prime super
surprisingly straightforward

Prime Super

Prime Super has been managing the retirement savings of working Australians for almost a quarter of a century.

Forged as the super fund for farmers and agriculture, more recently Prime Super has expanded its focus to the regions of Australia more generally and then to the Health and Aged Care sectors.

Prime Super is neither an industry fund or a retail fund. We operate in a competitive environment where relative investment performance is critical, particularly over the medium and long-term.

Our investment philosophy is to be measurably different compared to industry funds and we aim to deliver above-average performance to our members over a rolling three-year basis.

Prime Super reported strong returns across many investment options for members in 2018-19. Our MySuper option placed us in the top quartile of super funds assessed over three, five and seven years, and delivered an 8.53% return over a 10-year period.

Prime Super is proud to manage more than $5.2 billion for more than 130,000 members.

Prime Super - position summary

The three pillars - the Government-funded age pension, compulsory superannuation and voluntary savings - are the key to reviewing retirement income, in the opinion of Prime Super.

While compulsory superannuation can work well for 60 percent of the population, there are many people who will not save enough through this scheme to contribute in a meaningful way to their retirement. This makes a Government-funded age pension an important safety net.

Most superannuation funds would advocate for an increase in compulsory contributions. However, we think we need to be realistic. Although the current 9.5 percent compulsory rate is not enough to grow superannuation savings for a comfortable retirement, Australia is in a period of low wage growth therefore an increase in the contribution rate is not realistic at this point in time.

An area of the system that Prime Super advocates for change is the rules for self-managed super funds. These funds are used by a number of Australians as a tax management tool, but the Australian Taxation Office believes asset diversification within them is not at a suitable level.

Of the total superannuation assets of $746.2 billion, more than a quarter are invested in self-managed superannuation funds. Individual funds holding less than $500,000 have more than 30% of their assets held in cash and are essentially overly conservative.

If this is the only retirement savings these individuals have access to, a more appropriate asset allocation would be to focus a much higher allocation on growth assets. Existing asset allocation will not support a retirement income stream for any significant length of time.

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To ensure the integrity of the overall superannuation system, additional controls should be established to manage the self-managed superannuation sector. Consideration should be given to a higher level of regulation over this sector, or a change to the tax regime for self-managed superannuation as a recognition the level of oversight of this sector is presently lower than public offer superannuation funds.

The superannuation system was set up with insurance playing an important aspect of the scheme. The group insurance arrangements, where a good level of cover is offered at a reasonable cost, benefits all Australians.

Yet it is the area which makes super complicated. Insurance is generally provided by a third party and there is not a level playing field across all funds. Prime Super would advocate that a better solution is for a National Insurance Fund separate to superannuation.

The investment performance of superannuation funds has been the focus of government and regulators. The stated possibility of removing the bottom quartile of underperforming funds means all funds are moving towards using similar strategies in asset allocation to ensure their performance is not too far from the average. This is having a side effect of increased risk to the system as a whole, as everyone underperforms in the long term.

Consultation questions

The review has put forward a number of questions for consideration by those making submissions. Prime Super has chosen to respond only to those that are relevant, or where we believe we have an important point to make.

Purpose of the system and role of the pillars

4. **What are the respective roles of the Government, the private sector, and individuals in enabling older Australians to achieve adequate retirement incomes?**

   The Government has a key role to play in establishing a system that ensures quality of life for those Australians living in retirement, and for providing a framework to allow more Australians to save enough to fund their own retirement.

5. **The Panel has been asked to identify the role of each of the pillars in the retirement income system. In considering this question, what should each pillar seek to deliver and for whom?**

   Pillar 1 – Government Funded Age Pension
   The Government-funded Age Pension is a safety net level of income for retirees throughout the full period of retirement. The safety net must be aimed at ensuring retirees are able to live with dignity in their retirement.

   Consideration must be given to whether an individual lives as a single or in a relationship. It must be accepted that the cost of living as a single is not simply half that of the cost of living as a couple.

   The Government has an additional role to ensure that the increasing risk to the retirement system posed by longevity risk (individuals living longer) is covered.

   Pillar 2 – Compulsory Superannuation
   The compulsory superannuation system must ensure taxpayers save an amount for their retirement. Amounts accumulated at the point of retirement (above a certain threshold)

should not be available for lump sum payments but should be rolled into authorised annuity-based pension products.

The system should be constructed in such a way that individuals are encouraged to fully fund their own retirement. This will mean higher income earners are encouraged to fund their retirement through superannuation rather than personal savings. Where funds are accumulated through superannuation, and then transferred to regulated pension products (similar to MySuper products) and withdrawals are solely to fund retirement, the net benefit to the country will be through a reduced requirement to pay pensions in the future. This does come at the cost of current taxation revenue to the Government.

The funding of pension payments through existing superannuation funds will ensure retirement monies are professionally managed, thereby leading to a better accumulation of funds for individuals and a more sustainable income stream for a member.

At the national level, the superannuation system has an implicit underwriting from the Government through the pension system. Therefore, the aim of the superannuation system must be to provide a pension higher than the Government pension for a period of time that the invested funds last.

It is important to note that superannuation is limited in its ability to perform by the value of the money invested into superannuation during an individual's life. Those with broken work patterns or low income levels will never contribute enough to superannuation to enable the superannuation system to accumulate sufficient funds to provide a reasonable pension in retirement. It is however critical that all Australians, regardless of income levels, are required to make superannuation contributions.

To ensure the integrity of the superannuation system, all working Australians need to make contributions to superannuation. Existing limits on fees and other deductions ensure a low income individual's superannuation account will grow at an adequate rate. If there is an ability for low income earners to exit the system, this increases the risk of others finding ways to not be included in the system.

Pillar 3 – Voluntary Savings
Voluntary savings must be included in the overall retirement savings plan. Means testing should be in place to ensure the full pension is paid to those Australians that require it, and those with sufficient self-funded assets are drawing less from the pension.

6. **What are the trade-offs between the pillars and how should the appropriate balance between the role of each pillar in the system be determined?**

Not all Australians will be able to fund their own retirement. Superannuation cannot be considered as a catch-all solution for everyone, nor should it be considered a solution to minimise overall Government support for retirees.

The bottom third of all income earners (gender is not relevant) will not earn sufficient income over their working life to make sufficient contributions to the superannuation system to fully fund their own retirement.

The system should ensure contributions are made for all employees to superannuation and require a minimum pension amount to be paid. So if a person at retirement only has

$100,000 in their superannuation account, this should not be allowed to be taken as a lump sum. It must be taken as a pension.

This pension from the superannuation fund must be a minimum of whatever the age-based pension is for that individual, so that no Government Age Pension is payable. Once the accumulated amount is eroded, then the Government pension commences.

In this way every individual, no matter their circumstances, partially funds their own retirement. The Government then funds the period from the exhaustion of the personal savings throughout the remainder of the individual's life.

It is important that the ability of individuals to spend a lump sum (from the previously mentioned threshold) at the point of retirement is removed.

There is no benefit to providing incentives or bonuses to low income earners to increase their retirement savings. In the current system where Government provides additional contributions to match contributions made by low income earners, this money accumulates up to the point of retirement. At the point of retirement, the amount is cashed out and spent, and the individual then falls back on a full pension.

It is far better for the Government to not make additional contributions now, and simply fund the retirement through the Age Pension.

Self-Managed Super

While self-managed super is seen as being a part of the superannuation system it is in essence used by a number of Australians as a tax management tool. That is, business or other assets are purchased through the tax beneficial structure of a self-managed fund. In addition, data from the Australian Taxation Office highlights that asset diversification within self-managed funds is not at a level that would be expected of a suitable superannuation fund.

The following table is available from the ATO website:

https://www.ato.gov.au/About-ATO/Research-and-statistics/In-detail/Super-statistics/SMSF/Self-managed-super-fund-quarterly-statistical-report---March-2019/?anchor=Assetallocationbyassetvalue#Assetallocationbyassetvalue

2017	\$1–\$50k	>\$50–\$100k	>\$100–\$200k	>\$200–\$500k	>\$500k–\$1m	>\$1–\$2m	>\$2–\$5m	>\$5–\$10m	>\$10m
Listed trusts	1.34%	2.33%	3.36%	4.29%	4.79%	5.04%	4.65%	4.02%	5.74%
Unlisted trusts	2.28%	4.56%	6.12%	6.73%	7.69%	9.07%	11.00%	13.32%	16.63%
Insurance policy	0.00%	0.00%	0.01%	0.01%	0.02%	0.02%	0.02%	0.04%	0.04%
Other managed investments	1.08%	1.77%	2.62%	3.84%	4.41%	5.02%	4.97%	4.99%	4.01%

Cash and term deposits	54.11%	48.81%	45.71%	31.81%	27.04%	26.57 %	24.00%	20.04%	14.44%
Debt securities	0.17%	0.26%	0.36%	0.72%	1.18%	1.51%	1.84%	2.04%	1.85%
Loans	1.30%	1.76%	1.35%	0.65%	0.44%	0.47%	0.56%	0.73%	1.45%
Listed shares	23.64%	24.07%	24.54%	24.90%	26.95%	29.87 %	30.72%	30.67%	25.28%
Unlisted shares	2.29%	2.18%	1.79%	0.96%	0.61%	0.68%	0.87%	1.31%	2.83%
Limited recourse borrowing arrangements	0.03%	0.20%	1.27%	11.22%	10.74%	4.81%	2.83%	2.73%	6.04%
Non-residential real property	0.85%	1.72%	3.00%	5.48%	6.74%	8.37%	10.14%	11.27%	12.33%
Residential real property	0.90%	2.16%	2.90%	5.51%	6.28%	5.34%	4.82%	4.06%	2.64%
Collectables and personal use assets	0.27%	0.47%	0.31%	0.11%	0.06%	0.04%	0.03%	0.03%	0.00%
Other assets	10.37%	8.02%	5.21%	2.82%	2.23%	2.24%	2.36%	2.91%	4.27%
Overseas shares	0.63%	0.67%	0.65%	0.55%	0.46%	0.54%	0.72%	1.18%	1.62%
Overseas non-residential real property	0.06%	0.08%	0.05%	0.02%	0.01%	0.01%	0.02%	0.01%	0.08%
Overseas residential real property	0.20%	0.38%	0.24%	0.09%	0.04%	0.03%	0.02%	0.03%	0.01%
Overseas managed investments	0.13%	0.07%	0.08%	0.06%	0.07%	0.09%	0.10%	0.17%	0.17%
Other overseas assets	0.35%	0.49%	0.43%	0.25%	0.25%	0.28%	0.33%	0.44%	0.57%

Total	100.00%	100.00%	100.00%	100.00%	100.00%	100.00 %	100.00 %	100.00 %	100.00 %

Self-managed funds with less than $500,000 have more than 30% of their assets held in cash and are essentially overly conservative. Importantly, if this is the only retirement savings these individuals have access to, a more appropriate asset allocation would be to focus a much higher allocation on growth assets, as the existing asset allocation will not support a retirement income stream for any significant length of time.

The diversification of investments for self-managed funds is also limited when compared to regulated public offer funds.

Regulated public offer superannuation funds are required to comply with a vast range of regulatory requirements and have significant supervisory oversight by regulators. This provides added security to those members that invest their retirement savings with superannuation funds. However, these regulatory requirements come at a cost.

APRA superannuation statistics as at 30 September 2019 show the following

	September 2019
Total superannuation assets	$2,927.5 billion
Total APRA-regulated assets	$1,970.1 billion
Of which: total assets in MySuper products	$779.2 billion
Total self-managed super fund assets	$746.2 billion
Exempt public sector superannuation schemes assets	$150.9 billion
Balance of life office statutory fund assets	$60.3 billion

Of the total superannuation assets of $746.2 billion, 25.5% are invested in self-managed superannuation funds. This is nearly the same amount invested in the highly regulated MySuper products, where $779.2 billion is presently invested. The same report highlights there are 598,582 self-managed superannuation funds, and this number continues to increase.

A significant proportion of the Australian population therefore have their retirement savings managed through a self-managed fund, (92.8% of self-managed funds have one or two members, for a weighted average of 1.87 members per fund). The total number of individuals invested in self-managed superannuation accounts is therefore roughly 1.1 million.

To ensure the integrity of the overall superannuation system, additional controls should be established to manage the self-managed superannuation sector. Consideration should be given to a higher level of regulation over this sector, or a change to the tax regime for self-managed superannuation as a recognition that the level of oversight of this sector is lower than that for public offer superannuation funds.

Though the risk of the failure of an individual self-managed superannuation fund is minimal to the overall pension costs of the Government, significant and sustained under-performance is a risk where the total value invested in self-managed superannuation is equivalent to that invested in the highly regulated MySuper sector.

Principles for assessing the system

8. Are the principles proposed by the Panel (adequacy, equity, sustainability, and cohesion) appropriate benchmarks for assessing the outcomes the retirement income system is delivering for Australians now and in the future? Are there other principles that should be included?

Fundamentally these principles are reasonable.

However, it is important to acknowledge that superannuation is essentially a very simple product of investing a small amount over a long period of time, which then accumulates to a reasonable sum at retirement. The balance at retirement is entirely dependent upon contributions over a lifetime and the net investment earnings added, and the management of the costs associated with running a regulated superannuation product.

The principle of sustainability is largely dependent upon the contributions that have been made to a superannuation fund and the investment performance of that fund. A superannuation fund cannot solve the adequacy issue, as adequacy is determined by the level of contributions made. This is an employment issue.

A balance across the three pillars to provide these principles is required. No one pillar can hope to meet all four of these principles.

Investment performance

Much focus has been given to under-performing superannuation funds.

Caution needs to be exercised in this area, as performance can relate to many things. Where a fund has made a clear decision to de-risk the investment portfolio (while others maintain a higher allocation to growth assets) whether this is a valid decision is dependent upon an assessment of the investment environment and the needs of the members of the Fund.

The current focus on high investment performance, and 'removing the bottom quartile of under performers', will lead to a convergence of asset allocations between all public offer superannuation funds leading to increased investment risk in the system as a whole.

A key benefit of having a range of superannuation offerings, all with different investment strategies, is that where there is significant market correction (such as the GFC) there will be some funds that perform better than others.

In the current environment there is increased risk in being 'too far away from the pack', and as such Funds will move to have similar asset allocations to ensure performance does not lag too far behind the average. This move leads to an increased investment risk to the system.

A better outcome is to have varied strategies allowing for market variations that over the long term perform for members.

Insurance
Insurance is a key aspect of superannuation and has had much focus over recent years. Insurance in superannuation needs to be assessed on the following simple terms:

- every dollar deducted from a superannuation account for an insurance premium leads to a lower account balance at retirement;
- more than 90% of superannuation fund members will never make a claim on their insurance policy held through their superannuation fund simply because they do not need to;
- a significant benefit is achieved for all Australians through the offering of large broad-based group insurance products through superannuation, where products provide a reasonable level of insurance cover at a lower unit cost, and
- there is a benefit to society through the broad-based offering of insurance cover to all members of superannuation funds, as more individuals have a level of cover and thereby protection in the event of death or disability.

A solution to the complexity of having insurance within superannuation is to have a National Insurance Fund to cover all workers.

Adequacy

11. What measures should the Panel use to assess whether the retirement income system allows Australians to achieve an adequate retirement income? Should the system be measured against whether it delivers a minimum income level in retirement; reflects a proportion of pre-retirement income (and if so, what period of pre-retirement income); or matches a certain level of expenses?

It is important the retirement income system is based on being able to deliver an outcome that at a minimum provides a safety net. No Australian should be left without an income in their retirement. Equally, there is a need to help individuals maintain a lifestyle in their retirement not dissimilar from their pre-retirement lifestyle. Where it is not possible to maintain that pre-retirement lifestyle, there is a clear incentive for individuals to work around or outside of whatever system is established.

There must also be limits on what the retirement system should fund. In the same way there is a floor established through a safety net system, there must be an upper ceiling on what is retirement income. Asset based means testing is an important consideration for retirement income assessment. For example, passive income in retirement that is extreme should be taxed. A landlord that is retired on a large property portfolio with net taxable income should continue to pay tax.

Sustainability

19. What factors should be considered in assessing how the current settings of the retirement income system (e.g. tax concessions, superannuation contribution caps, and Age Pension means testing) affect its fiscal sustainability? Which elements of the system have the greatest impact on its long-term sustainability?

Self-Managed Superannuation – property investments
The current approach to self-managed superannuation is misaligned. Self-managed superannuation is currently used in many circumstances as a tax planning tool, as opposed to a retirement savings tool. This is best explained through consideration of a small business looking to manage its costs.

A simple consideration for a small business would be whether to purchase a property the business operates out of, to provide certainty into the future. It is more efficient from a tax point of view to own this property through a self-managed fund and through the business directly. This creates a risk to the individual because a portion of their retirement savings is intimately linked to the occupation.

There are two key issues:

- The investment by the self-managed superannuation fund is based not on sound long-term investment rationale, it is based on the current business' operating needs and tax considerations;
- Ongoing decisions about the retention of the property or possible sale are not based on a superannuation outcome, but are based on the individual's current business needs, and
- If their business is under performing at the time of retirement, it is likely the value of the property in the superannuation fund will also be adversely affected. This creates a negative outcome for the superannuation needs of the individual.

Self-Managed Superannuation – Government underwrites
Whilst there are restrictions around how self-managed superannuation operates and what can and cannot be invested in, there is an implicit underwriting of self-managed superannuation as all individuals have access to the full Government pension at the time of retirement.

Taking an extreme example: A self-managed fund can take an aggressive investment positioning (100% exposure to shares/property) and if it pays off there is a large pool of money for retirement. If the strategy does not work, there is the Age Based Pension to fall back on. This can have a high impact on Government's funding requirements for future pensions.

In a similar way self-managed superannuation funds are known for having lower diversification of asset classes and higher holdings of cash (refer to point 6).

Under-performance from this sector is also a cost to Government through the need for increased future pension payments.

For and on behalf of Prime Super.

Lachlan Baird
Chief Executive Officer