14 December 2011

Senate Standing Committees on Economics
PO Box 6100
Parliament House
Canberra ACT 2600
Australia

Dear Committee Chair

Minerals Resource Rent Tax Bill 2011 and related bills

The Financial Services Council (*FSC*) represents Australia's retail and wholesale funds management businesses, superannuation funds, life insurers and financial advisory networks. The FSC has 128 members who are responsible for investing $1.8 trillion on behalf of more than 11 million Australians. The pool of funds under management is larger than Australia's GDP and the capitalisation of the Australian Stock Exchange and is the fourth largest pool of managed funds in the world. The FSC promotes best practice for the financial services industry by setting mandatory Standards for its members and providing Guidance Notes to assist in operational efficiency.

The FSC thanks the Senate Economics Legislation Committee (*the Committee*) for the opportunity to make submissions in relation to the Minerals Resource Rent Tax Bill 2011 and related bills. The FSC wishes to confine its submissions to matters relating to the Superannuation Guarantee (Administration) Amendment Bill 2011 that is being considered as part of the package of bills before the Committee.

Increasing the superannuation guarantee contribution rate is a necessary reform

The decision to increase the Superannuation Guarantee (SG) from 9 to 12 per cent will result in significant long-term economic benefits and address the national shortfall in retirement savings.

With a SG contribution rate of 9 per cent, Australia has a significant Retirement Savings Gap (RSG). The 'retirement savings gap' is the difference between the amount required to be saved by the nation as a whole to ensure adequacy in retirement and the amount saved in the superannuation system, and estimated to be saved in future years up to retirement, by the current workforce. For the purposes of estimating the RSG, adequacy is considered to be a replacement rate of 62.5% of pre-retirement income.

A report by Rice Warner Actuaries (Appendix 1) for the FSC demonstrated that the 9 per cent contribution rate resulted in a retirement savings gap in 2010 of $897 billion.[1] The 2010 retirement savings gap takes into account non-superannuation assets and the Age Pension and,

[1] Superannuation Savings Gap at 30 June 2009, Rice Warner Actuaries, October 2010

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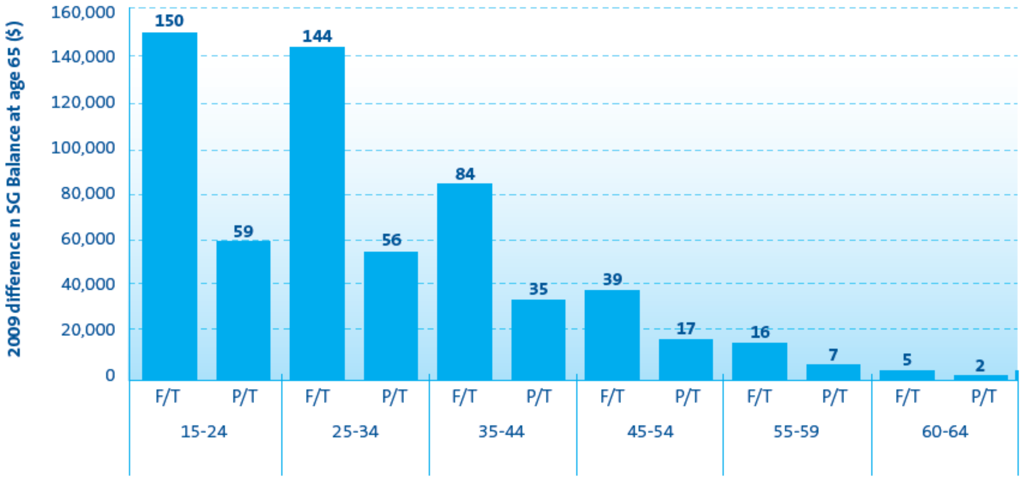
due to a variety of factors including the effect of the financial crisis on global markets, the gap has markedly increased from $452 billion in 2004.

Further research commissioned by the FSC (Appendix 2) demonstrated that the retirement savings gap is experienced more acutely by women than men. A 'typical woman', who takes a five-year career break at 27 years of age to have children, will have $91,400 or 35 per cent less than a 'typical man' in their superannuation account. A woman retiring at 67 years, however, must have 13 per cent more for retirement than a man in the same situation as she has a greater life expectancy.[2]

The retirement savings gap reflects the significant number of Australians who will likely not enjoy the standard of retirement that they otherwise expect and will be more reliant on the Age Pension than they would hope. The report demonstrates that a 9 per cent contribution rate will fail to provide most people with their expectations of a comfortable retirement.

A University of Canberra NATSEM Report modelled the following impacts of an increase in the guarantee of 9 to 12 per cent on individual account balances as shown in Table 1 below.

Table 1 - projected difference in super balance at age 65 by age group and labour force status[3]



Note: The values shown are the projected difference between SG contributions of 12% and 9% per annum until age 65. The projections assume real wages growth of 1% per annum and real superannuation returns of 4% pa.

Source: *NATSEM estimates based on HILDA data.*

The proposed increase would achieve a significant long term benefit for younger working Australians. Australians aged 15 to 24 will benefit from the increase in the SG to 12 per cent by the reform adding $150,000 to their retirement savings by age 65. The FSC shares the NATSEM Report's conclusion that "clearly an additional $150,000 in superannuation will make a major difference to a person's standard of living in retirement and help reduce the fiscal pressure on future governments."[4]

The benefits of the increase to the SG tapers down through older cohorts of workers, however the FSC notes that even those Australian workers approaching retirement, aged 45 to 54 years, would benefit from $39,000 added to their superannuation balance.

[2] Superannuation Savings Gap for Women at 30 June 2009, Rice Warner Actuaries, March 2010
[3] NATSEM Report, Saving Tomorrow April 2010
[4] NATSEM Report, Saving Tomorrow April 2010 at 24

The Government has also demonstrated that the increase in the SG from 9 to 12 per cent will significantly improve the savings of women in particular. A 30 year old woman earning around $70,000 will have an extra $108,000 in retirement savings providing her with an extra $2,900 to spend each year of her retirement.[5]

Implementation

The Government's measured approach to implementation of the increase to the SG rate provides for both a considerable lead time from 2011 to 2013 and a staged phase-in from 2013 until 2019. This approach provides sufficient time for individuals, businesses and the industry to adjust and accommodate the reforms, ensuring the increase is both affordable and sustainable. The implementation schedule is outlined in Table 2.

Table 2 – Implementation Schedule

Year	Rate (%)
2013-14	9.25
2014-15	9.5
2015-16	10
2016-17	10.5
2017-18	11
2018-19	11.5
2019-20	12

There is no evidence to support the proposition that the increase to the SG is a tax on business or negative for business generally. The implementation schedule allows employers to take the increased SG contributions into account when negotiating future wage settlements, ensuring that the incidence will largely fall on individuals.

Furthermore, the experience following the introduction of the SG and during the increase from 3 per cent to 9 per cent shows that business conditions in Australia actually improved significantly:

- Profits as a share of GDP increased during this period, growing from around 6 per cent of GDP in the early 1990s to around 8 per cent in the early 2000s.
- At the same time, productivity rose as real unit labour costs fell.
  - The decline in real unit labour costs was particularly pronounced between 1998 and 2003 when the SG rose from 6 to 9 per cent.
- The unemployment rate declined steadily through this period to its lowest level in decades.

In evaluating the impact on business of the increase in the SG all costs and benefits need to be considered, not simply the perceived short-term impact. As discussed below, by making

[5] Treasury estimate – The Hon Bill Shorten MP – Second Reading Speech to the Superannuation Guarantee (Administration) Amendment Bill 2011, 2 November 2011

retirees more self-sufficient less people in the future will need to rely on the aged pension. This reduces the burden on the Budget in the future and ultimately the taxes paid by businesses and others to fund the Budget. Allens Consulting Group estimates that superannuation delivers current savings on the Age Pension of $1.7 billion annually, without taking into account the long-term savings that will be generated by the increase to 12 per cent.[6]

Superannuation also played an important role in stabilising the Australian economy during the financial crisis by providing a domestic pool of funds on which Australian businesses were able to draw. As a result of the pool of superannuation funds, Australian businesses were, and will continue to be, less reliant on the vagaries of international credit markets. It is estimated that Australia accounted for $90 billion or 10 per cent of the world's total recapitalisation in 2009.

The larger pool of superannuation funds has lowered the cost of capital for Australian companies.[7] Relative to the rest of the world, Australia's equity risk has trended downwards since the early 1990s. The lower equity risk premium has meant more imaginative financing, higher investment, more jobs and more government revenue.[8]

The increase in compulsory superannuation contributions from 9 to 12 per cent by 2019 that is being considered by this committee will add half a trillion dollars to this pool of funds by 2035, further lowering the cost of capital and insulating Australia's economy from external shocks.

The budgetary impact of the proposed increase

Immediate fiscal impact

The increase in the SG from a 9 to 12 per cent should not be considered solely within a narrow debate around the costings of the reform in the short to medium term as the long-term benefits of the reform significantly outweigh the expected short-term budgetary implications.

Long-term fiscal impact

Australia's ageing population dictates that public sector finances will be under severe stress without structural reform due to an eroding taxation base. Personal saving rates are critical to relieving budgetary pressures over the longer-term.

The short term budgetary impact of increasing the SG from 9 to 12 per cent is therefore of far less importance than the long-term when assessing the strength of the policy. Treasury has estimated that increasing the guarantee to 12 per cent will directly result in a $10 billion per annum reduction in Aged Pension outlays from 2030.[9]

Higher levels of personal savings will alleviate inter-generational pressure on public finances resulting from demographic change in Australia's population. The Treasury projections outlined

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[6] Allens Consulting Group *Better living standards and a stronger economy: the role of superannuation in Australia* October 2009

[7] Treasury estimate – Address by the Hon Julia Gillard MP, Prime Minister - http://www.pm.gov.au/press-office/speech-financial-services-council-breakfast-sydney

[8] Treasury estimate – Address by the Hon Wayne Swan MP, The Treasurer - http://ministers.treasury.gov.au/DisplayDocs.aspx?doc=speeches/2011/019.htm&pageID=005&min=wms&Year=&DocType=1

[9] Treasury estimate – Address by the Hon Julia Gillard MP, Prime Minister - http://www.pm.gov.au/press-office/speech-financial-services-council-breakfast-sydney

in the 2010 Intergenerational Report (IGR) unequivocally demonstrated how the ageing of Australia's population will pressure public finances.

The IGR concluded that[10]:

- the ratio of working aged people relative to retired people will halve, from around 5 today to just 2.7 by 2050;
- between 2010 and 2050, the proportion of Australians aged 65-84 will double, whilst the proportion of people aged 85 and over will quadruple; and
- the proportion of Australians of working age will fall by seven percentage points to 60 per cent of the total populace in 2050.

These demographic changes will generate the problem of a shrinking tax base compounded by increased spending on health and pension costs. Health costs will almost double by 2050 to 27 per cent of GDP while pension costs are expected to rise from 2.7 per cent to 3.9 per cent of GDP over the next 40 years.

It is relevant to note that the failure of most European countries to deal with the rising costs of maintaining public sector pension schemes in the face of ageing populations, primarily through an aversion to engage in reform, has significantly contributed to the debt problems they currently face.

Australia has the opportunity to manage the significant budgetary implications of our ageing population in the present by strengthening our compulsory system of private savings. A higher level of personal saving through the superannuation system will safeguard public sector finances by ensuring a higher level of self-provision for retirement. As such, this is a critical reform that will greatly benefit current and future generations of working Australians.

Yours sincerely

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[10] The 2010 Intergenerational report, The Treasury - http://www.treasury.gov.au/igr/igr2010/