Policy approaches to promote private and occupational old-age provision in Australia

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Pension reform – advance funded old age provision: Aspects from Australia

As a preamble to this report it should be noted that Australia has one of the oldest formal retirement systems in the western world. While not following the experiences of the United Kingdom and Germany who strongly embraced a clearly defined pay-as-you-go (PAYG), the former British colony early in its nationhood (1909) adopted a flat rate old age pension that ensured that a basic level of welfare was provided to elderly Australian retirees.

Another milestone in the late 1930s relating to Australia's overall retirement system was the evaluation and planned development of a national insurance contribution system similar to that which exists in the United Kingdom was considered. With the outbreak of World War II, these plans were initially shelved and later abandoned.

In the early 1970s with the election of a social democratic Labour government, Australia closely examined the future directions of the nation's overall retirement provision. Discussions centred on the adequacy of the old age and disability pensions and also broadening the coverage of the voluntary second pillar. At this point the trade union movement began to advocate compulsory contributions into occupational second pillar schemes.

Following on these arguments a Labour government in 1987 and 1992 introduced varying elements of compulsory employer contributions that has seen dramatic increases in superannuation (pension) assets and the average balances of individual workers.

Essentially Australia in summary has implemented a retirement system that embraces the World Bank's three pillar mantra that sees the:

- Provision of an adequate public safety net;
- Compulsion of self-provision based on a set level of contributions for those in the labour force at the very least; and
- Encouragement of self-provision (by way of superannuation or other savings preserved until retirement).

Future issues that are likely to confront Australia will include greater fund and investment choice and the continued refinement of regulations to ensure that consumer detriment is minimised.

Part I: Background Information

I.1.a) Provisions of public schemes

Central to many Australians retirement planning decisions is the receipt of the old age pension and related benefits such as a health care card that provides discounted pharmaceuticals and medical treatment along with reductions in utility bills such as electricity and telephones.

Eligibility for this flat rate benefit that is equivalent to 26% of Male Total Average Weekly Earnings (MTAWE) is relatively generous. Such determinants include being an Australian resident for a total of at least 10 years, at least five of these years in one period or alternatively has been a resident in certain countries with which Australia has an international Social Security Agreement may count towards Australian residence. Another central point for eligibility of such a pension is that men are required to be 65 and for women 62 years. Eventually these ages will equate by 2014 as a result of government initiatives to lift the overall retirement ages for the old age pension in the early 1990s.

The basic rates for such pensions include $A402.00 per fortnight for a single person and $335.50 per person for couples. Such pensions are indexed for price movements with additional allowances being made of $A5.80 for pharmaceuticals.

While eligibility for such pensions is comparatively generous by international standards the associated income and assets tests are quite stringent. To generate a maximum allowable old age pension individuals can generate up to $A112 for a single person and $A200 for pensioner couples combined. In respect of the pension assets test limits, such requirements can be divided between home and non-home owners. To generate a full pension an individual with a house can have assets up to $A141,000 and to receive a part pension individuals can have assets that equate to less than $A277,000. For couples with a house combined assets can equate to $A200,500 and to receive a part pension individuals can have assets that equate to less than $A426,500. In contrast, an individual who does not have home ownership is allowed up to $242,000 in assets or less than $378,000 to generate a part pension. Couples without a house are permitted to have $A301,500 to generate a full pension or less than $527,500 to generate a part pension.

Based on the details contained in the assessment relating to the levels of income and assets; payments may be affected through:

- Assets, which are over the maximum payment settings, will see payments reduced by $3 per fortnight for every $1,000 (single or couple combined).
- Income over the amounts for maximum payment reduces the payment by 50 cents in the dollar (single), 25 cents in the dollar (each of a couple).

I.1.b) Income (imputed or real) from housing

"Housing satisfies the essential needs of people for shelter, security and privacy. Shelter is recognised throughout the world as a basic human right. The adequacy or otherwise of housing is an important component of individual wellbeing. The predominance of separate, freestanding houses situated on 'quarter acre blocks' within the mainland capital city areas is a feature of Australian urban development. More recently, governments have moved to promote higher housing densities, to provide greater choice of housing types and to make better use of existing infrastructure."[1]

Australia, like the Republic of Ireland has a significantly high level of home ownership. In 1995-96, of the 6.9 million households in Australia, 70% were living in their own home and 28% were renting their dwelling from public or private landlords. As we are aware the traditional retirement age in Australia is 65 years. At this time income levels and housing repayments dramatically reduce as Australians take second pillar retirement benefits in the form of a part or full lump sum and pay out existing mortgage balances upon retirement. Yet many couples upon retirement have already paid out their mortgages. As measured in 1995-1996, 90% of older couple households were owners without a mortgage with average weekly housing costs of $A17. For older couples who still had a mortgage, these repayments were also considerably lower than those of younger generations. Average repayments were $A62 per week. Explanations for this trend in housing in Australia centre on how Australia twenty years ago had relatively housing prices and forms of financing.

I.1.c) Resources needed for health care and long-term health care in old age

Australia like most OECD countries has a system of universal health care and subsidised long-term health care places in nursing homes for the elderly. The Medicare system provides a universal system of health insurance. Under the Health Insurance Act, the Commonwealth provides a Medicare benefit for services listed in the Medicare Benefits Schedule that are rendered by legally qualified medical practitioners, certain prescribed services rendered by approved dentists and optometrical consultations by optometrists. Medicare benefits are payable at the rate of 85% of the schedule fee for services. In effect the individual pays 15% of the scheduled fee for medical treatment along with the annual Medicare levy of 1.5% of income through the PAYE taxation system. Additionally on 1 July 1997 a further 1% Medicare levy was implemented for single individuals with taxable incomes in excess of $A50,000 per year, and couples and families with combined taxable incomes in excess of $100,000, who do not have private hospital cover through private health insurance.

The current Federal Government is strongly committed to encouraging private health insurance coverage. During the 1980s membership of private health funds steadily declined as individuals and families questioned the need to have private insurance coverage if the existing Medicare system provided the vast bulk of medical treatments. Yet as the population of Australia continues to age waiting lists for elective surgery grows steadily and the overall public hospital system shows continuing signs of stress. To address this issue the Federal Government introduced in 2000 a 30% rebate scheme for private insurance. Since its introduction the levels of private health insurance in Australia have increased from 28% to 42% in the past year.

Often a focus of retirement planning for retirees is to obtain upon retirement a Commonwealth Seniors Health Card. This card gives older Australians access to concessions on prescription medicines through the Pharmaceutical Benefits Scheme. To

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[1] W.McLennan: *1998 Year Book Australia*, Number 80, Australian Bureau of Statistics, Canberra, Australia, 1998, p. 259

get the Commonwealth Seniors Health Card and receive the Telephone Allowance[2] you must:

- Be an Australian resident and in Australia for a period of, or periods totalling 104 weeks;
- Have reached Age pension age, 62 for women and 65 for men; and
- Have annual income less than following amounts (as of 1 July 2001):
  - $50,000 (single)
  - $80,000 (couple combined)
  - $100,000 (couple combined and separated due to illness).

While no exact data exists for family support of those people aged 65, anecdotal evidence suggests that many Australian retirees at the age of 65 years lead an active and healthy lifestyle well into their late seventies. Like most western developed nations stroke, heart disease and cancer cause a large level of mortality in this age group. At or around an individual's late seventies or early eighties long term health care planning begins to be engaged. Many Australians enter organised retirement communities. Villa style communities provide independently supported lifestyles for the individual. As they increasingly age and health care issues become more prominent, hostel and finally nursing home care become increasingly important for ageing Australians. A useful guide that depicts the extent of long term healthcare in Australia is that total expenditure for nursing homes for aged is $A2,170.9m (recurrent) and the capacity of this sector of economy is equivalent to 1,494 nursing homes and 1505 hostels based on 1996-1997 data.

Long term health care (LTC) is largely a federal government issue whereby subsidised nursing home and hostel accommodation is provided to those individuals who meet certain asset and income test criteria. Nursing homes charge the individual a reduced rate for the place in the LTC centre. Increasingly people are buying villas or retirement lodgings within an overall community. No specific levies or charges are raised or linked with LTC in Australia. The costs associated with these treatments and services are met out of consolidated revenue sources.

Part II: Fully funded private, hybrid and occupational pension scheme

II.1.a) Target groups for mandated/subsidised pensions savings in this scheme

Australia is one of only three countries that have a mandated second pillar retirement system. The genus of this policy position came about through largely trade union agitation for compulsory contributions by employers into complying employee pension or superannuation accounts. These policy initiatives were initially enacted in 1987 and later strengthened by the Superannuation (Industry) Supervision Act 1994. Today the

[2] The telephone allowance is directed towards old age pensioners who receive a full or part pension on the basis of adequacy. This telephone allowance normally takes the form of reduced line rentals offered by the partly state owned telecoms provider, Telstra Australia.

Superannuation Guarantee Charge Act 1992 requires all employees to contribute to a complying superannuation fund at a level that increased from 3% per annum in 1992 to 9% per annum by 1 July 2002. All Australians who are between18-70 years and receive a gross salary payment of $450 per month are required to make these contributions whether or not they are in part-time or full time work.

II.1.b) Government approach to make target group take part in this scheme

Mandated participation is required under the second pillar superannuation programme prescribed by the Superannuation Guarantee Charge Act 1992. It is important to note that coverage levels have increased from 40% of the workforce in 1983 to 91% in 2000 as a result of the introduction of compulsion.

No explicit tax incentives exist for employers or employees to make contributions via the Super Guarantee. The incentive for employers to make prescribed contributions is that they receive ordinary tax deductions for these payments. If no contributions are made by the employer a superannuation charge is imposed that seeks to gain payment via the taxation system. This charge is not tax deductible unlike other voluntary contributions.

Some personal taxation deductions exist for the self-employed and lower income workers but these taxation allowances are largely minimal as most people earn over the earnings threshold. It is important to note that as the system is compulsory and the taxation approach for employees is T (tax the contributions), T (tax the income generated from the superannuation fund) and T (tax the resulting benefit) under the Dilnot model, thus there is little need for the government to provide incentives. Preferential treatment of other forms of savings exists for the family home, which is tax free in terms of all capital gains generated from the sale of associated renovation. Some tax concessions in the form of negative gearing also exist for investment properties.

One of the more common criticisms of the Australian model centred on the ability for people upon retirement to take benefits largely in the form of lump sums rather than annuities or 'drawdown' policies. To discourage this trend by retirees, the Federal Government acted through providing more favourable taxation considerations for retirees if they purchased a traditional annuity or allocated pension product (akin to a drawdown policy. Unlike taking a lump sum whereby higher taxation will be levied, income streams generate more favourable tax considerations for the individual based on individual income calculations and cash concessions in retirement.

II.1.c) Volume of required/subsidised contributions to this scheme

As indicated previously by 1 July 2002 all full time or part time workers will be required to contribute 9% of their salaries into complying superannuation funds. Linked with these contributions, prescribed contribution ceilings for individual salaried workers are detailed below.

Superannuation guarantee - maximum superannuation contribution base

Income year	Per quarter
2001/2002	$27,510

2000/2001	$26,300
1999/2000	$25,240
1998/1999	$24,480
1997/1998	$23,630
1996/1997	$22,590
1995/1996	$21,720
1994/1995	$20780
1993/1994	$20,160
1992/1993	$20,000

Source: http://www.ato.gov.au/content.asp?doc=/content/Professionals/super/itl06.htm

Age Based Contribution Limits

Income year	Under age 35	Age 35 to 49	Age 50 and over
2001/2002	$11,912	$33,087	$82,054
2000/2001	$11,388	$31,631	$78,445
1999/2000	$10,929	$30,356	$75,283
1998/1999	$10,600	$29,443	$73,019
1997/1998	$10,232	$28,420	$70,482
1996/1997	$9,782	$27,170	$67,382
1995/1996	$9,405	$26,125	$64,790
1994/1995	$9,000	$25,000	$62,000

Source: http://www.ato.gov.au/content.asp?doc=/content/Professionals/super/itl01.htm

II.1.d) Providers

The Superannuation (Industry) Supervision Act 1994 prescribes certain solvency and compliance conditions which a free standing superannuation fund has to meet or alternatively a life insurance company is required to undertake before it can offer superannuation products. In the case of life insurance companies these details are largely covered in the Life Insurance Act 1994 which prescribes how certain capital requirements need to be met for the company to operate in Australia.

In respect of the right of choice this issue has been pursued by the current Federal Government with some legislative vigour. The theoretical argument behind legislation to promote choice of fund was that the current government was concerned that through award (labour) agreements some employees may be restricted to simple, under performing superannuation funds that could have significant levels of poor performance. As the compulsory superannuation system had been originally promoted by the trade union movement in Australia it is no surprise to understand that such retirement savings are intertwined in employment law and industrial relations.

Australia's employment conditions are largely detailed in state or federal award agreements. Such a rigid approaches to joining a particular employer designated superannuation scheme were often defined in these conditions. For example mining and construction workers who entered employment linked with these two sectors of the economy were required to join industry superannuation funds that were initially established through award conditions to provide retirement savings accounts for workers in these associated industries eg C+BUS. In contrast some small business providers simply provide a group superannuation product purchased through a retail fund offered by a life insurance company or alternatively are able to channel SGC into specific accounts nominated by the employees such as RSAs or individual retail superannuation accounts.

The latter are simplified defined contribution, grouped retirement vehicles offered to individuals via banking channels. They usually are invested in low risk investment structures such as fixed interest securities. So in effect their investment options are limited but they provide low levels of fees and charges. These products would be similar to a bond fund and were largely developed by banks to compete head on with superannuation funds for deposits.

As such no one answer can be applied to the Australian retirement system. Thus a correlation exists between whether the employee is required to take up superannuation provisions dictated by the employer and the associated employment conditions, type of industry and the overall size of the employer's business.

The approach of supervising Australia's superannuation industry is quite different compared with other OECD nations. Two regulatory bodies were created in 1998, one the Australian Prudential Regulation Authority (APRA) was deemed to be in charge of solvency requirements for all financial services entities. The second, the Australian Securities Investment Commission (ASIC) was designated to be in charge of consumer protection and detriment issues linked with the distribution and effective performance of these products.

Again the Superannuation (Industry) Supervision Act 1994 plays a central role in defining the arrangements that are attached to the supervision of superannuation funds. In the Act and associated legislation, requirements exist for the annual lodgement of returns detailing the performance, investment strategies and overall financial soundness of the superannuation fund. Along with the lodgement of returns, requirements exist for a regular external audit of the fund plus a clearly defined investment strategy being agreed to by trustees. Important also in the supervision of funds is the selected auditing programs and educational seminars undertaken by APRA and ASIC along with related industry association educational programs sponsored by the Australian Institute of Superannuation Trustees (AIST) for trustees. Combined these proactive and passive regulatory initiatives have tended to minimise consumer detriment and add to the need for regulators to be both responsive to potential fraud but also contain or be objective to the related compliance costs for operating an occupational superannuation fund.

II.1.e) Regulation of permitted financial products within this scheme

Lump sum death benefits, and benefits for total and permanent disability, are commonly provided as part of the superannuation plan. In a defined benefit fund, benefits are generally equal to the projected retirement benefit, using salary at the time of occurrence of death or disability as the basis for benefit calculation.

For accumulation funds, the benefit is typically the sum of the member's accounts in the fund, plus an insured benefit equal to a multiple of salary. The multiple could be fixed at all ages, or be based on a multiple that reduces as age increases.[3]

Short-term salary continuances benefits (providing monthly income benefits of up to 75% of salary, payable for between two to five years) are increasingly available in the event of total and temporary disablement of the employee. Long-term disability income benefits, which would normally exist in place of lump sum total and permanent disability benefits, are not as common.

Portfolio regulations in Australia unlike examples in countries like Switzerland or Chile are less prescriptive. Such regulations generally follow the 'prudent person' rules and concepts that are outlined in the OECD's publication centring on private pensions.[4] Central to this minimalist approach to portfolio regulation is the requirement that superannuation fund trustees have a detailed investment strategy that outlines the overall investment priorities that seeks to maximise returns for fund members. On this basis it would be difficult to sustain an investment strategy that was not balanced in terms of asset allocations. As such having a superannuation fund with 100% of its assets invested in one type of tangible asset would be considered outside the current spirit and detail of existing superannuation legislation.

No guaranteed minimum performance is prescribed for superannuation funds in Australia. The fundamental argument contained in legislation and efficient disclosure rules is that the plan member should have access to communications that allows he or she to judge whether the trustees should act to correct poor investment. Some limited protection against losses attributed to superannuation funds exist in Australia with the ability for the Federal Treasurer to enact a special levy on existing superannuation funds and thus fund members where a superannuation fund of significant scale collapses due to fraud or mismanagement.

With reference to flexibility regulations, limited contribution adjustments exist under the mandated requirements of the second pillar retirement system of Australia. Some debate in recent years has surrounded the issue of choice linked with the structures of superannuation. Primarily most if not all superannuation funds have a wide variety of choice of investment. These investment choices have grown in response to individuals' average balances increasing over time. Debate on a political and industry level has also focussed on proposed choice of fund legislation that would require employers to provide their employees with a choice of superannuation funds to invest in eg industry, RSA or retail fund for example. At this point such proposed legislation has not been passed by the Australian federal parliament with objections being raised along the lines of higher compliance and increased administrative costs.

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3 Watson Wyatt Data Services: B*enefits Report Asia/Pacific*, Watson Wyatt Worldwide, 2000/2001, p. 61

4 OECD 2000, Private Pension Systems and Policy Issues – Insurance and Pensions.

Some limited restrictions on charges are related to superannuation funds in Australia. Unlike stakeholder pensions in the United Kingdom where an explicit cap of 1% is placed on corresponding charges for fund members, no such caps exist in Australia in respect of superannuation funds. For politicians and bureaucrats alike a common concern towards charges and superannuation products centred on small accounts. Initially Small Holding Account Reserves (SHARs) were established to allow superannuation accounts with less than $1000 to be managed by the government. Such accounts were promoted as having vastly reduced fees but as the proceeds were invested in government bonds, returns were largely modest. Ongoing solutions to this problem were seen in Retirement Savings Accounts and Eligible Rollover Funds that again provided consumers with low cost alternatives to more main stream superannuation products but with a trade off of lower returns. A broad generalisation that can be made is that accounts with less than $1000 attract no fees and charges thus avoiding the complete erosion of overall superannuation balances.

The overall transparency and information regulations linked with superannuation products has been dramatically improved in Australia during the 1990s in the wake of fierce criticism by consumer protection and industry regulators. In educating fund members about the performance and characteristics of the superannuation product two fundamental tools are employed. The first is the member statement of contributions, charges and investment returns and secondly the customer information brochure that details important key features and the overall policy illustration of how the product is likely to perform over time. Regulatory requirements ensure that member statements are issued on an annual basis (at a minimum). These statements are required to highlight employer and employee contributions, returns generated from the fund and associated administrative fees. Under new requirements contained in the Financial Services Reform Act 2001 all fund members are to be provided with information that highlights the key features of the product. An additional requirement is that product illustration are generated through prescribed methods, as detailed by regulatory bodies and finally important information should be provided that gives greater definition on how the consumer can make complaints or resolve disputes. An important aspect linked with this feature of Australia's superannuation industry is the integrity of the intermediary and how well they spell out to the plan member the important features and functioning of the product.

II.1.f) Ensuring retirees can rely on their assets in old age

This section largely does not relate to Australia with the exception of prudential solvency standards and actuarial standards that ensure that funding assumptions are maintained for superannuation funds that operate on a defined benefit and defined contribution basis. Prescribed rights exist for fund members whereby the business entity ceases trading and the resulting possible shortfall can be recovered via the liquidation of business assets in some instances. Unlike 401(k) products in the United States, member fund benefits cannot be withdrawn before the preservation age of 55 years or used for housing or consumer expenditure. Such withdrawals are only permitted whereby clearly defined hardship can be determined or identified after review by corresponding federal government agencies.

II.1.g) Vesting periods

Vesting has progressively been coming down in Australian over time. Some funds have immediate vesting but most have one or two year vesting. The previously horrid situations of ten vesting for example has now been abandoned.

Part II.2: Specific scheme: Regulation in withdrawal phase

II.2.a) Withdrawal point of time in this scheme

As indicated Australian workers can begin withdrawing their funds from superannuation plans from the age of 55 years. Many Australian workers tend to move their funds into eligible rollover vehicles until they reach the age whereby they qualify for the old age pension, for example at 65 years for men. Earlier withdrawals are permitted in some cases where poverty or severe hardship can be proven through extended periods of unemployment. Many Australian retirees attempt to take most of their retirement benefits at the same time as qualifying for the old age pension.

II.2.b) Need to annuitise pension assets in this scheme

Unlike the United Kingdom, no mandatory requirements exist in Australia for compulsory annuitisation. In the past Australian retirees had traditionally taken their retirement benefits in the form of a lump sum. With changes in the taxation approach, Australians still can still take retirement benefits in the form of lump sums but such retirement disbursements will be taxed more heavily when compared with traditional annuity products or allocated pension products that are similar to the more commonly recognised draw down products. During the 1990s Australia witnessed a rapid growth in allocated pension products in response to high rates of return being generated in equities markets. Equally these products provide much more flexibility when compared with traditional retirement annuities that are seen to provide income streams that are significantly lower when compared with managed funds products.

II.2.c) Permitted design of annuities in this scheme

In Australia, both term and lifetime annuity products are sold by financial planners to associated retirees. Age and gender are the two primary factors that shape the pricing annuity type products. It is important to note that drawdown or allocated pension type products also play a major role in Australia.

II.2.d) Do private/occupational pension payments from this scheme reduce social assistance/social security benefits?

As already identified, the old age pension in Australia is determined through the interaction of an income and assets test. Complying pension or annuity products as determined by the Department of Family and Community Services allow the individual to receive a pre-defined income stream along with qualifying for an old age pension. Such income streams and residual capital invested in an annuity product will have an impact on the old age pension through either the income or assets test.

Part II 3: Experience with this scheme

With the mandated characteristics of Australia's retirement system being central to coverage, the question effectively does not pertain to this model. It should be stressed that in 1983 Australia had only 40% of the workforce covered by voluntary superannuation programmes with $A32 billion being attributed to such financial services products. During this period, employment associated with middle class, white, male and government vocations tended to have superannuation accounts. In contrast if you were a woman, from a multicultural background who was employed in industries with low union coverage, it would be expected that such people did not have superannuation accounts.

As the compulsory nature and level of superannuation contributions has increased the cumulative levels of savings in bank accounts has continued to decline. It seems clear through anecdotal evidence that strong increases in funds management and superannuation accounts have taken place in Australia during the 1990s. Such deferred consumption behaviour has seen many banks acquire life insurance or funds management subsidiaries in an effort to offset falling low interest bank account balances.

Part III: Financial Education policies

Little formal research has been conducted in this area in Australia. It should be stressed that Australia launched a formal public education campaign sponsored by the Federal Government in 1994-1995 that outlined features of the new superannuation system introduced largely in 1992. By dedicating $A11 million of public funds towards the production of public education materials for every Australian households and education kits for school, a clear signal was being sent out on the importance of public education.

Since this point Australia has entered a policy vacuum linked public education and retirement savings. Some initiatives have been launched by the Australian Institute of Superannuation Trustees (AIST) and a fund manager in the late 1990s to help provide education kits for schools that discussed the broad details linked with Australia's savings and investment culture. Additionally trade union groups and industry associations like ASFA and IFSA also provide broad generic educational materials for plan participants and the general public. Additionally some retirement pre-planning is being conducted by Centrelink, the government agency who is responsible for the Old Age Pension in Australia. These seminars discuss the details of pension benefits provided by the government and how the income and assets test may impact on the final level of payment.

A cross national survey and international study is currently being undertaken in this area of financial education and is due to be published at the end of November 2001. Such research contains more detailed analysis and will be forwarded to your organisation in December 2001.

Part IV: Personal Assessment

In general the position of old age pensioners has tended to deteriorate in the last 10 years. With the old age pension being indexed only to prices and also having a replacement rate of 26% of male total average weekly earnings, purchasing power has tended to decline. Moreover government assistance programs have tended to be tightened in the areas of transport and rural assistance that has led in some cases to a political backlash.

The impact of superannuation reform changes has not really been felt to any great extent by these groups of pensioners. Added to the declining purchasing power of the old age pension was the recent introduction of a goods and services tax which has tended to favour people who are not in fixed incomes. Moreover declining interest rates on deposits has meant that for self funded retirees, returns on capital have declined over the ten year period. I would add that the full benefits of superannuation reforms in the early 1990s will not 'crystallise' until well into this century.

Overall government assistance and welfare payments are becoming more targeted through the interaction of the income and assets test and specific legislative requirements targeting particular demographic and income related groups of the overall pensioner population.

Taxation of occupational pensions and more generally income has undergone major changes in the last twenty years in Australia. A continual change to the way superannuation is taxed has caused much confusion for plan participants and trustees alike. This complexity is due to varying governments of differing political persuasions having altered policy positions on how deferred savings should be taxed. All industry associations are pushing for a comprehensive review of how superannuation is taxed. My only feeling is this concern and anguish falls on deaf ears with Commonwealth Treasury receiving strong revenue growth from superannuation in the last decade. By its very nature, mandated retirement savings allows very little opportunity to minimise taxation be paid by the plan participant as a result of the strict adherence to the TTT approach adopted in Australia. Taxation incentives for encouraging further retirement savings on top of compulsory contributions is considered to be a poor policy alternative by many bureaucrats in terms of the fiscal expenses and the imperatives of both political parties (Liberal/Coalition and Australian Labour Party).

In general, Australia's approach to retirement saving has received tremendous support and recognition by domestically and internationally. The United States Congress for example has evaluated the Australian retirement model five times before committees who are considering social security reforms in the United States. In general terms the model has dramatically lifted retirement savings and improved the future prospects of baby boomer and Generation X retirees. Comparatively low administration costs, wide investment choice and minimal mis-selling has meant that consumer detriment has been minimised. It still remains a challenge for the system to maintain higher levels of contributions, with a voluntary basis or top up against the backdrop of competing investment vehicles such as unit trust or managed products. Simply put, 9% mandated contributions will not be enough for an individual to replace their level of income and maintain their lifestyle in retirement. The downside of the Australian superannuation model has been the plethora of individual accounts that have been created. Over 20 million accounts exist for just over nine million workers and this feature has caused unnecessary duplication and administrative costs to be incurred. Many superannuation funds are seeking also to streamline the process of transferring superannuation accounts. This attempt at simplifying administration protocols will benefit the whole of the superannuation industry. A further critic of the Australian superannuation model is included which is based on my oral testimony before the House Ways and Means Committee, Subcommittee on Social Security.

"It should be stressed from the outset that I do not think that one particular country has provided solutions to all the challenges of executing successfully social security reform. Moreover I believe international experiences provide a composite of important simulations or experiences that the United States can take onboard. Thus, in the case of Australia, many cultural links and social behaviours are shared in common which can help smooth or translate important features into the American context. Both countries for example experienced a sharp baby boom in the middle part of the twentieth century. In effect both countries' demographic profiles are very similar.

The Old Age Pension in Australia is seen by many as providing both a foundation and an important source of income for those retirees who have limited resources to sustain themselves in retirement. Its origins date back to 1909 where a flat rate benefit was provided to individuals upon reaching a prescribed retirement age. Policy planners during this period turned their back on the notion of an ear-marked PAYG model that Bismarck had used to forge a single Germanic nation. Many older Australians who are retired, or have retired in the past, often have not built up sufficient retirement savings. A common perception in the past by many workers was that they were entitled to an old age pension after paying taxes all their working life. Largely this view was encouraged by many governments but increasingly in the 1980s, the Commonwealth Treasury and the Federal Government expressed concerns over the direction of expenditure for providing the first pillar of Australia's retirement framework. Increasingly expenditures in providing the first pillar were also linked to a concern over the demographic position of Australia in the next century. Today these benefits are means tested and equate to a maximum of 26% of male total average weekly earnings.

Clearly to engineer or make such a significant shift in the overall retirement structure of any country requires a strong political resolve, a basis of consensus between political parties and a vision for the future of a nation's citizens. In Australia's case, more through coincidence and luck, a popular Federal Government through trade union support, was able to convey to the nation the impending problems Australia would confront, if it did nothing about addressing its ageing population. I want to stress to you today it is a social democratic, trade union supported political party that continues to support the need for ongoing retirement reforms.

For trade unions, which had strongly supported the election of a Federal Labour government in 1983, increasing superannuation coverage was seen as a major priority. Before the introduction of mandated, second pillar, superannuation accounts, the extent of coverage of superannuation was limited to roughly 40 percent of the workforce. Typically employees who were covered by superannuation were employed in middle class, 'white collar' jobs where usually women and people from minority groups were under-represented.

By 1986 circumstances were ideal for the introduction of a widespread employment-based retirement incomes policy. A compulsory 3% employer contribution was generated through centralised wage fixing. Such an approach proved difficult to administer and to gain increases in the levels of contributions.

The Superannuation Guarantee Charge Act 1992 requires all employees to contribute to a complying superannuation fund at a level that increased from 3% per annum in 1992 to 9% per annum by 1 July 2002. Additionally on average voluntary contribution equate to 4% per annum on top of compulsory levels of contributions into superannuation accounts.

Another method by which the Federal Government was able to engineer significant change to the retirement system was through the use of an effective public education campaign in 1994-1995, which was co-ordinated by the Australian Taxation Office. Overall the total cost of the public education campaign amounted to some $AUS 11 million. Through the comprehensive use of the electronic and print media, the Federal Government displayed strong political savvy in being seen as introducing a retirement system that not only benefited the individual but the nation as a whole. These two themes of individualism and collectivism were to be stressed throughout the media campaign.

With regard to the taxation of superannuation, Australia has pursued a course which is quite unique and which on the whole I cannot agree with in terms of design and the overall rate of taxation applied. Based on Andrew Dilnot's model developed at the Institute of Fiscal Studies in London, Australia's taxation of superannuation can be described as TTT. Taxation of contributions at a rate of 15%, along with possible additional taxation of 15% for members' contributions earning over a certain threshold. A further tax of 15% is levied on the investment income of superannuation fund and finally the benefits can be subjected to varying tax treatment of between 0-30%, depending on timing of the contributions. Yet this taxation levels are more favourable to simple savings that is taxed at the highest marginal taxation rate.

The profile of the second pillar of Australia's retirement system depicts both a diversity and adequacy of return that reflects strong and vigorous competition among the financial services industry in Australia. Through a trustee structure, superannuation funds are managed in the most efficient and effective manner for members.

I would like to now turn briefly to the mechanics associated with selling, distribution and withdrawal of benefits from the superannuation account. One of the reasons why Australia has been so successful in keeping administrative costs low and also avoiding the problems associated with mis-selling is through effective and cost efficient regulation. Strict rules govern how superannuation policies are sold and switched. Moreover consumers are required to receive minimum levels of information about the superannuation products at the time of sale and also on a regular basis. Clearly it is felt that, as this is the largest financial transaction that a consumer will enter into in their life, effective disclosure should be provided to encourage transparency in the transaction. Increasingly superannuation account holders are being provided with greater investment choices. Some retail funds for example offer between 5-7 investment choices and proposed legislation by the Federal Government will force employers to offer choice of funds. Additionally specialised administration companies have developed services that allow superannuation fund trustees to outsource much of their investment and administrative functions. This intense competition has led to in part returns being maximised and administrative fees being minimised.

The success of consumer policy and integrated distribution platforms has meant that large-scale consumer detriment has been minimised in Australia with its move towards a more fully funded system. Through sound regulatory transparency and significant improvements in the competency levels of distributors eg financial advisers and financial planners public confidence in the overall retirement system has continued to increase significantly. This perception of security has nurtured a steady increase in the level of overall voluntary contributions made into superannuation accounts. In effect through sound regulation has come an acceptance by most Australians that saving for one's retirement is beneficial on both an individual and national basis.

Statistical and Demographic Highlights

By March 2001 the Australian superannuation system had combined assets of \$A497.1 billion (\$US253.00 billion). For just over nine million workers this level of retirement savings is considered to be quite significant. It is important to note that 19.8% of these assets are invested internationally. Furthermore a large level of the superannuation assets are invested in equities and unit trusts. This investment category has grown sharply during the 'bull market' period and is now estimated to be 42% of superannuation assets in Australia.

Like the United States, Australia has a demographic profile that depicts a significant baby boomer population. As detailed below, Australia and the United States' demographic profile will continue to deteriorate over time. Such an effect is compounded by the growing cost of each nations' pensions unfunded liability. Moreover the seriousness of both countries' demographic positions are highlighted in the two tables linked with life expectancy and the elderly/youth ratio. Yet it should be noted that both countries' demographic positions are much healthier when compared with countries like Germany or France.

Administration costs continues to be a sensitive issue within the Australian political and financial services environment. These costs can vary widely between the types of superannuation funds found in Australia. Through an authoritative survey conducted by the Association of Superannuation Funds of Australia (ASFA), an average estimate of \$1.28 (\$US0.65) per member per week was made for overall administration costs in 1999-2000. It should be noted that this figure has declined from \$1.66 (\$US0.84) per week two years earlier. Expressed in another way, costs as a percentage of assets in June 2000 were calculated to be 1.29%. It is anticipated that this level of costs as a percentage of assets will decline as the system matures.

Conclusions

For the United States the challenges of social security reform may seem immense if not impossible from initial observations. Yet what countries like Australia demonstrate is the ability for a nation to give its people a greater ability to craft out a sufficient and appropriate level of retirement wealth to meet expected future needs and demands. Certainly no one country's experiences with regard to social security reform can be easily translated to another. Yet what countries like Australia can demonstrate to public policy planners in the United States is the strong propensity that the individual is ideally placed to determine his or her own retirement needs."

Life Expectancy of Selected Developed Nations

	1950 - 1955	1960 - 1965	1970 - 1975	1980 - 1985	1990 - 1995	2000 - 2005	2010 - 2015	2020 - 2025	2030 - 2035	2040 - 2045
Australia	69.57	70.91	71.70	75.21	77.60	78.74	79.74	80.67	81.48	82.29
Canada	69.08	71.44	73.15	75.92	78.50	79.47	80.40	81.20	82.00	82.80
Chile	54.75	57.92	63.44	70.57	74.21	75.65	76.88	77.95	78.84	79.61
China	40.76	49.53	63.18	66.56	68.37	71.18	73.49	75.53	77.15	78.46
France	66.52	70.96	72.35	74.72	77.15	78.75	79.70	80.60	81.45	82.24
Germany	67.50	70.30	71.00	73.80	76.00	77.82	78.89	79.84	80.67	81.45
Ireland	66.91	70.29	71.28	73.10	75.34	77.36	79.09	80.57	81.37	82.16
Italy	66.00	69.92	72.11	74.54	77.16	78.83	79.80	80.69	81.46	82.24
Japan	63.94	68.96	73.30	76.91	79.50	80.34	81.09	81.86	82.65	83.44
	72.11	73.38	73.96	75.98	77.26	78.39	79.34	80.27	81.06	81.86
Sweden	71.81	73.54	74.72	76.27	77.86	79.34	80.62	81.60	82.39	83.19
Swiss	69.23	71.67	73.81	76.16	77.67	79.13	80.04	80.91	81.69	82.49
UK	69.18	70.76	72.01	74.04	76.17	77.97	78.95	79.95	80.80	81.59
USA	69.02	69.96	71.30	74.48	75.66	77.35	78.67	79.67	80.57	81.36

Source: United Nations: World Population Prospects 1950-2050 (1998 Revision)

UN Elderly/Youth Ratio for selected developed countries

	1950 - 1955	1960 - 1965	1970 - 1975	1980 - 1985	1990 - 1995	2000 - 2005	2010 - 2015	2020 - 2025	2030 - 2035	2040 - 2045
Australia	0.24	0.23	0.22	0.28	0.37	0.47	0.62	0.77	0.90	0.97
Canada	0.20	0.18	0.20	0.29	0.40	0.55	0.73	0.91	1.04	1.06
Chile	0.09	0.10	0.10	0.12	0.15	0.22	0.31	0.43	0.58	0.65
China	0.10	0.10	0.09	0.10	0.15	0.24	0.35	0.54	0.83	1.01
France	0.38	0.36	0.39	0.46	0.50	0.67	0.80	0.95	1.09	1.15
Germany	0.32	0.40	0.46	0.58	0.69	0.92	1.14	1.31	1.57	1.57
Ireland	0.29	0.28	0.28	0.27	0.31	0.42	0.50	0.63	0.76	0.90
Italy	0.24	0.29	0.34	0.43	0.65	1.06	1.34	1.66	2.01	2.15
Japan	0.11	0.14	0.22	0.30	0.45	0.97	1.26	1.44	1.54	1.66
Netherlands	0.21	0.24	0.28	0.37	0.50	0.63	0.91	1.19	1.38	1.43
Spain	0.20	0.23	0.27	0.30	0.49	0.82	1.01	1.26	1.72	2.18
Sweden	0.35	0.40	0.49	0.62	0.72	0.77	1.09	1.18	1.26	1.29
Swiss	0.32	0.32	0.37	0.50	0.62	0.68	0.93	1.19	1.49	1.62
UK	0.37	0.39	0.41	0.52	0.61	0.67	0.84	0.96	1.11	1.15
USA	0.24	0.24	0.26	0.35	0.43	0.46	0.59	0.78	0.91	0.93

Source: United Nations: World Population Prospects 1950-2050 (1998 Revision)

Projected future state spending on pensions as a percentage of GDP

	1995	2000	2010	2020	2030	2040	2050
Australia	2.6	2.3	2.3	2.9	3.8	4.3	4.5
Canada	5.2	5.0	5.3	6.9	9.0	9.1	8.7
France	10.6	9.8	9.7	11.6	13.5	14.3	14.4
Germany	11.1	11.5	11.8	12.3	16.5	18.4	17.5
Italy	13.3	12.6	13.2	15.3	20.3	21.4	20.3
Japan	6.6	7.5	9.6	12.4	13.4	14.9	16.5
Netherlands	6.0	5.7	6.1	8.4	11.2	12.1	11.4
New Zealand	5.9	4.8	5.2	6.7	8.3	9.4	9.8
UK	4.5	4.5	5.2	5.1	5.5	4.0	4.1
USA	4.1	4.2	4.5	5.2	6.6	7.1	7.0

Source: OECD, cited in Johnson (1999)

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