Mythbusters

Myths that a 12 per cent SG is not needed

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Myth 1

Employees would be better off with money in their pockets rather than additional super contributions

***Fact:* In the absence of the legislated increase to 12 per cent a substantial proportion of future retirees will not have the standard of living they quite reasonably want or deserve**

The Superannuation Guarantee (SG) needs to increase to improve standard of living in retirement

The fact is, the system is already delivering significant increases in retirement living standards for all Australians.

This is the case even for those earning well under average weekly earnings.

For instance, for a person aged 30 on $40,000 a year (below even median employment earnings), with a current balance of $20,000, the compulsory superannuation system will deliver an estimated $263,500 at retirement. All of these figures are in today's dollars, as are the other examples in this paper.

This will increase retirement income from $23,662 a year (the Age Pension including allowances) to $34,078 a year. Contrary to the assertions made by the Grattan Institute, the superannuation savings will only decrease the Age Pension entitlement by a small amount.

Even an extra few thousand dollars a year will make a real difference in retirement – including allowing people to undertake essential home repairs, visit the dentist, better heat and cool their homes and have an occasional meal at the club.

Compulsory superannuation makes a substantial difference to the adequacy of retirement income.

What Australians need and want

Once the legislated increase in Superannuation Guarantee to 12 per cent of salary is introduced, ASFA projects that 50 per cent of Australians will be living comfortably in retirement by 2050, just over double the current proportion.

There is clear evidence that the ASFA Comfortable standard is what a large proportion of the community want and need. The very large and ongoing Household, Income and Labour Dynamics in Australia (HILDA) Survey of the Australian population has obtained information from people aged 45 and over, who were not yet retired, about their expectations for the (after-tax) income they will require in retirement in order to have a standard of living which they regard as satisfactory[1].

These expectations on average align remarkably closely with the ASFA Comfortable budget standard. In April 2018 the annual expenditure needed to support a comfortable lifestyle in retirement was $60,264 for a couple and $42,764 for a single.

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1 Wilkins, R. The Household, Income and Labour Dynamics in Australia Survey: Selected Findings from Waves 1 to 15. Melbourne Institute: Applied Economic & Social Research. Accessed from http://melbourneinstitute.unimelb.edu.au/__data/assets/pdf_file/0010/2437426/HILDA-SR-med-res.pdf

The HILDA survey indicates that the mean required income reported in 2015 was $43,128 for single people and $62,340 for a couple. Unsurprisingly, being partnered increases expected income requirements, since the income needs to support two people.

Respondents to the question on income requirements were also asked how much they had thought about their income needs in retirement. The survey results indicate that those who had given a lot of thought to the matter had higher expectations of their income requirements in retirement.

The HILDA researchers also concluded that, based on pre-retirement spending, people do not have unreasonably high expectations of their income requirements in retirement. This is in clear contrast to claims by the Grattan Institute that the ASFA Comfortable Standard involves expenditure in retirement that is much higher than individuals were spending prior to retirement.

This is confirmed by other available statistics. For instance, data from the ABS Household Expenditure Survey 2015-16 indicate that even when allowance is made for differences in housing costs both the average and median disposable incomes for households with a household head aged 55 to 64 are higher than the levels set by the ASFA Comfortable retirement standard. The circumstances of such households are directly relevant to assessing the adequacy of retirement income as such households contain individuals who are approaching retirement in the not too distant future[2].

The average disposable income for such households in 2015-16 was $95,160 and the median disposable income was $76,230.

The current scheduled increases in the SG are crucial for more Australians achieving their desired standard of living in retirement, which for the great bulk of persons is at a level well above the Age Pension alone.

This is true across a range of income levels and circumstances.

Some specific examples are provided in the box below.

Box 1: Consequences at the individual level of not getting to a rate of 12 per cent for the Superannuation Guarantee

Example 1:
David is currently thirty years old, earning $70,000 per year in an office job, receiving the benefit of 9.5 per cent Superannuation Guarantee (SG) which will lift to 12 per cent by 2025. He is on track to reach the ASFA Comfortable standard of living by the time he retires at 67 with $568,600 if he currently has $50,000 in his super. If the SG stays at 9.5 per cent David would be projected to have $497,000 at retirement, a much lower figure.

Example 2:
Ann is a thirty-year old park ranger. She earns $60,000 per year, and currently has a superannuation balance of $20,000. With the SG rate increasing to 12 per cent by 2025, Ann will have $422,000 in superannuation savings at retirement (age 67). This is around $66,000 more than if the SG remains at its current rate. Ann will have a higher standard of living in retirement if the SG rate increases. With an annual retirement income of $40,900, compared with $39,200, Ann will be able to afford an extra holiday in Australia each year.

Example 3:
Maria is fifty-five years old. She works part-time in a local book store, and earns $40,000 per year. Maria's superannuation balance is currently $100,000. With the SG rate increasing to 12 per cent by 2025, Maria will have $189,000 in superannuation savings at retirement (age 67). This is around $7,000 more than if the SG remains at its current rate. Maria will also have a higher retirement income ($32,900 per year compared with $32,600). Maria will be able to afford an extra trip to the movies each fortnight or have a buffer of $7,000 to deal with any unexpected home repairs or health costs in retirement.

2 Australian Bureau of Statistics 6530.0 – Household Expenditure Survey, Australia: Summary of Results, 2015-16, September 2017. Accessed from http://www.abs.gov.au/ausstats/abs@.nsf/0/97E70263E0B479CFCA257059007E19B6?OpenDocument

Myth 2

Increasing compulsory superannuation blows out the Budget

***Fact:* Increasing compulsory superannuation significantly reduces Age Pension expenditure**

The changes made to the Age Pension means test, with effect from 1 January 2017, mean that the Age Pension savings from an increase in the rate of the Superannuation Guarantee to 12 per cent will be much greater than projected by the Treasury in 2013.

This is confirmed by research undertaken by Willis Towers Watson and The University of Melbourne using projections based on HILDA data.

Under the changes to the assets test, the taper rate doubled from $1.50 to $3.00 per fortnight for each $1,000 of assessable assets above a minimum threshold, meaning that eligibility for partial Age Pension payments phases out more rapidly and at lower amounts than previously. At the same time there were some increases to the lower thresholds used in the assets test.

The research indicates that the tighter means test will see the proportion of couples expected to achieve a comfortable level of retirement income falling, with a reduction from 62 per cent to 51 per cent. On the other hand, singles will be affected less with a reduction from 38 per cent to 37 per cent in the proportion of singles expected to achieve a comfortable level of retirement income.

The groups that have been most affected by the changes to asset test are those that would receive the greatest benefit from the increase in the SG to 12 per cent. The combined effect of not going to 12 per cent with the tighter means test would mean that middle Australians would have a standard of living lower than what has been their reasonable expectation.

There also would be implications on Age Pension expenditures and the extent to which retirees are partly or fully self-funded.

Currently, on the basis that the scheduled increases in the SG to an eventual rate of 12 per cent will occur, the proportion of the population aged over 65 receiving a full or part Age Pension will fall from the current 70 per cent to 60 per cent by 2055, with 60 per cent of those receiving the Age Pension on the full Age Pension falling to 40 per cent over the same time period. Not going to 12 per cent would mean that the reduction in the proportion on the Age Pension would be not be as great, perhaps only to 65 per cent or so. As well, the proportion on the full Age Pension would be higher than 40 per cent in 2055.

Myth 3

Women and low income earners do not benefit from moving to 12 per cent

***Fact:* Increasing the SG to 12 per cent will benefit women and low income earners and improve their retirement experience**

It has been argued that many Australians would be better off if they received higher wages rather than an increase in the rate of compulsory superannuation contributions.

There are a number of flaws in that argument.

No guarantee of higher wages or higher take home income

In the current economic environment it is unclear if wages would be significantly higher than they would otherwise if the SG were not gradually increased from 9.5 per cent to 12 per cent.

Currently wages growth in the private sector is averaging less than 2 per cent per year, and that is over a period when there has been no increase in the SG. Failing to increase the SG is not a recipe for strong wages growth. There is no evidence that individuals receiving wages of less than $450 a month have been compensated with higher wages given that no SG contributions are made.

It also needs to be acknowledged that superannuation remains an attractive savings vehicle for Australians, including low income earners. For an individual on less than $37,000 a year the effective tax rate on superannuation contributions is zero when the impact of the Low Income Superannuation Tax Offset is taken into account. Outside of superannuation the tax rate, including Medicare levy, is 21 per cent for those who earn above $18,200.

For individuals on an income of $37,001 to $87,000 the tax rate including Medicare levy is 34.5 per cent, compared to a 15 per cent tax rate within super.

Further, it needs to be acknowledged that the interaction between the social security system and the tax system can be complicated for lower income earners.

Higher wages can impact on income tested Family Tax Benefits (FTB) and Child Care Benefit (CCB). Part-time workers who are on other social security payments can see higher wage payments result in lower Centrelink payment. Compulsory superannuation contributions do not form part of the income test for social security purposes and deferring wages through superannuation can make a significant difference in retirement.

For example, a second earner whose income is in the FTB B withdrawal range, and whose partner's income is in the range over which FTB A and CCB are both withdrawn can cause the family to lose 50 to 75 cents of benefits per extra dollar that they earn. Under the present income tax scales they would be paying 21 cents tax, facing an effective marginal tax rate of 70 to 95 per cent, keeping only 5 to 30 cents per dollar.

For many low to middle income earners, especially those with young families, forgoing superannuation contributions would lead to little if any increase in their current income and consumption. The main winner would be the Federal Budget.

Currently contributions above the current SG rate do not favour low income earners or women

ABS data indicate that around 4 per cent of employees receive employer contributions above minimum compulsory payments. This is on top of the 10 per cent or so of employees who are in defined benefit superannuation schemes where notional contributions are generally well above 9.5 per cent on average.

However, there are significant differences between various groups in the likelihood of having employer contributions above the minimum compulsory amount.

While 4.7 per cent of males have the benefit of such contributions, only 2.8 per cent of women do.

Amongst managers and professionals, nearly 6 per cent of employees receive the benefit of such contributions while less than 2 per cent of employees who are community and personal service workers, sales workers and labourers do (who tend to be low income earners).

There are also marked differences between employees in different industries. Over 7 per cent of employees in the public administration and safety industry, over 10 per cent in financial and insurance services, and over 7 per cent of employees in the public administration and safety industry. Only around 2 per cent of those in the retail trade and in health care and social assistance industries receive the benefit of such contributions.

Failure to move to 12 per cent compulsory contributions would have a greater impact on those already relatively disadvantaged in the paid labour market.