Submission (II) to the

Australian Government

Re:think – Tax discussion paper, treatment of retirement income

UnitingCare Australia

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UnitingCare Australia is the national body for social services in the Uniting Church in Australia, supporting service delivery and advocacy for children, young people, families, people with disabilities, and older people

Table of Contents

1 UnitingCare Australia

UnitingCare Australia, the national body for UnitingCare, provides advocacy and support for the network of UnitingCare agencies operating nationally across more than 1,600 sites in metropolitan, regional and remote Australia. Our network is one of the largest providers of community services to children, young people and families, older Australians, Indigenous Australians, people with disabilities, the poor and disadvantaged, and people from culturally diverse backgrounds. The network makes a strong contribution to the Australian economy with an annual turnover in excess of $2.5 billion, employing 39,000 staff supported by the work of over 28,000 volunteers.

UnitingCare Australia works with, and on behalf of, the UnitingCare network to advocate for policies and programs that will improve people's quality of life. Our work is grounded within the theological framework of the Uniting Church, particularly the Church's social justice perspectives, and our commitment to speaking with and on behalf of those who are the most vulnerable and disadvantaged is an expression of the Christian vision of inclusion and equality of opportunity for all people.

2 Recommendations

This submission adds further to the comments and recommendations made in our original submission[1] to the taxation review. In making this second submission we have been mindful of the key findings of the 2014 Financial System Inquiry and of the 2015 Intergenerational Report with regard to the economic and social challenges of an ageing population and also the Productivity Commission's superannuation policy post-retirement research paper.

UnitingCare Australia believes that taxation treatment of superannuation and retirement income must be centred on the principle of seeking to maximise the ability of people to self-fund their retirement in order to increase the resources available to government to provide an adequate safety net for those individuals who are unable to be financially self-sufficient in retirement. A comprehensive review of retirement income and the mechanisms, including the age pensions and superannuation, that are available to help people financially prepare for increased longevity is urgently needed.

We recommend that a retirement income review examine how policy settings can better enable more people to save sufficient income, through superannuation and other private savings, to allow them to live fulfilling lives in retirement without reliance on the age pension. This approach to the retirement income debate should deliver policy outcomes which assist more people to be self-sufficient in retirement and allow for a more targeted and appropriately government funded retirement income safety net for those who need it.

We believe that that the following issues should be addressed within the scope of a retirement income review:

1. Set a policy goal to reduce dependency on the age pension;
2. Introduce superannuation contributions to the Government's Paid Parental Leave scheme and remove the 15% contribution tax on these contributions;
3. Consider removing the 15% contribution tax for low paid workers;
4. Expedite the introduction of the 12% superannuation guarantee rate;
5. Increase the availability and range of annuities products attached to the superannuation system and make it a compulsory offering once the market for annuities is further developed;
6. For taxation purposes income derived from superannuation should be treated as ordinary income; and
7. Changes to the superannuation system be subject to a phase transition.

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[1] Submission to the Australian Government Re:think – Tax discussion paper, *UnitingCare Australia*, June 2015, p.9

3 Introduction

Australia's ageing population brings with it social policy challenges and opportunities which we as a society need to embrace. Increasing longevity requires us to think through how best welfare, superannuation and private savings coalesce to enable individuals to live a fulfilling life in retirement. UnitingCare Australia believes that our nation needs to engage in a thoughtful debate about how we best fund our future retirement income needs.

The shifting demographic balance of the Australian population, the move away from typical work patterns and the changing shape of families and communities offers us an opportunity to properly examine current retirement income policies and mechanisms to ensure that they meet our changing social environment. Key to this consideration is the role of superannuation and whether or not the policy framework underpinning it remains fit for purpose both now and into the future given.

Superannuation does not sit in isolation from the range of other income mechanisms and supports for older people. For most working Australians superannuation is and will continue to be a critical asset to fund their retirement, and if the current trend of declining home ownership continues it will likely surpass the home as the primary asset owned by retirees. Therefore the role of superannuation savings is critical in any meaningful discussion around adequate retirement income.

UnitingCare Australia believes that consideration of retirement income within the context of the taxation review is important because taxation is a key mechanism to fund essential government services and supports for older people in need. However, as outlined in our recommendations, we believe that a comprehensive review of retirement income should increase the options available to enable more people to self-fund their retirement whilst further supporting the sustainability of a retirement income safety net for those who are unable to do so.

4 A comprehensive review of retirement income and superannuation

UnitingCare Australia believes that any review of retirement income should consider developing a new compact between the government and older Australians in which the role of government becomes one of promoting and protecting private savings and superannuation for retirement rather than simply providing income through the age pension. A new compact to enable more people to self-fund their retirement should ease spending on the age pension whilst not diminishing the responsibility of government to provide an adequate retirement income safety net for those in need.

We suggest recalibrating the age pension and superannuation guarantee scheme by setting a measured policy goal to reduce dependency on the age pension, for example to shift the dependency ratio from 70:30 to 30:70. Achieving this would, we believe, significantly reduce pressure on government spending and free-up financial resources to facilitate more targeted support for government services and supports, including the age pension.

Within the scope of a retirement income review we encourage the Government to develop a greater number of better options; in order to enable whole-of-working-life superannuation contributions and increase the number of self-funded retirees. Doing so will address particular concerns we have with current superannuation policy settings that are failing a significant proportion of Australians to prepare for retirement, especially women and mothers because they more likely to spend less time in paid work and receive lower pay than men[2].

It is important to get the superannuation policy settings right for women as evidence shows that they are likely to continue to live longer than men and require greater access to aged care services. Further, we believe that the trade-off for those individuals who take time away from the paid workforce to care for children or other family members should not be financial insecurity in retirement nor increased dependency on the age pension.

We believe there is significant merit in identifying new products and mechanisms to increase certainty of income in retirement as well as the capacity to save for the costs of aged care needs. The Productivity Commission has identified that many older Australians are asset rich but income poor[3] and we encourage further consideration of unlocking the value of the principal residence to help people self-fund their retirement and aged care needs whilst maintaining a decent standard of living.

5 Recalibration of the age pension and superannuation policy settings

The traditional compact between older Australians and the Government is that when individuals retire they will have access to a government funded age pension. However in 1992, as part of a major reform package addressing Australia's retirement income, the then

[2] Research Paper Volume 1: Chapters - Superannuation Policy for Post-Retirement, *Productivity Commission*, July 2015, p.49

[3] Research Paper, An Ageing Australia: Preparing for the Future, *Productivity Commission*, November 2013, p.16

Government introduced compulsory "Superannuation Guarantee" system as the third pillar of retirement income policy. The three pillars are:

- A safety net consisting of a means-tested government age pensions system;
- Private savings generated through compulsory contributions to superannuation; and
- Voluntary savings though superannuation and other investments.

We believe that the founding three pillars of the Australia's retirement income system are as relevant today as they were in 1992 and that they must continue to be the foundation of retirement income policy in Australia.

The bedrock of Australia's retirement income policy is the means-tested government age pensions system. The 2015 Intergenerational Report[4] states that in 2055 that around 70% of Australians will continue to access the age pension. The report also notes that the proportion of part-rate pensioners relative to full-rate pensioners is expected to increase, however the proportion of retirees receiving no pension is not projected to decline. The report also states that expenditure on the age and service pensions is expected rise as a percentage of GDP from 2.9% of GDP in 20014-15 to 3.6% in 2054-55[5].

The current superannuation system is still maturing and while changes to the superannuation system over the past three decades have provided some individuals with the capacity to retire comfortably, many Australians do not have sufficient superannuation balances to meet their retirement needs.

While 90% of all employed persons are covered by superannuation, concerns remain about the adequacy of savings to provide even a modest[6] level of retirement income. To achieve a modest level of superannuation income (that is $23 000 p.a), the balance on retirement required by a single person is around $475 000 while for those seeking a "comfortable" level of retirement income will require a superannuation balance of around $869 000. Both "modest and comfortable" retirement income rates are predicated on access to at least a part age pension, ownership of a home and access to the Commonwealth Seniors Health Card (CSHC).

In 2011-12[7] the average balance at retirement was $197 000 for men and $105 000 for women, which leaves most retirees heavily dependent on the age pension to meet their

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[4] 2015 Intergenerational Report Australia in 2055, *The Treasury*, March 2015, p.67
[5] Ibid p.69
[6] Spending patterns of older retirees: New ASFA Retirement Standard, *The Association of Superannuation Funds of Australia*, September 2014, p.5 (Modest income is valued at $23 000 p.a, comfortable income is valued at $42 000)
[7] An Update on the level and distribution of retirement savings, *The Association of Superannuation Funds of Australia*, March 2014, p.3

daily living costs. These balances suggests that unless more is done now to improve the capacity of employees to contribute to their superannuation balances; dependency on the age pension will continue for many working Australians for at least several more generations.

In order to establish more adequate contribution targets we believe policy makers must gather up-to-date data to identify the likely minimum superannuation balance individuals will need on retirement in order to self-fund a decent standard of living until the end of their lives. Home ownership and the capacity to pay for age care services will be variable elements within this consideration.

Under the current age pension income test, a retiree would not be eligible for the age pension if they earn $1868 per fortnight ($47568 p.a) or more. Further access to the CSHC ceases once a retiree earns more than $51500 p.a. The value of the CSHC according to the Productivity Commission[8] is unclear but estimates suggest that it is upwards of $1600 p.a. Based on these figures, when we set a nominal retirement income value for a single retiree not accessing the age pension or CSHC then that that value would be $53100 p.a ($51500 plus $1600 value of the CSHC), which means that a superannuation balance on retirement needed to achieve this level of annual income is about $1.1 million with a retirement period of 25 years and presuming home ownership and no special provision for age care needs (i.e. current non-concessional rules will apply to aged care). Again we believe that policy makers need more timely data to gain an accurate understanding of the balance of savings that self-funding retirees will require on retirement.

Based on the nominal retirement value outlined above ensuring that individuals are able to achieve an adequate level of income in retirement from private and voluntary savings will require a number of retirement income policy changes. Primary amongst these is a more rapid change in the rate of increase in the superannuation guarantee rate to 12%. Under the current policy the full 12% contribution will not be achieved until 2025-26. We also believe that there needs to be stronger mechanisms to support the saving capacity within the superannuation system for those individuals who are unable to make whole-of-working-life contributions because of temporary unemployment and work needs to be done to identify how the superannuation system can be used as a vehicle to enable individuals to meet their future age care costs.

We recognise that these changes will have an impact on government revenue and we therefore recommend that changes are made to the taxation treatment of superannuation

[8] Research Paper Volume 2: Supplementary Papers - Superannuation Policy for Post-Retirement, *Productivity Commission*, July 2015, p.167

drawdowns, in particular to the tax free income applicable to retirees over the age of 60, as well as those drawing down lump sum payments from their superannuation balances.

6 Increasing the superannuation guarantee rate and annuities

We envisage that delivering an adequate level and certainty of retirement income as well as self-funding aged care will require an increase in the superannuation rate to at least 12%. While we welcome the Treasurer’s 2015-16 Budget announcement that the target rate will be lifted to 12% we are increasingly concerned about the impact of further delaying its introduction to 2025.

We know that a super guarantee rate of anything less than 12% will continue to see many thousands of Australians have inadequate retirement savings and prolong high dependency on the age pension. Therefore we urge reconsideration of the timetable. If it is not possible to adopt the 12% rate for all workers before 2025 then we ask the Government to consider a staggered introduction to better support those who have yet to enter the workforce, for example by introducing the 12% rate for employees born in or after 2000, and to relieve future pressure on the age pension.

The 12% contribution is an important signal about the maturation of the superannuation system. Those employees who commence work under this regime and are able to contribute towards their superannuation balances for their entire working life at this rate will more likely achieve self-sufficiency in retirement as compared to all previous generations. That said, it will be important that a number of policy settings complement this new level of contribution and subsidised whole-of-working life benefit through changes to the taxation treatment of superannuation and most critically the manner in which it is used.

Income security is an important issue for everyone, in particular for self-funded retirees who often have little or no capacity to supplement income through employment or other means. We recommend that further work be done to encourage the use of annuity products attached to the superannuation system and indeed make it a compulsory offering once the market for annuities is further developed.

7 Saving to meet aged care needs

The ongoing experience of the UnitingCare network of aged care providers shows us that the upward trend in the demand and need for age care packages continues to exceed supply. The Australian Institute of Health and Welfare reports that women make up the greater proportion of aged care clients than men[9] and the Productivity Commission reports that there will be a sizeable increase in the quantum of people requiring complex aged care and support over the next 40 years. The Commission's 2011 report *Caring for Older Australians* raised the question of who should pay for aged care[10].

In considering who should pay we note that the current practice, where possible, for many retirees is to use their home as an asset to fund retirement and aged care. While we recommend that more work is done to unlock the potential of the home to self-fund retirement we also know that home ownership in Australia is in decline and that for many low income and disadvantaged people it is unachievable and that the risk of poverty is often greater for non-home owners than for home owners. Therefore we believe we need to increase the options that are available to help people save for retirement and aged care costs which are not dependent on home ownership.

Under the current superannuation system there are a range of products, such as invalidity insurance, which provide additional protection for an individual in the event that specific circumstances unfold. However, as outlined above, the increasing longevity of Australians is increasing the number and type of aged care services they need to access.

UnitingCare Australia has previously advocated for the expansion of the superannuation system to include the capacity for it to meet the costs of an individual's aged care needs. We continue to believe that there is a pressing need for the Government to harness the capital growth mechanisms of superannuation to enable individuals to fund their aged care needs by quarantining a percentage contribution over the full term of their working life for this purpose. In seeking to model this proposal we have consulted superannuation industry representatives and looked to the collective experience of the UnitingCare network of aged care providers to identify typical aged care pathways and costs. Based on our findings we estimate that a percentage contribution of approximately 1.5% would be sufficient to enable most individuals to self-fund their aged care needs[11]. However, we provide this only as an initial figure and suggest that the next step would be actuarial assessment and further working in order to give a more precise determination.

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[9] Aged care packages in the community 2010-11: A statistical overview, *Australian Institute of Health and Welfare*, September 2012, p.vii

[10] Productivity Commission Inquiry Report Volume 2 Caring for Older Australians, *Productivity Commission*, June 2011, p.6

[11] Submission to the Treasury consultation on the Better regulation and governance, enhanced transparency and improved competition in superannuation discussion paper, *UnitingCare Australia*, February 2014, p.7

8 Opening new pathways to save for retirement

Under the current superannuation system absence from the workforce more often than not leads to a lower superannuation balance. This makes women and those unable to participate in the workforce particularly vulnerable to poverty in retirement and increases their dependency on government support in old age unless they are financially supported by family members or have access to other funds.

Since the introduction of the compulsory superannuation scheme Australian demographics have changed considerably and will likely continue to move away from the settings of the early 1990s. In particular there has been a significant change in the shape of households and family types as we increasingly see blended or step-families and lone person households with the traditional nuclear family becoming less prevalent.

The Australian Institute of Family Studies (AIFS) reports that one in four Australian households is a lone-person household and that more women live alone than men. 39% of women who live alone are aged over 70 compared to 19% of men and the number of older people living alone is increasing.[12] The AIFS also reports that 86% of one-parent families with dependent children are headed by mothers[13].

The Australian Bureau of Statistics reports that life expectancy at birth in the decade to 2011 has, on average, been higher for females than males. A boy born between 2009 and 2011 can expect to live, on average, 79.7 years, while a girl born in the same period can expect to live 84.2 years.[14] The AIWH reports that most people living in residential aged care facilities are women (70%), the majority are over 80 years old (77%) and the average length of stay for permanent residents is increasing – in 2010-11 it was 145.7 weeks, an increase of 11% since 1998-99.[15]

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[12] Demographics of living alone, Australian Institute of Family Studies, https://aifs.gov.au/publications/demographics-living-alone, accessed 15 July 2015

[13] Australia households and families, Australian Institute of Family Studies, https://aifs.gov.au/publications/australian-households-and-families, accessed 15 July 2015

[14] Life Expectancy, *Australian Bureau of Statistics*, http://www.abs.gov.au/ausstats/abs@.nsf/Lookup/4125.0main+features3110Jan%202013, accessed 30 June 2015

[15] Residential aged care in Australia 2010-11: A statistical overview*, Australian Institute of Health and Welfare*, September 2012, p.vii

Awareness that women are a particularly vulnerable group in terms of the debate around superannuation policy is not new. In 2001 the National Centre for Social and Economic Modelling (NATSEM) raised the financial situation of women in retirement as a major public policy issue. NATSEM highlighted that superannuation policy does not best support women because their average earnings even when employed full-time are only 84% of male average earnings, they are more likely to work irregular or part-time hours and women's careers are more likely to be interrupted due to child bearing and rearing. The result being that they able to accumulate substantially less than superannuation than men[16].

The Productivity Commission's recently published research paper into superannuation policy notes that women who care for children are projected to have less than half the superannuation of someone who has been in full-time employment for 40 years or more[17].

Although we have acknowledged earlier in this submission that many changes have been made to superannuation policy it appears that superannuation policy has not yet comprehensively addressed the challenge of how best to enable women, who are likely to need a longer retirement income than men, to financially prepare for retirement.

As such we believe that there is a pressing need for the Government to investigate other pathways to enable individuals to continue or begin contributing to their superannuation when absent from the workforce and to increase the number of ways in which additional contributions can be made to "top-up" an individual's superannuation. Also to ensure that any unintended consequences of the current arrangements do not continue to undermine the ability of women and mothers to accumulate savings.

A first step might be to introduce superannuation contributions to the Government's paid parental leave scheme. While the Government contribution could be at the minimum wage rate, the value of that contribution could be enhanced by ensuring that this contribution is not subject to the 15% contribution tax.

We also believe that there is a pressing need to investigate how low-income and disadvantaged individuals might contribute to superannuation so that they too can take advantage of the concessions which government applies to superannuation. We suggest that this would require consideration of exempting low paid workers from the superannuation contribution tax.

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[16] SPRC National Social Policy Conference Paper, Women and Superannuation in the 21st Century, NATSEM, July 2001, p.4

[17] Commission Research Paper, Superannuation Policy for Post-Retirement, *Productivity Commission*, 7 July 2015, Vol.I p.

9 Unlocking the potential of the home on retirement

Community and neighbourhood are important to the wellbeing of older people, particularly those with limited mobility and low incomes as they will spend the majority of their time at home. Remaining local in old age supports the independence and social connectedness of individuals which benefits both their physical and mental health.

While home ownership is not a possibility for many low-income earners at any life stage we believe that using the principal place of residence as an asset to enable more people to self-fund their retirement must be given special consideration, in part because it will free up resources to support non-home owners in retirement.

Whilst the principal residence is given special treatment within the taxation and transfer system we believe that further consideration should be given to its role and use for retirement purposes. For example, how might retirees who choose to remain at home be able to unlock this capital to self-fund their retirement and/or meet aged care costs? We also believe that there is merit in exploring different ways in which the tax and transfer system as applied to property might better support retirees who sell their home to remain in their local area whilst self-funding their retirement.

Affordable and appropriate housing is a critical issue for older Australians and, in the absence of local solutions, remaining at home is often a significant financial burden for retirees but one that provides important emotional and social support that they would not have should they leave.

10 Interaction with the government pension

The superannuation system intersects with a number of government policy and funding settings, in particular the aged pension and benefits card.

The measures announced by the Minister for Social Services on 16 June 2015[18] to increase the amount of assets a person can hold before their pension is reduced are steps in the right direction. Although these changes will primarily affect people with assets over a million dollars they will also support increases for those individuals who have less.

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[18] Media release, *Department of Social Services*, http://scottmorrison.dss.gov.au/media-releases/government-s-fairer-and-sustainable-pension-budget-changes-secure-critical-senate-support accessed 30 June 2015

We believe that the government should further consider the thresholds at which self-funded retirees access the age pension and benefits to ensure that only those with inadequate superannuation income or non-principal place of residence assets can access it. For example, we note that the current settings provide more support to a retiree with a $1.5 million home and $300 000 in assets receives than to some of the poorest Australians in receipt of Newstart payments.

We suggest that in order to introduce more sustainable superannuation and retirement income policy settings a phased transition would be a sound approach. The following outline is intended to inform thinking and consideration as to how this might best be undertaken:

New Superannuation requirements for those born after 1 Jan 2000

- Superannuation Funds including SMFs include a compulsory annuity pension product
- Superannuation Funds including SMFs provide aged care product/prescribed purpose account specifically to meet the cost of aged care needs
- Pre-retirement lump sum withdrawals taxed at full marginal rates
- Post-retirement lumps sum withdrawals except for prescribed purposes treated as income
- Annuities and superannuation income withdrawn attract tax a rate of 37% tax rate excluding the Medicare levy) for income between $80 001 and $ 180 000. Income in excess of $180 001 will pay tax of $37 000 ($54 547 - $17547) plus 47% and the (Temporary Budget Repair Levy if applicable) for each dollar over $180 000.
- Mechanism to enable people who are temporarily absent from the workplace to redress the lower superannuation lump sum

Transitional arrangements for those people born before 31 December 1999

- Pre-retirement lump sum withdrawals taxed at full marginal rates
- Post-retirement lump sum withdrawals except for prescribed purposes treated as income
- Annuities and superannuation income withdrawn attract tax a rate of 37% tax rate excluding the Medicare levy) for income between $80 001 and $ 180 000. Income in excess of $180 001 will pay tax of $37 000 ($54 547 - $17547) plus 47% and the (Temporary Budget Repair Levy if applicable) for each dollar over $180 000.
- Superannuation Funds offer an aged care product/prescribed purpose account within the individual's fund with the contribution to the aged care fund or product in addition to the current pre-tax contribution
- Mechanism to enable people who are temporarily absent from the workplace to redress the lower superannuation

11 Taxation treatment of retirement income and superannuation

UnitingCare Australia believes that taxation treatment of superannuation and retirement income must be centred on the principle of seeking to maximise the ability of people to self-fund their retirement in order to increase the resources available to government to provide an adequate social services safety net that people in need can access at any life stage.

The 2014 Financial System Inquiry identified that tax concessions in the superannuation system are not well targeted at improving retirement incomes. This in turn increases the cost of the superannuation system to taxpayers and contributes to a lower standard of living for Australians in retirement.[19]

The current superannuation system provides incentives for people to save for their own retirement; however most of the billions of dollars in tax concessions benefit only the highest wealth individuals. We believe that this inequity needs to be addressed to more sustainably fund the future income needs of older Australians.

We believe that income derived from superannuation should be treated as ordinary income and we see little merit in allowing superannuation income to be tax free for people over the age of 60. Retirement income derived through the superannuation system has been subject to preferential tax treatment through the generous tax concessions applicable to contributions.

Under the current tax arrangements an employee earning $90 000 a year ($1730 per week) pays around $23 000 in income tax, yet a superannuant over 60 years of age would pay no income tax on a similar income drawn down from their superannuation balances. We recognise tax on a superannuant's contributions has been paid, over the life of their contributions to a maximum of 30%. Accordingly, we suggest that any taxation payable on any withdrawals from superannuation balances be offset against tax already paid on those earnings. As such we propose that income derived from superannuation balances should be tax free up to $80,000 per annum. Any income earned between $80,001 and $180,000 should be subject to the marginal tax rates of 37% (excluding the Medicare levy) and 45% (excluding the Medicare levy) for incomes $180,001 and over.

[19] http://fsi.gov.au/publications/final-report/chapter-2/ accessed 15 July 2015

These proposals would assist in offsetting the increase in tax expenditure as a result of an increase in the compulsory superannuation guarantee.

12 Conclusion

The current retirement income and superannuation policy settings are a complex set of arrangements that impact or will impact on the lives of nearly all Australians and we are concerned that the current framework is failing far too many. The current settings will likely see most Australians, women and mothers in particular, rely on the age pension and other government supports to meet their retirement and aged care needs and continue to increase the pressure on government spending for older Australians.

UnitingCare Australia believes that the primary requirement of superannuation must continue to be to support individuals in retirement to live a decent and dignified life, including when they require access to aged care and services. The continuation of an adequate safety net through the age pension must continue to be a key element of our superannuation system and we believe that enabling more people to self-fund their retirement will further the sustainability of this important safety net.

UnitingCare Australia is therefore calling on the Government to take prompt action to comprehensively review retirement income and superannuation policy settings and to make the necessary changes in order to enable a greater proportion of the population to self-fund their retirement and aged care needs. Increasing the number of individuals who self-fund their retirement combined with more appropriate taxation treatment of retirement income and superannuation will free-up resources that can be redirected to provide an adequate safety net for those in need.