

ISN BRIEFING
NOTE

INTEGRITY IN AUSTRALIA'S SUPERANNUATION SYSTEM

INDUSTRY SUPER'S
BLUEPRINT FOR
AUSTRALIA'S
SUPERANNUATION
SYSTEM

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Industry
Super
Network

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About Industry Super Network

Industry Super Network (ISN) is an umbrella organisation for the industry super movement. ISN manages collective projects on behalf of a number of Industry Super Funds with the objective of maximising the retirement savings of five million industry super members. Please direct questions and comments to:

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| FOREWORD

Industry Super's Blueprint for Australia's Superannuation System

Industry Super Funds are broadly supportive of Government measures that have arisen from the three reviews into the taxation system and the superannuation and financial planning industries.

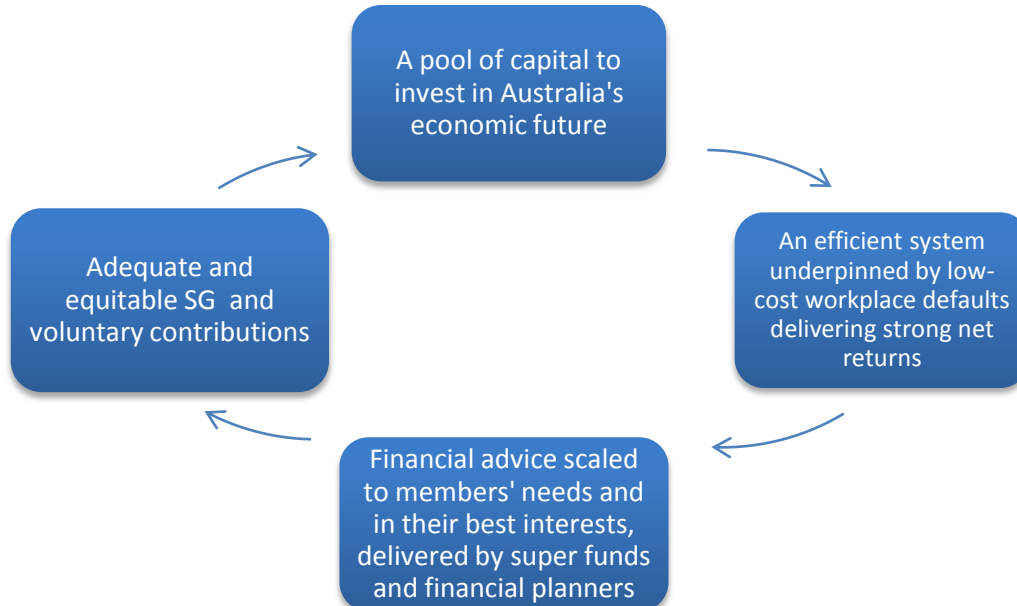
Carefully implemented, the proposed reforms will supercharge retirement income, providing dignity for Australians in retirement as well as building a formidable pool of capital to reinvest back into the economy to support jobs, productivity and wages.

Getting the policy settings for superannuation right will enhance the integrity, confidence and trust in the system and limit the need for future policy changes.

ISN's blueprint to build integrity, confidence and trust in the system includes:

- Low-cost workplace default funds delivering strong net returns determined through Fair Work Australia (FWA) and industrial parties;
- Financial advice which is scaled to members' needs and in their best interests; and
- A contributions system which is equitable and delivers members adequate retirement incomes.

These steps are the building blocks for a super system that is becoming one of the key economic foundations of Australia's future.



| EXECUTIVE SUMMARY

Superannuation is one of Australia's greatest public policy success stories. Prior to the introduction of the Superannuation Guarantee (SG) in 1992 and the National Wage Case decisions that preceded it, superannuation was the preserve of a minority of Australian workers who were employed in the public sector or who were highly paid executives in the private sector. Today almost all Australian workers can look forward to a better standard of living than can be provided by the Age Pension alone.

Since the inception of the SG, the system has gone from strength to strength. Today the superannuation system comprises over \$1.2 trillion in assets and this is estimated to almost triple in size to \$3.2 trillion by 2022.

The system has become much more than just a retirement savings vehicle. During the recent Global Financial Crisis (GFC) Australia's superannuation system acted as a critical pool of capital in the economy. In doing so, the Australian superannuation system provided liquidity and bolstered confidence, asserting itself as an important macroeconomic stabiliser.

The superannuation system is also a significant contributor to innovation and capital deepening in the Australian economy. As members' contributions are received they are invested back into the economy in a multitude of ways, supporting growth and jobs.

1.1 Setting the system up for the future

Despite our superannuation system being the envy of many advanced economies, there are a number of weaknesses that must be addressed. Under current policy settings, the system will not meet the retirement income expectations of a large proportion of Australians. There is too much leakage from the mandatory system due to fees and commissions prevalent in the retail fund sector, and around half of Australians do not make the additional voluntary contributions necessary to bring their retirement incomes up to scratch.

Given the compulsory nature of superannuation, the government and the financial services industry have a higher duty of care to fund members. This is compounded by the low levels of engagement amongst members.

At an aggregate level there is a strong case to suggest the \$22 billion in annual tax concessions are not delivering the best possible national savings outcomes. This is a concern for taxpayers, not only now, but also in the future should the superannuation system not take pressure off the Age Pension system as intended.

Getting the policy settings right now will ensure the system maximises retirement outcomes, builds confidence and trust in the system, and reduces the need for future policy changes.

1.2 An efficient system

Maximising the efficiency of the superannuation system can be best delivered through low-cost defaults delivering superior net returns, the publication of transparent fund performance data, and modernising the administrative systems to reduce transaction costs and duplication.

1.2.1 Strong workplace defaults

Almost all employees have the right to choose their own super fund. However, the majority of workers do not choose and rely on the default arrangements at their workplace. Further, there is very little switching between funds.

The government has a duty of care to ensure the regulatory framework protects their interests as fund members and, given the significant tax concessions at stake, it is a public interest necessity that default funds are low cost and provide superior net returns.

ISN has advocated for a transparent process to determine workplace default funds and this precludes a process where employers alone select the fund.

Suitable objective criteria should be established to determine funds that are eligible to be workplace default funds. These objective criteria should set a high bar and included within the MySuper framework. Setting a high bar is essential to ensure only funds which deliver strong net returns and appropriate member services are eligible to be selected as a workplace default fund. .

Under the auspices of FWA industrial parties (employer associations and unions for Awards) and employers and employees/unions for enterprise agreements should select workplace default funds from the list of eligible funds. This bipartite approach is fundamental for the integrity of the system. This bipartite approach should extend to the tendering of corporate funds and/or large employer contracts.

1.2.2 Super fund performance League Tables

For members who exercise 'Choice of Fund' and seek to choose a fund other than their workplace default, transparent reporting of super fund performance is fundamental. Industry Super Funds support the publication of whole of fund Rates of Return (ROR) superannuation performance League Tables by the regulator, Australian Prudential Regulation Authority (APRA). Industry Super Funds also support the publication of League Tables by private agencies on the basis that reported returns are net of all taxes, fees, commissions and other costs.

1.2.3 Modernising administrative systems

Administrative systems need to be modernised to reduce transactions costs and to consolidate inactive accounts for the majority of members who do not deliberately have more than one super account. Tax File Number (TFN) matching and mandatory electronic data standards will reduce administrative costs for members and, all things being equal boost net returns. The reforms outlined in the Cooper Review's Superstream proposals would deliver these outcomes.

1.3 Financial advice scaled to member needs and in their 'best interests'

Sales commissions, other incentive payments and fees are siphoning billions of dollars a year from the superannuation savings of Australian workers. Commissions are often presented as an affordable way of paying for financial advice however the structure of the payments means fees are deducted long after any service is provided.

Commissions and like payments are not only expensive, they can act to distort financial advice provided to consumers resulting in underperforming or risky products being recommended.

The solution is clear:

- A fiduciary duty should be introduced to ensure financial advisers act in the 'best interests' of their clients;
- All conflicted remuneration practices and structures (including commissions, ongoing asset-based fees, volume rebates, soft dollar commissions and conflicts inherent in platforms need to be prohibited (including on risk products available through superannuation) and replaced with transparent fee for service charges;
- Effective annual opt-in arrangements to ensure individuals are only charged for services provided; and
- There should be an expansion of scalable intra fund advice to provide an efficient low cost means for workers to obtain financial advice tailored to their circumstances.

Financial advice reforms based around these principles will transform the industry and result in an expansion of lower cost tailored advice (often delivered through the use of new technologies) appropriate to an individual's circumstances.

1.4 Adequate and equitable contributions

Central to the success of Australia's mandatory superannuation system is the provision of generous tax concessions on contributions and super fund earnings. However, due to changes in the structure of Australia's personal tax system, a large proportion of the Australian workforce does not receive its fair share of the tax concessions. Part of improving the adequacy of the system is not only to lift mandatory contributions but to also ensure all employees receive equitable tax concessions, and for older workers, the flexibility to adjust their contributions as circumstances permit.

1.4.1 Tax concessions

Over three million low and middle income earners currently obtain no tax concession on their mandatory super contributions with some of the lowest income earners paying more tax on their contributions than their ordinary income.

More progressive contribution tax arrangements are needed to ensure low and middle income earners obtain more equitable superannuation tax concessions.

Under existing settings, the largest tax concessions typically accrue to the highest income earners who are likely to save in any case. The demographics and member balances of the SMSF sector see a disproportionate share of the estimated \$24 billion in tax concessions on superannuation accrue to this sector (Treasury 2010).

1.4.2 Contribution caps

The lifecycle savings patterns of most individuals means they often don't have the discretionary income for additional saving when they are raising a family and repaying a mortgage.

Concessional contribution caps need to take this into account and permit older workers to make catch-up contributions to their super. The concessional contribution cap for over 50s should remain at \$50,000 per annum rather than being halved in 2012.

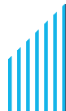
1.4.3 Lifting the SG to 12 per cent

Even when mature, the nine per cent SG is not sufficient to provide an adequate retirement income for most Australians. Only around half of workers make the additional savings necessary to top up the SG to a reasonable level, the other half don't.

A phased increase in the SG from 9 to 12 per cent is the most efficient and comprehensive means to raise retirement incomes, with little offset in other private savings.

Combined with the efficiency and equity measures outlined above it will be sufficient to raise retirement accumulations by between 50 and 75 per cent.

A combination of measures have the potential to increase the pool of savings available to be invested in the economy by around half a trillion dollars over the next 25 years.



2. Towards a more efficient system

2.1 Market failure in Australia's superannuation system

Superannuation is a creature of regulation and therefore regulatory change can have a substantial beneficial or deleterious effect on individual savings and aggregate national savings.

The majority of consumers are passive and disengaged in their superannuation; a majority of workers do not choose their own super fund and members excessively discount their future needs.

The lack of consumer sovereignty has led to market failure that in the short to medium term can only be addressed through changing the regulatory settings.

Since the introduction of fund choice the proportion of individuals choosing to change their super provider has been steadily falling from 6.5 per cent in September 2005 to 2.5 per cent in June 2009. In 51 per cent of instances individuals switch only because they change jobs.

Member inertia, low levels of engagement and distortions in financial advice is hindering a shift in the market towards better value, better performing products and resulting in market failure.

Research by ISN has shown that there is a negative relationship between fees and performance – for every 1 per cent extra paid in fees, net performance falls by 1.5 per cent. Millions of workers are members of higher cost, lower performing retail funds by default and the effects on national savings are quantifiable and profound.

2.1.1 Strong workplace defaults

Table 1 shows the long term underperformance of the retail super sector compared to Industry Super Funds. This underperformance is caused largely by higher fees and the twofold effect of sales commissions – not only to directly erode members' savings, but to direct savings away from better performing Industry Super Funds to underperforming retail funds.

Table 1: Retail super funds' underperformance in annual net returns

SOURCE	Period	No. of years	Basis	Retail super funds (per cent)	Industry Super Funds (per cent)	Difference (percentage points)
APRA	1997-2009	13	Whole sector rate of return	3.59	5.47	1.88
SUPERRATINGS	2000-2009	10	Median fund net benefit	3.70	5.72	2.02
RAINMAKER	2004-2009	6	Large fund average net return	4.99	7.20	2.21

Sources: APRA (2009), SuperRatings (2010) and Rainmaker (2009).

2.1.2 The drain on national savings caused by market failure

The retail sector uses financial planners as its main distribution mechanism and commissions make up 85 per cent of financial adviser revenue.

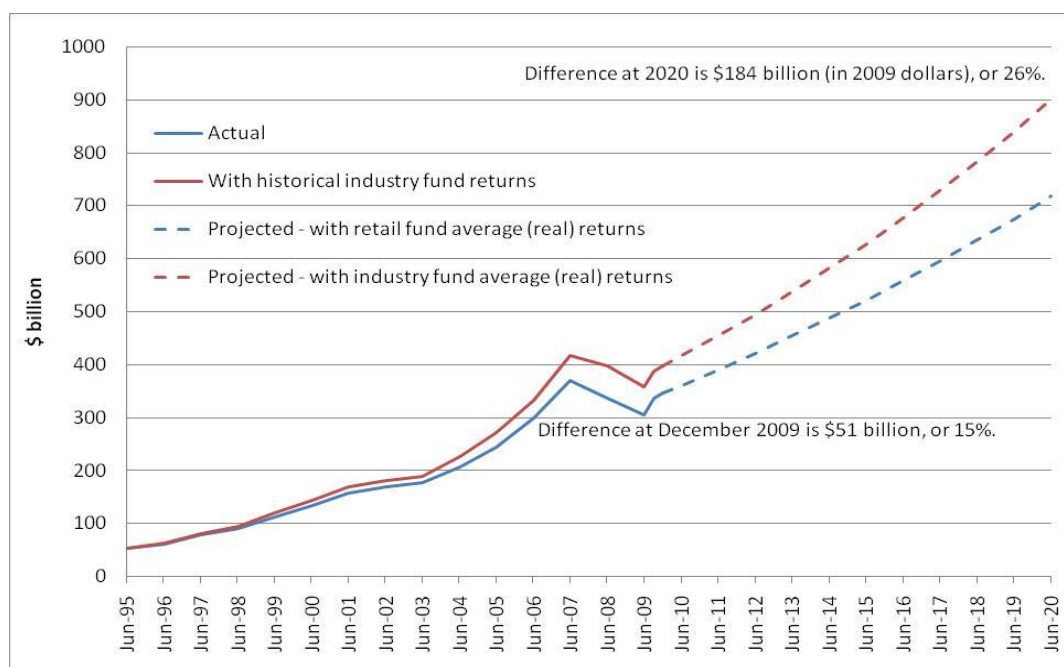
Commissions paid by retail super funds to financial planners are an inertia cost in the super system and are deducted from member accounts even if there is no service provided. Over 4 million retail fund members are paying commissions for advice which they don't receive.

Between 2006 and 2009 it is estimated \$6.5 billion in commissions was deducted from member accounts. In 2009 \$1.5 billion was deducted (43 per cent on mandatory SG contributions).

The difference between the performance of Industry Super Funds and retail super funds has a material impact on aggregate superannuation savings and the cost will continue to compound for each additional year that the problem is left unaddressed. The chart below shows the impact on superannuation savings had the retail funds sector achieved average industry fund returns.

Commission remuneration for financial advisers has resulted in a significant drain on national savings and will increase reliance on Age Pensions into the future, triggering additional pressure on the Commonwealth Budget.

Chart 1 – Lost Savings in the Retail Funds Sector



This loss of savings not only reduces individuals' retirement accumulation, it will impact on government finances through increased Age Pension outlays, and it reduces the pool of savings available to be invested in the economy, potentially detracting from future economic growth.

For a typical member on \$50,000 a year the difference in performance (due to fees only) will amount to around \$78,000 by retirement (SuperRatings).

2.2 Strong workplace default funds set through bipartite agreement

Given the extent of consumer disengagement and low levels of switching the most efficient way to address systemic underperformance is to strengthen arrangements for setting workplace defaults and have adequate protections to ensure workers' accounts are not automatically 'flipped' to more costly funds upon changing employment.

To achieve a system of strong workplace defaults, ISN has proposed:

- A transparent process to determine workplace default funds should be established and this precludes a process where employers alone select the fund.
- Suitable objective criteria should be established to determine funds that are eligible to be workplace default funds. These objective criteria should set a 'high bar' and included within the MySuper framework. There should be high barriers to entry to be eligible to become a workplace default fund.
- Under the auspices of FWA industrial parties (employer associations and unions for Awards) and employers and employees/unions for enterprise agreements should select workplace default funds from the list of eligible funds. This bipartite approach is fundamental for the integrity of the system.
- This bipartite approach should extend to the tendering of corporate fund and/or large employer contracts.
- There should be protections to ensure individuals accounts are not automatically 'flipped' into a more expensive fund on leaving employment.

2.3 Transparent and comparable fund performance data

There is growing recognition of the importance of transparent and consistent data on superannuation investment returns. Since June 2009, APRA has been publishing whole-of-fund ROR, so members can assess the effectiveness of their trustee's overall investment strategy. The Cooper Review has recommended that super funds report both gross and net returns, according to uniform standards set by APRA.

Data published to date clearly demonstrate that fees and commissions erode the retirement savings of super fund members. ISN's *Supernomics* report found that there is a persistent but negative relationship between price (fees and commissions) and performance (net returns). On average, for each additional 1 per cent of assets per annum paid in fees and commissions, net returns fall by almost 1.5 per cent.

ISN's analysis of APRA's quarterly superannuation statistics reveals that over the 15 years from June 1995 to June 2010, the industry super fund ROR averaged at 6.55 per cent per annum, while the retail super fund ROR averaged at only 4.67 per cent. These findings are consistent with League Tables published by private ratings agencies.

Industry Super Funds have long argued for the publication of superannuation League Tables, and that data be presented net of tax and all fees and costs. This approach enables members to see what ROR they will actually receive. It also accords, with the recommendations of the Cooper Review Panel, which declared in its report, that:

'It is illogical and misleading for investment returns to be reported to members on anything other than an after tax-basis and after all costs have been deducted.'

ISN supports the publication of League Tables by the regulator and private agencies so long as the reported returns are net of all taxes, fees, commissions and other costs.

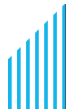
2.3.1 Reforms to administrative systems

Administrative systems need to be modernised to reduce transactions costs and to consolidate inactive accounts.

Currently, an unacceptably high number of transactions in the super system are paper based, adding unnecessarily to administrative costs paid by members.

Also, the inability to use the TFN as a unique identifier in the super system has compounded the problem of multiple accounts. These are inefficient as multiple administrative fees and insurance premiums are deducted reducing overall net returns to members.

TFN matching and mandatory electronic data standards will reduce administrative costs for members and all things being equal boost net returns.



3. Reforming financial advice

Financial advice is typically seen through the prism of the financial planning industry and a bias towards higher net worth retail investors. Instead, financial advice should be seen through the prism of how to make financial advice accessible, affordable and suitably scaled to all Australians with compulsory super and other financial advice needs.

3.1 Demand for financial advice

ABS statistics reveal that outside property and super, the investable assets of most Australian households are negligible.¹ The average balance of a superannuation account in Industry Super Funds is \$16,600.²

While Industry Super Funds are very cognisant of the positive role that financial advice can play in bettering the financial outcomes for their members, the needs of most members, especially in the earlier stages of accumulation are reasonably straightforward and generic in nature.

To test the level of demand for financial advice, ISN commissioned Forethought Research to undertake an important study into the attitudes of Australians with respect to financial advice in late 2009.

Forethought Research surveyed 804 adult Australians with superannuation about their demand for financial advice in the two years to November 2009, and the results were as follows:

- Two-thirds of all respondents sought no advice at all in the two years between November 2007 and November 2009.
- Less than 20 per cent of workers earning under \$100,000 sought ongoing complex financial advice in the two years to November 2009.
- Less than half of those seeking financial advice (13.8 per cent of all respondents) obtained ongoing complex advice from a financial planner.
- The two most popular matters of advice – tax/entitlements from government and mortgages/loans – are not regulated matters and were overwhelmingly delivered by tax agents and mortgage brokers.
- The next most popular matter of advice was investment choice within superannuation, with superannuation funds being the preferred provider.
- Forethought's survey also confirmed that the major consumers of full financial advice are high wealth individuals and those close to retirement. In the two years to November 2009, 82 per cent of respondents with an annual gross personal income less than \$100,000 did not seek ongoing complex financial advice.
- Moreover, over half of all respondents (of any income) who sought ongoing complex financial advice were aged 55 and over.

The Forethought Research confirmed the view long advocated by ISN, that only a small proportion of Australians seek financial advice and they tend to be higher net worth and close to or already in retirement, and that the vast majority of the population's financial advice needs are currently not being met by the mainstream financial planning industry.

¹ Australian Bureau of Statistics, *Household Wealth & Wealth Distribution 2005-6*, issued 9 November 2007

² APRA *Annual Superannuation Bulletin*, June 2009, see <http://www.apra.gov.au/Statistics/upload/June-2009-Annual-Superannuation-Bulletin-PDF.pdf>

3.2 Introducing a ‘best interests test’ and prohibiting conflicted remuneration practices

A ‘best interests test’ or fiduciary obligation on financial planners is necessary, but of itself is insufficient. Reforms are needed to prohibit commissions and other forms of conflicted remuneration on superannuation and other financial products. The introduction of transparent fee-for-service charging for financial advice is also necessary.

The regulatory reform framework should be weighted towards super given the tax concessions involved and that it constitutes two thirds of funds under management. In particular:

- Reforms must address poor consumer financial literacy and inertia costs;
- Fees should only be charged on services provided and expressed in dollars;
- Ongoing percentage-based fees are inappropriate for ordinary retail consumers as they could permit fees being charged when no advice is provided;
- Fees could be deducted from member accounts provided the advice meets the sole purpose test;
- Commissions should also not be permitted on risk products offered through superannuation (permitting them would result in a back door drain on savings); and
- Grandfathering could be considered so long as genuine reform is achieved, allowing the industry to transition effectively. The design of the grandfathering of commissions and other conflicted forms of remuneration should be carefully considered to ensure the integrity of the reforms. A process that entrenches the status quo must be avoided to protect passive and disengaged investors.

3.3 The importance of annual ‘opt-in’ provisions

ISN considers that asset-based or percentage-based fees should not be permitted as a way to charge for financial advice. The exclusion of such fees on leveraged products reflects the concern that such fees increase based on funds under management rather than service delivered to the client.

The government’s proposals to reform the financial planning industry ‘Future of Financial Advice’ permit the charging of asset-based fees on the condition that clients ‘opt-in’ on an annual basis. The only way that such fees can be permitted under a new advice regime is with an annual renewal requirement in the form of this annual opt-in mechanism.

3.4 Expanding intra-fund advice

Industry Super Funds have pioneered the provision of intra-fund advice to their members. Central to intra-fund advice is that it relates only to advice to a member about their existing interest in the superannuation fund.

ISN supports the expansion of topic areas that could be delivered through intra-fund advice on this basis.

3.5 Positive impacts of financial advice reforms

A shift to fee for service will reduce the average cost of financial advice and significantly increase demand. Rice Warner Actuaries has completed a study on the transformation of the advice industry and found:

- **The number of people obtaining financial advice will more than double.** By 2023, advisers will supply 1.64 million pieces of advice per annum rather than 733,000 if no regulatory change occurs. This is an increase of 125 per cent.
- **There will be a higher rate of national saving** as a result of the regulatory change. Total investment business (super and other investments) is anticipated to be \$117 billion higher by 2024. This represents a 10 per cent increase in saving compared to the no-reform scenario. The increases are driven by:
 - a reduction in commission income in 2024 of 0.24 per cent of GDP (\$2.5 billion in 2009 dollars or \$3.9 billion in future dollars), and
 - stemming the leakage of mandated SG savings and some additional saving from the increased provision of financial advice across the community.

Major retail institutions will need to transition from a business model built on distribution of its own products to making advice a profitable business in its own right. The reforms will require industry participants to innovate and provide better value superannuation and other financial services products.

4. Equitable and adequate compulsory contributions

Improving the adequacy of Australia's retirement income system will not only help improve retirement incomes but will also boost the pool of savings available for productive investment in the economy.

It is important to note that improvements in adequacy can be achieved through improving the efficiency of the existing system through financial services reform, account consolidation and back office efficiencies and more equitable distribution of tax concessions. However these measures alone will not be enough to provide an adequate retirement income for Australian workers.

4.1 Are we saving enough?

While many Australians are achieving substantial replacement rates through our three-pillar retirement income system, a substantial proportion are not.

- Around half of all workers will not undertake additional superannuation saving by the time they reach retirement;
- Most Australians, especially women, will not achieve SG contributions for a full working life after taking into account time out of the workforce for family, study, and illness;
- Existing behaviour suggests less than 50 per cent of accumulations are converted into income stream products in retirement (the balance is used to retire debt and allow some short term consumption);
- Replacement rate analysis undertaken by Treasury presents an overly optimistic outcome by assuming 100 per cent of accumulations are converted into a longevity income stream and a consumer price index deflator is assumed.

In short, the existing system will only be adequate for those who are employed for their full working life, make additional voluntary contributions, convert all of their retirement accumulation into a longevity income stream and are then satisfied with an income which falls below community living standards (wages growth).

The existing structure and distribution of superannuation concessions is inequitable, with more than 3 million low-income Australian workers denied comparable superannuation contribution tax concessions extended to higher income workers.

- A more equitable distribution of concessions has the potential to improve retirement incomes especially for low and middle income earners.
- Flexible contribution arrangements are also necessary to ensure older workers can make catch up contributions as their discretionary income allows.
- Compulsory contributions levels should be lifted to 12 per cent.

4.2 Existing taxation arrangements

Individuals often face complex choices about whether their contributions are made from pre-tax or post tax income to maximise their concessions. For some employees particular choices may not be available depending on their employer (for instance the availability of salary sacrifice).

Existing contribution tax concessions are highly contingent on individual circumstances, but the broad outcome is such that the concession increases in line with the tax wedge between the contribution tax rate of 15 per cent and an individual's personal marginal tax rate.

As a consequence the level of concession on an individual's SG component increases with income, although the outcome is not transparent or predictable due to the interaction of means tested tax offsets (such as the low-income tax offset) with the marginal tax rate schedule (see table 2).

Table 2. Superannuation tax concessions by income (assuming \$1,000 of SG savings)³

INCOME	Marginal tax rate	Contribution tax rate	Effective concession on contributions (%)	Marginal tax on \$1000	Cont. tax on \$1000	Concession \$
\$0	0%	15%	-15.0%	0	-150	-150
\$16,000	16.5%	15%	1.5%	-165	-150	15
\$30,000	20.5%	15%	5.5%	-205	-150	55
\$37,000	35.5%	15%	20.5%	-355	-150	205
\$67,500	31.5%	15%	16.5%	-315	-150	165
\$80,000	39.5%	15%	24.5%	-395	-150	245
\$180,000	46.5%	15%	31.5%	-465	-150	315

For low-income earners the concession on SG and any pre-tax contributions is negative as the contribution tax rate may be greater than their marginal tax rate. This impact is affecting more individuals every year as the effective tax-free threshold increases in line with the changes to the Low Income Tax Offset (LITO). Treasury has estimated there are in excess of 3 million tax payers who receive no benefit or a negative concession.

It should be noted that this will have a disproportionate impact on the retirement savings of women who comprise more than two-thirds of part-time workers which dominate workers on lower incomes.

4.3 More progressive contribution concessions

There are a number of ways in which contribution concessions could be made more equitable.

In its submission to the Henry Review, ISN proposed comprehensive reform which would involve abolishing the contributions tax and making all contributions to super (including SG) from after tax income. The concession could then be provided by a tax offset (or government co-contribution) paid at a flat rate equal to at least 25 per cent of the gross contribution. This tax offset (or government contribution) would be paid directly in to the member's account.

The approach adopted by the government can be implemented relatively quickly through refunding the contributions tax paid by lower income earners. In effect lower income earners would pay zero contributions tax as a consequence. This relatively simple measure would go a long way towards making the contribution tax concessions more progressive.

³ Includes impact of Medicare Levy and Low Income Tax Offset (2010-11 year)

Analysis by ISN suggests such an approach would add up to \$66,000 to the retirement payout of a low income earner over their working life.

4.4 Concessional contribution caps

The capacity for individuals to save varies considerably throughout their life time in line with income and consumption preferences.

Younger workers are often on lower incomes and use any available discretionary income for leisure activities or to save for a deposit on a home.

Typically the next phase involves an increase in income but additional responsibilities such as costs associated with raising children and servicing a mortgage. Often it is only as these responsibilities taper off that individuals have sufficient discretionary income to consider additional superannuation contributions.

Currently there is a concessional contribution cap of \$25,000 per annum for super. Any unused portion of the cap cannot be rolled over into a subsequent year. There are currently transitional caps for over-50s that permit a higher level of concessional superannuation contributions. The cap for over 50s is \$50,000 per annum but is due to phase down to \$25,000 from 2012.

The government's proposal to introduce a higher contribution cap for over-50s is an essential equity measure to enable older workers to make catch up contributions as their circumstances allow. A range of more flexible options for contribution caps should be considered in time.

4.5 Lifting the SG to 12 per cent

The most efficient and comprehensive way to improve the adequacy of the system is to increase mandatory SG contributions.

A recent OECD report has highlighted the importance of the mandatory 'second pillar' of compulsory retirement savings by noting that 27 per cent of elderly Australians solely reliant on the public pension have fallen into poverty, the fourth highest level in the OECD (behind Ireland, Korea and Mexico).

An increase from 9 to 12 per cent would provide a significant improvement in retirement outcomes. For example, a worker on average full time earnings would increase their retirement accumulation by around \$110,000.

Despite the decentralised nature of today's IR system, a phased increase in SG with sufficient lead time would be affordable for business and could be a matter for consideration in future wage negotiations just as it was as the SG increased from three per cent to nine per cent during the 90s and early years of the new millennium.

Increases in mandatory saving would be maximised if accompanied by financial services reforms and improved equity of tax concessions.

4.6 Combined outcomes of reforms

ISN has modelled the combined effects of the proposed reforms to the superannuation and financial planning industries. The most significant impacts are experienced by low and middle income earners who will increase their retirement accumulations by up to 77 per cent as a result of the three key reform areas.

Table 3: Combined impact of efficiency, equity and adequacy reforms

Income (\$ p.a)	15,000	30,000	36,000	45,000	60,000	90,000
Multiple of average earnings	0.25	0.50	0.60	0.75	1.00	1.50
Accumulation before reform	74,289	148,579	178,294	222,868	297,157	445,736
Accumulation after reform	131,397	262,794	315,353	335,063	446,750	670,125
Reform impacts						
12% Super Guarantee	32,849	65,699	78,838	83,766	111,688	167,531
Low income tax break	14,782	29,564	35,477	0	0	0
Commissions/efficiency	9,476	18,953	22,743	28,429	37,905	56,858
Total Gain	57,108	114,216	137,059	112,195	149,593	224,389
Per cent increase	77%	77%	77%	50%	50%	50%

5. National savings impacts and flow on investment

Boosting the SG combined with efficiency and equity measures will have a strong positive impact on the level of national savings in the economy, increasing the economy's resilience to external shocks and increasing the pool of funds available for productive investment.

Research undertaken by the Reserve Bank of Australia (RBA) has found that the SG is an effective mechanism to boost national savings as there is only a small offset to private savings. According to analysis by RBA researchers up to 90 cents in each additional dollar of SG contributions, flows through directly to increased net household savings.

According to the government, the reforms it has proposed will boost the aggregate pool of superannuation assets by at least half a trillion dollars over the next 25 years. There are exciting possibilities which flow from this:

- While a share of these additional savings will flow to equities and other financial instruments, a significant proportion would be available to finance nation building investment. Infrastructure is not highly correlated with the performance of equities so it is a prudent alternative investment within a balanced investment portfolio.
- Australia's infrastructure problems are well catalogued with governments often not having the finances or expertise to get projects off the ground and manage them efficiently. In the years ahead, the role of the superannuation sector in building and managing the infrastructure needed to keep the wheels of the economy moving will be critical.
- There have been some tremendous success stories – many from within the Industry Super Funds sector which have pioneered direct infrastructure investment.
- There are significant investments across a diverse range of sectors including renewable energy, airports, roads, ports, and social infrastructure such as hospitals and schools. As well as financing and managing critical infrastructure and the employment and social benefits that flow from it, the investments have delivered exceptional returns to superannuation fund members.

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