Our Response to Consultation Paper:
"Legislating the Objective of Superannuation"
And Associated Current Policy Discussion

Introduction: *As recipients of **Defined Benefit Pensions** from Commonwealth Superannuation Corporation (CSC), which cannot be commuted to a lump sum when needed nor can be bequeathed (i.e. **exhausted at the death of both partners**), we have **made savings via a self-managed superannuation fund (SMSF)** in order to meet certain large expenditures in the future. We were motivated to do so by the governmental policy failures and inadequate funding for the public hospital system as well as for retirement and nursing home accommodation.*

We are not alone in this way of thinking as there would be several hundred thousand families of retired public servants and military service men and women receiving Defined Benefit Income Streams who are facing similar concerns.

*Here, we present the case for a rethink how the Total Superannuation Balance is derived. We propose that the **'Current Residual Value'** of a Defined Benefit Income Stream, which takes into account the remainder of an individual's life expectancy, should be utlilised rather than the legislated 'Special Value'.*

We also address the broader question "What is the purpose of Superannuation Savings?"; and propose an alternative statement of its Objective.

1. The Objective of Superannuation

The Stated Objective of Superannuation is to **preserve savings** to **deliver income** for a **dignified** retirement, alongside **government support**, in an **equitable and sustainable way**.

We suggest the following changes to the above statement of the Objective:

1. Replace "income" with the words "**financial means**";
2. Replace "alongside" with the words "**minimising the need for**"; and
3. Add the words, "**reassured by stable government policy**", after the phrase "equitable and sustainable way";

so that the Objective reads as follows: "**The Objective of Superannuation** is to **preserve savings** to **deliver <u>financial means</u>** for a **dignified** retirement, **<u>minimising the need for</u>** **government support**, in an **equitable and sustainable way, <u>reassured by stable government policy</u>."**

2. Purposes of Superannuation in achieving a dignified retirement

We regard our preserved superannuation savings as having multiple purposes, all directed towards **'minimising'** or eliminating reliance on 'Government Support'. This is entirely consistent with the utterances of past Treasurers, in particular, Mr Paul Keating and Mr Peter Costello, who were rightfully concerned about the ever-growing demand on the public purse by people who had not saved sufficiently for their expenditure in retirement.

Purpose A: Regular Pension Income for a lifetime in retirement;

Purpose B: Lump Sum withdrawal: In the twilight of our lives, the ability to pay upfront money for a self-contained fully serviced unit in a retirement establishment (may need in excess of $1 million);

and / or to pay upfront money for a high care room in a nursing home (may need in excess of $600,000); in addition to the upfront payment, there is also the requirement to meet ongoing fees and charges of these retirement facilities.

Purpose C: Lump Sum withdrawal: Make use of our long standing private hospital insurance, to be treated in a private hospital and afford gap payments as well as pay for expensive privately provided ancillary services.

3. Discussion:

Above purposes of superannuation savings, if fully acknowledged and supported by appropriate and affordable concessional treatment by the Federal Government, would help retirees **to overcome policy failures and funding inadequacies of successive Federal Governments.**

What is wrong with the word "income" – why replace it with the term "financial means"?

The relevant Acts and Regulations of Australian Federal Parliament speak of a 'Retirement Income Stream 'emanating from a Retirement Phase account; such income is clearly distinguished from occasional 'Lump sum' withdrawals from an Accumulation Account. By replacing the word "income" with the term "financial means", a potential conflict with the language in the Acts and Regulations would be avoided.

Why should the phrase "reassured by stable government policy" be added?

We believe that certain Superannuation amendments which became effective in the last ten years or so would have eroded public confidence. There are many who believe negatively geared property investment is a better proposition for achieving financial means for retirement.

Current policy discussion, only highlighting the cost to the budget of Tax concessions for Superannuation, we suggest, should be balanced by a proper in depth analysis of the economic value of Superannuation savings. In particular, the cost to the budget, in the total absence of Superannuation savings should also be presented in the interest of informed decision making.

We wish to draw attention to two cases; **(A)** the reduction of the 'Cap' on concessional contributions (e.g., via salary sacrifice), from $50,000 to $25,000 about 10 years ago, without testing an individual's need for enhancing their Superannuation balance; and **(B)** the unjust 'Special Value' calculation applied to Defined Benefit Retirement Income Streams (2016/2017).

(A) The above mentioned 'Cap' on concessional contributions has evolved to something more restrictive, and has been applied in a broad brush manner. Now, the Federal Treasurer, and perhaps others, laments the poor total superannuation balance achieved by many women.
If this lament is genuine, then the 'Cap' should be replaced by a range of allowances that is higher where an individual's Superannuation Balance is still low upon reaching a certain working age. As a budgetary measure, the allowance should be gradually reduced to the Cap's current level, as an individual's Superannuation Balance surpasses a sustainable threshold.

(B) The unjust 'Special Value' calculation: with the advent of the 2016/2017 Amendments to the Superannuation Laws, annual Defined Benefit Income Streams were multiplied by factor 16 to derive its 'Special Value' for the purposes of the application of the Transfer Balance Cap.

Defined Benefit Income Streams, of the type paid to Federal Government Public Service and Military Service retirees, cannot be commuted to a lump sum and cannot be bequeathed upon the death of the retiree and the partner. For this reason, when converting a member's accumulated lump sum to an annual defined benefit income at the time of retirement, the remainder of the member's life expectancy was taken into account by CSC.

We wish to provide a specific example; A person retiring from the Australian Public Service at the end of FY 2014 at the age of 65 years, was given the option of either taking a maximum Defined Benefit Income Stream of $74,820 per annum (before Tax) or, in lieu of this entitlement, take out a lump sum amount of $770,161 (before Tax).

The principle applied by CSC is that the lump sum plus earnings over the remainder of that person's life expectancy **would be exhausted** if paid at the rate of $74,820 pa.

On the other hand, the 'Special Value' calculation yields $1,197,120 (16 * $74,820), irrespective of the remainder of life expectancy. The over-statement of value amounts to $426,959. This is not a minor matter; because this over valuation resulted in excessive commutation of that person's pension account in their SMSF (that excess was transferred to an Accumulation Account and 15% earnings tax applied from 1 July 2017).

This broad brush application of factor 16 in the calculation of 'Special Value' of a Defined Benefit Income Stream would not have passed the "pub test". For example, a person who was at an advanced age, say 85 years, would have been grievously disadvantaged should the calculated 'Special Value' have forced the commutation of pensions from other sources so as to meet the Transfer Balance Cap. In reality, the residual value of that person's Defined Benefit Income Stream would have been negligible.

For the same reason, in the present discussion of the higher tax threshold value for Total Superannuation Balance, that 'Special Value' must not be applied to Defined Benefit Income Streams; rather, a 'Current Residual Value' calculation, as proposed here should be introduced.

In the interest of equity, the methodology applied in the derivation of 'Current Residual Value' of a Defined Benefit Income Stream, should correspond to the methodology applied by the pension provider (e.g., CSC) in the first instance, as evident from the example provided above (when calculating a Lump Sum amount in lieu of the maximum Defined Benefit Income Stream). Most importantly, the remainder of life expectancy must be taken onto account.

RECOMMENDATIONS:

A. Consider the proposed alternative statement of Superannuation objective;
B. Replace the current 'Cap' on concessional contributions by a range of allowances that is higher where an individual's Superannuation Balance is still low upon reaching a certain working age;
C. Introduce a 'Current Residual Value' calculation for Defined Benefit Income Streams, as proposed above for the derivation of the Total Superannuation Balance, before applying the proposed higher tax threshold.

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