AustralianSuper

24/04/15

The Treasury
Email: superannuation@treasury.gov.au

Dear Sir \ Madam,

RE: REVIEW OF RETIREMENT INCOME STREAM REGULATION – CONSULTATION ON OPTIONS

AustralianSuper welcomes the opportunity to respond to options arising from the review of retirement income stream regulation.

About AustralianSuper
AustralianSuper is Australia's largest super 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 2.1 million members and manage over $85 billion of members' assets. Our sole focus is to provide the best possible retirement outcomes for members.

We have responded only to those questions raised in the three consultation papers that affect our fund.

Please do not hesitate to contact me on 03 8648 3847 if you wish to discuss this further. We are happy to provide further information on request.

Yours sincerely

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<u>Paper 1 - Revising the annuity and pension rules ("Paper 1")</u>

Rationale for the annuity and pension rules

1. A purely principles-based approach

Discussion question

1. Do you consider that a purely principles-based approach is practicable? If so what principles should apply? If not, why not?

A principles based approach should include the following general principles;

1) AustralianSuper contends that the purpose of superannuation is to assist in providing a reasonable retirement benefit for Australians. This should include a bias towards retirement incomes rather than lump sums as a guiding principle. We do not agree however, that one of the objectives of the current regulatory regime should be to facilitate the provision of a 'smooth' level of income.
2) Some level of flexibility in retirement spending needs to be maintained as a guiding principle. The spending patterns of retirees necessarily include some lumpy expenditures (eg. home renovations, aged care bonds, out of pocket health expenses), in direct contradiction to the paper's assumption that a 'smooth' level of income is what is required for retirement incomes.
3) AustralianSuper fully supports a regulatory objective to ensure that large amounts of concessionally taxed superannuation savings are not passed on as bequests.

2. Broadening the existing rules

Discussion questions

2. Would the restrictions proposed (re: Category A and B regarding regulating access to capital) combine to ensure that a complying product would provide for the bulk of the capital to be drawn down over the course of the person's retirement?

Response to question 2

The restrictions proposed above would appear to combine to ensure that a complying product would provide for the bulk of the capital to be drawn down. It is an open question as to whether this product would be commercially viable and whether there would be member interest. This is not something that AustralianSuper has tested at this point in time.

3. Do you have any concerns with how these rules would operate? Do you foresee any unintended consequences?

Response to question 3

It would be difficult to achieve product developments that meet one or other of the category requirements presently.

4. Would it be possible to replace the minimum drawdown requirement with a diminishing capital value requirement, that is, have only Category A products?

Response to question 4

AustralianSuper disagrees with this proposal as it severely restricts the ability of retirees to access their capital if and when the need arises, such as with major unexpected expenses as described above.

5. Would the depreciation schedule described above be appropriate? If not, why not, and what would be a better alternative?

Response to question 5

AustralianSuper does not think the depreciation schedule shown would be appropriate.

6. How could or should an equivalent freeing up of the income payment rules apply in the case of a defined benefit type interest where members accrue an entitlement to a fixed income and there is no explicit purchase price?

Response to question 6

It is neither necessary nor appropriate to apply this to existing defined benefit arrangements.

7. Is there a need for a maximum drawdown rule? How could this be designed?

Response to question 7

AustralianSuper does not believe there is a need for a maximum drawdown rule.

8. Do you agree there should be restrictions on who can offer products that fall under this category? If so, what restrictions?

Response to question 8

Lifetime guaranteed income stream products should be offered by life offices, public sector schemes and defined benefit funds.

The 'promise' of a 'guaranteed' income can only be met where there is a separate third party capital reserve, otherwise where the promise is not met members of the scheme pay for it out of reduced returns.

Discussion question

9. If you do not support the approach outlined in this paper, how else could the annuity and pension regulations be re-cast so as to accommodate a wide range of retirement income products, provide appropriate levels of integrity and certainty, and not act as a barrier to future innovation?

There are four key areas of pension/annuity regulation reform required, which do not exclusively focus on annuities, but which would make transitioning to a retirement income more accessible to consumers. These can be addressed without creating unnecessary additional complexity in the retirement incomes system. They are as follows:

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; or
(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) 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, in conjunction with point 1(a) above 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, and allow deferred annuities to be purchased over a defined period rather than at one point in time.

c) Default pension

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. This is a matter that can be appropriately dealt with at the regulatory level by the Australian Prudential Regulation Authority (APRA), acknowledging that some minor amendments to the current pension requirements would also need to be made to accommodate the following:

- Deferral of minimum drawdown for a specified period to give time for contacting members and taking payment instructions.
- 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.
- A 'no detriment' test covering fees, investment strategy and insurance is required.
- Alternatively, instead of transferring from a MySuper product to a default income stream, it is preferable that regulatory settings are changed so that the MySuper product may be the vehicle from which pension type drawdowns occur.

Recommendation: Establish a Treasury and APRA-supported working group applying the Retirement Incomes policy-making principles outlined above to development of a Prudential Standard that deals with default pension products.

Paper 2 - Purchase options for income streams (including in accumulation phase) – ("Paper 2")

Discussion questions

1. Is it the case that the existing pension and annuity rules are impeding the development of innovative income stream products which provide greater longevity insurance in (a) the accumulation and (b) the drawdown phase?

Response to question 1

Yes current rules do impede the development of innovative income stream products.

See above for suggestions on how to provide more flexibility in pension and annuity rules.

2. Given that fund members often do not start to engage with their superannuation until a few years prior to retirement, are changes to facilitate the purchase of annuity products in the accumulation phase desirable? Would changes be likely to encourage the development and take-up of such products in the absence of additional incentives?

Response to question 2

AustralianSuper supports regulatory changes to enable consumers to purchase annuity products in stages during the accumulation phase. It is an open question as to whether this will be sufficient incentive to purchase annuities. The desire to purchase annuities changes with market conditions.

Discussion question

3. Would it be feasible for funds to ensure that where an income stream product is purchased in the accumulation phase, the earnings tax exemption only applies after the member commences an income stream?

Response to question 3

Yes. The earnings tax exemption should only apply after the member commences an income stream.

Discussion question

4. Is the purchase of a single income stream product in tranches a workable option?

Response to question 4

Yes, the purchase of a single income stream product through multiple premiums is a workable option.

Discussion question

5. Would a *de minimis* rule set by the Government which allowed the return of premiums and earnings to policyholders be necessary to facilitate the purchase of annuity products in tranches in the accumulation phase? Would the same rules also be appropriate in the drawdown phase?

AustralianSuper supports the use of a *de minimis* rule, set by the Government, to allow the return of premiums and earnings to policyholders. We do not think however, that it should be available beyond accumulation phase and it would be disproportionately expensive to administer in retirement phase.

Paper 3 - The minimum drawdown amounts for account based pensions (“Paper 3”)

Discussion question
1. Does smoothing or increasing the flexibility of the minimum drawdown requirement warrant increasing the complexity of the system?

Response to question 1

AustralianSuper contends that increasing the flexibility of the minimum drawdown requirement is worthwhile if the flexibility is chosen by the member/retiree.

To introduce more age bands into the current schedule with adjustments to the percentages is to increase complexity for all, to address the concerns of only a percentage of retirees.

The second option, the carry-forward drawdown requirement, whereby members could choose to drawdown as little as 50% of the minimum drawdown requirement in any given year, triggering a carry-forward drawdown requirement, only increases the complexity of the system for those who choose to avail themselves of this option.

AustralianSuper supports the second option – optional carry-forward drawdown requirement.