

Productivity Commission  
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## To whom it may concern

I read in the recent 13<sup>th</sup> October editions of “The Australian” and “The Canberra Times” articles on Mr Costello’s views on Superannuation and that your organisation was examining the idea that the Government itself should run default Super. I support that concept, and in 2015 I wrote the attached letter to a Federal MP outlining details as to how such a scheme could be developed. I would appreciate that letter be considered as a submission to the Productivity Commission in relation to that current enquiry. I have no record that I have already made this submission previously, but if I had made one, please ignore this submission.

The accompanying “letter” contains references to attachments. These have not been included in this electronic submission, but the data is available on the Internet, should you need to see it.

Yours sincerely

John Gregan  
*15 October 2017*

The Hon XXXX  
Parliament House  
CANBERRA ACT 2600

Dear X

I have been following the debate on superannuation and the age pension in “The Australian” and the “Canberra Times” in the lead up to the budget and subsequently. According to Judith Sloan in The Australian, 10 March “The real purpose of the age pension is to cover the reasonable living expenses of those with the fewest resources.” That may be the view of economists and ACOSS and the Greens, but it is not the view of the average tax payer. Most people feel that they pay taxes all their life and that some of that goes towards the old age pension. In European countries all citizens are entitled to a government age-pension on retirement. I have worked for a short time in UK and at home here in Australia (I still have a copy of my first tax return to the ATO in 1957) and see advantages in both systems. In the current debate one only sees the views of economists, journalists and politicians, never the views of “the average Joe” who is the end-point of all this activity. It was my understanding that the introduction of superannuation was to provide adequate funds for the average worker to cover their retirement living expenses and hence take the pressure off the old age pension. As Judith Sloan opines, quite clearly that has not worked. The problem is that in Australia we have tried to ‘privatise’ the pension, solely using insurance companies and other financial entities to market superannuation products, and as an “Australian” editorial rightly points out (21 April) “Super fees are sapping savings”. Not only that, but because superannuation is linked to the stock market, when retirees seek to access their Super they sometimes find that its value is less than their contributions over the years – hardly a recipe for a system to sustain old age – they would have done better to put it in a bank savings account and let compound interest work its magic.

According to the Constitution, the Commonwealth Government has the responsibility and the head of power (51.(xxiii)) to make laws to provide for “Invalid and old-age pensions”. The tax power (51. (ii)) covers income tax and applies to people who earn income, not to those who are unemployed or unable to earn income, in relation to income tax. However, ‘old age’ applies to everyone, whether they are earning income or not. The steps below could lead to a base universal age-pension in Australia and be adequately funded.

- Increase the retiring age to 68 or 69 – not 70. To most people, retiring at 70 sounds cruel (69 sounds better – like those car ads - 19,990 – drive away – but 20,000 sounds like a lot). This is more likely to pass through Parliament.
- People (tax-payers) feel their taxes, paid over their lifetime, should fund a universal basic government pension when they retire. I agree. See proposal below.

- Retirees who have been savers want a reasonable interest rate on their cash deposits. Introduce a Pensioner Bond Scheme as per UK where the interest is a bit better than what the Banks give.
- Super Funds and Insurance Companies who provide “super” products to have access to mandatory contributions from tax-payer during working life. See proposal below.
- After retiring age, a person can continue to work, without their employer or themselves having to make super contributions, but paying normal tax and receiving only the universal basic pension. (Same as politicians and public servants).
- Allow a component of ‘super’ contributions to be taken as a lump sum and another component as a private pension. See proposal below.
- Allow young people to borrow against their contributions to their super fund for their eventual lump sum to assist in the purchase their first home. See proposal below.

### **UNIVERSAL OLD-AGE PENSION**

- Introduce the PAYE system similar to what they use in Britain which has two components whereby they pay a slightly lower rate of personal income tax than we do in Australia but also pay an additional amount called the “National Insurance” which goes towards the old age pension and health costs. Put together, they amount to bit more than our rate of income tax payable. (I have enclosed copies of the tax scales of the two countries). The public in UK know that National Insurance is for their old age and is designed to cover their pension and some health costs and so are happy to contribute.
- The “Medicare Levy” here in Australia (2%) is similar to the healthcare component of the UK National Insurance levy, but we do not have an identifiable component of our income tax payable that represents provision for the old-age pension. In Britain the National Insurance levy is 12%. Currently, the Superannuation Guarantee of 9.5% of the employee’s salary is paid into a private fund by the employer. This does not impact on the employee’s pay packet and the employee does not see it as a deduction from the payslip. This 9.5% employers’ contribution should be paid to the Government in cash, and instead of going to the chosen private super fund it would go to a government “Pension Fund” similar to the “Future Fund” that was set up to cover the pensions of politicians and public servants. The employee would be not affected, and in effect, the Government would now have access to a new source of income (as in Britain) without imposing any new taxes. It is a win-win for the Government and the tax payer – Government has more money, and personal income tax is lower and a basic pension in retirement is assured.

From the employee’s point of view their contributions to this government scheme would not be linked to the stock market, as is currently the case with insurance/super funds and on

reaching the retirement age they would not find they are getting less than what they put in (whether that be for a lump sum and/or the basis for a private pension).

### **INSURANCE COMPANIES/SUPER FUNDS/BORROW**

- Naturally, these two industry groups would resent losing the 9.5% Superannuation Guarantee. To compensate, you could introduce a 4% (or 2%) mandatory payslip deduction (pre-tax) that goes to the fund chosen by the employee to be accessed on retirement **only as a private pension** from the fund. This is similar to what many are doing now as “salary sacrifice”, except that this proposal is mandatory (like the Superannuation Guarantee) and not voluntary. That is one element - and the 9.5% + 4% is much the same as the 12% for the National Insurance in UK, (plus in Australia the Medicare Levy.)
- Since 2007 the ‘voluntary’ side of super contributions out of the individual’s pay packet has dropped significantly as they saw what happened to their contributions when the stock market crashed. Hence the other element is to allow *voluntary* post-tax additional contributions (with or without limit) in superannuation investment (in funds for cash, shares etc – same as now), to be redeemed as a lump sum on retirement. Earnings derived from this latter investment towards a final lump sum should be taxed annually at 7.5% as recommended by the Henry Tax Review in 2009. This 7.5% tax is to be paid separately by the super funds at the end of each financial year directly to the ATO and not be aggregated with a person’s personal income, (similar to the scheme for taxing share dividends.) No tax should be paid on withdrawal at the time of retirement. The other aspects of the ‘voluntary’ contributions are:
  1. Employees can add extra money to the mandatory 4% contribution for a private pension, so as to have a bigger private pension on retirement, or alternatively use that extra private contribution as a lump sum, as outlined above.
  2. The money that is contributed to the lump sum component of super could be used ,after contributing for say 10 years, as collateral for a deposit for a first home, as recommended by the treasurer. This would be no different to the practice of using of money in Life Insurance policies to fund a house deposit.

The above proposals would seemingly suit all the players, particularly the Insurance/Super Funds. By keeping the universal basic government old-age pension at a modest level, employees would be encouraged to contribute more to the private sector. In UK, the current State Pension is GBP 151.25 per week (\$A302.50). That is only \$A15,730 per annum. If that was reduced to say \$A14,000 per annum for the new Australian universal pension, then that would encourage employees to contribute more into the insurance/superannuation sector, in order to obtain a better income in retirement. Of course, you would have to have a safety net, similar to the existing one, where those who have little assets or income on retirement will have to have a ‘top up’ on the base pension in order to survive. If the government gets the 9.5% Superannuation Guarantee (SG) to fund the base

pension, and because the SG is not taken out of their pay, the employees cannot complain that they have paid taxes all their lives and cannot get a pension but others can.

### **PENSIONER BOND SCHEME**

- The UK Government has introduced a “Pensioner Bond Scheme” whereby pensioners can buy special Government Bonds that yield a return greater than the usual bank interest. It provided billions of pounds for the government and made a lot of pensioners happy. We should have a similar arrangement here. The response in UK was dramatic. I have enclosed a short report on this issue.

Most people, as retirement approaches, realise they will need some cash as well as a pension. This is to buy that last car after a few years in to retirement, undertake inevitable home maintenance (painting, plumbing etc), funeral expenses, unexpected emergencies, and so on. They are very conscious of not having that hefty weekly salary coming in to sustain their living standards. This saved money they put in the bank and use the interest it generates to buy clothes or go on the occasional holiday etc. If the interest rate plummets, this presents a dilemma. They don't want to put the money under the mattress where it will earn nothing, but they also don't want a low return on their cash investment. Some are tempted to go back into housing or the stock market for an increased yield, but those investments can always go backwards and they are loathe to get back less money than they put in. But most of these people don't trust the stock market or housing or insurance companies any more so they suffer the low yields from a cash deposit. You saw that after 2007-8 when cash deposits increased dramatically. Offering them an alternative repository in the form of special bonds would not only help them but would also help the government. If the government is prepared to borrow money from outsiders and pay them X% interest why can't they do it from their own citizens? The British government has realised this and has created a new source of revenue (See enclosed copy of a BBC article).

## **Summary**

The above proposals lack micro detail which I am sure your Department could examine by appropriate economic modelling, and if proved economically feasible would stabilise the retirement income issue.

If people consider they pay taxes towards a government pension, they expect to get a pension. It has nothing to do with “a sense of entitlement” as pushed by ACOSS, doctrinaire economists and the Greens. It would remove a lot of anger in the electorate if everyone who paid their taxes in their working life got a base government pension, lower than what it is now. Those with other income sources in their retirement could have it reduced to a means tested part-pension, but never lose the fundamental entitlement, no matter how low their part-pension goes, even if it went down to a dollar. For most people it is the principle that counts. Those who do not have access to this additional private income could receive a modest supplement to the low universal pension to enable them to cover basic needs and bring it up to current standards (as is the case now). Such a scheme would take a lot of heat out of the pension debate. People get furious when they prepare for their retirement over

many years on the basis of one financial paradigm, only to find it pulled out from underneath them when the time to retire arrives. You can't go back and start again. It is not a problem for me (I retired in 2011) but many of my baby boomer friends on the cusp of retirement are getting edgy, with all these proposals currently being floated in the media.

Another advantage if the above system is adopted, more money will flow to the superannuation funds and insurance companies who sell superannuation products. After the GFC in 2007-8 and subsequent shenanigans involving 'financial advisers', people have been diverting their savings away from Super Funds and Insurance companies and putting their money in term deposits in banks. This is well recognised. In an article in the Canberra Times of 21 April 2015, under the heading "Life industry insures a lack of trust", the reasons for this situation are discussed. A relevant quote was: "The Assistant Treasurer and Minister responsible for financial services, Josh Frydenberg has rightly called for industry leadership in this matter ..... The sustainability of the sector is suffering from a failure by its leaders to build trust..."

I am confident that if all the 'players' in the retirement income space can have a rational discussion on the issue, it could result in an outcome satisfactory to all. There is no need to reply to this letter – please consider it as a commentary in the current debate on pensions.

Yours sincerely

John Gregan

*8 June 2015*