

06/04/2016

By email: superannuationobjective@treasury.gov.au

Division Head
Retirement Income Policy Division
The Treasury
Langton Crescent
PARKES ACT 2600

Dear Ms Wilkinson,

Re: AustralianSuper submission to Treasury on the proposed Objective of Superannuation

AustralianSuper welcomes the opportunity to make a submission to the Treasury on the objective of the Australian superannuation system.

About AustralianSuper

AustralianSuper is Australia's largest single superannuation fund and is run only to benefit members. We don't pay commissions to anyone to recommend us, nor do we pay dividends to shareholders. We have over two million members and manage over \$90 billion of members' assets. Our sole focus is to provide the best possible retirement outcomes for our members.

FSI Recommendation

AustralianSuper strongly endorses the recommendation of the Financial System Inquiry (FSI) to "seek broad political agreement for, and enshrine in legislation, the objectives of the superannuation system". Without clarity of purpose, superannuation and retirement policy and regulatory architecture cannot be aligned and therefore, cannot deliver the right outcomes.

The FSI recommended that the primary objective of superannuation should be *to provide income in retirement to substitute or supplement the Age Pension*. It also recommended the consideration of a number of subsidiary objectives supporting the primary objective.

AustralianSuper agrees that a single primary objective cannot possibly encompass all aspects of the purpose of superannuation. However, AustralianSuper believes that the FSI recommended primary objective reflects more what the Government, as the superannuation system's architect and administrator, feels the purpose of superannuation should be, rather than what the superannuation fund *member* believes the purpose of superannuation to be.

AustralianSuper Recommendation

AustralianSuper believes that the purpose of superannuation is:

To provide adequate requirement income for Australians to improve their quality of life in retirement.

There are two key components of this definition:

- 1) Adequacy
- 2) Confidence in quality of life

All of AustralianSuper's policy advocacy focusses on measures to ensure that our members are able to achieve adequate retirement income – this largely affects regulatory, competition and taxation settings around the accumulation of superannuation.

The second component relates to the ultimate outcome for members – obtaining quality of life in retirement. This is only possible if fund members trust the superannuation system in Australia, and can then have confidence to create a quality life for themselves in retirement, in the drawdown phase. What is important for members in this stage of their lives is not only income, but shelter (home) and health.

AustralianSuper's research from its 2 million members reveals that confidence is paramount in considering the purpose of superannuation, as a lack of confidence leads to behaviours that are sub-optimal or do not align with the intent of the system.

AustralianSuper's policy positions are developed within the framework of the objectives of *adequacy* and *confidence* for our members, rather than merely the preservation of favorable regulatory settings for superannuation.

Accumulation Phase – Adequacy

AustralianSuper understands that the concept of adequacy is highly subjective and will mean something different to each retiree.

With this in mind, AustralianSuper actuaries have generated a matrix of superannuation balances that illustrates a range of retirement income effects at different retirement balances.

AustralianSuper has interpreted the entry level of the 'adequate' range to be the ASFA Comfortable Standard, which is an income of \$42,861 a year. Extrapolating this amount using a series of assumptions detailed below AustralianSuper has determined that generating the ASFA Comfortable Standard income requires a lump sum at 65 of \$515,000.

If Australian Super believes that *the purpose of superannuation is to provide adequate retirement incomes for all Australians to improve quality of life in retirement* then logically all Australian Super's policy positions around accumulation are focused on helping our members and others reach a lump sum balance of \$515,000 at age 65.

TABLE 1 - The range of retirement outcomes

	Age Pension	ASFA Modest Standard	ASFA Comfortable Standard	“Million Dollar Myth”	Mid	Mid +	High	High +	Very High +
Balance at Retirement at age 65	0	\$26,000	\$515,000	\$1m	\$1.5m	\$2m	\$2.5m	\$3m	\$3.5m
Projected income from balance over 25 years	\$22,442	\$23,662	\$42,861	\$58,769	\$80,544	\$104,266	\$128,665	\$153,437	\$178,412
Income as a Multiple of Age Pension \$22,442	1.0	1.1	1.9	2.6	3.6	4.6	5.7	6.8	7.9
Income as Multiple of ASFA comfortable standard \$42,861	0.5	0.6	1.0	1.4	1.9	2.4	3.0	3.6	4.2
Income as a Multiple of Average Earnings \$77,388	0.3	0.3	0.6	0.8	1.0	1.3	1.7	2.0	2.3
<p>Assumptions</p> <ul style="list-style-type: none"> - Projections to produce level income in real terms over 25 years from super account drawdown and Age Pension combined, assuming: <ul style="list-style-type: none"> • 5.5%pa returns in retirement net of fees • AustralianSuper Choice Income fees of \$78pa plus 0.11% account balance (max \$750) • All figures are in today’s dollars, discounting at the wage inflation rate of 3.5%pa - Age Pension assumes single/homeowners, Age Pension rate as at August 2015, Assets/Income Test thresholds that will apply from 1 January 2017 - Modest and & Comfortable Retirement Standards sourced from ASFA 									

Drawdown Phase – Confidence

AustralianSuper believes that the purpose of superannuation is *to provide adequate retirement incomes for Australians to improve quality of life in retirement.*

A quality of life in retirement requires a superannuation fund member to have *confidence* that their retirement savings will provide for their:

1. Income

When addressing income in retirement the issue is not only one of adequacy. It also one of confidence that the income is being received in a vehicle that is tax effective, secure, cost effective, flexible enough to meet the needs and circumstances of the individual retiree and addresses longevity risk.

2. Housing

Confidence in retirement relies not only on income but on having a place to live, feel safe and call home. This may be the family home, a downsized home, a long-term rental property, age-specific accommodation option, retirement village or aged care facility.

Because the family home is concessional tax it has always made housing an attractive vehicle for investment, but for pensioners there is the additional incentive of the exemption of the family home from the assets test.

The family home serves a purpose beyond accumulation of assets to sustain someone in retirement; it also meets the need for shelter. Pensioners who do not own their own home face additional costs and stresses to meet this requirement. For this reason, the family home is often considered an additional pillar of the retirement income system.

Confidence in retirement around shelter requires policies that both reassure retirees that they will have an appropriate place to live in all stages of retirement and discourage suboptimal behaviour around home access and ownership.

3. Health

Confidence to be in a position to address health concerns as they arise is a significant issue for retirees. Over 30% of current retirees believe their health outcomes will be worse in five years' time¹. For retirees, the concern is whether they will be able to afford to pay for high quality healthcare when they need it. If health outcomes are not considered, people will not feel confident to spend their retirement incomes in line with their needs and will instead preserve their income to address potential future financial pressures, generating a lower quality of life in retirement.

Confidence in retirement around health requires policies that address health confidence concerns and discourage suboptimal behaviours.

Because Australian Super believes that *the purpose of superannuation is to provide adequate retirement incomes for all Australians to improve quality of life in retirement*, logically it follows that all Australian Super's policy positions around the drawdown phase of superannuation are focused on helping our members and others achieve confidence in their retirement plans.

Points to consider suggested in the Discussion Paper

The Treasury discussion paper invited comment on a number of issues raised by the FSI's subsidiary objectives. Some of these are addressed below:

1. Retirement income or standard of living in retirement

Australian Super believes that the purpose of superannuation is *to provide adequate retirement incomes for Australians to improve quality of life in retirement*. Referring to adequate income and quality of life in retirement rather than standard of living in

¹ Nationals Seniors Australia, 3rd *Seniors Sentiment Index*, National Seniors Australia and Challenger, August 2015, p.9. http://nationalseniors.com.au/system/files/06151196CRP_Challenger_SeniorsSentimentIndex_0.pdf

retirement is intentional and has significant implications. Income helps to meet costs of living. Standard of living is a broader concept and by implication includes use of not only income but also assets. Quality of life in retirement is a much broader concept again because it invokes not only access to income and assets, but *confidence* that income and assets will:

- be invested in the tax and cost optimal vehicle
- flexible enough to meet the needs of the individual retiree
- address longevity risk concerns

2. Wealth accumulation and estate planning

AustralianSuper believes that if the purpose of superannuation *to provide adequate retirement incomes for Australians to improve quality of life in retirement*, that clearly excludes estate planning and wealth accumulation beyond that required for an adequate retirement income from the objectives of the superannuation system. However, it is important to acknowledge that often restricted spending behavior is less about accumulation of wealth for the next generation and more a by-product of a lack of confidence around the ability to address potential housing or health issues in retirement.

3. Help people manage financial risks

AustralianSuper believes that risk management is important to retirees who have less opportunity to recover from losses. Products that address inflation risk, investment risk and longevity risk should be accessible, however there is legitimate concern that the cost of the mandating such products may outweigh the benefits they offer. Flexibility, choice and cost-efficiency are paramount in risk management solutions.

4. Adequacy

As discussed in detail above, AustralianSuper believes that adequacy is a relative concept that will mean something different to different people. AustralianSuper has chosen to use the ASFA Comfortable Standard as a **base rate** of adequacy.

5. Fiscal sustainability

AustralianSuper believes that the fiscal sustainability should be an objective of the superannuation system, not necessarily because of budgetary considerations, but more because sustainability engenders *confidence* that the contribution, accumulation, taxation and drawdown rules around superannuation can be relied upon.

6. Increase national saving

The original objectives of the superannuation system may have included a national savings objective. However, with the maturation of the superannuation system and the Australian financial system as a whole, an increased pool of national savings is now a less relevant objective of the superannuation system and more an ancillary benefit.

7. Invested in the best interests of members, simple and efficient

AustralianSuper agrees that a subsidiary objective of superannuation should be simplicity, efficiency, and to invest in the best interest of members because this is the

quickest and most effective way to accumulate sufficient retirement savings to generate an adequate income in retirement. AustralianSuper is a profit to members fund and operates under an ethos of 'members first'.

Location of Objective

AustralianSuper agrees that the purpose of superannuation should be enshrined in legislation.

AustralianSuper is comfortable with the FSI's recommendation that the purpose and objectives are enshrined in a preamble to a major piece of relevant legislation such as the *Superannuation Industry (Supervision) Act 1993*. It does not necessarily need to be in a stand-alone Act.

Thank you to both Treasury representatives and the Assistant Treasurer for encouraging AustralianSuper to make a submission on this important issue.

If you have any questions please do not hesitate to contact me on 03 8648 3992 or AustralianSuper's Head of Policy, Louise du Pre-Alba on 03 8648 3847.

Yours sincerely

Jane Hume
Senior Policy Adviser