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Dr Ken Henry
Chair
Australia's Future Tax System Review
AFTS Secretariat
The Treasury
Langton Crescent
Parkes ACT 26000

Dear Dr Henry

Re: Longevity Risk, Superannuation and the Age Pension

This letter responds to the call for a first round of submissions to Australia's Future Tax System Review.

In recent years the direction of public debate on superannuation has focused predominantly on the adequacy of superannuation contributions and benefits. The most recent simplification reforms achieved a significant improvement in the adequacy of retirement incomes both by removing the tax on benefits and halving the taper rate on the assets test for the Age Pension. The removal of the tax on superannuation benefits for those 60 years and over has also provided a significant incentive for additional savings within the superannuation environment.

However these changes have been accompanied by a loss of focus on any policy that addresses the need for retirees to use their retirement savings to make their own arrangements which specifically address longevity risk. Previously the social security system provided incentives in the form of assets test exemptions for complying income streams that addressed that risk.

These have been replaced by a less severe taper to the assets test, which has provided additional Age Pension payments regardless of whether the private pension arrangements the retiree has chosen address longevity risk. As a result, significantly more retirees are now receiving at least a partial Age Pension. On current policy settings the number will increase further as a result of the foreshadowed increase to the single rate Age Pension.

In the future many retirees will become more dependent on the Age Pension as their own retirement savings deplete. While there is no documented evidence of retirees being other than cautious with their retirement savings, the projections for benefits indicate that most people's private retirement savings will not be sufficient to maintain a modest but comfortable standard of living over their expected lifetime.

There are two sets of consequences of this lack of focus on longevity in the superannuation pension rules. The first is that many retirees' private savings will be exhausted and they will become completely dependent on the Age Pension. The second is that this dependency on the Age Pension, despite the significant tax concessions given to support private retirement savings, has implications for future Commonwealth outlays.

There are constraints to the government's fiscal capacity to add, either by tax concessions or outlays, to the retirement savings of those who, on current policy settings, will have insufficient resources to provide for their own expected longevity.

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This raises several sets of issues which we believe need to be considered in the context of both the Henry and Harmer Reviews:

1. Targeting of the Age Pension;
2. Targeting of any additional budgetary support for retirement savings to those for whom adequacy will continue to be a major issue; and
3. Impelling a proportion of tax free superannuation benefits to be taken in a form, or according to a general set of rules, which effectively addresses the retiree's longevity risk.

Challenger will contribute to further stages of the Review to advance these policy concepts.

This submission is authorised by Richard Howes, Challenger's Chief Executive, Life. I can be contacted at Challenger on 02 9994 7256 or by email at dcox@challenger.com.au .

Yours sincerely

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