying Retirement Income Principles.

Another barrier to people under 40 contributing to superannuation is psychological – a combination of an inability to visualise becoming older; an implicit assumption \ expectation of being "taken care of" by the government – reinforced by family members anticipating, and receiving, the Age Pension; an increasing trend towards consumption not saving and a tendency to procrastinate – "there's plenty of time".

These psychological barriers are best addressed through a mix of education and incentives. Education can take many forms but is generally most effective when targeted at the young, through such vehicles as school curriculum. Over time, some of the most valuable forms of education occur through family and personal experience – seeing first hand the "magic of compound interest" and the amount of superannuation grow.

The final barrier to people under 40 contributing to superannuation is lack of disposable income. Not only do people generally not attain their peak earning capacity until around 40 years of age, the period prior to 40 tends to coincide with the incurring of significant financial commitments, such as paying off one or more HECS debts, entering into a mortgage and raising young children, with its attendant reduction in income and additional expenditure.

2. Current incentives in place to encourage voluntary superannuation contributions

Currently the main incentives to encourage voluntary superannuation contributions take three forms: -

1. the concessionally taxed environment of superannuation generally;
2. the co-contribution for low-income earners; and
3. for the substantially self-employed – the tax deductibility of superannuation contributions.

An additional incentive is the spouse contribution tax rebate. The maximum available rebate is $540 per annum and reduces to nil once the spouse's "total income" (assessable income plus reportable fringe benefits) reaches $13,800.

The Government's proposal to allow the splitting of superannuation contributions between spouses from 1st July 2006 may also act as an incentive as it enables each party to access the tax free threshold in respect of any benefit payment received by them (currently $129,751) as well as affording each spouse their own Reasonable Benefit Limit ("RBL"). Where one spouse has little or no superannuation this can effectively serve to double both the amount of benefit available tax-free and the amount which, by virtue of being under the RBL, will be concessionally taxed.

1. The concessionally taxed environment of superannuation generally

The income of superannuation funds (and like products), including taxable contributions made to the fund, is taxed at the rate of 15 percent. For individuals whose marginal tax rate is above 15 percent, the difference between the 15 percent tax levied on contributions to a superannuation fund and the tax they would otherwise have paid on that amount were it not contributed to superannuation represents an incentive to contribute to superannuation.

2. The co-contribution for low-income earners

Currently a person who earns under $58,000 "total income" per annum (assessable income plus reportable fringe benefits) and who makes undeducted (after-tax) contributions to superannuation is generally eligible for a co-contribution (subject to meeting some other conditions). The amount of the co-contribution is the lesser of: -

- one and a half times the amount of contributions made, up to a maximum of $1,500 (for a contribution of $1,000); and
- an amount determined by the person's total income. For those earning under $28,000 per annum there is no reduction in the potential amount of co-contribution. For those earning in excess of $28,000 per annum the amount of potential co-contribution is phased out at a rate of 5 cents for every dollar of taxable income in excess of $28,000, reducing to zero at $58,000.

The table below indicates the amount of co-contribution for a range of "total income" and undeducted contribution amounts. [1]

Superannuation Co-contribution sliding scale

	From 1 July 2004, if your personal super contribution is:			
	$1000	$800	$500	$200
And your income is:	Your Super Co-contribution will be:			
$28,000 or less	$1,500	$1,200	$750	$300
$30,000	$1,400	$1,200	$750	$300
$32,000	$1,300	$1,200	$750	$300
$34,000	$1,200	$1,200	$750	$300
$36,000	$1,100	$1,100	$750	$300
$38,000	$1,000	$1,000	$750	$300
$40,000	$900	$900	$750	$300
$42,000	$800	$800	$750	$300
$44,000	$700	$700	$700	$300
$46,000	$600	$600	$600	$300
$48,000	$500	$500	$500	$300
$50,000	$400	$400	$400	$300
$52,000	$300	$300	$300	$300
$54,000	$200	$200	$200	$200
$56,000	$100	$100	$100	$100
$58,000	$0	$0	$0	$0

1 Source – ATO Publication – "The Superannuation Co-contribution is now even bigger and better" – NAT 10596 – 03.2005

The co-contribution has proven to be successful in encouraging voluntary contributions. To quote the Treasurer, Mr Costello, in his Media Release of 24th March 2005 – No. 24: -

> *"[The co-contribution] has been immensely successful - more than half a million Australians took up the co-contribution offer last financial year, making personal contributions to their retirement savings and receiving an average top-up to those savings of $530".*

3. For the substantially self-employed – the tax deductibility of superannuation contributions

Provided an individual earns no more than ten percent of their income from employment they are entitled to claim a tax deduction in respect of contributions made to superannuation, up to an amount determined in accordance with the age-based limits, as follows: -

Age in years	**Deduction Limit (2005-06 financial year)**
Under 35	$14,603
35 – 49	$40,560
50 and over	$100,587

3. Improving their awareness of the importance of saving early for their retirement

Improving the awareness of the importance of saving early for retirement needs to address the psychological barriers to contribution outlined in 1) above.

One possible approach may be to demonstrate that, while it is there as a safety net, reliance upon the Aged Pension does not afford the lifestyle to which most people under 40 will aspire in retirement, especially given increasing longevity and improving health.

This could be coupled with reinforcement of the "magic of compounding" - the message that a small sacrifice today (the proverbial "cup of coffee") can, over time and with investment, amount to a considerable difference in the standard of living achieved in retirement.

The main psychological barrier to overcome is the most fundamental – that the young, while intellectually accepting the inevitability of aging, generally have difficulty visualising it occurring to them – their vision of an older person is almost disengaged from their self-image. This, together with a natural tendency toward procrastination and a feeling that "there's still plenty of time", makes raising awareness among the under 40s challenging.

4. Suggested incentive to encourage voluntary contributions among the under 40s

Consideration could be given to introducing an age-based tax deduction, or possibly a rebate, for voluntary contributions made to superannuation, akin to the Lifetime Health Cover loadings but in reverse, commencing with the maximum available deduction at age 18 and phasing out to zero after age 40.

This could be achieved by means of allowing 1) a sliding scale percentage (subject to a maximum amount) or 2) a fixed dollar amount. As a matter of policy, interaction with the existing co-contributions measure will need to be determined.

By way of illustration, deductions could be available on the following basis: -

Age as at 30th June	1) % of contribution claimable as deduction \ rebate	1) Maximum $ amount 2) Fixed $ Amount
18	100%	$5,000
19	100%	$5,000
20	100%	$5,000
21	95%	$4,750
22	90%	$4,500
23	85%	$4,250
24	80%	$4,000
25	75%	$3,750
26	70%	$3,500
27	65%	$3,250
28	60%	$3,000
29	55%	$2,275
30	50%	$2,500
31	45%	$2,225
32	40%	$2,000
33	35%	$1,750
34	30%	$1,500
35	25%	$1,250
36	20%	$1,000
37	15%	$750
38	10%	$500
39	5%	$250
40	5%	$250

There are two main benefits to this scheme. Firstly, as preservation acts as a considerable disincentive to making superannuation contributions, especially for those under 40, a deduction or rebate may prove a more effective incentive than a co-contribution. Being returned at year-end as part of the tax return and assessment process (as opposed to being contributed to a superannuation fund as a co-contribution) may prove to be of particular assistance to younger persons and to those with little disposable income.

A deduction \ rebate is also relatively readily administered by the Australian Taxation Office as part of the annual tax return and assessment process.

Secondly, the annual reduction in the available deduction \ rebate, with the "window of opportunity" closing at the end of each financial year, may act as an incentive and serve to overcome procrastination, which is only exacerbated in the under 40s by the view that retirement is so far off there is little immediate need to provision for it.

While a deduction \ rebate may not be the preferred outcome under Retirement Income Principles, and needs to be costed, if the relative immediacy of a deduction or rebate overcomes the preservation barrier this will result both in an enhanced level of contributions being made to superannuation and in the establishment of a pattern of behaviour – an increase in saving. Even if the deduction \ rebate were to be spent at year-end, nevertheless, two valuable policy objectives have been achieved and the initial saving has at least taken place and has occurred within the superannuation environment where it will be preserved.

Should you have any queries with respect to this, please do not hesitate to contact the writer.

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