Superannuation & retirement incomes

ACOSS Policy Paper

21st September 2020

ACOSS has a long history of policy and advocacy regarding Australia's retirement income system. The purpose of ACOSS advocacy is to ensure that retirement income policy will deliver an adequate standard of living across a person's life course, particularly for people on lower incomes and from more disadvantaged circumstances. ACOSS policy is informed by the interests of people on low incomes and from more disadvantaged circumstances and consultation and engagement with its members and available evidence.

In 2019, the Federal Government announced its Retirement Income Review. The ACOSS Submission to the Review was made in February 2020 and can be found here.

Since February 2020, Australia has entered a pandemic and is now in the deepest recession since the 1930s. In response, the Federal Government has made some major temporary changes to income support for people of working age, including the $275pw Coronavirus Supplement which almost doubles the rate of Jobseeker Payment for people who are unemployed. The government proposes to reduce the Supplement to $125pw from 28 September 2020, and it is scheduled to end on 31 December.

There is also an emerging debate over whether legislated increases to the Superannuation Guarantee (SG) from 9.5% of wages to 12% should proceed.

This Policy Paper sets out ACOSS's key policy positions on superannuation and retirement incomes. It includes the recommendations contained in the ACOSS Submission to the Government's Retirement Incomes Review in February 2020 and reflects recent developments since that time.

Key points from ACOSS' submission to the Retirement Incomes Review (February 2020)

Improvements in public income support are essential and urgent for those on the lowest incomes

This includes a permanent, adequate increase in Jobseeker and related payments and in Commonwealth Rent Assistance, both of which would have a greater impact on the lives of older people on the lowest incomes than any other reform. ACOSSs policy is outlined in our Next Steps in Income Support policy brief.

Compulsory super should continue as a universal system

ACOSS does not support 'carve outs' for people with low incomes, or making any contributions at 10% of wages or below voluntary.

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The next increase in the Superannuation Guarantee (SG) from 9.5% to 10% of wages in July 2021 should not be opposed

Collective pay agreements may have already taken this increase into account (discounting pay increases) when setting wages. On its own, its impact on wages is likely to be minimal.

For increases beyond 10%, the evidence on whether it's worthwhile for people with low and modest incomes to save more than this for retirement needs to be assessed first

The evidence indicates that increases in compulsory employer super contributions mainly come from lower wage increases. This is supported by research undertaken by the Grattan Institute (see evidence below), and is the view of the Reserve Bank and most economists.

The issue here is not whether wage increases are high or low, but whether they are lower *than they would have been* without increases in compulsory super contributions.

Along with the Age Pension, the main purpose of superannuation is to enable workers to avoid a major drop in their living standards after they retire. To the extent that SG contributions are in effect *compulsory saving* (rather than *extra payments from employers*), the SG should be set at a level which – together with the pension – enables people on low and modest incomes to come close to maintaining in retirement the living standard they had throughout their working lives.

Making people on low and modest incomes save when they are under financial pressure (e.g. with children, mortgages, when they are in and out of employment, or after a marriage separation) to achieve a higher living standard after retirement than the one they have now would not make sense.

Research indicates that with a super guarantee of 9.5%, many people with low lifetime incomes will have higher living standards after retirement than they had, on average, through working life (see evidence below). This is due to a combination of the Age Pension, home ownership, and the absence of dependent children after most people retire.

So to work out the 'right' level for the superannuation guarantee, we should compare incomes and living standards in working life and after retirement ('income replacement rates'), including any new evidence from the Retirement Income Review.

''Any increase in compulsory retirement saving above 10% of wages should be based on a careful assessment of the needs of low and middle-income workers before and after retirement, which we hope the Review will undertake.''
(ACOSS submission to Retirement Income Review, February 2020)

ACOSS view on the existing $450 threshold is the same as that on the SG increase. ACOSS proposes that, before it is removed an assessment is made to determine whether this will benefit people on the lowest incomes, taking account of wages, tax breaks and superannuation fees.

In any event, tax breaks for superannuation contributions should be restructured to make them fair before the SG increases above 10%.

Another reason to question the benefits of higher compulsory contributions for people on low and modest incomes is that they receive little or no support from $40 billion a year in superannuation tax breaks.

Currently, a worker earning $20,000 (more likely to be a woman) receives no tax support for employer contributions while another worker on $200,000 (more likely to be a man) saves 32 cents in tax per dollar contributed. This is due to the way their marginal tax rates interact with the inequitable 15% 'flat tax' on employer contributions.

ACOSS proposes that this flat-rate superannuation tax be replaced with a rebate that provides the same or greater support for each dollar of contributions for people with low incomes as that provided to middle and high income-earners. This would be paid for by reducing tax breaks for people with high incomes

''Further, the superannuation guarantee should not rise above this level until tax breaks for super contributions are reformed to make them fair for people with low and modest incomes.'' (ACOSS submission to Retirement Income Review, February 2020)

Separately from the SG, superannuation fund earnings after retirement (in ''pension phase'') should be taxed at the same rate as in the ''accumulation'' phase (15%), minus a tax credit for people on the lowest incomes, instead of completely tax-free as at present.

This (and a tightening of the income definition for the Medicare Levy) should be linked to improved public funding and service guarantees for aged care. [1]

Developments since February 2020 regarding retirement incomes

The Retirement Incomes Review has become politicised: this is a problem.

There are differing views on whether the SG should increase. ACOSS is concerned that the deeply polarised debate on the SG in advance of the release of the Retirement Income Review makes it less likely that its findings will inform good policy development, especially if the Report is not released in advance of government decisions on superannuation.

Increases in the SG beyond 10% still need to be justified, and reform of inequitable super tax breaks must occur.

The SG was a structural reform, and any increases should be justified on their merits. Reform of the tax treatment of superannuation is long overdue.

[1] We do not propose to tax superannuation benefits paid to retirees, just the investment income of the fund. This would be phased in over 3 years, raising $2.5B in the first year and much more in later years. The Medicare Levy change would raise $1.2 billion in the first year.

In ACOSS's view, whether or not the SG is increased beyond 10% is an important issue for the future, but not the most pressing issue right now.
The next increase in the SG beyond 10% (to 10.5%) is not due until July 2022. The priorities now must be protecting health and recovering jobs and incomes.

The Coronavirus Supplement should not be reduced until Jobseeker Payment and related Allowances are increased permanently to cover essential living costs.
That should include a permanent, adequate increase in 'Allowance' payment rates together with supplements to assist with the costs of disability and caring for children alone (single parents).

Many older workers are on the Jobseeker Payment, which is $185pw less than the Age Pension because they are unable to find paid work and face age discrimination or have significant disability. There is no good reason for this gap in income support between people of different ages with the same financial needs.

Maximum rates of Rent Assistance for people with low incomes renting privately should be increased by 50% so that they can afford to live in places such as our largest cities where rents have risen well above the maximum rent thresholds for that payment.
An increase in Rent Assistance is the single most effective way to lift the living standards of older people in greatest hardship.

Evidence

This section summarises the available evidence in relation to:

- Income replacement after retirement with a 9.5% Superannuation Guarantee (SG);
- Whether compulsory employer contributions come out of wages; and
- Inequities in superannuation tax concessions.

1. Many people on low lifetime incomes are likely to reach a higher living standard after retirement than the one they had through working life

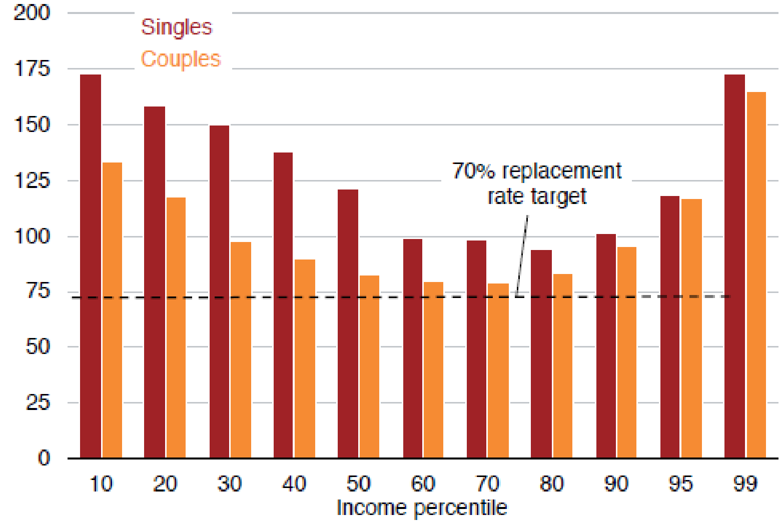
Modelling by the Grattan Institute indicates that, even at the existing 9.5% contribution rate, many people on low incomes reach a higher living standard in retirement than they do during their working life. Grattan set a benchmark of 70% of previous income to take account of the lower costs of children and housing post-retirement (graph below).
This is similar to the goal set by the previous Labor Government when it legislated to increase the superannuation guarantee from 9% to 12%:
''We measure adequacy through a simple test: what percentage of your income can you generate in your post-working life? This is what is known as the replacement

rate. Something in the order of 65% or, even better, 70% of average earnings prior to retirement, I believe, constitutes the winning tape for adequate retirement.''

Employment Minister Shorten in his second reading speech on the SG Bill in the House of Representatives in 2011 (which lifted the rate from 9-12%)

ACOSS called for the Retirement Incomes Review to undertake its own modelling to take those factors directly into account in determining an appropriate compulsory saving rate.

Disposable income for households 65-84 years of age in 2015, as a proportion of that for households 45-54 years in 1995 (in 2015 dollars)

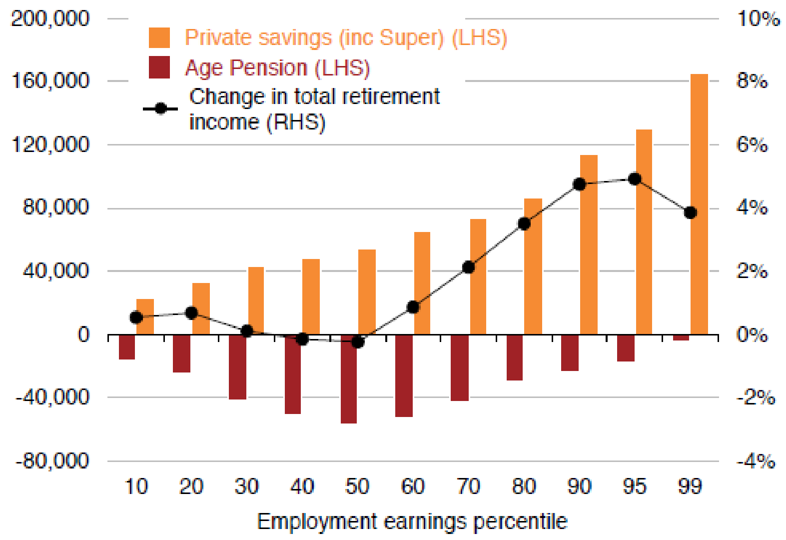


Source: Grattan Institute (2019) Money in retirement.

The above modelling is for people retiring now. When the super guarantee matures in about 30 years, income replacement rates will be higher.

If the superannuation guarantee is increased to 12%, a substantial portion of the increases in superannuation would be clawed back from people on low incomes after retirement (appropriately) through the Age Pension income and assets tests.

Change in retirement income from an increase in the superannuation guarantee from 9.5% to 12% in 2015-16 dollars (indexed to CPI)



Grattan Institute (2019) Money in retirement

2. Workers mostly pay for compulsory employer contributions

The conventional view, including from those who designed the SG and pressed to lift it from 9% to 12% of wages, is that in the long run, employees pay for most employer contributions via lower wage increases.

This was the accepted view within government when legislation was tabled to introduce the SG in 1992 and to increase it in 2011:

'The increased self-provision for retirement will permit a higher standard of living in retirement than if we continued to rely on the age pension alone,'

Treasurer Dawkins, First Reading Speech, Superannuation Guarantee (Administration) Bill 1992.

'Super's core objectives are implemented by: compelling people to save for the long term, by deferring access to a portion of current-day wages, in order to enjoy a better standard of living in retirement'

Superannuation Charter Group report to Treasurer Bowen (2011), p23

'Over the period when the superannuation guarantee charge grew from three to nine percent of employer contributions, unit labour costs fell. This meant that the cost of superannuation was rarely borne by employers. It was absorbed into the overall wage cost. Had employers not paid nine percentage points of wages as superannuation contributions to employee super accounts they would have to have paid it in cash as wages.

As former Prime Minister Keating said in 2007, 'When you hear conservatives these days speak of superannuation as a tax on employers they are either ill-informed or they are lying. The fall in unit labour costs and the upward shift in the profit share during the period of the superannuation guarantee charge is simply a matter of statistical record. It is not a matter of argument.'

Employment Minister Shorten in his second reading speech on the SG Bill in the House of Representatives in 2011

The Henry Report on tax and transfer reform had taken this view in 2009, and argued against an increase in the super guarantee above 9% on the grounds than enforced saving above that level was not warranted.

Recently, the conventional view has been contested:

Jim Stanford from the Centre for Future Work rightly argues that this view has not been tested empirically in Australia. He cites international studies that found that around 70% of the cost of employer Payroll taxes is paid by employees.

In his own research on employer contributions in Australia, he finds no correlation between higher superannuation contributions and lower overall wage rises in Australia since the SG was introduced in 1992. However, due to data limitations this research may not have taken sufficient account of the many other factors impacting on pay increases, and the diversity of those impacts, to reach a firm conclusion.

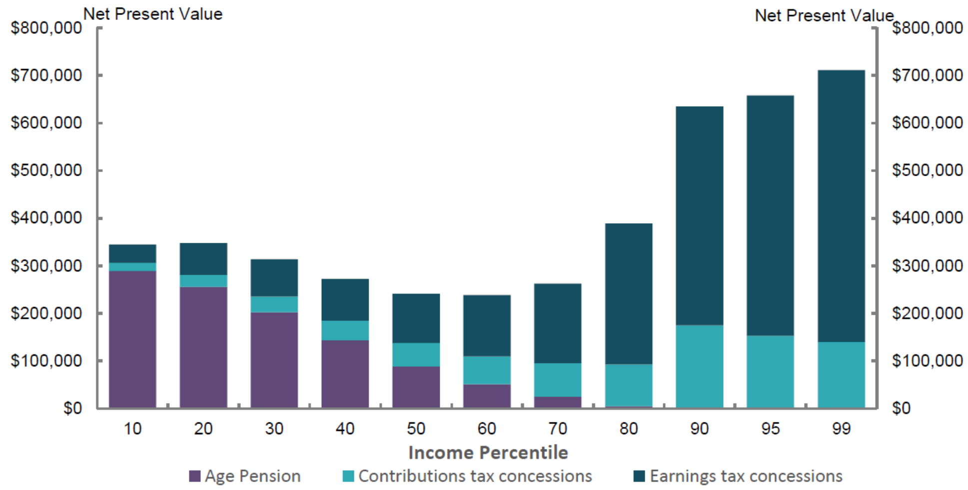
The Grattan Institute uses data from a large number of enterprise agreements over around 30 years to assess the impact of the super guarantee on wages. It finds that, after controlling for other factors, around 80% of employer contributions were paid for through lower wage rises. While only 30% of workers are covered by these agreements, Grattan argues that they represent outcomes for workers in a

relatively strong bargaining position. The [Reserve Bank](#) recently supported this conclusion.
Some argue that workers are unlikely to receive substantial pay rises in any event under the present depressed economic and labour market conditions. At the same time, under these conditions the bargaining power of employees is weaker and it's possible that employers under financial pressure would cut paid working hours.[2]

3. Tax concessions for superannuation are costly and inequitable

Tax concessions for superannuation – which now cost about the same as the Age Pension (around $40 billion a year) - mainly go to people with higher incomes.

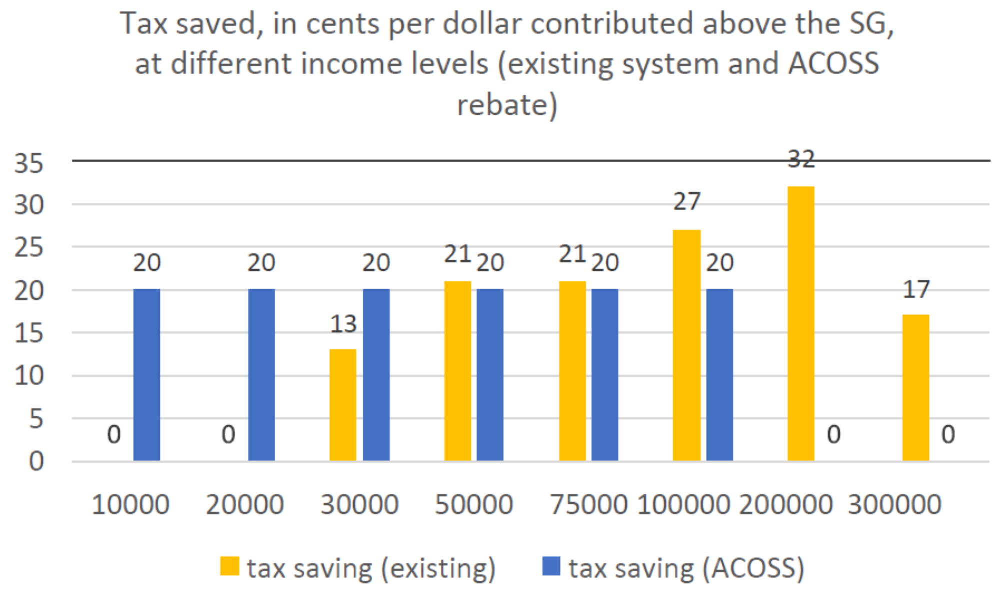
Figure 4: Lifetime government support provided through the retirement income system[9]



Source: Retirement Income Review Discussion Paper (2020)

Employer super contributions are currently taxed at a flat rate of 15% (with a 15% surcharge for people with incomes above $300,000). That means low income earners receive no benefit from these tax breaks (despite the Low Income Superannuation Tax Offset) and many high income earners save 32 cents in tax per dollar contributed (compared with the tax rate that would otherwise apply to their wages) – see graph below

[2] In any event, most of the legislated increase to 12% is well into the future (up to 2025).



Note: Marginal tax rate of additional employer contributions above the superannuation guarantee. The existing 15% tax is offset by a rebate for those below the tax-free threshold, so that the tax concession in those cases is effectively zero.
The proposed rebate is more generous for SG contributions for middle income earners than the present 15% tax rate, so most middle income-earners would be financially better off.

So in addition to foregoing wage increases for superannuation, people with low incomes receive little or no benefit from the tax breaks. The highest benefits per dollar saved go to people earning $90,000 to $300,000.

Reform of super contributions tax to make it fair (so everyone receives around the same tax benefit per dollar contributed, and tax concessions are capped at lower contribution levels) has been widely supported in the past, including by the ACTU, Industry Super Australia and the Financial Services Council.

We propose a revenue-neutral reform to replace all tax breaks for contributions with a simple rebate off people's marginal tax rates. The tax saving *per dollar contributed above the super guarantee* from this system is shown in the graph above.

We argue for tax breaks on contributions to be capped at a lower level than the present $25,000 a year so that average wage earners are not subsidising ('luxury') retirement living standards well above those which they themselves have now. This would pay for increased tax support for superannuation saving by people on the lowest incomes.