

SUBMISSION TO RETIREMENT INCOME REVIEW

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Personal Background:

This submission is a personal submission. I have an honours degree in economics, maths science degree, medical degree, and am a Fellow of the Royal Australian College of Administrators. I have a long standing interest in Government policy and economics. I have worked in health system administration and am currently a part-time medical member appointed to the Administrative Appeals Tribunal. This submission does not reflect the views of my employer.

Superannuation's effects on Australia's economy are the most important considerations in any changes to its design

1. The strength of the Australian economy as measured by income per capita and net assets per capita is the key determinant of potential sustainable retirement incomes and potential well-being of retirees.

Actual well-being will then depend on what share of those assets retirees own and how evenly it is distributed amongst them.

The pool of superannuation savings is so large that the impact of the retirement system on the economy as measured by rising income per capita and net assets per capita is the most important long run factor in determining potential well-being of people of retirement age.

This applies to all parts of the retirement incomes system. A strong economy can fund higher retiree incomes and higher retiree well-being whatever the retirement income system is.

A stronger economy can provide sustainable higher Age Pensions, higher superannuation savings, and higher voluntary savings. It can also result in a higher tax base and enable provision of higher levels of medical care and support to the aged.

And conversely a weak economy reduces the ability to do all these in a sustainable manner.

Recommendation 1. The objective of superannuation policy should be to maximise well-being of retirees commensurate with the rest of Australia.

Recommendation 2. The well-being of the least well off retirees should be regularly measured to ensure it meets basic needs for housing, living costs, and medical and aged care.

Maximising high return investment of as much of the superannuation pool as possible is optimal in the long run. This is basic maths.

2. The higher the superannuation savings rate and the higher the long run average percentage return on the savings pool the stronger the economy will be.

High savings rates and higher percentage rates of return on superannuation and other savings also increase the strength and size of the Australian economy through increased productive investment and increased net assets per capita.

In the short run this entail higher risk, but in the long run the risk is well worth the benefit.

An overseas example of high savings is Singapore where Central Provident Fund contributions are 17% of pay for employers and 20% for employees, much higher than Australia's 9½% and this high level of savings has resulted in Singapore achieving income per capita well in excess of Australia within one generation.

A stronger economy with greater net assets has greater capacity to manage future economic setbacks and challenges.

Recommendation 3. Increase compulsory savings rates whenever possible as this maximises savings and will increase the long run overall wealth of Australia.

Recommendation 4. Favour policy settings that encourage investment of superannuation savings in high return productive investments such as the sharemarket, infrastructure, etc.

The more equal the distribution of retiree income the better for Government budgets and better for overall retiree wellbeing

3. The more equal the distribution of superannuation and other assets in retirees the less the cost of the Age pension will be.

Government support for superannuation savings for people whose net assets at retirement remain below the cut-off for the Age Pension has an offsetting reduction in future Age Pension costs. Government support for savings beyond the Age Pension cut-off has no offsetting reduction in future Age Pension costs.

Retirees on high incomes get very little in extra wellbeing for extra income compared to those whose retirement income is at or near the Age Pension level.

Recommendation 5. The provision of government subsidies to superannuation via tax deductions, benefit limits etc should be biased towards lower income earners.

Recommendation 6. In the event the Government is concerned an increase in the SGC from 9½% to 12% for lower income earners impacts on their disposal income the Government should consider directly funding the increase for minimum and low wage earners itself.

Retiree risk is unavoidable and the current Australian retirement system has effective inbuilt stabilisers

4. Sustainability

The Australian system has the inbuilt stabilisers:

- Poor investment returns in superannuation encourage working longer and saving more
- Universal means tested Age Pension hedges individual risk of poor returns and encourages higher return investment
- Higher risk, higher return investment benefits the Government budget as the Government save more Age Pension expenditure on those whose investments do better than expected than it loses on those who do worse than average. This is mathematically so because the average return over the entire population and over time is higher.

Defined benefit systems have inbuilt destabilisers

- Poor economic conditions encourages early retirement rather than saving more and working longer
- Changing benefit levels or changing retirement age is very difficult politically
- Poor investment results in privately funded defined benefit systems frequently result in scheme failure
- Many generous unfunded pension schemes in countries with low birth rates will inevitably fail or need to drastically reduce benefits as demographic changes plays out

Longevity risk is unlikely to be addressed by any private sector insurance mechanism

5. Longevity risk / CIPRS

Any product that provides a lifetime guaranteed income must either invest in guaranteed investments with very low returns, or have a promoter who provides the guarantee. The cost of this guarantee is either very high if genuinely guaranteed, or moderate where the purchaser takes the risk of the promoter and the product failing.

In either case the difference between the return on equity type investments and safe interest bearing investments is so high that the products are necessarily unattractive to any financially educated investor.

Pooled products invested in higher return investments could potentially alleviate some longevity risk.

However the variance in life spans in retirement is highly variable – ie from 1 day to 40 years. There is also quite a high degree of predictability of longevity based on medical risk factors, existing medical problems, and increasingly accurate genetic testing and new medical technologies.

This means pooled products are highly subject to moral hazard and would need to be risk rated to a degree that is very unlikely to be achievable.

The current system is highly cohesive in many ways

6. Cohesion

The Australian retirement system has many elements contributing to a cohesive system of incentives encouraging desirable behaviour and being seen as fair and equitable.

The 9½% of earnings compulsory contribution is very important as it transparently meets the “contributory principle” which is important for perceived fairness. Every employee makes a compulsory contribution based on their earnings and this ensures every employee is making at least a proportional contribution to the retirement system and not “free riding” on others.

Compulsion is required otherwise low income earners would have an incentive to opt out as they would then receive the Aged Pension and much of their superannuation just lowers their Age Pension.

Means testing the Age Pension is generally accepted as fair in Australia as it is funded by taxation and the less spent on it the more Government funding there is available for other services important to retirees such as health and aged care.

Future retirement incomes cannot be guaranteed and this needs to be widely explained and implemented in an appropriate manner

The current defined contribution system has the very desirable characteristic that it explicitly does not guarantee future retirement incomes for anyone – other than the fall back means tested Age Pension.

It is highly desirable that this guarantee is not made because it can only be made if there is another group accepting the financial risk involved in making that guarantee. That group of course is the working age taxpayer.

Under defined contribution superannuation retiree income is contingent on economic circumstances in the economy, individual savings decisions, and retirement age decisions.

Just as the entire economy has to adjust to changed economic circumstances so should retirees have to make adjustments. Albeit particularly low income retirees have limited capacity to adjust and need to be protected by the Age Pension, Medicare, and aged care policies.

I believe this concept is well accepted by many levels of the community and is fair and equitable.

Tax and related matters

7. Superannuation rule improvements

The egregious double dipping of two tax free thresholds

Currently a retiree can transfer \$1.6m to a pension account where no tax is paid on the income, and a further tax free threshold outside of superannuation.

This seems to me to be an egregious and totally unnecessary case of double dipping.

Recommendation 7. There should be a pro rata loss of the income tax tax-free threshold for people with amounts between the Age Pension cut-off assets amount and \$1.6m in superannuation in the 0% tax pension phase. That is if you have \$1.6m or more in the tax free pension phase you should completely lose the ordinary income tax free threshold, and for amounts less than \$1.6m lose part of the tax free threshold outside superannuation.

Individual superannuation above \$2.6m should be taxed at the company tax rate

Recommendation 8. Tax on pension phase assets should be progressive. The assets test taper of the Age Pension is too steep. The 15% tax rate for superannuation beyond the \$1.6m transfer amount should only apply to a maximum balance of an extra amount, say, \$1m, and the remainder should be taxed at the company tax rate or be removed from the superannuation environment.

Limiting use of superannuation as a savings vehicle for bequests

Recommendation 9. Beyond age 67 all amounts above the \$1.6m transfer cap taxed at 15% should have a higher minimum withdrawal amount than for those sums within the \$1.6m tax free amount. I suggest double the minimum. This reduces the capacity to use superannuation as a vehicle to save for bequests.

Small SMSFs in pension phase for couples with less than \$1m should cost nothing to administer and regulate

The only criteria a small pension phase SMSF has to meet is for the minimum withdrawal to be made each year. As each member of the couple has one income tax free threshold the minimum withdrawal could generally be re-invested tax free outside superannuation.

Not making the minimum withdrawal is of course a 100% victimless crime and does not require policing.

This means the entire regulatory structure of the super fund, trustees, calculating minimum withdrawal rates, compulsory regular audits, etc is entirely pointless and could be dispensed with and replaced by a yearly statement of net assets and income.

I estimate 150,000n people with medical problems preventing them from working have been excluded from the disability support pension since 2012

8. Long-term Newstart Allowance recipients in their in their 50's or 60's who can't work due to medical problems and don't qualify for the disability support pension are a highly disadvantaged group.

People who have medical problems preventing them from working and who don't qualify for the disability support pension are a highly disadvantaged group who often have to spend much of their superannuation savings from the age they are too sick to work, often in their 50's, up to retirement age.

They often spend many years on Newstart Allowance too sick or impaired to work and trying to manage chronic medical problems and survive financially on very little money. Because the Newstart Allowance is not designed to be enough to live on let alone pay for medical costs of chronic disease people in this situation have little choice but to run down savings, sell assets, access superannuation early, and rely on support from other family members.

This situation has become more common since changes to impairment tables for qualification for the disability support pension were introduced from 1January 2012.

I estimate there are between 125,000 and 175,000 people who would previously qualified for the disability support pension on the basis of being unable to work 15 hours per week and scoring 20 impairment points but with the new impairment tables don't qualify for many years because they don't score the 20 impairment points.

The new tables impacts particularly severely on people who have worked in manual and unskilled jobs where at least a moderate amount of physical work is required, and have few transferable skills for other types of work, and low levels of education.

Qualification for the disability support pension requires meeting both of 2 criteria

- Scoring 20 impairment points from the Governments impairment tables; and
- Being permanently unable to work 15 hours per week in any normal job

Prior to 1 January 2012 the second of these criteria being unable to work 15 hours per week was the one that most often determined whether a person qualified for the disability support pension or not.

From 1 January 2012 legislation was passed that implemented new impairment tables that made it very much harder to score 20 impairment points particularly for heart, lung, and musculoskeletal conditions.

The new impairment tables can be downloaded from the internet at

https://www.dss.gov.au/sites/default/files/documents/05_2012/dsp_impairment_final_tables.pdf

With the new tables it was much harder for people with heart or lung conditions or musculoskeletal conditions to score the required 20 impairment points and this became the main criteria determining whether these people qualified or not, rather than whether these problems prevented them range of movement working in normal employment.

The report of the Australian National Audit Office titled Disability Support Pension Follow-on Audit, available at <https://www.anao.gov.au/work/performance-audit/disability-support-pension-follow-audit> provides the following figures regarding numbers of people on the disability support pension and the numbers of claims granted and rejected

| Year | DSP Current Recipients | Claims granted | Claims rejected |
|---------|------------------------|----------------|-----------------|
| 2009/10 | 792,581 | | |
| 2010/11 | 818,850 | 89,561 | 60,709 |
| 2011/12 | 827,460 | 63,942 | 68,993 |
| 2012/13 | 821,738 | 54,455 | 71,891 |
| 2013/14 | 830,454 | 57,219 | 83,714 |
| 2014/15 | 814,391 | 41,281 | 71,201 |
| 2015/16 | 782,891 | 26,835 | 78,816 |
| 2016/17 | 758,911 | 27,435 | 69,510 |
| 2017/18 | 756,960 | 31,000 | 73,000 |

The figures show disability support pension claims granted was as high as 89,561 in 2010/11, the last year the previous impairment tables were used, and fell to a low of 26,835 in 2015/16.

If claims had continued to be granted at a rate of 75,000 per year for the years 2011/12 to 2017/18 there would have been in round figures another 225,000 people who would have been granted the disability support pension in this period.

If the numbers of people on disability support pension had grown at 1.6% per year based on population growth plus a little more to account for the rising of the age pension age to 65½ as of 1 July 2017.

Six years of growth at 1.6% from the 827,460 recipients in 2011/12 would have added $827,460 \times 9.6\% = 79,436$ extra disability support pension recipients. Instead the number dropped by 70,500.

This gives an estimate of 150,000 people who would have previously qualified for the disability support pension based on inability to work 15 hours per week and 20 points under the old tables, but with the new impairment tables no longer qualified.

There are some other factors which would be expected to have increased the number of older people on the disability support pension over this time including:

- The raising of the pension age for all people to 65½ as of 1 July 2017
- The phasing in of raising pension age for women from 60 to 65 prior to this

- Changes to Workers Compensation rules exiting many people from Workcover payments in all states

Exactly how many of these 150,000 people are in their 50's and 60's cannot be estimated from the information available to me but I consider it is likely to be about 120,000 of whom perhaps 100,000 become long term Newstart Allowance recipients and virtually all would need to begin superannuation pensions well in advance of the Age Pension age, or seek early access to superannuation to survive.

Some specific tables and qualification for the disability support pension

Table 4 – Spinal Function has the following criteria for 10 and 20 impairment points:

| | |
|----|--|
| 10 | <p><i>There is a moderate functional impact on activities involving spinal function.</i></p> <p>(1) The person is able to sit in or drive a car for at least 30 minutes, and at least one of the following applies:</p> <ul style="list-style-type: none"> (a) the person is unable to sustain overhead activities (e.g. accessing items over head height); or (b) the person has difficulty moving their head to look in all directions (e.g. turning their head to look over their shoulder); or (c) the person is unable to bend forward to pick up a light object placed at knee height; or (d) the person needs assistance to get up out of a chair (if not independently mobile in a wheelchair). |
| 20 | <p><i>There is a severe functional impact on activities involving spinal function.</i></p> <p>(1) The person is unable to:</p> <ul style="list-style-type: none"> (a) perform any overhead activities; or (b) turn their head, or bend their neck, without moving their trunk; or (c) bend forward to pick up a light object from a desk or table; or (d) remain seated for at least 10 minutes. |

Low back pain and neck pain and spine problems are very common as people get older due to degenerative arthritis.

Most manual and unskilled workers with low back pain are obviously unable to work when they meet the 10 point criteria of being unable to pick up a light object at knee height or needing help to get out of a chair.

Yet they may need to wait many years until their back condition gets sufficiently worse that they meet the more stringent 20 point criteria.

Table 3 – Lower Limb Function has the following criteria for 10 and 20 impairment points:

| | |
|----|--|
| 10 | <p><i>There is a moderate functional impact on activities using lower limbs.</i></p> <p>(1) At least one of the following applies:</p> <ul style="list-style-type: none"> (a) the person is unable to walk far outside their home and needs to drive or get other transport to local shops or community facilities; or (b) the person is unable to use stairs or steps without assistance; or (c) the person is unable to stand for more than 5 minutes; and <p>(2) The person is able to use public transport or a motor vehicle and walk around in a shopping centre or supermarket.</p> <p>(3) This impairment rating level includes a person who can:</p> <ul style="list-style-type: none"> (a) move around independently using a wheelchair and can independently transfer to and from a wheelchair (e.g. can use a wheelchair accessible toilet independently); or (b) move around independently using walking aids (e.g. quad stick, crutches or walking frame). <p><i>Note:</i> The person may require additional time and effort to move around a workplace, may need to use disabled access entries, lifts and toilets, and may not be able to access some areas of a workplace or training facility.</p> |
|----|--|

| | |
|----|--|
| 20 | <p><i>There is a severe functional impact on activities using lower limbs.</i></p> <p>(1) The person:</p> <p style="margin-left: 20px;">(a) is unable to do any of the following:</p> <p style="margin-left: 40px;">(i) walk around a shopping centre or supermarket without assistance;</p> <p style="margin-left: 40px;">(ii) walk from the carpark into a shopping centre or supermarket without assistance;</p> <p style="margin-left: 40px;">(iii) stand up from a sitting position without assistance; and</p> <p style="margin-left: 20px;">(b) requires assistance to use public transport.</p> <p>(2) This impairment rating level includes a person who requires assistance to:</p> <p style="margin-left: 20px;">(a) move around in, or transfer to and from a wheelchair (e.g. the person needs personal care assistance to use a toilet); or</p> <p style="margin-left: 20px;">(b) move around using walking aids (e.g. a quad stick, crutches or walking frame), that is, the person needs assistance from another person to walk on some surfaces and could not move independently around a workplace or training facility, even when using a walking aid.</p> |
|----|--|

Knee and hip osteoarthritis and other lower limb conditions are very common.

For most manual workers it is impossible to work when they meet the 10 impairment points criteria such as being unable to walk up steps, can't walk far, can't stand for 5 minutes, or use a wheelchair for mobility.

Again they need to wait many years till they meet the 20 point criteria of needing help to walk around a shopping centre and help to stand from a sitting position or being in a wheelchair and needing help to go to the toilet.

Many people with heart problems and / or lung conditions such as chronic obstructive airways disease get significant shortness of breath on exertion and have their impairment rated under this table.

Again if a person is suffering from shortness of breath or fatigue and meets the 10 impairment points criteria of being unable to walk far outside the home or have difficulty with tasks such as changing sheets on a bed or sweeping a path they are clearly unfit for any type of manual work.

Table 1 - Functions requiring Physical Exertion and Stamina has the following criteria for 10 and 20 impairment points:

| | |
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| 10 | <p><i>There is a moderate functional impact on activities requiring physical exertion or stamina.</i></p> <p>(1) The person:</p> <p>(a) experiences frequent symptoms (e.g. shortness of breath, fatigue, cardiac pain) when performing day to day activities around the home and community and, due to these symptoms, the person:</p> <p>(i) is unable to walk (or mobilise in a wheelchair) far outside the home and needs to drive or get other transport to local shops or community facilities; or</p> <p>(ii) has difficulty performing day to day household activities (e.g. changing the sheets on a bed or sweeping paths); and</p> <p>(b) is able to:</p> <p>(i) use public transport and walk (or mobilise in a wheelchair) around a shopping centre or supermarket; and</p> <p>(ii) perform work-related tasks of a clerical, sedentary or stationary nature (that is, tasks not requiring a high level of physical exertion).</p> |
| 20 | <p><i>There is a severe functional impact on activities requiring physical exertion or stamina.</i></p> <p>(1) The person:</p> <p>(a) usually experiences symptoms (e.g. shortness of breath, fatigue, cardiac pain) when performing light physical activities and, due to these symptoms, the person is unable to:</p> <p>(i) walk (or mobilise in a wheelchair) around a shopping centre or supermarket without assistance; or</p> <p>(ii) walk (or mobilise in a wheelchair) from the carpark into a shopping centre or supermarket without assistance; or</p> <p>(iii) use public transport without assistance; or</p> <p>(iv) perform light day to day household activities (e.g. folding and putting away laundry or light gardening); and</p> <p>(b) has or is likely to have difficulty sustaining work-related tasks of a clerical, sedentary or stationary nature for a continuous shift of at least 3 hours.</p> |