

Director
Superannuation Insurance and Governance Unit
Member Outcomes and Governance Branch
Retirement, Advice and Investment Division
The Treasury
Langton Crescent
PARKES ACT 2600

28 February 2023

By email: superannuationobjective@treasury.gov.au

Dear Director,

Superannuation objective consultation

I refer to Treasury Consultation Paper (dated 20 February 2023) "*Legislating the objective of superannuation*" (the "Paper"), and make the following submissions.

I am a Chartered Tax Adviser and Chartered Accountant who has practised in taxation law for over 40 years, which included 27 years as a Tax Partner at KPMG.

In summary, I submit that:

1. The proposed definition is simplistic, ambiguous and not fit for purpose.
2. An acceptable alternative may be to legislate detailed policy objectives of the superannuation system.

Question 1.: What do you see as the practical benefits or risks associated with legislating an objective of Australia's superannuation system?

Retirement income and superannuation have been significant themes for the Commonwealth Government since Federation. The three pillars that underpin Australia's retirement income system are:

1. the social security Age Pension,
2. compulsory superannuation contributions made under the superannuation guarantee regime, and
3. additional private savings, often made through additional voluntary superannuation contributions.

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Employer-based superannuation has been a feature of employment in some Australian industries from the mid-1800s, notably salaried employees in the public service and the financial sector. However, it was not until 1992 that a universal mandatory contribution scheme for retirement savings was introduced through the introduction of the superannuation guarantee.

Section 62 of the Superannuation Industry (Supervision) Act 1993 imposes the “Sole Purpose” test on the trustees of each superfund. Superannuation has survived and grown over 150 years without a legislated purpose. Why is a legislated purpose needed now?

Before defining a purpose for the superannuation system, one must define or describe the superannuation system itself. Broadly, the current Australian superannuation system is a mandatory savings scheme to help each Australian save money for him or her to access in retirement.

At its simplest, the superannuation system broadly involves:

1. establishing a lifetime savings vehicle, i.e., superannuation fund,
2. a member’s employer(s) and/or member making contributions to the superannuation fund,
3. the superannuation fund investing the funds it receives, and
4. the superannuation fund ultimately making payments to a member during his or her retirement.

It is therefore self-evident that the purpose of the superannuation system is about saving money for a person’s retirement.

Australian superannuation legislation is already extremely complex that contains significant compliance requirements (audit, reporting, ensuring no prohibited investments are made).

The 2009 Henry Review, chaired by Dr Ken Henry, stated that:

“Superannuation’s sole purpose is to provide a lifetime savings vehicle, and savings should be invested to maximise returns without being subject to competing policies that would require, for example, specific asset allocation”.

The 2014 Financial Systems Inquiry (“2014FSI”), chaired by David Murray AO observed that:

“Evidence suggests that the major worry among retirees and pre-retirees is exhausting their assets in retirement. An individual with an account-based pension can reduce the risk of outliving their wealth by living more frugally in retirement and drawing down benefits at the minimum allowable rates. This is what the majority of retirees with account-based pensions do, which reduces their standard of living. The



difficulty in managing this risk is also exacerbated by the uncertainty as to how long a retiree will live.”¹

The 2014 FSI noted:

“The potential gains to members, the economy and taxpayers from a more efficient retirement phase are significant and warrant intervention. Higher income in retirement and a wider range of retirement income products would better meet the varied needs of retirees. The economy will benefit if the growing proportion of people in retirement can sustain their level of consumption.

Combinations of products enable retirees to balance the three desired features of retirement income products: high income, risk management features and flexibility. Pooling of longevity risk would give retirees greater confidence to consume. Alternatively, by improving the superannuation system’s efficiency in providing retirement income, people may be able to save less during their working lives to reach a given level of retirement income.”²

Having identified the absence of a comprehensive income product for retirement (CIPR) and the lack of confidence in the adequacy of retirees’ account balance at the end of their working life, it is not surprising that the 2014 FSI Recommendation 9 was that Government should seek broad agreement on the following primary objective for the superannuation:

“to provide income in retirement to substitute or supplement the Age Pension.”

The drafting of any legislated purpose must, inter alia:

- a. be concise and simple, and
- b. use terms that are absolute in their meaning, i.e., terms should be unambiguous (e.g., devoid of subjective or vague language that may be open to interpretation).

The 2014 FSI definition clearly satisfies these tests and was adopted in Section 5 (1) of the *Superannuation (Objective) Bill 2016*, which lapsed on 1 July 2019.

The 2020 Retirement Income Review (“2020 RIR”), chaired by Mr Mike Callaghan AM PSM, suggested the objective for the retirement income system be expanded around the following broad goal:

“To deliver adequate standards of living in retirement in an equitable, sustainable and cohesive way.”

¹ Footnotes omitted.

² Page2 120, 1.



However, the 2020 RIR report then had to explain what the Committee meant by the words “in an equitable, sustainable and cohesive way”. Hence, such definition clearly fails the tests of simplicity and unambiguity.

Accordingly, the superannuation purpose test that I favour is the 2009 Henry Review definition.

However, it is submitted that merely legislating a superannuation purpose will not render the superannuation system more efficient, being what is critical to help Australia meet the economic and fiscal challenges of an ageing population.

Question Two: Does the proposed objective meet your understanding of the objective of the superannuation system in Australia?

The proposed objective states:

*The objective of superannuation is to **preserve savings** to **deliver income** for a **dignified** retirement, alongside **government support**, in an **equitable and sustainable** way.*

No, the proposed definition does not meet my understanding of the objective of the Australian superannuation system because:

- a. it conflates purpose with Government policy objectives, and
- b. fails the abovementioned tests of simplicity and unambiguity.

My comments on the proposed definition include:

1. The words “*preserve savings*” is a restrictive policy that ignores the fundamental superannuation purpose of creating and growing savings. Hence, it should be deleted.
2. The words “*deliver income*” are satisfactory.
3. The adjective “*dignified*” is otiose and unnecessarily introduces an element of subjectivity that will mean different things to different people.
4. The phrase “*alongside Government support*” qualifies the words “income for ... retirement” and refers to something that is extrinsic to (not within) the superannuation system (e.g., age pension and other governmental support). These words should be deleted.
5. The words “*in an equitable and sustainable way*” reflect policy objectives or principles that are capable of very broad interpretation and are therefore ambiguous. Each of these words have very different meanings depending upon the context in which they are used. Academic public finance textbooks are replete with discussions about the various nuances of what these concepts entail in the limited context of fiscal policy.



Even the explanation of these words in the Paper includes aspects that are not obvious from their ordinary meanings.

- a. The word “*equitable*” is ambiguous, though intended to refer to “delivering similar outcomes to people in similar situations and targets support to those most in need.”.
- b. The word “sustainable” is equally ambiguous, though intended to refer to the system being “robust to demographic, economic and social change, and should be cost-effective for taxpayers in achieving retirement outcomes. ... Beyond a certain level of income, additional Government support through tax concessions is not necessary or appropriate.”

The idea of removing tax concessions for retirement income above certain income levels [e.g., where a member’s superfund balance exceeds (say) \$3M³] totally contradicts the intended meaning of “equitable” as it will create a further separate class of superfund members that will be treated differently to other members. Moreover, it penalises those members who:

- a. Made contributions within statutorily permitted limits when made, and
- b. had superfund trustees that:
 - i. complied with statutory investment rules,
 - ii. took a cautious risk management view of how much money might be required during a member’s remaining years after exiting the workforce (perhaps 30+ years, instead of a lower actuarial life expectancy) to maintain the quality of life of the member and his or her dependants, and meet the health and care costs of old age, and
 - iii. invested more wisely than other trustees receiving similar levels of contributions.

It also flies in the face of the equitable principle of grandfathering⁴. Superannuation is a long-term series of investments made each year on the understanding that any law changes will not adversely affect a member’s superannuation entitlements at the time of the law change.

³ Part of such balances might be explained by permitted higher-level contributions made before maximum reasonable benefits (“MRBs”) were legislated to apply from the 1996 income year, which balances have been effectively grandfathered since statutory MRBs were legislated, apart from the

⁴ Grandfathering involves the preservation of the treatment of pre-existing arrangements when rules are changed. For example, if a person has been able to accumulate a superannuation balance that exceeds \$3m within the superannuation laws that operated during the accumulation period, then grandfathering would require that balance to continue to benefit from the rules that existed before any law change affecting balances over \$3m.



It follows that the words “*in an equitable and sustainable way*” are too broad in potential meaning in superannuation and revenue statutes where precision of meaning is required. Accordingly, they should also be deleted.

Accordingly, this reduces the proposed purpose definition to:

*“The objective of superannuation is to **deliver income** for retirement.”*

However, such definition is too general to be meaningful against which to measure proposed legislative changes to superannuation laws.

Question Three: Is the proposed approach to enshrining the objective in legislation appropriate? Are there any alternative ways the objective could be enshrined?

What may be more valuable than a single-sentence-legislated purpose is to have a clear statement of the Government’s agreed policy objectives or principles that the legislative framework of superannuation law must meet and against which proposed amendments may be measured.

Such objectives or principles may include:

- A. The system should confirm the sacrosanct principle that a member’s balance in a superfund belongs only to that member.
- B. A superfund should be managed for the sole benefit of its members, which means the investment focus should be on maximising risk-adjusted returns, net of fees and taxes, over the lifetime of a member.
- C. The system should deliver similar outcomes to people in similar situations⁵.
- D. The system should facilitate people to reasonably maintain their standard of living in retirement.
- E. The system should be cost-effective for taxpayers in achieving adequate outcomes.
- F. The system should not be unnecessarily complex for consumers or trustees: complexity is less appropriate for a compulsory system, as it tends to add to costs.
- G. The system should provide an equitable distribution of concessions for people with different incomes, consistent with the degree of progressivity in the personal income tax rates scale⁶.

⁵ This raises the issue as to why Federal politicians, political staffers and public servants are entitled to a superannuation contribution of a standard rate of 15.4% of salary compared to 11.5% compulsory superannuation for the rest of Australia’s working population.

⁶ One example might be an updated and simplified version of the contributions tax changes proposed in the Henry Review, where everyone gets the same tax advantage out of a dollar going into super, with a standard concession of (say) 15 cents in the dollar for both high- and low-income earners.



- H. The system should be sufficiently flexible to enable a member to transfer his or her balance from one fund to another fund.
- I. Superannuation compliance costs (funds and members) should be minimised.
- J. Superannuation fund trustees should be free to make investment decisions that maximises returns for members. This means:
 - a. government should not impose compulsory investment requirements (e.g., low-yielding social housing) as was the case before 1984 when the “30/20” rule required compulsory investment in Government Bonds, and
 - b. the trustee should not incur expenses that are not related to the derivation of income, e.g., donations to charities or political parties.
- K. The board of a corporate trustee of a public offer superannuation fund should have a majority of independent directors, including an independent chair.
- L. Given the compulsory nature of SG contributions, the system needs prudential oversight and should provide good outcomes in both the accumulation and retirement phases for disengaged fund members.
- M. Changes in superannuation laws should be consistent with these principles, but also not:
 - a. add complexity or costs to the superannuation system,
 - b. operate retro-actively, or
 - c. reduce a taxpayer’s after-tax entitlements as at time of law change (grandfathering).

This is not intended to be a complete list.

Question Four: What are the practical costs and benefits of any alternative accountability mechanisms to the one proposed?

I suspect the cost of the alternative would be the same as the proposed mechanism.

The practical cost of a legislated purpose that creates uncertainty about a person’s lifetime savings and the risk of outliving his or her wealth may cause him or her to make investments in other areas that lack the integrity of the existing system.

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Should you have any queries, please contact me.

Yours sincerely



Edgar Baltins