SUBMISSION
TO THE
SENATE SELECT COMMITTEE
ON
SUPERANNUATION & FINANCIAL SERVICES

SUPERANNUATION AND STANDARDS OF LIVING IN RETIREMENT

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SUPERANNUATION & STANDARDS OF LIVING IN RETIREMENT

"The adequacy of tax arrangements for superannuation and related policy to address the retirement income and aged and healthcare needs of Australians".

1. Introduction

This submission is lodged by Maurice Blackburn Cashman on behalf of the Neurological Alliance[1] and the Chronic Illness Alliance Inc.[2] in relation to the Reference to the Senate Select Committee on Superannuation and Financial Services as to "the adequacy of tax arrangements for superannuation and related policy to address the retirement income and healthcare needs of Australians".

The reference requested that the Committee focus on "…people's standards of living in retirement and the factors which contribute to that – including retirement incomes, contribution levels and taxation arrangements for superannuation and meeting the aged and healthcare needs of Australians".

This submission focuses on the inadequacy of the retirement incomes of Australians with chronic illnesses and acquired disabilities and how superannuation laws could be amended to improve their standards of living in retirement and healthcare needs and reduce their reliance on the welfare system.

2. Incidence of Disability

The number of Australians of working age with disabilities that affect their capacity to work and thereby their ability to accrue superannuation for retirement is substantial and rising.

In 1993, the Australian Bureau of Statistics reported that 15% of the working age population (ie. persons between the ages of 15 and 65) had a disability causing limitations, restrictions or impairments lasting six months or more. 11% of the working age population had a handicap which limited the performance of daily living tasks including employment and 2% had a severe or profound handicap requiring help or supervision in the areas of self care, mobility or verbal communication[3].

By 1998, 3.6 million or 19% of the Australian population had a disability and 510,000 or 3% of the working age population had a severe or profound handicap.[4]

[1] The Neurological Alliance is a disability support network whose members include the MS Society, Motor Neurone Disease Association, Australian Huntington's Disease Association, Parkinson's Victoria, Headway Victoria, Brain Foundation Victoria, Muscular Dystrophy Association, Alzheimer's Association of Victoria and Paraquad Victoria.

[2] The Chronic Illness Alliance is an alliance of various chronic illness groups undertaking a range of projects aimed at developing a better focus in health and related policies for all people with chronic illnesses.

[3] See Australian Bureau of Statistics "Australian Social Trends 1997 Work – Paid Work: Employment of people with a handicap", page 2.

[4] See Australian Bureau of Statistics "Australian Social Trends 2002 Income and Expenditure – Income Support: Trends in disability support", page 1.

The increase in the number of people with severe or profound disabilities affecting their ability to work has translated to progressive and substantial increases in the numbers of recipients of the disability support pension.

The number of people in receipt of disability support pensions has progressively risen from 229,200 or 2% of the Australian population in 1980 to 602,300 or 3% of the population by June 2000, at a cost to taxpayers of $5.2 billion[5]. The number is now nearing 650,000 people[6].

In the year 2000, 31.7% of the recipients of disability support pensions had musculo-skeletal disabilities, 21.5% suffered from mental illnesses, 5.5% had circulatory system problems, 3.1% had respiratory system problems, 2.6% suffered from acquired brain injuries and 2% suffered from cancer.

The number of recipients in the above categories increased as a percentage as recipients grew older – in contrast to recipients with learning or intellectual disabilities which decreased from 38.4% of the total number of disability support pension recipients in the 16 to 29 age group to 2.2% of those in the 50 to 64 age group. Similar reductions were reflected in the number of people suffering congenital abnormalities.[7]

These statistics indicate that the number of people of working age with disabilities is on the increase and that people with acquired or progressively degenerative disabilities are leaving the workforce prematurely and being forced to subsist on the disability support pension.

As the Australian Bureau of Statistics observed "*…[the] numbers of disability support pension recipients have increased due to improvements in the mortality of Australians. Medical advances combined with personal lifestyle choices, mean that more people, including those with a disability are surviving at every age. As a result, people who are receiving the disability support pension do so for longer periods of time*".[8]

This situation is being exacerbated by Australia's aging population with people in the age bracket 50 to 65 having higher rates of severe or profound handicaps.[9]

Accordingly, as the "baby boomers" enter the 50 plus age bracket, this will cause a blowout in the proportion of the working age population on disability support pensions.[10]

The increase in the number of people with disabilities and disability support pensioners is also having an impact on the number of carers ceasing or reducing their work to provide assistance to those needing help because of a disability.

[5] See Ibid, page 1.
[6] See Federal Government publication: Australians Working Together – "People with a disability", 16 July 2002.
[7] See op cit Australian Bureau of Statistics: Australian Social Trends 2002, page 2.
[8] See Ibid, page 4.
[9] See Ibid, page 4.
[10] See Ibid, page 5.

In 1998 approximately 2.3 million people, usually family and friends, were providing care to disabled persons. In some cases this can result in families going from 2-income households to no income, a scenario which would dramatically reduce the capacity to accrue adequate retirement incomes[11].

3. People with Disabilities – Problems in Employment

People with disabilities are perhaps the most vulnerable and marginal group in Australian society. They have to contend with difficulties associated with their disabilities including physical and psychological pain, health management issues and day-to-day living problems with self-care, travel and communication. Many suffer from discrimination because of their disabilities and others have social and domestic problems.

Specifically, people with disabilities often suffer from discrimination in the workplace ranging from being marginalised in relationships with fellow employees and managers, not being offered modified work conditions or hours of employment to accommodate their disabilities, or being forced to resign or sacked outright. Once out of one job, it is then problematic to find alternative employment which would accommodate their restrictive disabilities. Many prospective employers require details of pre-existing disabilities and are then reluctant to take on those whose capacity to perform a full range of employment duties may be compromised.

Accordingly, many peoples with disabilities have fractured working lives or at least are unable to maximise their earnings capabilities by not being able to advance their employment status and earnings or by being limited in overtime or extra duties.

The result is that many people with disabilities of working age experience severe financial problems by having limited disposable income from employment earnings. Given that many face substantial additional outlays for medical, pharmaceutical and travelling costs to manage their disabilities, suffering from a chronic illness or acquired disability is often a recipe for being mired in a poverty trap.

4. Compulsory Superannuation

The centrepiece of the retirement incomes policy of successive Federal Governments has been compulsory employment-based superannuation.

Introduced by a Federal Labor Government following the growth of award superannuation from the mid 1980's, the *Superannuation Guarantee (Administration) Act* 1992 ("SGAA") mandated employer-sponsored superannuation contributions for most of the employed workforce.

Supplemented by voluntary superannuation contributions and other retirement savings, compulsory superannuation was seen as the main vehicle to ensure that the "baby boomer" generation and generations beyond provided for their own retirement and were not an intolerable burden on the welfare system.

[11] See Australian Bureau of Statistics – "Income and Welfare Caring – Australia" 1998.

Tax incentives and restrictive preservation rules were also key planks in the superannuation retirement incomes strategy.

However, whilst the debate has raged over whether the level of superannuation support mandated under the SGAA is sufficient for adequate retirement incomes, attention needs to be given to the level of retirement incomes for those who leave the workforce prematurely because of disability.

5. Occupational Superannuation for People with Disabilities

The linkage of compulsory superannuation to employment inevitably means that only those with 30 to 40 years in the paid workforce have reasonable prospects of accruing sufficient superannuation for retirement.

Those with limited working lives are severely disadvantaged under the existing retirement incomes regime.

The Committee sitting as the Senate Select Committee on Superannuation has previously reported into the impact of occupationally-linked superannuation on the retirement incomes of women with broken work patterns and made a number of recommendations to alleviate the problems.[12]

However, perhaps more dramatic is the impact of the premature exit from the workforce of many people with disabilities. As detailed above, those with chronic illnesses, degenerative conditions and acquired injuries often have to leave the workforce before normal retirement age or struggle on in a reduced capacity.

The result is that many people with disabilities are not able to accrue anything like adequate superannuation for their retirements and are inevitably dependent upon the welfare system not only during their working lives, but even more so in retirement.

As the number of people with severe disabilities increases, so will the proportion of the Australian population dependant upon the welfare system in retirement, unable to self-fund for their retirements in the compulsory superannuation regime.

6. Disability Benefits in Superannuation

Although not compulsory, disability benefits are a feature of many regulated superannuation funds.

Government and employer-sponsored corporate plans have for decades offered defined benefits including disability (and death) pensions or lump sums calculated under the same formulas as for normal age retirement.

The philosophy behind such benefits is that but for disability or death, the members could/would have accrued adequate retirement benefits. They (or their

[12] See 17th Report of the Senate Select Committee on Superannuation “Super and Broken Work Patterns”, November 1995.

dependants) are therefore "compensated" for the loss of retirement benefits by being put in the same position as if they had continued working until retirement.[13]

Industry and retail superannuation funds have for the most part offered disability benefits in accumulation plans, although usually not at the same level as Government or corporate plans. Some Retirement Savings Accounts also offer disability benefits.

The disability benefits are usually total and permanent disability ("TPD") lump sums provided under group insurance policies contracted between the trustees and life insurance offices. Most offer basic levels of cover (perhaps up to $50,000.00) on an automatic acceptance basis with the option of purchasing extra units of cover subject to underwriting.

Some funds offer disability income streams – usually monthly benefits of up to 75% of base salary for 2 years or perhaps up to retirement age. The benefits are also usually provided pursuant to group insurance policies and may be subject to some underwriting.

The disability income streams are sometimes offered in conjunction with TPD lump sums or in substitution of those lump sums. A minority of industry and retail superannuation funds offer no disability benefits.

7. The Value of Disability Benefits

The current reality is that most Australians within the compulsory superannuation regime are covered for disability benefits in some form. With the exception of generous defined benefit Government and corporate plans, most superannuation disability benefits supplement accrued benefits rather than provide full retirement incomes.

That is not to say that superannuation disability benefits are not valuable. For many people, particularly those who are forced to leave the paid workforce well before normal retirement age, a TPD lump sum is much more valuable than any superannuation they have been able to accrue.

Long term disability income streams can also be valuable, particularly if coupled with cover for superannuation guarantee contributions. Income streams limited to 2 years or those not also providing for superannuation contributions are of limited value as they do not provide for the accumulation of retirement incomes – only basic working life income replacement.

The value of substantial employment-based superannuation disability benefits is no better illustrated than for those with chronic illnesses or acquired disabilities. The existence or otherwise of superannuation disability benefits can make the difference between some financial security in retirement or poverty and dependence on the welfare system.

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[13] The philosophy behind superannuation disability and death benefits is often misunderstood as compensation or substitution for a loss of income. They are in fact compensation for a loss of retirement income and not for a loss of working life income.

Case Study No. 1

Mr Kemel Dogancili, a 31 year old Turkish born Australian suffered a back injury at work in 1999. He has suffered from severe pain to the back and legs and has been advised he won't be able to return to work. He is in receipt of Worker's Compensation weekly payments.

Mr Dogancili was a member of the Meat Industry Employees' Superannuation Fund through his work as a butcher but the Fund did not have any disability cover. He has very little 'accrued' superannuation and will almost certainly be dependent on compensation or welfare payments for the rest of his life.

Case Study No. 2

Mr John Hill of Glenroy is 59 years old and was employed by Ansett Australia as a technical officer. He suffers from Leukemia and was forced to cease work on medical advice in September 2001. He has been advised he will not be capable of returning to work because of his disability.

Mr Hill was a member of the Ansett Australia Ground Staff Superannuation Plan which was a defined benefit fund and included a Total and Permanent Disability Lump sum the equivalent of the age retirement benefit, and a Total and Temporary Disability monthly income benefit. Mr Hill made claims for both benefits and both claims have recently been accepted. He will be paid superannuation disability benefits which will provide substantial retirement income security.

8. Relevant Superannuation Laws

Although TPD and disability income benefits are a fact of life in most regulated superannuation funds, they are not mandatory and the disability benefits offered by superannuation funds vary widely.

Most disability benefits are insured or underwritten under group life insurance policies which last for 3 years and are therefore subject to periodic variations under new or renewed policies.

Some funds have changed from offering TPD lump sums to disability income benefits, others have moved to offer both, some funds have increased the amount of disability insurance cover that can be taken up whilst others have moved from compulsory to optional levels of cover.

It can be very confusing for members to identify what cover they have or may be entitled to – a situation that will only be exacerbated with the introduction of choice of fund legislation.

Superannuation taxation arrangements do provide some incentives for disability benefits. TPD benefits and disability income benefits for a maximum of 2 years and the associated insurance premiums qualify for complying superannuation fund concessional tax treatment[14]. Indeed, post 1 July 1994, TPD benefits are tax-free.

Some superannuation funds and their insurers have experienced difficulties in pricing superannuation disability benefits and some have had adverse claims experiences. Superannuation disability benefit disputes have also featured prominently in the Superannuation Complaints Tribunal's statistics and have been the cause of some angst between trustees and members.

However, the introduction of the SISA and the *Superannuation (Resolution of Complaints) Act* 1993, has resulted in trustees and insurers progressively and substantially improving their claims and dispute resolute procedures such that the vast majority of claims are satisfactorily resolved and only a fraction are subject to review decisions by the Superannuation Complaints Tribunal[15].

9. Suggested Improvements in Superannuation Laws for People with Disabilities

9.1 Mandating Superannuation Disability Cover

The lack of minimum levels of compulsory disability cover in superannuation leads to a gross imbalance in the retirement incomes of disabled and able-bodied superannuants. Further, there are distortions in the retirement incomes between disabled Australians, dependent upon which superannuation funds they were members of and the levels of disability cover when forced to leave the workforce prematurely.

Mandatory minimum levels of disability cover would go a long way towards making people with disabilities self-reliant in retirement and relieve the growing problem of the burgeoning number of disability support pensioners.

Superannuation disability benefits are usually funded by members through insurance premium deductions from superannuation contributions or account balances. Accordingly, mandatory disability cover is consistent with the self-funded retirement philosophy of the retirement incomes policy.

Conversely, it is inconsistent with a retirement incomes strategy to have a compulsory occupationally-linked superannuation regime in place which does not provide for the retirement income needs of such a significant and growing section of the Australian community.

It could be said that to mandate minimum levels of disability cover could create problems for superannuation funds operating in high-risk industries with adverse claims experiences.

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[14] See *Superannuation Industry (Supervision) Act* 1993 ("SISA") definition of "ancillary purposes" (s62(1)(b)) and *Income Tax Assessment Act* 1936 ("ITAA") definition of "death and disability benefit" (s267), s27G and s279(1)).

[15] See generally the Superannuation Complaints Tribunal quarterly and annual reports for statistics on the comparative levels of enquiries, complaints and review decisions.

However, the move by many funds to become public offer funds provides the opportunity to broaden the membership base and mandatory minimum levels of cover would dramatically reduce the risks and costs associated with anti-selection; so often touted as the main problem with automatic acceptance group insurance.

Setting minimum cover at relatively modest levels would not be overly burdensome even for funds with high risk membership profiles and the savings in group insurance as opposed to individual insurance cover means that the employed population will have access to relatively inexpensive disability cover[16] to protect their retirement incomes without any real impact on the retirement incomes of able-bodied Australians.

Whether the minimum level of cover was a TPD lump sum of say $50,000.00 or perhaps insurance cover to be purchased at the discretion of trustees for the benefit of members at a minimum insurance premium of say $2 to $3 per week, the rates should be actuarially set and reviewed periodically.

9.2 Taxation Incentives

9.2.1 Extending Superannuation Disability Income Benefits

As is detailed above, concessional tax treatment of superannuation income stream disability benefits is limited by the operation of the SISA and the ITAA.

In particular, disability income streams offering benefits of more than 2 years duration do not qualify for complying superannuation fund concessional tax treatment whilst those offering benefits for upto 2 years do[17].

It is submitted that there is no good policy reason to discriminate between income streams of more or less than 2 years duration. To the contrary, the provision of a long term income stream, particularly if coupled with payment of the equivalent of superannuation guarantee contributions is more likely to add value to the retirement income of a person with a disability than a benefit that expires after 2 years. Such a limited term disability income benefit would simply leave a long term disabled person with the prospect of dependency on welfare support and with little or no prospect of accruing an adequate retirement income.

Accordingly, it is submitted that the SISA and ITAA should be amended to extend the definition of disability benefits in relation to a member of a complying superannuation fund to include disability

[16] See Superannuation Funds article headed “Choice Hits Insurance”, July 2002 p. 16, which refers to a comparison of 27 retail insurance premium rates for combined death and TPD insurance which found that two thirds of superannuation funds offered comparatively better insurance deals than the average retail policy.
[17] See Section 267 of the *Income Tax Assessment Act* 1936 definition of “Death and Disability Benefit” which includes a permanent disablement benefit and an income benefit payable upon the incapacity to perform the normal duties of a member’s employment for a period not exceeding 2 years.

income stream benefits payable to a member incapacitated for his/her usual occupation for any period of time – and not just for a maximum of 2 years.

9.2.2 Superannuation Contributions with Disability Income Benefits

The definition of disability benefits should also be amended to specifically include additional benefits representing superannuation guarantee contributions payable for the benefit of the member under the SGAA. Further, given that such additional benefits would be payable as superannuation guarantee contributions, the benefits should be subject to the Payment Standards of Part 6 of the Superannuation Industry (Supervision) Regulations 1994 as preserved benefits in regulated superannuation funds on or after 1 July 1999.

9.2.3 Tax Rebates for Welfare Recipients

Finally, it is submitted that consideration should also be given to encouraging low income earners such as disability support pension recipients to contribute to superannuation by way of tax rebates.

Those people with disabilities who have left the workforce prematurely without adequate retirement incomes have little or no prospect of enhancing their retirement incomes. However, if they were eligible to claim rebates for contributions to be paid into regulated superannuation funds, they might have the capacity to enhance their retirement incomes.

9.3 Default Funds-Choice

The latest choice of fund legislation reintroduced to Federal Parliament for consideration in June 2002, the Superannuation Legislation Amendment (Choice of Superannuation Funds) Bill 2002, includes a provision that default funds under the choice of fund regime must include minimum standards including offering minimum levels of death insurance cover as prescribed by regulation[18].

However, curiously, the Bill does not include disability cover in the minimum standards. It is submitted that it is incongruous to prescribe as a minimum standard the protection of dependants of fund members against inadequate retirement incomes and not the protection of the members themselves; particularly since death rates amongst the working age population are falling whilst disability rates are rising.

The importance of default funds in a choice environment cannot be understated due to the combination of a lack of comparative knowledge about superannuation in the Australian population and inertia when making a choice between superannuation funds.

[18] See Superannuation Legislation Amendment (Choice of Superannuation Funds) Bill 2002 Section 32K(4)(b).

Many people know little about their superannuation entitlements and would be daunted by the prospect of having to compare the disability benefits offered by a range of potential superannuation funds. The end result would be that many people could lose valuable disability cover without realising which would only exacerbate the inadequacy of retirement incomes for people with disabilities.

Accordingly, it is submitted that if the Bill is to pass into law, it should be amended to prescribe minimum levels of disability insurance cover being offered by default funds.

10 Healthcare Needs of People with Disabilities

The Reference to the Committee included consideration of the healthcare needs of Australians related to superannuation retirement incomes.

Whilst it is submitted that the bundling of retirement incomes with healthcare expenses is questionable, any such linkage is more problematic for people with disabilities.

People with chronic illnesses and acquired injuries will invariably have greater healthcare needs than other Australians and will use more resources – whether funded from their own retirement incomes or Government healthcare services.

Indeed, any linkage of retirement incomes from superannuation and the healthcare needs of Australians only serves to highlight the necessity for Governments to address the inadequacy of retirement incomes for people with disabilities.

11 Summary

The current retirement incomes system will in all likelihood not provide adequate retirement incomes for most Australians. Unless the level of compulsory employment-based superannuation contributions is lifted beyond the current 9% and unless the complex taxation arrangements are simplified and made less onerous, the outcome is likely to be a continued reliance by a significant proportion of retirees on the age pension.

This scenario is perhaps at its worst in respect of people with disabilities who are more likely to leave the workforce prematurely and less likely to have sufficient retirement incomes.

The growing number of people with significant disabilities affecting their ability to work and the explosion in recent years in the numbers of disability support pension recipients highlights the urgent need to address the inadequacy of retirement incomes for people with disabilities and to put in place policies to promote self-funded retirement.

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