Submission to the Retirement Income Review Consultation Paper

29 January 2020

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Submission to the Retirement Income Review Consultation Paper, November 2019

The Centre for Independent Studies (CIS) welcomes the opportunity to provide a submission in response to the Retirement Income Review Consultation Paper of November 2019.

The CIS is a leading independent public policy think tank in Australasia. Founded in 1976, its work is driven by a commitment to the principles of a free and open society. The CIS is independent and non-partisan in both its funding and research, does no commissioned research nor takes any government money to support its public policy work.

As a Senior Fellow in the economics program at the CIS, I undertake research into a wide range of public finance issues and regularly comment in the media on taxation and other budget issues. Before joining the CIS, I was a senior official with the New South Wales Treasury and in that role was responsible for advising the state government on taxation policy and federal/state financial relations. Prior to that, I was a senior official with the Australian Treasury in Canberra, and both the World Bank and the International Monetary Fund in Washington, DC.

As with other CIS researchers, I have written extensively on retirement income matters in recent years, including the following publications:

> Robert Carling, *Superannuation Taxation*, The Tax Policy Journal, vol 7, 2011 (The Taxpayers Research Foundation Limited, Sydney, 2011)
>
> Stephen Kirchner, *Compulsory Super at 20: 'Libertarian Paternalism' Without the Libertarianism,* Policy Monograph 132, CIS, 2012.
>
> Simon Cowan and Matthew Taylor, *The Age Old Problem of Old Age: Fixing the Pension,* Research Report 3, CIS, 2015.
>
> Robert Carling, *Right or Rort? Dissecting Australia's Tax Concessions,* Research Report 2, CIS, 2015 (especially pp 14 – 16)
>
> Robert Carling, Simon Cowan, Terrence O'Brien and Michael Potter, articles on 'Saving Super' in *Policy,* vol 32 no 3, CIS, Spring 2016
>
> Simon Cowan, *Millenials and Super: the case for voluntary superannuation,* Policy Paper 20, CIS, May 2019.

The attached submission, consistent with Review's terms of reference, focuses on selected issues involved in constructing a 'fact base' of the current retirement income system, rather than dwell on policy choices that are beyond the terms of reference.

I stand ready to expand on the points in the attached submission, or to provide further information, if his would assist the Review.

Yours sincerely,

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SUBMISSION TO THE RETIREMENT INCOME REVIEW CONSULTATION PAPER

Effect of superannuation system on age pension numbers and costs

The Review should bring an independent perspective to bear on the question of the effect of the superannuation system in reducing the number of age pension beneficiaries receiving a full pension or part pension, and in reducing budget expenditures on pensions and associated benefits. These estimates should separately cover (a) the period from 1992 up to now and (b) a long projection period (say up to 2050) to when the superannuation system will be fully mature. Such estimates are an important element in assessing the benefits of the superannuation system. Availability of independent estimates endorsed by the Review panel would help clarify the issues in light of the conflicting claims made in the public discussion of superannuation about the effects of the system in reducing age pension numbers and costs.

Interaction between superannuation and age pension systems

It is often claimed that the increase in the pension asset test taper rate in 2016 produced the perverse outcome that, over a certain range of superannuation balances, those relying on superannuation benefits could actually be worse off than those on the age pension. Testing by the Review of the veracity of these claims and the seriousness of the problem would be helpful to a public understanding of the interaction between the age pension and superannuation systems.

Frequency of changes to superannuation system parameters

It is often stated that the frequency of significant changes to superannuation rules and relevant tax laws has undermined confidence in the superannuation system. The Review would perform a valuable service by tracing the history of superannuation since the late 1980s, including a listing of all significant changes in parameters such as contribution limits, access rules and taxes. This would form an important part of the 'fact base' the Review is tasked with compiling.

Lifetime government support

The Review has chosen to illustrate the distribution of 'public support' for retirement incomes by producing Figure 4 ("Lifetime government support provided through the retirement income system"), which adds together age pension benefits and tax concessions at various income percentiles. Figure 4 appeared to attract more attention than any other aspect of the Consultation paper when it was released in November. This is unfortunate, as Figure 4 is misleading on a number of counts:

a. The graph implies that tax expenditures are conceptually equivalent to outlays on pensions, but this is not the case. There is a big difference between a taxpayer-financed payment to a social benefit recipient and a taxpayer paying less tax than they would under a different set of tax rules.
b. The tax concessions component of the graph rests on the concept of tax expenditure, but disregards the well-documented weaknesses in the

measurement of tax expenditures — particularly that it depends heavily on the behavioural response of those affected by a policy change. Moreover, the graph appears to use the 'comprehensive income' benchmark for measuring tax expenditure, ignoring the fact that this benchmark has been contested. It can be argued that the 'expenditure tax' benchmark is more appropriate, and this benchmark results in much lower estimates of tax expenditure (for more detail, see my submission to the House Tax Committee Inquiry into the Tax Expenditure Statement, August 2015).

c. The graph implies that dollars spent on the age pension and dollars 'spent' on tax concessions are equivalent and that funds could therefore easily be reallocated from one to the other. However, it would be very risky for the budget to attempt to finance an increase in pension outlays from a reduction in tax concessions, as the latter may well not yield the expected savings once the behavioural response is factored in.
d. The graph appears to assume that individuals remain in the same income decile throughout their lives, whereas in fact there is considerable movement across deciles by most individuals.
e. Age pension expenses are included but it is not clear whether all the other benefits directly linked to pension eligibility are included. If not, the public support to age pension recipients is being understated.

Inconsistent indexation arrangements

Current legislation provides for a diverse range of indexation arrangements for the age pension, superannuation contribution limits and various thresholds; such as for the superannuation transfer balance cap. Some are indexed to the CPI, some to average earnings and some not at all. The review should document these different provisions and examine the implications and whether there is any rationale for them.

Fiscal sustainability

The fiscal sustainability of age pension and superannuation arrangements cannot be judged in isolation from long-term projections of the budget as a whole — such as those contained in the Intergenerational Report. For the reasons stated above, estimates of tax expenditure are not useful to an analysis of fiscal sustainability of superannuation, where the focus should be on superannuation tax revenue actually received rather than some hypothetical concept of tax revenue that could be received but is not.

Adequacy

While the notion of adequacy is meaningful in relation to the age pension and to calculations of the retirement incomes that the Superannuation Guarantee Charge is likely to be capable of generating in the future, it is unclear what 'adequacy' means in relation to voluntary saving for retirement. Adequacy of voluntary saving is a matter of individual choice and preference. Policy should not attempt to prescribe an 'adequate' level of voluntary saving but to correct for anti-saving biases in the tax and social security systems.