Executive summary

A need for further changes?

ASFA considers that there is no urgency to make changes to superannuation. Any changes need to be well considered and examined as part of a holistic review. The Tax White Paper process provides that opportunity.

ASFA also endorses the government's objective of ensuring a desirable level of stability of policy settings for superannuation. This will assist in maintaining consumer confidence in superannuation.

In ASFA's submission in response to the Tax Issues Paper, we reviewed superannuation system against the objective and principles of the system. In particular we reviewed the system against the principles of:

- adequacy
- equity
- sustainability
- simplicity.

That submission outlined how the superannuation system is operating well against these principles. It is already reducing the cost of the Age Pension by $7 billion a year and as a result of superannuation, the proportion of people expected to receive the full pension has fallen from 44 per cent in 2000 to 25 per cent today, and will fall to 23 per cent by 2023.

Over the past five years, there have been a substantial number of reforms to the system that have only recently been implemented, or are in the process of being implemented, or are being legislated, or are yet to be fully considered. These changes have had a significant impact on superannuation fund members and the industry. The changes need time to take full effect and for consequences and costs to come to light.

While ASFA sees no urgent need for reform, in our first submission to the Tax White Paper we presented two reforms for discussion and consideration over the long term to develop a more sustainable and equitable system. These reforms arise from ASFA's review of the system against the objectives and principles of superannuation and they should be given full and in depth consideration as part of the holistic Tax White Paper process. The recommendations are:

1. There should be a ceiling where the system stops providing taxpayer support for accumulating retirement savings, or supporting incomes in retirement, and the appropriate level in today's dollars is a balance of $2.5 million. It can be argued that tax concessions above this level contradict the equity and sustainability principles of superannuation.
2. There are also gaps in the system, in particular regarding those who have broken work patterns.

In response to the expansion of the mandate for the Tax White Paper to include the full retirement incomes system, ASFA has undertaken additional analysis. In doing so, ASFA has again applied the principles of the superannuation system. Arising from this, ASFA has concluded there is no urgent need for reform. However, ASFA is recommending two additional changes to the retirement income system that should be considered in the long term and has reviewed several positions outlined in the first submission.

The two additional recommendations are:

1. Broaden the coverage of superannuation
2. The social security system should provide limited immediate incentives for income streams offering long-term longevity protection.

Improving adequacy of retirement incomes and spreading coverage of superannuation

There is a strong policy case to extend the compulsory superannuation regime to include some or all of the self-employed. Nearly ten per cent of the labour force is self-employed. Only a relatively small number of the self employed have business assets sufficient to support a comfortable standard of living in retirement. While tax concessions have led to some self-employed saving for retirement through superannuation, average balances and coverage have remained relatively low.

While account balances are growing as the superannuation system matures, many people will still retire with inadequate superannuation savings to fund the lifestyle they want in retirement.

There should be no further delay to the scheduled increases in the Superannuation Guarantee (SG) to eventually reach 12 per cent of wages, and desirably the timetable should be condensed. Women in particular benefit from the compulsory superannuation system.

The Low Income Superannuation Contribution (LISC) should be retained after 2017 as it assists low-income earners to achieve adequacy of retirement incomes. It also is consistent with the general principle of providing appropriate levels of support for individuals across the income ranges. Women form the majority of recipients of the LISC given that they make up nearly 70 per cent of part time workers.

ASFA considers that there needs to be greater flexibility in the system to allow those with broken work patterns to catch up.

Adoption of all these measures would particularly benefit women in terms of improving their financial independence and the adequacy of their income in retirement.

Impact of the changes to the Age Pension asset test

While the asset test will be less onerous at relatively low asset levels after 1 January 2017, it leads to a substantial reduction in Age Pension when higher levels of superannuation and other assets are held.

The changes to the asset test will have a mixed impact on the achievement of the objectives for the system proposed by ASFA. They will assist in containing the annual costs in aggregate of Age Pension payments and tax concessions for superannuation to below six per cent of GDP, principally through containing Age Pension expenditures at around three per cent of GDP. The changes will have little, or no effect, on the proportion of the population receiving the full Age Pension.

On the other hand, the changes will have an impact on adequacy of retirement incomes, reducing the average replacement rate in retirement from 65 per cent to below 60 per cent and reducing the proportion of the retired population, reaching the level of the ASFA Retirement Standard comfortable level from around 50 per cent of the population, to just over 40 per cent.

Couples will need to save around $130,000 more in order to finance a comfortable standard of living in retirement. For a single person, the additional amount is around $115,000.

The preservation age for superannuation

ASFA considers there are grounds for the preservation age being linked to the Age Pension age, such as a specified period less than the Age Pension age. ASFA suggests that such a gap generally should be five years. If this were done then the preservation age would increase automatically, and in synchronisation with, the Age Pension eligibility age.

However, if the eligibility age for the Age Pension were increased beyond 67, then the preservation age for superannuation should not automatically be increased, but be reviewed in light of labour force, health and disability experience of older workers at that time.

ASFA recognises that, as the Productivity Commission recently highlighted, there are many in the workforce who will not be able to continue to be employed beyond 60. If the preservation age were to increase to above age 60, the conditions of release in the *Superannuation Industry (Supervision) Regulation 1994* would need to be reviewed.

Better integration between superannuation income streams and the provision of the Age Pension

In order for the system to achieve its key objectives, superannuation should be used for retirement income and not for the provision of a bequest or the repayment of significant levels of debt. Providing incentives for people to take up an income stream can help achieve this objective.

Incentives could include giving beneficial social security treatment for at least some income streams. For example, income streams that meet certain prescribed criteria could be treated differently for Age Pension asset or income tests.

Recommendation 1

The Superannuation Guarantee be increased to 9.75 per cent as at 1 July 2016 and then increase by at least 0.25 per cent each year until it reaches 12 per cent.

Recommendation 2

The Low Income Superannuation Contribution be retained beyond 2017.

Recommendation 3

Broaden the coverage of superannuation.

Recommendation 4

A limit of $2.5 million be placed on the superannuation funds an individual can rollover to commence an income stream in retirement. Amounts above this ceiling should remain in the accumulation phase and continue to attract the nominal earnings tax of 15 per cent or be removed from superannuation.

Recommendation 5

Non-concessional contributions should also be capped at $1 million over a lifetime to prevent very large balances from accruing in the future as an integrity measure to complement the $2.5 million capital cap.

Recommendation 6

Concessional contribution caps should be changed in such a way that individuals with broken work patterns are able to make sufficient contributions. Further work also needs to be undertaken to evaluate methods for improving flexibility in superannuation to allow individuals with broken work patterns to make "catch-up" contributions to achieve a higher income in retirement.

Recommendation 7

The preservation age should be linked to the Age Pension age and should be set at five years less than the Age Pension age, up to a maximum age of 62.

Recommendation 8

The social security system should provide limited immediate incentives for income streams offering long-term longevity protection.