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By email: superannuation@treasury.gov.au

Personal and Retirement Income Division
The Treasury
Langton Crescent
PARKES ACT 2600

REVIEW OF THE RETIREMENT INCOME STREAM REGULATION

AustralianSuper welcomes the opportunity to respond to the Treasury Consultation Paper on Retirement Income Stream Regulation.

AustralianSuper is one of Australia's largest super funds 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 2 million members and manage over $78 billion of members' assets. Our sole focus is to help members achieve their best possible retirement outcome.

AustralianSuper supports legislative reforms that would allow more types of retirement products to come to market. This should only be done however, with appropriate regard to competition and consumer protection issues that arise in the retirement income space. Commissions paid on retirement products currently contribute substantially to the expensive nature of private retirement in Australia and this issue is equally in need of government consideration.

We note that the much of the benefits of regulatory reform relating to retirement income streams is enjoyed by high net worth retirees. We hope that improved product settings will lead to part-pensioners - those who are contributing retirees who partially fund their own retirement – being able to have more certainty in their use of superannuation monies in retirement in a manner that benefits them as well as the economy. A default income stream pension would be a significant boost to the financial wellbeing of many future contributing retirees in Australia.

On the issue of reducing minimum drawdown amounts, AustralianSuper suggests that this matter be referred to the Tax White Paper for further consideration – this issue needs to be considered in the context of the sustainability of the superannuation system and the tax concessions applied to superannuation. At best this should only be available as a permanent option to low account balance holders so as to avoid excessive taxpayer burden in funding retention of monies in superannuation.

Please contact me on 0412 710 290 if you wish to discuss this further.

Yours sincerely

Louise du Pre-Alba
Head of Policy

This information is of a general nature and does not take into account your personal objectives, situation or needs. Before making a decision about AustralianSuper, consider your financial requirements and refer to the Product Disclosure Statement (PDS). AustralianSuper Pty Ltd ABN 94 006 457 987 AFSL 233788, Trustee of AustralianSuper ABN 65 714 394 898. Industry SuperFund logo used with permission of Industry Fund Services (IFS). This consent had not been withdrawn at the date of publication.

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Regulatory arrangements

1: What types of income stream products would enable retirees to better manage risk in the retirement phase (in particular longevity risk and investment risk)?

- Deferred Lifetime Annuities
- Growth focused account-based income stream products.
- Collective defined contribution plans (these products are not available in Australia presently – they require fixed contributions from the sponsor, and are invested in a pooled manner. Collectively, the members and pensions bear all the risks (eg investment risk, longevity risk, interest rate risk, inflation risk, etc. The member does not have an account, but an interest in receiving a retirement income at a specified time).

2: Do the annuity and pension rules constitute an impediment to the development of new products and if so, what features of the rules are of most concern from a product innovation perspective?

Yes. Retirees in Australia would benefit from the use of income stream products instead of lump sum withdrawals by making income stream rules more flexible to enable a seamless transition from accumulation to drawdown phase.

Ideally, the move from accumulation to drawdown should be a seamless part of the system with one account servicing both purposes, as is the case with SMSFs. This would reduce costs to consumers and is entirely consistent with the intention of changing regulatory settings to enable consumers to more easily transition to retirement. There are further discrete measures that would also assist in making this transition more efficient and cost effective for consumers:

a) Ability to pay lump sums into income stream (pension) accounts.

There are circumstances where a member would have a valid reason to place an additional lump sum into their income stream account, including inheritance, downsizing the family home, a transition to retirement transfer from an accumulation account, or a redundancy payment.

Currently if a member wants to add money to their existing income stream (pension) account they have two options:

(a) Open a new pension account. This requires the pensioner to roll their old pension account and any additional money into the new pension account.

(b) Open a second pension account.

Both of these options result in an unnecessary administration burden and extra costs (which erode retirement savings) being imposed on retirees.

Recommendation: Amend pension requirements to allow for the topping up of pension accounts.

b) Default pensions

AustralianSuper contends that creating a default income stream derived from members' accumulation account balances is a constructive step in engaging members and potentially reducing

the prospect of lump sum withdrawals in the system. It takes away the reflex action of withdrawing a lump sum from superannuation when it is not necessary, and not in the member's best interest. A default income stream supports the philosophy that this is a retirement incomes system rather than a wealth accumulation system.

There are some issues to be considered further. Amendment to the current pension requirements would also need to be made to accommodate the following:

- Deferral of minimum drawdown for a short specified period for member contact for retrieval of relevant payment information.
- Enable the member to top up the default income stream (as described above).
- Transfer to pension at a specified age, in specified circumstances, without member instruction. Alternatively, a Centrelink notification of benefits receipt may trigger this consideration.
- A 'no detriment' test covering fees, investment strategy and insurance is required.
- A 'no detriment' test applying when a default pension member decides instead to choose a different retirement option.

Recommendation: Establish a Treasury and regulator-supported working group applying the Retirement Incomes policy-making principles outlined above to consider this issue further.

3: What changes could be made to the annuity and pension rules to accommodate a wider range of income stream products while having regard to the need to protect against abuse of the earnings tax exemption and to promote appropriate and prudent retirement income objectives?

Tax treatment of deferred annuities

The existing law requires that income streams must make payments at least annually. As a deferred annuity does not meet this requirement, it does not qualify as an income stream, and therefore is not entitled to the associated concessional tax treatment that applies to earnings on superannuation assets supporting income streams.

As a consequence a deferred annuity is not an attractive option in retirement yet it meets a longevity risk need.

Further, retirees may need the flexibility of being able to purchase a deferred annuity over a period rather than with a lump sum. This period may be before retirement, after retirement or a combination of both.

Recommendation: Amend taxation of deferred annuities to assist in providing a product that enables retirees to better manage longevity risk in retirement. Allow deferred annuities to be purchased over a defined period rather than at one point in time.

4: Would such changes lead to new products being brought onto the market?

Yes, it is likely that changes as suggested above would definitely lead to new products being brought onto the market as well as changes to current income stream products on offer.

Deferred lifetime annuities

5: Should people only be able to purchase a DLA with superannuation money?

No, purchasers should be able to add other money to it – provided that there is no ability to offer a death benefit, and no cashability, this would avoid any perceived estate planning concerns that may arise.

6: Should people only be able to purchase a DLA for an up-front premium or should other purchase options also be allowed? If an annual premium approach is allowed, what should be the consequences if the premium payments cease?
An annual premium approach should be allowed – but this should not operate such that a DLA interest ceases if annual payments cease. Instead, an annual premium approach can be applied where an interest in a DLA accrues with every payment of premium. In this scenario, if payments cease, the investor still has an interest in a DLA.

7: Should there be an upper limit on the amount that can be invested in a deferred lifetime annuity?
Yes, but arguably it is not needed if providers of DLAs are not permitted to offer a death benefit as part of the product.

8: Should there be a minimum deferral period for a DLA? If so, what would determine the period?
Arguably it is not needed, but the preservation requirements contained in the *Superannuation Industry Supervision Act 1993* are relevant here.

9: Should there be a maximum deferral age or period? If so, what should it be?
The maximum referral date should be the expected life expectancy of the individual at the time of purchase of the DLA. This figure would change over time as expected life expectancy increases.
To allow for longer periods is against the interests of the purchaser of the DLA and potentially unconscionable.

10: Do the payment features described in paragraphs 51 and 52 (non-commutable, payable for life from the age specified, guaranteed payments) strike the right balance in allowing people to insure against longevity risk while avoiding unnecessary restrictions on product development?
Yes

11: Should providers of DLAs be able to offer a death benefit? If so, should there be restrictions on the size of the death benefit that could be offered? If so, what restrictions?
No as this is inconsistent with the construction of the entire product. Account-based pensions already provide this.

Minimum payment amounts
12: Are the current minimum payment amounts for account-based products appropriate to achieve the objectives outlined above, given financial conditions can change?
We think that there should be some flexibility built into the system to enable lower minimum account balances to be withdrawn in the specified circumstance of significant adverse investment market performance.
We are of the view that the burden of taxpapers needs to be considered in the context of minimum withdrawals. The taxation and regulatory settings around income streams should not provide excessive scope for deferral of income, particularly in a tax free environment.

With this in mind we have provided an example of outcomes for account balances holders (from $75,000 up to $5,000,000) if they were able to reduce their minimum withdrawal amount to 75% of the minimum withdrawal, 50% and 25% respectively (see Attachment 'A').

13: Should there be an automatic mechanism for adjusting the minimum drawdown amounts in response to significant adverse investment market performance? If so, what should that mechanism be? How would this also satisfy the rationale for setting minimum payment amounts?

No. Minimum drawdown relief should only be available to all where there is an investment 'shock.' It should only be available automatically where the account holder is a small account balance holder (less than $200,000). This measure confirms that retirement monies should be used for retirement purposes only rather than generating a continuing taxpayer subsidy for private estate planning.

14: Should the minimum drawdown amounts also increase in response to very strong market performance? Would the mechanism be similar to that for decreases? Would this satisfy the rationale for setting minimum payment amounts?

It would be preferable if the arrangements had a floor, but not a ceiling. The case has not been made that contributing retirees deliberately exhaust their savings, but instead are generally quite frugal.

15: For how long should the change remain in place? Should it be left in place only for the year in which the shock occurs, or until balances have 'recovered' by a particular extent?

AustralianSuper contends that minimum drawdown relief for all income streams should only be available for the year in which the shock occurs.

As it is, any reduction in minimum pension drawdown requirements will apply as a blunt instrument capable of applying across all pension investments, even those that may not have been affected by a market shock. Many retirees invest in cash where the market 'shock' may not even affect their investments in the short term.

16: What other issues need to be considered if the minimum drawdown amounts should fluctuate?

The purpose of minimum drawdowns is to ensure that superannuation monies which attract tax concessions are actually being used for retirement purposes, and not preserved for later estate planning and bequests at the taxpayers expense.

With this in mind, a reduction in the minimum drawdown requirements is less likely to provide 'relief' to high account balances holders (for example, those with over $5,000,000 in superannuation). This is because they are less likely to exhaust their capital before death as they have excessive benefits in superannuation.

The reverse is true for small account balance holders who are part pensioners contributing to their own retirement. They are actually more likely to exhaust their capital before death as they do not have sufficient savings in retirement. This is further exacerbated by the tendency of small account holders to invest in cash in retirement as they are less tolerant to adverse investment performance. See attachment 'A' on how a small account balanced holder would benefit from a reduction in minimum drawdown without undue retention of monies in superannuation.

Any consideration of a reduction in the minimum drawdown needs to be considered alongside the equity issues of taxation in superannuation in the upcoming White Paper on Taxation. This issue should ultimately be considered after taxation reforms are dealt with.

It is difficult to see how the current model of income stream provision that is tax free on earnings is sustainable in the long term without some upper limit on tax concessions being imposed on account

balances. Taxpayers simply should not have to fund tax free earnings on amounts over a particular level after which retirement costs have been well and truly provided for.
To consider a reduction in the minimum drawdown without a wider tax consideration on this point alone is not appropriate and is not in the interests of the taxpayer.
We note that some suggest increasing tax that applies on withdrawals, including death benefits, instead of facing the bigger issue of imposing an upper limit to tax concessions. We are concerned that it would be unconscionable to now impose higher taxes on those who actually use their superannuation monies for retirement purposes whilst not considering this much bigger and more expensive question of further enablement of retention of monies in superannuation by those with excessive amounts held in superannuation accounts.

Attachment 'A'

Low Account Balance Drawdown Scenarios - varying Minimum Drawdown %s

We have provided figures for small account balance holders with amounts starting at $75,000, then $100,000 and then $200,000.

The projections stop at $200,000 because once an account balance exceeds $200,000 the single assets test applies – this is an appropriate signpost to amounts less than $200,000 being considered to be small account balances for retirement income purposes.
The effect of the changed minimum drawdowns on account balances has been projected at 5 year intervals into retirement up to a period of 25 years - the maximum period allowed by ASIC for retirement projections.
The lines coloured blue represent a figure that is an appropriate reduction in a minimum withdrawal figure for small account balance holders – 50%. The figures demonstrate that to withdraw more than this (75%) provides little effective relief for the retiree in terms of managing their minimum drawdown. The figures also demonstrate that to allow less withdrawal (25%) means that there remains a considerable amount of the original sum invested remaining after 25 years.
The 25% figures shown in each of the tables confirm the leakage in the system to estate planning, thereby increasing the taxpayer burden in funding tax concessions on monies retained in superannuation.
When these numbers are applied to larger account balances they confirm the heavy taxpayer subsidy. AustralianSuper suggests that a reduction in the minimum drawdown amount does not apply at all to amounts over $200,000 unless a one-off event such as the GFC is repeated. To provide this permanently simply applies too much financial burden on the taxpayer.

The projections assume investment in a mixture of around 60% growth assets (e.g. shares, property) and 40% defensive assets (e.g. fixed interest, cash) which is modelled assuming a real rate of return of 3%pa above CPI. The figures are expressed in today's dollars and further assume AustralianSuper's fee structure for income products ($78 a year plus 0.11% of assets capped at $750pa). In addition:

- Projection A assumes the current minimum drawdown rules apply and the member draws down at this level
- Projection B assumes the current minimum drawdown limits are reduced by 25% and the member draws down at this level
- Projection C assumes the current minimum drawdown limits are reduced by 50% and the member draws down at this level
- Projection D assumes the current minimum drawdown limits are reduced by 75% and the member draws down at this level
- Projection E assumes that 5% is subtracted from the current minimum drawdown levels, subject to a minimum drawdown factor of 1% and members draw down at this level

(a) $75,000 balance at retirement

Scenario	Account Balance at end of year					
	0	5	10	15	20	25
(A) Invested Conservative Balanced	$75,000	$63,604	$52,785	$41,533	$30,283	$19,747
(B) Conservative Balanced / 75% of Min Drawdowns	$75,000	$67,796	$60,322	$51,615	$41,782	$31,204
(C) Conservative Balanced / 50% of Min Drawdowns	$75,000	$72,206	$68,808	$63,924	$57,291	$48,751
(D) Conservative Balanced / 25% of Min Drawdowns	$75,000	$76,841	$78,349	$78,910	$78,105	$75,399
(E) Conservative Balanced / MD less 5% (min 1%)	$75,000	$77,796	$80,711	$82,108	$77,888	$66,736

(b) $100,000 account balance at retirement

Scenario	Account Balance at end of year					
	0	5	10	15	20	25
(A) Invested Conservative Balanced	$100,000	$84,923	$70,595	$55,662	$40,697	$26,647
(B) Conservative Balanced / 75% of Min Drawdowns	$100,000	$90,516	$80,657	$69,134	$56,080	$41,997
(C) Conservative Balanced / 50% of Min Drawdowns	$100,000	$96,398	$91,986	$85,580	$76,821	$65,491
(D) Conservative Balanced / 25% of Min Drawdowns	$100,000	$102,582	$104,722	$105,599	$104,649	$101,150
(E) Conservative Balanced / MD less 5% (min 1%)	$100,000	$103,856	$107,876	$109,869	$104,347	$89,526

(c) $200,000 account balance at retirement

Scenario	Account Balance at end of year					
	0	5	10	15	20	25
(A) Invested Conservative Balanced	$200,000	$170,201	$141,836	$112,177	$82,355	$54,248

(B) Conservative Balanced / 75% of Min Drawdowns	$200,000	$181,394	$161,998	$139,210	$113,274	$85,170
(C) Conservative Balanced / 50% of Min Drawdowns	$200,000	$193,169	$184,698	$172,203	$154,943	$132,449
(D) Conservative Balanced / 25% of Min Drawdowns	$200,000	$205,546	$210,215	$212,355	$210,825	$204,152
(E) Conservative Balanced / MD less 5% (min 1%)	$200,000	$208,096	$216,535	$220,916	$210,182	$180,684

High Account Balance Drawdown Scenarios - varying Minimum Drawdown %s

We have provided similar projections for high account balance holders with amounts starting at $1,000,000, then $2,000,000 and then $5,000,000.

The effect of the changed minimum drawdowns on account balances has been projected at 5 year intervals into retirement up to a period of 25 years - the maximum period allowed by ASIC for retirement projections.
The coloured blue highlights what will be left as an account balance after 25 years with a continuing reduction in a minimum withdrawal figure for the high account balance holders.
The figures demonstrate that in nearly every example (one has $431,878), the retiree is left after 25 years with way more than what is required under the ASFA Comfortable Retirement Standard to retire, and this is *after* drawing in down in retirement for a period of 25 years.
At its most blatant the extent of taxpayer subsidy of estate planning and bequests can be seen in table (f) dealing with $5,000,000 account balances. If a permanent reduction in the minimum drawdown rules apply so that they are reduced to less than 5% of the original minimum drawdown rate (subject to a minimum of 1%), a $5,000,000 account will have $4,662,118 left after 25 years which will invariably not be used for retirement purposes, but estate planning purposes.
This demonstrates that high account balance holders have little need for a permanent reduction in minimum pension drawdown for the purpose of ensuring their retirement benefits last, and to provide such a reduction confirms the continuing heavy taxpayer subsidy of high balance account holders in superannuation.
AustralianSuper suggests that any permanent reduction in the minimum drawdown amount does not apply at all to amounts over $200,000 unless a one-off event such as the GFC is repeated. To provide this permanently simply applies too much financial burden on the taxpayer.

The projections assume investment in a mixture of around 60% growth assets (e.g. shares, property) and 40% defensive assets (e.g. fixed interest, cash) which is modelled assuming a real rate of return of 3%pa above CPI. The figures are expressed in today's dollars and further assume AustralianSuper's fee structure for income products ($78 a year plus 0.11% of assets capped at $750pa). In addition:

- Projection A assumes the current minimum drawdown rules apply and the member draws down at this level
- Projection B assumes the current minimum drawdown limits are reduced by 25% and the member draws down at this level
- Projection C assumes the current minimum drawdown limits are reduced by 50% and the member draws down at this level
- Projection D assumes the current minimum drawdown limits are reduced by 75% and the member draws down at this level
- Projection E assumes that 5% is subtracted from the current minimum drawdown levels, subject to a minimum drawdown factor of 1% and members draw down at this level

(d) $1,000,000 account balance at retirement

Scenario	Account Balance at end of year					
	0	5	10	15	20	25
(A) Invested Conservative Balanced	$1,000,000	$853,580	$713,193	$565,446	$416,459	$275,615
(B) Conservative Balanced / 75% of Min Drawdowns	$1,000,000	$909,767	$814,812	$701,969	$572,584	$431,878
(C) Conservative Balanced / 50% of Min Drawdowns	$1,000,000	$968,868	$929,225	$868,924	$783,998	$671,817
(D) Conservative Balanced / 25% of Min Drawdowns	$1,000,000	$1,030,997	$1,057,840	$1,072,133	$1,067,942	$1,037,551
(E) Conservative Balanced / MD less 5% (min 1%)	$1,000,000	$1,043,796	$1,089,689	$1,115,484	$1,064,875	$918,385

(e) $2,000,000 account balance at retirement

Scenario	Account Balance at end of year					
	0	5	10	15	20	25
(A) Invested Conservative Balanced	$2,000,000	$1,710,925	$1,433,260	$1,139,511	$840,985	$557,047
(B) Conservative Balanced / 75% of Min Drawdowns	$2,000,000	$1,823,393	$1,636,916	$1,414,016	$1,156,626	$874,252
(C) Conservative Balanced / 50% of Min Drawdowns	$2,000,000	$1,941,693	$1,866,188	$1,749,008	$1,581,939	$1,359,389

(D) Conservative Balanced / 25% of Min Drawdowns	$2,000,000	$2,066,050	$2,123,899	$2,156,649	$2,152,252	$2,095,014
(E) Conservative Balanced / MD less 5% (min 1%)	$2,000,000	$2,091,668	$2,187,724	$2,243,564	$2,145,703	$1,854,318

(f) $5,000,000 account balance at retirement

Scenario	Account Balance at end of year					
	0	5	10	15	20	25
(A) Invested Conservative Balanced	$5,000,000	$4,282,960	$3,593,461	$2,862,461	$2,117,879	$1,407,578
(B) Conservative Balanced / 75% of Min Drawdowns	$5,000,000	$4,564,270	$4,103,227	$3,550,157	$2,909,471	$2,204,560
(C) Conservative Balanced / 50% of Min Drawdowns	$5,000,000	$4,860,166	$4,677,080	$4,389,258	$3,975,760	$3,422,118
(D) Conservative Balanced / 25% of Min Drawdowns	$5,000,000	$5,171,208	$5,322,077	$5,410,197	$5,405,181	$5,267,401
(E) Conservative Balanced / MD less 5% (min 1%)	$5,000,000	$5,235,284	$5,481,831	$5,627,801	$5,388,187	$4,662,118