CHANGING THE WAY we spend our youth

FOR PEOPLE UNDER 40, RETIREMENT IS USUALLY FAR FROM THEIR THOUGHTS. SUPERANNUATION EXPERT ROSS CLARE LOOKS AT SOME NEW PROPOSALS AIMED AT ENCOURAGING PEOPLE TO START SAVING FOR THEIR RETIREMENT BEFORE THEY GET TO 40.

GETTING the Australian superannuation system right is a task that has been consuming much time of the parliament, the government and the superannuation sector itself.

As far as parliament is concerned, for over a decade there was the Senate Select Committee on Superannuation (and its variously named predecessors). Following the demise of that committee, the baton has been passed more or less to the House of Representatives Economics Committee, with the Corporations and Financial Services Committee also taking an interest in superannuation.

In May last year the House Economics Committee commenced an inquiry into improving the superannuation savings of people aged under 40. Just over a year later the committee produced its 159-page report, after receiving submissions from various organisations and individuals and conducting hearings around the country.

The committee found that reforming superannuation is not an easy task. Chaired by Bruce Baird (Member for Cook, NSW), the committee contained a number of up and coming members of parliament. Some of them, such as Malcolm Turnbull and Andrew Robb, had to resign from the committee in February 2006, prior to the inquiry being completed, due to their promotion in government ranks.

The committee also had to contend with the release in the May 2006 budget of the government's plan to simplify and streamline superannuation, which Treasurer Peter Costello has claimed (with some justification) to be the

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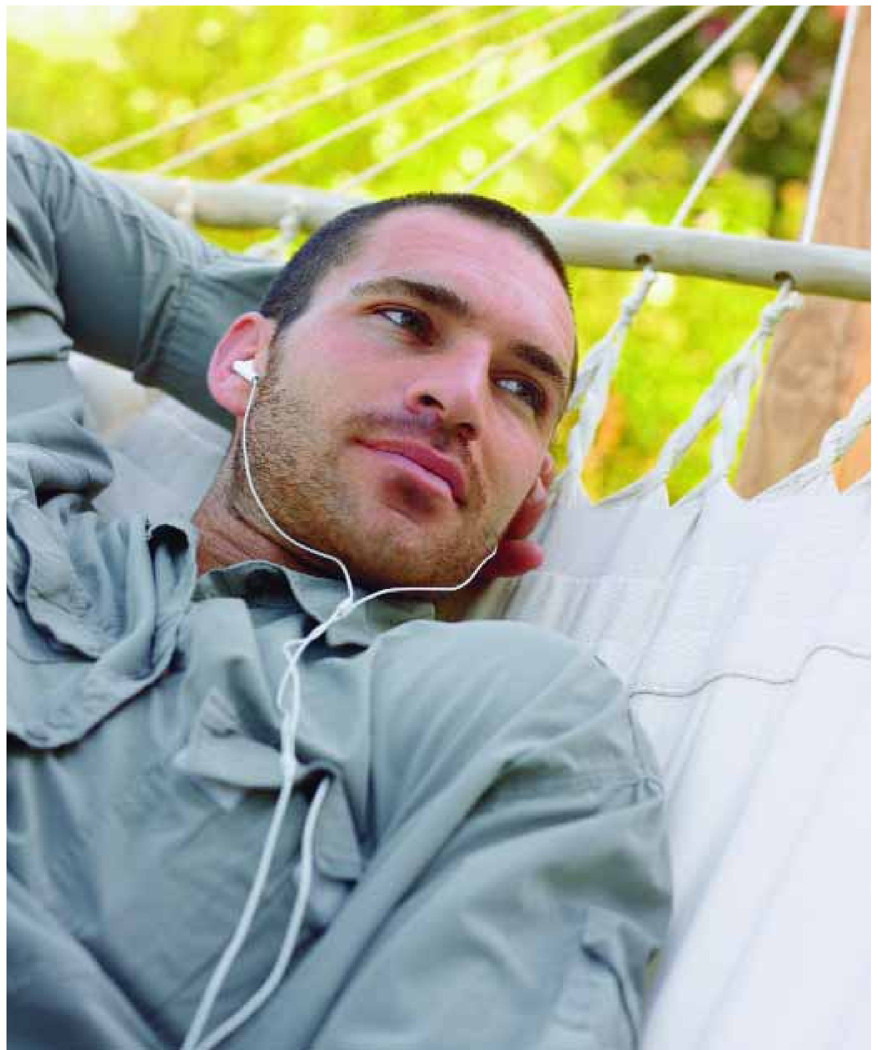

most significant initiative in regard to superannuation in the past 20 years (or perhaps ever, given not much happened in the first 80 years of superannuation in Australia). Some, however, might contend that the introduction of compulsory superannuation in 1992, and the subsequent establishment of regulatory arrangements on top of the fairly minimal tax and trust law controls that previously applied, is also a contender for the title.

Regardless of whether the government's recent proposals are the most substantive ever, a number of these proposals clearly cut across the considerations of the committee, or at the very least required substantial rethinking by the committee late in its process of deliberations.

On top of all of this was the challenge of putting together recommendations which appropriately focused on assisting those aged under 40, while at the same time avoiding any inappropriate discrimination based on age. Quite a few (just about all?) issues relevant to those aged under 40 are relevant to the population as a whole, and suggesting a solution just for the under 40s would not be very equitable.

In my last article for *About the House* dealing with the committee's inquiry (Issue 25, November 2005), I picked up some helpful advice for the under 40s from the lyrics of the song *Father and son* by Cat Stevens, namely being young is their fault but it is something they will overcome. Seeking further musical inspiration I am now picking up on the lyrics of a more contemporary pop song, *Forever young* by the aptly named Youth Group, which implies that many of that cohort want to be forever young, asking the question do they really want to live forever.

Being forever young, while no doubt an attractive notion, does not really prepare you for eventual retirement. This is especially the case if you do not progress beyond the attributes of many young people such as disrupted paid work patterns, large credit card bills, very modest contributions to superannuation, and associated relatively low superannuation account balances. The challenge is to get the under 40s to change some of their behaviours while still allowing them to enjoy their relative youth and to deal with other competing priorities during a challenging part of the lifecycle.

In this context, and despite the various setbacks and constraints it faced, the committee produced a well researched and coherent report with a number of recommendations worthy of support. On a personal note I was glad to see research I had undertaken and evidence I had presented to the committee being quoted in the report.

The committee's report is refreshing in that it kept its recommendations to a manageable 13, hopefully a lucky number in this context. Also refreshing is that the recommendations were supported by all committee members, with no minority reports or splits along party lines.

The recommendations are a mixture of substantial and less substantial, specific and less specific, with there being nothing necessarily wrong with that. Both the big picture and the more limited canvas are important in superannuation reform, and given the complexities that are often involved there can be hazards in being too specific.

The recommendations relating to adequacy of saving for retirement and improving the financial literacy of fund members are perhaps the most interesting and potentially useful.

Chief among this group of recommendations was that when a new employee commences work they be automatically placed in a voluntary contribution arrangement that they could choose to opt out

from at any time, preferably operating through salary sacrifice. The starting point would be a default rate of 3 per cent of salary with periodic adjustments.

Opt out arrangements of this type have been very successful in the United States when offered by employers enrolling new employees in company sponsored retirement savings plans. Legislated versions of opt out retirement savings schemes are also being planned for New Zealand and the United Kingdom. Adoption of such arrangements in Australia would substantially boost retirement savings and adequacy of retirement incomes. However, a number of practical problems would need to be addressed, such as the constitutional basis for any legislative scheme. That said, even voluntary take-up of such arrangements by employers following government urging would be a very good thing.

The report also focuses on improving the financial literacy of those under 40 (and the population more generally). The recommendation that the Financial Literacy Foundation and superannuation funds work together to improve Australians' interest in, and knowledge of, superannuation is worthwhile, but this cooperation has been happening in any event. However, the report goes further in recommending that the government develop a benchmark retirement savings target. The report also recommends that the government require all superannuation funds to provide individualised superannuation projections to their members in annual statements so as to assist members in deciding on how much to save for retirement.

The committee's report makes a useful contribution to the adequacy debate by rejecting calls to dilute the sole purpose test relating to superannuation. The report considers that muddying superannuation's purpose with early access schemes (allowing access for housing deposits and the like) would not only increase complexity but would also lead to inequities. The committee also recommends that the superannuation guarantee threshold not be increased by the government and that consideration be given to reducing it after consultation with employers and employees. This follows calls by some employers, often in industries not terribly keen on paying much in the way of wages let alone superannuation, for the threshold to be increased in order to reduce compliance burden. The reality is that paying superannuation based on every dollar of wages actually is simpler and easier to administer in most cases, along with being equitable.

The report also has some recommendations relating to the self employed, ranging from broad to narrow policy matters. On the broad front, the committee recommends consideration be given to bringing unincorporated small business owners into the superannuation guarantee system. This is currently something of a gap in retirement savings arrangements, as many small business owners are not able to sell their business for a significant (or any) amount of money when the main asset is the input of the owner. The report also recommends the government align the tax treatment of invalidity payments of the incorporated and unincorporated self employed. It would be fair to say that this latter recommendation is one of the smaller issues considered by the committee, though no doubt important to those who provided submissions on that topic.

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In addition, the report considers the situation of another group of persons who are not employees with a superannuation guarantee entitlement (and often under age 40 as well), namely women on unpaid maternity leave. The committee recommends that consideration be given to having a component of the maternity payment apportioned to the superannuation

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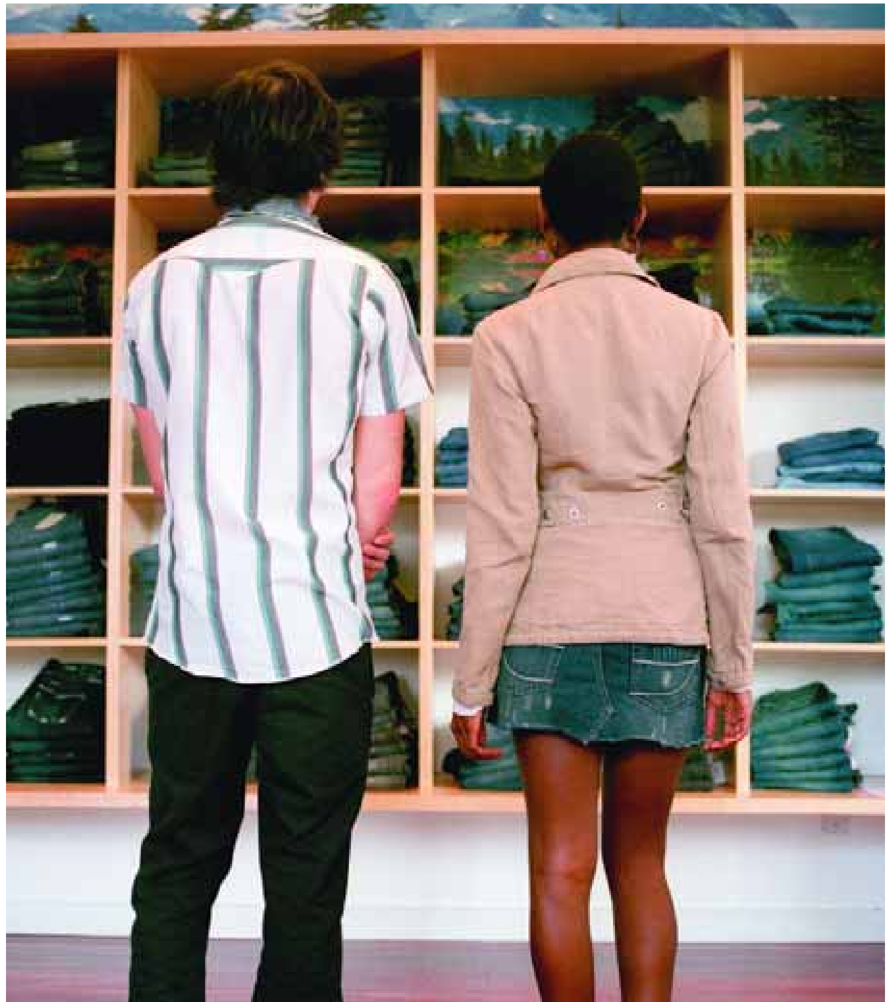

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The report and its recommendations have made a significant contribution to public debate.

guarantee. This proposal is not without its attractions, but given that maternity payments are not that large in the scale of things, a superannuation guarantee component may be a very modest amount.

The report also deals with the qualification criteria for receipt of the co-contribution, under which a person must earn 10 per cent of their income from eligible employment. The committee recommends that the government remove this requirement (where the government makes a payment on top of personal contributions made by certain low to middle income earners). This would open up the arrangements to women on unpaid maternity leave, and to stay at home parents, unemployed persons and students more generally. Again this proposal is not without its attractions, but only a proportion of such individuals would have the financial capacity to make personal contributions. Of those that did have that capacity, equity might require some consideration to be given in designing a revised co-contribution to the wealth of such individuals (rather than just their taxable income) and any assistance provided by a higher income individual in their household.

There are at least two recommendations in the report that would not receive the support of every superannuation fund, perhaps justifiably so on public policy grounds. The first such recommendation is that all superannuation funds, not just employer default funds, be required to offer a minimum level of death and total or permanent disability insurance, on an opt out basis. While addressing the underinsurance of many Australians relative to their needs and those of their dependants, such an arrangement raises a very real risk of adverse selection where individuals who know they are likely to make a claim could get insurance cover at a price that does not truly reflect the actuarial risks involved.

The other contentious recommendation is that the government introduce a default fund for casual employees, so that where a casual employee does not wish to choose their superannuation fund, that employee is automatically placed in a government-determined fund. Exactly how the government would determine which funds or fund would be used is not explored in the report, and the notion of government determined default funds would be a significant departure from the current system where default funds are determined by employers, industrial agreements and awards. While current arrangements are not flawless, they have led to more or less standard default funds for many casual workers on an industry by industry basis.

Taken as a whole, the report and its recommendations have made a significant contribution to public debate on the appropriate direction of further enhancements to the Australian superannuation system. It will be interesting to see what the government's response will be. However, given the extensive changes currently being made to the system following the May 2006 budget announcements, it may be some time before any further changes are made. ■

Ross Clare is policy officer for the Association of Superannuation Funds of Australia (ASFA). The House Economics Committee report into improving the superannuation savings of people under 40 is available at www.aph.gov.au/house/committee/efpa or email efpa.reps@aph.gov.au or phone (02) 6277 4587.

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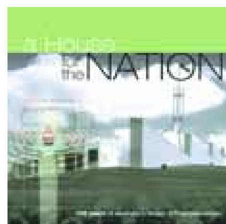

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