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Barton Deakin Brief: Retirement Income Review

20 November 2020

Overview

Treasurer the Hon. Josh Frydenberg MP and Assistant Minister for Superannuation, Financial Services and Financial Technology Senator Jane Hume released the final report into retirement income today.

The review concludes that the retirement income system is "effective, sound, and its costs are broadly sustainable." There are no specific recommendations in this review, but the Government is expected to consider its observations in the design of future policy.

In broad terms the review suggests that the three pillars of retirement income are working effectively to support Australian retirees. However, the retirement system is complex and there is a need to improve understanding of the system. The system would benefit from a clear objective to establish a performance assessment framework and guide future policy.

Background

This review was announced in September 2019 following a recommendation of a Productivity Commission review into efficiency and competitiveness in superannuation. The independent panel comprised Mike Callaghan AM PSM as Chair (former IMF Executive Board member and Treasury official), and Carolyn Kay (Future Fund Guardian) and Deborah Ralston (RBA Payments System board member) as panel members.

The terms of reference sought to identify: how the retirement income system supports Australians in retirement; the role of each pillar in supporting Australians through retirement; distributional impacts across the population and over time; and the impact of current policy settings on public finances.

Key Observations

- A significant number of older Australians who are renting in the private market need additional assistance. Increasing the rate of Commonwealth Rent Assistance will only have a small impact. A new approach is required.
- The system favours home owners, such as through the exemption of the principal residence from the Age Pension assets test.
- The weight of evidence suggests that increases in the Super Guarantee rate result in lower wages growth, and would affect living standards in working life.
- Other than for lower-income earners, replacement rates that compare income in retirement with income while working are the most appropriate basis for assessing whether the

retirement income system delivers adequate retirement incomes. Replacement rates align with the objective of achieving a reasonable balance between living standards in working life and retirement. The suggested benchmark replacement rate is 65-75 per cent.

- Under the legislated increase in the SG to 12 per cent, the projected replacement rate for future retirees with typical working lives exceeds the suggested 65-75 per cent benchmark rate across most income levels.

- More efficient use of savings in retirement can have a bigger impact on improving retirement income than increasing the SG. If the SG remained at 9.5 per cent, and retirement savings were used more efficiently, most people would achieve 65-75 per cent replacement rates.

- Using superannuation assets more efficiently and accessing equity in the home can significantly boost retirement incomes without the need for additional contributions.

- A range of measures could help people have the confidence to use their assets more effectively, including focusing retirement planning on income streams rather than balances, better quality and more accessible advice and guidance, and advancing the concept of the Retirement Income Covenant so funds guide members into effective retirement strategies.

- The Pension Loans Scheme is an effective option for accessing equity in the home for both age pensioners and self-funded retirees. The current exemption of the principal residence from the Age Pension assets test is a disincentive to using the equity in the home to support retirement incomes.

- Changes raised by stakeholders that could improve the fairness of the retirement income system include removing the $450-a-month threshold when the SG is paid; paying the SG on employer paid parental leave and the Government's Parental Leave Pay; giving greater visibility of superannuation balances in divorce settlements; extending the SG earnings base to include overtime; and ensuring people receive the SG they are entitled to, such as by paying the SG at the same time as wages and better enforcing sham contracting laws.

- The design of superannuation tax concessions increases inequality in the system. Tax concessions provide greater benefit to people on higher incomes.

- Government expenditure on the Age Pension as a proportion of GDP is projected to fall slightly over the next 40 years to around 2.3 per cent. The cost of superannuation tax concessions is projected to grow as a proportion of GDP and exceed that of Age Pension expenditure by around 2050. This is due to earnings tax concessions. The increase in the SG rate to 12 per cent will increase the fiscal cost of the system over the long term.

- The evidence suggests that tax concessions encourage saving in tax-preferred forms, but they may displace other forms of saving and have a limited impact on overall saving.

- There are areas where superannuation tax concessions are not a cost-effective way to help people achieve adequate retirement incomes. In particular, the cost of the earnings tax exemption in retirement will grow faster than the growth in the economy as the system matures and provides the greatest boost to retirement incomes of higher-income earners.

For more information:

- Minister’s Press Release
- Final Report

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