PRICEWATERHOUSECOOPERS

**PricewaterhouseCoopers**
**ABN 52 780 433 757**

Darling Park Tower 2
201 Sussex Street
GPO BOX 2650
SYDNEY NSW 1171
DX 77 Sydney
Australia
Telephone +61 2 8266 0000
Facsimile +61 2 8266 9999
Direct Phone Enter your phone number
Direct Fax Enter your fax number
www.pwc.com/au

Review of Australia's Future Tax System
Retirement Income Consultation Paper

27 February 2009

Dear Sir or Madam

**PricewaterhouseCoopers submission to the Retirement Income Consultation Paper**

PricewaterhouseCoopers (PwC) is delighted to participate further in the Review of Australia's Future Tax System by making this brief submission to the Retirement Income Consultation Paper.

The Consultation Paper provides a balanced and succinct overview of the current policy approach to retirement incomes. We consider that the central pillars of Australia's retirement savings system are sound, including:

- the Age Pension safety net;
- the 9% Superannuation Guarantee; and
- voluntary contributions to augment superannuation/retirement incomes.

However, the current global financial crisis (GFC) has highlighted some issues in the existing retirement income arrangements. For example:

- some current and pending retirees over 60 will need to draw down their superannuation savings for living costs when equity values are at 5 year lows which may reduce the self-funded period of their retirement.
- some people near retirement age have needed to extend their working life. Part of this issue may have been mitigated by fuller awareness of the merit of switching fund allocations to lower risk options in the years approaching retirement. A related concerning issue is some of these people are belatedly switching to cash based options at this low point in equity markets which may see them also miss any market recovery. Overall, there is a need to improve education levels on superannuation issues to improve the ownership, control and understanding the community has on optimising their retirement savings. As the GFC hopefully moderates, there will be a need to rebuild voluntary contribution participation rates in some demographic groups.

Aside from these immediate concerns, there are significant weaknesses in the existing system that limit its flexibility and ability to generate long term savings patterns, potentially undermining its long term sustainability.

**Review of Australia's Future Tax System**
**27 February 2009**

We would like to offer the following comments to assist the review team in assessing amendments to Australia's Future Tax System.

### Q1.1 The retirement income system

The objectives of the retirement income system should be to ensure that retiring persons have *adequate* income to meet their essential needs.

Does the current system achieve this? Not always, particularly for certain demographic groups, such as those people who spend time away from paid employment such as women with children, small businesses who do not fully participate in the superannuation guarantee system, and those that are unable to contribute for long periods due to issues such as illness or having unpaid (yet critical) roles as carers for others.

An important part of the challenge to provide adequate retirement income is to improve and simplify incentives to make voluntary contributions. This is increasingly becoming a policy priority, given the findings of the Inter-Generational Report about the future rising cost of our ageing population, which imposes a Government funding constraint on expanding the role of the first (safety net) pillar. In addition, the business competitiveness constraint makes lifting the guarantee level above 9% a challenge. Without boosting voluntary contributions, the likely outcome is greater safety net dependence or inadequate self-funded retirement income streams for many Australians.

Hence the bulk of the comments we make in this submission principally address the need to improve the rate and level of voluntary contributions over the long term.

### Q3.1 An acceptable retirement income system

It is important that the retirement income system considers the needs and preferences of individuals before and after retirement.

The low level of voluntary contributions and dissatisfaction with the adequacy of retirement income for many groups suggests that many Australians find that the current retirement income system limits flexibility, and disincentivises people from making voluntary contributions to superannuation over the longer term.

For instance, the existing system prohibits withdrawals on contributions before retirement, and fails to reward long term savings over short term savings in rewarding tax benefits at retirement.

This links closely to the (unmet) objectives of the retirement income system if the incentives to make voluntary contributions over the longer term are undermined, which results in over-reliance on other pillars to provide adequate income in retirement.

To improve flexibility and reflect the diverse needs of Australians, it is important that the retirement income system creates appropriate incentives for individuals to allocate their savings for future use, and be flexible enough to accommodate the wide range of work and retirement patterns.

To ensure that the system is flexible and more able to encourage voluntary contributions, the review should consider the following.

- Create a more understandable and more significant set of incentives for individuals to make contributions (above the mandated 9%) to their retirement income.
- Promote long term savings by incentivising individuals to save just as much in their early years as when they approach retirement. Currently many younger people are not convinced on the merit of making extra contributions to superannuation due to retirement being decades away and other financial goals such as home ownership being of stronger focus.
- Be flexible enough to reflect the diverse working arrangements and saving patterns of individuals and families.
- Have broad based coverage to ensure that all retiring persons have sufficient retirement income to meet their essential needs to minimise the need to rely on income from the Aged Pension.

These features could be improved by the following:

- Introducing a mechanism to recognise, and reward for, the length of time for which people have saved.
- Providing flexibility around the age of retirement to reflect the decisions of many Australia's to work beyond age 60, take career breaks, retire early, be semi-retired etc in ways that does not disadvantage retirement savings.
- Expand the ability to make modest or specific purpose pre-retirement withdrawals to improve the perceived flexibility/attraction of superannuation. Expanding the ability to

access super early may also need to be subject to the maintenance of a designated minimum balance that increased with age to further encourage voluntary contributions.

## Q5.1 A simple and approachable retirement income system

It is widely accepted that the current retirement income system is too complex and difficult to understand, which leads to informed decision making. Improvements to improve these aspects of the system include the following:

- Improve the ability of Australians to make informed decisions about retirement by reducing the complexity of products, and require greater transparency on superannuation fees and commissions, with prescribed maximum levels.

- To improve transparency on future income available from the Aged Pension and thereby encourage planning, consider setting the Pension at a fixed proportion of average weekly ordinary time earnings.

## Q6.1- Q6.3 A sustainable retirement income system

There are several changes to various parts of the retirement income system that could improve its sustainability. These include the following:

- Examine the need to reform pension eligibility criteria to better control gaming behaviour utilised by some people. For example, people taking superannuation as a lump sum and then deploying these funds with related parties (eg the mortgages of family members) before seeking access to the safety net pension.

- Allow non-superannuation money to be paid into retirement income streams after retirement.

- Explore more options for providing self funded retirees that do not qualify for the Aged Pension with other means of support, possibly through the Commonwealth Senior's Health Card, subject to appropriate means testing.

- Better target eligibility to the Aged Pension to those most in need, such as through excluding access to people with property valued at more than $1million, or say 3 times median average national house values.

- As part of an overall strategy to improve the targeting of current concessions, reduce the emphasis on contributions taxes. This may not lead to greater demands on the budget if the reduction in front end tax increases final retirement income, thereby reducing the reliance on social security benefits. A reduction in contributions tax should be prioritised over reductions in personal income tax to promote savings rather than over-stimulate consumption.

We hope that these comments assist the review to make a series of adjustments to improve the adequacy of retirement savings through better use of the voluntary contributions pillar, and improve the sustainability of the system by making it more flexible for all Australians.

We would be happy to further elaborate on this views and can be contacted on (02) 8266 2765.

Yours sincerely

Scott Lennon
Partner

Tim Cox
Partner