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Committee Secretary
Senate Standing Committee on Economics
Department of the Senate
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Parliament House
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AUSTRALIA

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Dear Committee Secretary,

**The Objective of Superannuation**

The Association of Superannuation Funds of Australia (ASFA) is pleased to provide this submission on the Superannuation (Objective) Bill 2016 ("the Bill").

**About ASFA**

ASFA is a non-profit, non-political national organisation whose mission is to continuously improve the superannuation system so people can live in retirement with increasing prosperity. We focus on the issues that affect the entire superannuation system. Our membership, which includes corporate, public sector, industry and retail superannuation funds, plus self-managed superannuation funds and small APRA funds through its service provider membership, represent over 90 per cent of the 14 million Australians with superannuation.

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If you have any queries regarding the contents of our submission please contact Julian Cabarrus on (02) 8079 0815 or by email jcabarrus@superannuation.asn.au, or me on (02) 8079 0808 or by email gmccrea@superannuation.asn.au,

Yours sincerely

Glen McCrea
Chief Policy Officer

## Introduction

ASFA continues to be strongly committed to the formalisation of an objective for superannuation that reflects the core purpose of the system in providing adequate retirement outcomes for all Australians.

The community deserves to be financially confident in retirement. People spend their working lifetime contributing a portion of their income to a compulsory savings system, and reasonably expect a dignified retirement commensurate with this sacrifice in return. Preservation of savings requires the community to forego expenditure today, so that they can enjoy a comfortable standard of living in retirement. The Bill must enshrine an enduring commitment to the achievement of retirement outcomes that meet these community expectations.

Clear and effective benchmarks to measure superannuation proposals against in years to come are required to guard against constant political tinkering. ASFA recommends benchmarking against the social and fiscal goals of the system. We recognise that improvements to adequacy over time must be delivered in a fiscally sustainable manner.

However, as the system matures and the pool of private savings grows, future governments should be discouraged from trading away retirement objectives to achieve unrelated policy goals. The Bill must protect against this and give Australians confidence that their retirement savings are safe from such erosion now and into the future.

If policy makers act consistently with an appropriate objective for superannuation many more Australians will have an adequate income that meets their needs, both expected and unexpected, throughout retirement. This will minimise the number of retirees living in poverty or relative poverty, and maximise the number living in comfort and with dignity. Achieving a comfortable standard of living in retirement is the aspiration of all Australians and the objective should support that aspiration.

## Superannuation (Objective) Bill 2016

**Primary Objective**

A concept of adequacy must be incorporated in the objective. The core purpose of the superannuation system is to deliver income which affords a dignified and comfortable standard of living in retirement, over and above what the Age Pension delivers.

The primary objective proposed by the Financial System Inquiry (FSI) is a sound starting point for the development of a more holistic objective. It recognises that the superannuation system must provide income to retirees in conjunction with the Age Pension. However, it fails to articulate the social goal of the system to maximise the number of Australians living in comfort and dignity in retirement.

There are significant risks with this objective. A future government considering the compatibility of superannuation policy settings against the terms of the primary objective proposed in the Bill could narrowly conclude:

- “Substitute” as a like for like replacement of the age pension with superannuation in effect being a privately funded alternative to the Age Pension. On this interpretation it would be possible to put in place a means test where there is no benefit to an individual from superannuation, all the benefits flow to the government in the form of reduced Age Pension expenditures; and

- The word “supplement” is preceded by the word “or”, implying that superannuation policy settings do not necessarily have to be cast in such a way that superannuation savings will support a total retirement income in excess of the full Age Pension.

On this basis, a future government could put in place policy settings that were aimed at the achievement of super balances that were no more than necessary to provide an income stream equal to the Age Pension, with no Age Pension entitlement for a person with such a balance. This would be an extremely poor policy outcome that would have negative repercussions on the retirement outcomes of Australians.

ASFA supports a concept of substitution that infers a greater level of self-funding in retirement so that the Age Pension is not required for a subset of the community and retirement incomes generally are higher. The availability of superannuation should provide a higher standard of living to Australians in retirement than what is provided by the Age Pension alone.

For example, the critically important bipartisan policy of increasing superannuation guarantee to 12% that will result in increased levels of self-funding in retirement may be brought into question when viewed alongside the Bill’s proposed objective, rather than prioritised in line with an objective of the system more focussed on adequacy. The consequence of deferring the previously planned increase has been a reduction in adequacy, resulting in a decreased Global Pension Index rating for Australia[1].

The terms of the Explanatory Memorandum do not substantively address the potential shift in policy settings that may arise through implementation of the primary objective as proposed in the Bill. It is not stipulated what the “limits to the level of government support provided”[2] are. Future governments will be left to fill this vacuum with their own interpretation as to the level of support to be provided to superannuation savers. This will perpetuate the setting of policy in the context of the annual budget cycle and further erode confidence in the system.

The references to self-sufficiency in the Explanatory Memorandum are made in the context of alleviating fiscal pressures on government. Whilst it is important to recognise that greater self-sufficiency will indeed alleviate fiscal pressures, the link between self-sufficiency and achieving a dignified and comfortable standard of living in retirement also needs to be addressed. The purpose of superannuation goes well beyond that of the Age Pension’s role as a safety net.

We note that the recently legislated $1.6 million superannuation balance pension cap and $1.6 million balance cap for making non-concessional contributions are examples of policies that encourage self-reliance and the achievement of adequate retirement incomes through the superannuation system. They also increase equity by setting an appropriate monetary ceiling where the system stops providing taxpayer support for accumulating retirement savings and supporting retirement incomes. These policies reflect the core purpose of the system and ASFA contends the Bill underpinning future superannuation policy should do the same.

Accordingly, we recommend the following objective replace that contained in the Bill:

[1] Melbourne Mercer Global Pension Index 2016
[2] EM paragraph 1.20

***Recommendation:***
*The primary objective of the superannuation system is to provide an adequate income to ensure all Australians achieve a comfortable standard of living in retirement, supplementing or substituting the Age Pension.*

**Subsidiary Objectives**

ASFA agrees that "a single primary objective cannot possibly encompass all aspects of the purpose and attributes of the superannuation system".[3] Superannuation policy decisions should be required to meet the primary objective and fit within the terms of the subsidiary objectives. To effectively achieve this, subsidiary objectives should be incorporated in the Bill, rather than the Explanatory Memorandum.

The Bill doesn't refer to the subsidiary objectives or contain any mechanism for their consideration. The Explanatory Memorandum indicates that addressing the subsidiary objectives in the statement of compatibility (which is only required to consider compatibility with the primary objective) is considered to be "best practice", rather than a prescribed step. [4] Adopting this approach will entrench ambiguity and uncertainty in the policy development framework.

The Explanatory Memorandum also introduces the concept of auxiliary benefits, such as insurance, which are not considered in the Bill. An Explanatory Memorandum should facilitate the understanding of a Bill rather than introduce entirely new concepts. An Explanatory Memorandum can assist in interpreting a law but it doesn't stand as law in its own right.

ASFA believes the following subsidiary objectives should be incorporated in the framework:

| **Subsidiary objective** | **Why the objective is important** |
|---|---|
| Be equitable in its outcomes for current and future generations | The superannuation system must be equitable in its outcomes.<br><br>Intra-generational equity in the system ensures individuals are treated fairly after taking into account different levels of income and net worth. Inter-generational equity describes the burden or benefit one generation has compared with another.<br><br>Treating individuals fairly promotes confidence and belief in the system. As the system matures, this will manifest itself in higher levels of voluntarily engagement by superannuation members to achieve better retirement outcomes. |
| Protect members who suffer misfortune or personal tragedy | The provision of group insurance is a crucial part of the superannuation system that assists Australian's who suffer misfortune.<br><br>These arrangements alleviate underinsurance and the potentially devastating economic implications for individuals and their families who face personal tragedy. Lack of cover also adds to the call on the public purse through increased social security benefits including disability payments and single parent allowances. |

[3] Treasury, Objective of Superannuation Discussion Paper p.3, 9 March 2016
[4] EM paragraph 1.18

The subsidiary objective relating to insurance should clearly define the purpose of valuable insurance arrangements provided through the superannuation system. It is not adequate to state that "A range of other benefits may also be provided through superannuation, for example insurance."[5] This fails to reflect the broader policy role that insurance in superannuation now fulfils in the community.

Earlier this year ASFA made a submission to the Productivity Commission in the context of efficiency that dealt with the objective of insurance in superannuation. Building on the Commission's proposed objective, ASFA recommends that the subsidiary objective of insurance in superannuation is as follows:

***Recommendation:***
*The superannuation system provides insurance that delivers valuable protection to the community and meets members' needs at reasonable cost*[6]

**Impacts on Low Income Earners**
For a person on $40,000 a year (below median employment earnings) compulsory superannuation contributions supported by tax concessions have important roles to play in improving retirement outcomes for low income Australians.

For such a person aged 30 and with a current balance of $20,000, the compulsory superannuation system will deliver an estimated $236,500 at age 67, the future eligibility age for the Age Pension. According to the ASIC MoneySmart calculator, this will increase retirement income for a couple from $33,716 a year (the Age Pension) to $44,104 a year in total, a 31% increase.

For a single person the increase is from $22,365 to $32,517, a 45% increase.

These increased levels of resources in retirement substantially improve the standard of living for retirees, even though they may have been low income during their time in paid employment and will receive a full or substantially full Age Pension in retirement. Means test thresholds result in the low income retirees gaining close to 100% of the benefit of having private retirement savings.

In terms of the improved outcomes that the higher level of income arising from having such a superannuation balance support, these include:

- Ability to pay off any remaining housing debt at the time of retirement
- Greater capacity to pay for home repairs or improvements during retirement
- More or better food in retirement
- More and/or better clothing and footwear
- Ability to fund out of pocket medical expenses rather than total reliance on public health system for major medical issues
- Able to afford a better car and greater maintenance and repairs
- Able to afford more holidays within Australia or trips to visit family
- More generally, having savings that can be used to meet unexpected expenses during retirement

[5] EM paragraph 1.28
[6] ASFA submission to the Productivity Commission's Draft Report – How to Assess Superannuation Competitiveness and Efficiency p. 9

While the Age Pension is sufficient for a home owner to avoid poverty in retirement, other resources are needed to support greater enjoyment of life in retirement.

ASFA remains concerned that a future government, referencing the proposed objective in the Bill, could establish policies that decrease retirement income adequacy for low income earners and determine this to be aligned with the objective of super.

**Statements of Compatibility**

The Bill requires statements of compatibility to be prepared in respect of proposed superannuation regulation, including an assessment of whether the regulation is compatible with the primary objective of the system and we are supportive of this accountability measure. Similar consideration must be extended to an appropriate suite of subsidiary objectives incorporated in the legislation.

We are also concerned with the carve-out of regulatory instruments from this requirement, as detailed in the Explanatory Memorandum:

*"The primary objective of the superannuation system does not affect the meaning of any law of the Commonwealth (other than this Bill). This means that the primary objective cannot be used to interpret any Commonwealth law other than this Bill.*

*As such, the primary objective of the superannuation system will not be applied to instruments issued, or decisions made, by regulators of the superannuation system, such as the Australian Taxation Office (ATO), the Australian Prudential Regulation Authority (APRA) and the Australian Securities and Investments Commission (ASIC), in administering relevant superannuation laws."*[7]

ASFA believes the Bill should be applied in situations where the relevant instrument is not purely administrative or mechanical in nature and it imposes additional requirements above and beyond legislation (for example an APRA Prudential Standard). This will ensure accountability and transparency for any agency involved in setting superannuation policy so that the system is delivering on its promise to members.

In addition, ASFA does not support the inclusion of subsections 6(5) and 7(4) of the Bill, which state that if a statement of compatibility is not prepared for a Bill or regulation relating to superannuation, this will not affect the validity, operation or enforcement of the Act or regulation. It is unclear under what circumstances the non-preparation of a statement of compatibility would arise, or why this would be deemed acceptable, given it will be a legislative requirement for such a statement to be prepared.

**Measuring the System**

ASFA believes the Bill should incorporate a set of objective measures to test policy proposals against and track the success of the system in achieving its objective over the long run. Objective measures will eliminate ambiguity and build trust and confidence in the system. It will protect against detrimental changes that erode this trust and confidence and support policies that deliver an adequate standard of living in retirement.

The spending required to live a comfortable retirement should be analysed, including the gap between the full age pension and this level of income. The questions that must be answered in defining and measuring the objective are:

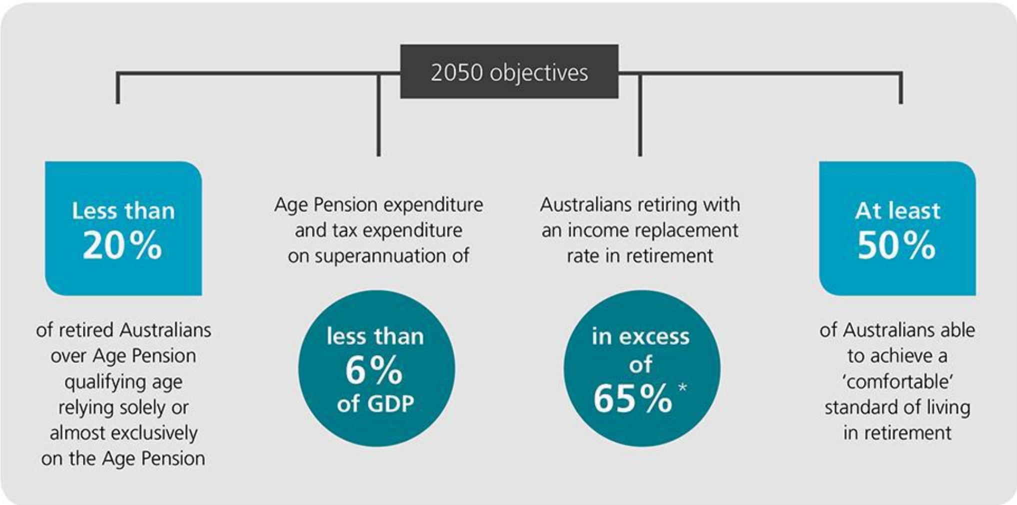
[7] EM Paragraph 1.14

- What standard of living is the system aiming to deliver to the community in retirement?
- How much income is required to achieve this?

One of the most important steps in establishing what is an adequate retirement income is calculating how much is needed to be spent each year in retirement to support a comfortable lifestyle. However, many people struggle when it comes to developing a budget for their future needs, particularly when their retirement is many years away.

The ASFA Retirement Standard has been developed to help solve this problem by objectively outlining the annual budgets appropriate for various categories of Australians to fund their needs in their post-work years. It provides benchmarks for both a comfortable and modest standard of living, for both singles and couples, and is updated quarterly to reflect changes to the consumer price index (CPI).

ASFA has proposed four quantitative measures to guide the design of superannuation and retirement income policy settings and measure the outcomes that are being achieved. These measures focus on the cost of the Age Pension and tax concessions for superannuation relative to GDP, levels of reliance on the Age Pension, the level of income replacement in retirement and the percentage of the retired population living at a standard equivalent at least to the ASFA Retirement Standard 'comfortable' level.




*To maintain equity, there should be a ceiling where the system stops providing taxpayer support for accumulating retirement savings or supporting incomes in retirement.

Further detail regarding these measures and the underlying rationale behind ASFA's retirement standards, including budget breakdowns, is contained in our 6 April 2016 submission to Treasury.[8]

**Tracking the System**

ASFA's recommended measures examine both social and fiscal aspects of the system. They are aspirational in nature with a 2050 timeframe; however we recommend the system should be progressively tracking towards these in the interim. The FSI recommended that government "report publicly on how policy proposals are consistent with achieving these objectives over the long term"[9]. Statements of compatibility do not go far enough in this regard. The FSI suggested that:

[8] ASFA submission to Treasury pp.7-13, Objective of Superannuation Discussion Paper, 6 April 2016

[9] FSI Final Report p.95

“In addition (to Regulatory Impact Statements), government could periodically assess the extent to which the superannuation system is meeting its objectives. This could be done in a stand-alone report or as part of the Intergenerational Report, which is prepared every five years.”[10]

ASFA agrees that periodically assessing how the system is tracking will provide regular benchmarks to measure performance against, facilitating informed policy decision making. Policy decisions should be removed from the annual budget cycle and tax expenditures statement. Consistency with long-term objectives is appropriate given the long-term nature of superannuation savings.

We believe such an approach will provide a higher degree of stability, integrity and accountability in relation to superannuation policy. It will guard against short-termism and drive transparent, consistent in decision making. A likely outcome of this will be increased confidence in the system, promoting member engagement and voluntary savings.

As recommended by the FSI, one approach is to incorporate periodic reviews in the Intergenerational Report (IGR) produced by the government every five years. The IGR assesses the long-term sustainability of current government policies and how changes to Australia’s demographics may impact on economic growth, workforce and public finances over the next 40 years.  Measuring progress against a broader set of measures within the IGR falls within its broad remit and would add value to its conclusions.

Alternatively, government could perform a separate review in tandem with the IGR process, whatever the mechanism, commitment to a process of ongoing measurement and review is required.

[10] FSI Final Report p.99