

Superannuation as a social policy - Retirement adequacy

The superannuation savings of Australians (until recently) were estimated as as much as \$1.8 trillion, and as such superannuation has a major economic impact for Australia. For example, the Australian Workers Union has signaled increased contributions are part of its preferred policy approach, not to ensure adequate retirement, but to counter any trends towards increased inflation¹. Superannuation plays a vital role² by creating savings which maintain the current account deficit at reasonable levels.

Because of the economic importance of superannuation savings there is considerable input into policy decisions from the finance and economic sectors. The Superannuation portfolio sits in Treasury, not in Department of Families, Housing, Community Services and Indigenous Affairs (FaHCSIA) which covers pensions.

There are many players in the discussion, such as ex-Prime Ministers, Ministers, Trade Unions, the Superannuation Industry, superannuants themselves, the Reserve Bank of Australia, finance industry and the Taxation Department (to name a few).

Australia was one of the first countries to introduce an old age pension in 1909. These pensions were (and still are) funded from general revenue. The pension was designed for poverty alleviation rather than as a comprehensive income support¹. However, by around the 1980s the uptake was around 85% as the system took the nature of a general entitlement.

Voluntary superannuation was also an important part of retirement planning for many, but had tended to be mainly among high income earners and public sector employees.

¹ Nielson, I. Superannuation contributions – the soft option, Research Paper, Parliamentary Library, 13 March 2008, No. 22, 2007-2008

² Edey, M. and Simon, J., Australia's Retirement income system: Implications for saving and capital markets. Research Discussion Paper 9603, Economic Research Department, Reserve Bank of Australia, September 1996.

In 1985 a new social policy was introduced which aimed to increase the self funding of old age. Its intention was to shift reliance on pensions to self funded retirement through superannuation for all working Australians. This was compulsory superannuation in which employers were required to make a 3% contribution. This came about in ACTU negotiations where the benefit was taken in lieu of a general wage increase, and was applied in employment awards.

The view taken at the time by Paul Keating, the then Prime Minister, was that superannuation should become an income replacement tool which would have workers' leave work on the same salary they had when they were working³. To achieve this, a compulsory super level of 15% would be required. By the end of Keating's term the compulsory level had risen to 9% and has subsequently remained at this level.

According to Paul Keating at a recent OECD conference on retirement three key points made by the former Pensions Commission Chairman from the UK were:

1. People are living longer and therefore they can't move onto the pension until they are in their 70s
2. The demographics of the baby boomers means there will be so many people on the pension they will have to reduce it
3. And called for the need to move to anti-destitution model (rather than an income replacement model).

In the view of Keating, Australia is not in such a situation because of the 9% contribution rate, but there are still concerns that this will not prove adequate for retirees.

Wayne Swan and Nick Sherry stated in November 2007 that an incoming labor government would not support raising the employer contributions to 15%, but "noted that it would be desirable to see additional incentives leading to a total superannuation contribution rate of 15% of a person's earnings"¹.

³ 7.30 Report interview with Kerry O'Brien 8 August 2008

The Combined Pensioners and Superannuants Association see an increase as necessary to ensure retirees have sufficient funds⁴. The Australian Superannuation Funds Association also believes the level needs to be increased⁵.

However, according to Neilson (2008) there is disagreement amongst experts about the ability of the current retirement income system to product an adequate retirement income – the 15% target might not be necessary. Some of this uncertainty results because there are still not retirees who have had their entire working life with compulsory superannuation.

Nonetheless there is definitely concern about the level of savings from various quarters, and the government (or opposition for that matter) has not yet taken a definitive position on what the rate should be, or how to attain it. On the agenda is removal of the 15% contribution tax, an increase in compulsory employer contributions beyond the existing rate of 9% and a new system of so-called "soft compulsion" that would see salary increases take the form of increased super contributions⁶. Other matters being discussed include an extension to the co-contribution scheme - where the Government matches the after-tax contributions of low-income earners - and improved access to salary sacrifice arrangements. Further topics include that no commissions be paid to intermediaries when contributions are paid into default funds, and a call from the Australian Institute of Superannuation Trustees for a super baby bonus, with money paid into a woman's super fund when she has a baby.

The tax option is being reviewed under the Henry Tax Review and Minister Nick Sherry is awaiting the results of that review before commenting⁷.

It appears the superannuation industry (Australian Superannuation Funds Association) has started to advocate a specific solution. The approach being advocated is a system called 'soft compulsion'.

⁴ ABC, The World Today – Pensioners back Keating's call for super boost, 7 August 2008

⁵ ASFA Conference 2007, Consumers give thumbs up to soft compulsion in super, research finds.

⁶ SMH 19 March 2008

⁷ ABC, AM, Keating hits out at Rudd over superannuation, 7 August 2008

Soft compulsion' is a way for individuals to voluntarily make regular extra contributions to super, by committing an extra 1% of wages per year (in addition to the 9% Super Guarantee). This would be up to a maximum of 3%. This could happen when an individual receives a wage increase or starts a new job. Individuals can stop the extra contributions at any time⁵.

This system assumes there will be inertia and procrastination in 'opting out' and therefore peoples' superannuation savings will increase ensuring adequate provisions for retirement.

Senator Nick Sherry has acknowledged some of the benefits of soft compulsion but stated "I'm pretty cautious about it because of the regulatory complexity, which would be another set of regulatory complexity we have to deal with in our system"⁸.

The chief executive of Australia's largest legal industry superannuation fund believes compulsion tactics will exacerbate Australians' general disengagement with their superannuation and undermine government and industry efforts to improve financial literacy⁹.

The working public does not seem to have yet had a voice on this subject, although the ASFA has undertaken survey research canvassing Australians about the scheme.

In Summary

In spite of the lack of clear evidence that super contributions need to be raised, the suggestion has a lot of support from different quarters – some of it relating to the financial markets, rather than retirement. The political parties are not yet prepared to take a position on this suggestion, and it may indeed recede once the recent media attention over Paul Keating's comments fades. The idea of soft compulsion to increase contributions has been met with a soft reaction, although it has been proved an effective way to increase savings levels.

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⁸ Sky News Australia, Sunday Agenda Sunday, 16 March 2008, 12.00 pm

⁹ MoneyManagement.com.au, http://www.moneymanagement.com.au/Articles/NEWS-UPDATE-Soft-compulsion-tactics-offtarget_0c05463d.html