Association of Independent Retirees (A.I.R.) Ltd
Submission to:
Australian Law Reform Commission Inquiry into "Grey Areas – Age Barriers to Work in Commonwealth Laws

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A copy of the online submission is set out below. It responds to Questions 1, 9, 10, 11, 12 and 20. There are no Introduction or Executive Summary sections. Due date for submission was 14 June 2012.

> **Question 1.** The ALRC has identified as framing principles: participation; independence; self-agency; system stability; system coherence; and fairness. Are there other key principles that should inform the ALRC's deliberations?

A.I.R. supports the six interlinking principles identified by the Inquiry: participation; independence; self-agency; system stability; system coherence; and fairness.

An individual's view of the need to participate in paid work, supported by community attitude, changes as an individual ages from 45 through 65 into retirement. Work to gain income to support an individual and/or family is an imperative between the ages of 45 and retirement; Government support can be an exception. After retirement, participation in paid work becomes one of the options for an individual to participate in the life of society to achieve a fulfilling retirement. The incentive to work is one of a number of competing retirement priorities and is often not the sole imperative driving financial wellbeing. The priority given to work depends on the need to supplement savings, eligibility to access Age Pension support, individual and family interests, and to some extent habit.

Realisation that there is a gap between desirable retirement living standards and available resources, and that this gap is likely to widen as retirement proceeds because of unknown health and maintenance costs is generating interest in maintaining some form of paid work during some period of retirement. However, the interest in and opportunity for paid work typically changes from a formal contractual structure to a flexible, informal, structure. Disincentives to work in a flexible manner at various stages during retirement can cause financial stress, impact negatively on health, and add to the need for additional age pension and government welfare support. This is not to say that some people will wish to continue in a formal employment structure during some of their retirement. The key issue is in recognising the great variability in interests and priorities of people in retirement and providing the flexibility for them to achieve their objectives and priorities. The principles of independence and self-agency, namely respect for the right of individuals to make decisions affecting them, should be overriding principles in setting legislation applying to people beyond the prescribed retiring age.

Incentive to participate in work during retirement tends to reduce as welfare support through Age Pension escalation and supplements increases. Welfare type subsidies, whether financial, health support, or social engagement, are seductive and reduce individual incentive. The challenge for government is how to provide the opportunity to live a full life without reducing the incentive for retirees to manage their own welfare, including using paid work as a financial supplement.

Superannuation is a stand-out example of this challenge. Because superannuation contributions are compulsory, a large group of the community take no interest in their superannuation savings. Government has been forced to require default superannuation funds to be provided. On retirement, many in this group may see superannuation as another pension to which they have entitlement. The pressure may be to increase the pension, rather than undertake supplementary paid work.

Legislation is often influenced by industry or government stakeholders. Disincentives to work can arise from legislation where the interests of third party stakeholders take precedence over the interests of the individual. The interests of tax collection, industrial unions, and the superannuation industry are examples where the third party stakeholder claim for system stability overrides the individual.

Superannuation management has developed into an extensive private sector industry, designed to transfer the investment risk from government. Legislation is focused on regulation of the industry, with little regard to the interests of its members. Unfortunately, the key principles espoused in the Super Systems Review have not always been followed. These principles are:

- Superannuation must always be for the benefit of members.
- The superannuation system does not exist to support intermediaries.
- Trustees must be relentless in seeking benefits for members.

Super Systems Review Panel, Super Systems Review (2010), pt 1, 4, principle 2

The personal taxation system is driven by the Australian Taxation Office, with quite different objectives to those of individuals. Personal taxation collection takes place through employers as third party stakeholders with the ability to influence the way it is collected at the expense of individuals. The principle of 'self-agency' — that an individual needs to be respected in the right to make decisions about matters affecting him or her — is not applied. One example is that a retiree with income below the tax threshold has tax collected on casual work and is unable to access it until after the end of the financial year. A retiree supplementing income in this circumstance seeks income from work to be immediately available. The need for system consistency, simplicity and transparency for individuals is a very low priority.

The framing principles of participation, independence, and self-agency should recognise that a different environment exists for driving the decision to participate in paid work during retirement to that which exists before retirement. The degree of welfare support in retirement should also be recognised as a disincentive to undertake paid work.

Recommendations:

- The principles of independence and self-agency, namely respect for the right of individuals to make decisions affecting them, should be overriding principles in setting legislation applying to people beyond the prescribed retiring age.
- That the framing principle of system stability needs to include the role of third-party stakeholders in building disincentives for individuals to undertake paid work.

Question 9. What other changes, if any, should be made to income tax laws to remove barriers to mature age participation in the workforce and other productive work?

A large amount of paid work in retirement is properly quite different to the formal practices applying to work for people between 45 and the prescribed retirement age. From a retiree's point of view, where the purpose of work is to supplement income, payment from undertaking work should be simple, and immediately available.

Many retirees who undertake paid work will have a taxable income below the tax threshold, even more likely with the proposed increase of the tax threshold to $18,200 from 1 July 2012. About one third of the 3 million people over 65 submitted tax returns in the 2008/2009 financial year. Of these about 650,000 submitted returns but paid no tax and another 9,000 paid tax with taxable incomes less than the new tax threshold of $18,200 (ATO Taxation Statistics 2008-09, cor0268761_2009PER). Many of those submitting a return but paying no tax can be assumed to have an interest in their retirement income beyond the Age Pension, for example in franked dividend recovery. They can be considered to be part of a target audience who could be encouraged to supplement their income through work. They fit the category of those undertaking informal and casual work, paying no tax and wishing to have cash-in-the-hand.

In many work settings, income tax is taken from pay irrespective of whether the employee will be required to pay tax at the end of the financial year or not. Income tax cannot be recovered without submitting a personal tax return after the end of the financial year. A delay of over twelve months in recovery of the tax paid is quite possible. Further, the individual concerned has to go through the administrative process of putting in the personal tax return. The statistics above indicate that the number of people over 65 paying no tax, some 650,000, is significant enough that the regulations should provide for them to be able to opt out of having tax taken from their earnings as an encouragement to undertake paid work by having their earnings immediately available. The present need to provide a personal tax return for people in this group can be further complicated where the individual has not worked for some years and not put in a personal tax return annually.

Recommendation:

- That the tax laws should be changed to allow a retiree to nominate that income tax should not be taken from earnings where the retiree does not anticipate paying tax in the financial year when work is undertaken.

Question 10. What changes, if any, should be made to the Superannuation Guarantee scheme, to remove barriers to work for mature age persons?

The superannuation structure has developed as a system regulating both the accumulation of retirement assets and also the drawdown of those assets. Linking these two phases, which have distinctly different objectives and characteristics, has led to increased complexity in the drawdown phase over that which exists in the accumulation phase and has led to confusion as to when compulsory deductions cease.

The objective of the SG system was to require employees to contribute a percentage of their earnings (presently 9%) into a superannuation fund to build their retirement assets. The age at which compulsion ceases and the assets used for retirement income purposes has become blurred. Recently, the Government has announced that the upper age limit for the SG will be removed and all employers must deduct superannuation from employees to any age. Ability to make voluntary contributions in retirement has also blurred the original objective; people can now make voluntary contributions, under restricted conditions, up to age 70.

The reason for removing the upper age limit for mandated SG contributions was to reduce the cost to employers of employing persons over the age of 70 by allowing them to claim tax deductions for employee SG contributions. However, while it might make employment of older people more attractive to employers, mandated contributions to superannuation will be a significant disincentive to retirees wishing to supplement their income as described in this submission. The Hon. Susan Ryan AO has stated that:

> The removal of the age limit on the superannuation guarantee will have positive benefits for those working into their 70s and beyond. In addition it will send a message that people are valued in the workforce, no matter what their age. *(ALRC - Working past our 60s. Reforming Laws and Policies for the Older Worker, the Hon. Susan Ryan AO, June 2012)*

The reasons for removing the upper age limit given by the Minister, the Hon. Bill Shorten, in the Media Release on the Bill, 3 November 2011, and the comments from the Age Discrimination Commissioner, the Hon. Susan Ryan AO above, highlight the lack of focus in legislation on the wishes and needs of retirees.

Requiring people who work beyond the prescribed retiring age to compulsorily save some of their earnings appears to have merit and in some cases can be an incentive to continue to work. One difficulty is that the regulations have age-based minimum drawdown conditions on pensions. For example, from age 65 to 74, five per cent of the mandated contribution (9%) must be withdrawn and from age 75 to 79 the amount increases to six per cent (these withdrawal percentages have temporarily been reduced by 25%). It is illogical to require a person to contribute 9% to superannuation, while at the same time requiring the person to withdraw 5% or more. A consequence of removing the upper age limit for mandated contributions is that the minimum drawdown conditions on pensions should be removed. Contribution fees further reduce the net funds available to employees from the compulsory SG contribution.

Investment of superannuation contributions is based on a long-term philosophy as a means of managing market variability over the working life of an individual. As has been demonstrated in recent years, many retirees do not have the financial resources or life span to cope with market variability. Retirees need to have the flexibility to judge whether it is in their interest to contribute further to superannuation in terms of their age, superannuation drawdown regulations, and other priorities for use of their retirement earnings. Abandonment of the taxation concession on interest, recommended by the Henry Tax Review, is a disincentive to retirees to work and save some of their earnings in the simpler and well-understood banking system as an alternative to forced contribution to superannuation.

Removing the upper age limit on SG contributions has meant that retirees undertaking supplementary work, even on a part-time basis, are required to make superannuation contributions, even though their income from work, and hence the SG amount, may be quite small. Contributions to superannuation attract 15% tax, as does the earnings on those contributions, even when the retiree is not required to pay tax. The Government has recently announced that the tax on such contributions can be recovered after the end of a financial year. However, the contributions will have attracted administrative fees and the retiree must go through the administrative process of recovering the amounts. Fees are also involved if a retiree wishes to convert the contribution to a pension.

Incentive to continue to work beyond the prescribed retiring age is best achieved by removing age-based barriers to superannuation including mandated contributions and minimum drawdown conditions.

The 15% tax on superannuation contributions and their earnings, and the contributions themselves cannot be recovered without making application. The monies cannot be recovered until after the end of the financial year. These restrictions are a very significant disincentive to undertaking paid work.

This is an example of the disincentive to paid work arising from third party driven legislation and regulations where practices are imposed on an individual retiree without taking into account the needs of the retiree, who is often looking for simplicity in a retirement environment. From a retiree's point of view, where the purpose of work is to supplement income, payment from undertaking work should be simple, immediately available, and the decision to contribute to superannuation should rest with the individual and not be imposed.

The target audience for encouraging people over the prescribed retirement age to supplement their income from work can be gauged from taxation statistics *(ATO Taxation Statistics 2008-09, cor0268761_2009PER)*. About one third of the three million people over 65 submitted tax returns in the 2008/2009 financial year. Of these about 650,000 submitted returns but paid no tax and another 350,000 paid tax with taxable incomes less than $100,000. Many of the these two groups will have superannuation assets significantly less than those required to sustain their accustomed standard of living over their retirement life, and less than the $500,000 asset limit that has recently been set as a measure of the cap at which contributions should be restricted. They can be considered to be a target audience who could be encouraged to supplement their income through work and would obtain benefit from so doing. They fit the category of those more likely to undertake informal and casual work and wishing to have cash-in-the-hand. Many are unlikely to be interested in the restrictions applying to full-time formal work, including mandated superannuation.

The principle of ‘coherence’ is not achieved in the accumulation phase but is breached even more in the drawdown phase, when simplicity and coherence is of great importance. The need of retirees for simplicity in accessing their savings and making additional contributions from paid work has been largely ignored because of the focus on regulation of the industry, rather than on the needs of retirees. The existing drawdown phase is inflexible. It contains many restrictions and complex administrative processes, which act as disincentives to senior Australians contributing to Australia’s economy through paid work.

Management of retirement income should be separated conceptually, and administratively, from the accumulation phase. Appropriate regulations should be developed for the retirement phase, which meet the principles of ‘independence’, ‘self-agency’, and ‘coherence’. That is, taxation and retirement income regulations should be consistent for all Australians, no matter how their retirement savings were accumulated, and should be simple and flexible.

Of the 40% (405,000) of people over 65 who paid tax of $6.71 billion in the financial year 2008/2009, only 50,000 (12%) people paid the bulk (two-thirds) of the total tax paid. These were people with taxable incomes above $100,000. The great bulk of people paying tax with taxable incomes less than $100,000, the target audience identified above as the appropriate one for encouraging greater participation in work, would have marginal retirement assets. Regulations aimed at restricting contributions to superannuation would not apply to the target audience and tax lost from removing the regulations from the target audience would be minimal. Regulation of the superannuation system to meet Government objectives for high-wealth individuals should not impinge on the very high proportion of retirees with marginal assets, the target audience for increasing work participation.

The complexity of the superannuation regulations is highlighted by the more than 50 clauses dealing with aspects of regulation in the Issues Paper (Clauses 68 through 122). The regulations do not match the needs and interests of retirees. Many were introduced as a means of limiting the size of an individual's retirement assets for taxation control purposes. They are highly discriminatory in that they apply to all retirees, irrespective of the level of their retirement assets. The focus of Government should be on simplicity and encouragement to supplement income for the very high proportion of retirees with marginal retirement assets, mostly those with full and part-age pensions.

Increasing complexity and continual change to superannuation regulations is a real disincentive for mature age people, including retirees, to engage formally in the workforce. Each time a change is made to superannuation regulations, older people have to factor in how working will affect their tax positions, their pension entitlements, and their overall retirement and estate planning program. They often have little expertise in making these decisions, which often require professional advice for which they are not prepared to pay, are frustrated by continual change, and often make bad decisions as a consequence. Continual change to regulations breaches the framing principles of coherence, self-agency and system stability.

The regulations have become so complex and convoluted that the Association believes that a public Review of the structure and regulation of retirees' income, including flexibility and removal of disincentives to partake in work within their personal retirement priorities, should be commissioned.

Recommendations:

- That differing individual needs of retirees demand deregulation of the SG system during the drawdown phase and maximum flexibility for individual decision-making.
- That compulsion should be removed for SG contributions above the prescribed retirement age and award conditions adjusted to protect those conditions over the prescribed retirement age.
- That the minimum withdrawal requirement on superannuation pensions should be abolished.
- That legislation and regulations relating to the retirement phase should be separated from the accumulation phase of superannuation.
- That regulation of the retirement phase of superannuation has become so complex that a major review and new approach is required to legislation for the retirement phase.

Question 11. The *Superannuation Industry (Supervision) Regulations 1994* (Cth) prescribe age-based restrictions on voluntary contributions. Members cannot: (a) make voluntary contributions from age 65 until age 75 unless they meet a work test; or (b) make voluntary contributions from age 75.
What effect do these restrictions have on mature age participation in the workforce?
What changes, if any, should be made to these regulations to remove barriers to work for mature age persons?

The superannuation regulations fail to meet the 'coherence' principle in that they are inconsistent in application and they increase complexity thus reducing simplicity and transparency.

The objective of the regulations is to limit the ability of people of wealthier means to build their superannuation assets to levels unacceptable to the Government. This objective is not attained because it can be readily circumvented by the target group. However, the effect is to limit the ability of those retirees most in need to increase their superannuation assets, namely age pensioners and low-wealth self-funded retirees.

Low-wealth self-funded retirees are defined here as having insufficient assets to maintain their accustomed living standards across their lifetime. As set out in the response to Question 10, about one million people over the age of 65 who submitted income tax returns in the financial year 2008/2009 paid no tax or had a taxable income less than $100,000 (50,000 people had a greater taxable income and paid two-thirds of the total tax paid). There is much evidence that few low-wealth self-funded retirees have sufficient assets to last through their retirement lifetime without having to resort to some Age Pension support. There is no evidence that the work/age barriers achieve their objective of containing tax concessions but there is much evidence that they act as serious disincentives to work.

It has been argued in the Issues Paper that work/age barriers can provide an incentive for superannuation members between the ages of 65 and 75 to obtain work and meet the work test to be eligible to add voluntary contributions to their Fund. There is no evidence that the restrictions provide such incentive. To the contrary, the definition of 'gainful employment', restricted to at least 40 hours in any 30 days in a financial year, is a significant disincentive to participate in work. The definition fails the framing principles of 'participation', 'independence' and 'fairness'.

As set out in the response to Question 10, the interest of many retired people in work is to supplement their income, not to meet basic living necessities. Many do not have an interest in, or the opportunity to undertake, 'gainful work' within the definition. They have been out of the workforce for some time and cannot find 'gainful work'. They face many of the barriers to work identified in the Issues Paper. Examples are:

- women who undertook family responsibilities in their younger life, relied on their spouse to provide household income and savings for retirement, and have lost their spouse;
- retirees who do not have the capacity, skills, or need to obtain work of this magnitude within a monthly cycle;

On the other hand, many people can meet the ‘gainful work’ test informally. For example, retirees with friends involved in small business can often arrange employment for one month in a year. The practice is common and effectively circumvents the intent of the legislation.

Retirees out of touch with work, or unable to work consistently because of voluntary or family care needs, can often obtain work on a short term basis, but outside the ‘gainful work’ requirement. Examples are:

- managing or manning polling booths at Local, State or Federal elections. The work can be over one or several days but less than forty hours in thirty days;
- emergency work such as teaching or nursing, which may involve one day per week, or full time for a week or two, or being paid to stand in for a family member unable to work for illness or family reasons.

Recommendations:

- That the work/age regulations set out in Question 11 should be removed.
- That removal of the work/age regulations will have little effect on tax revenue from the group who should be targeted to increase their participation in work.
- That the 'gainful work' test should be removed to increase the flexibility for retirees to work within their personal constraints.

> **Question 12.** The *Superannuation Industry (Supervision) Regulations 1994* (Cth) prescribe age-based restrictions in relation to members splitting contributions with a spouse and making contributions to a spouse’s fund. Members cannot:
> (a) split contributions for a spouse aged 65 and over;
> (b) split contributions for a retired spouse of preservation age and over;
> (c) make spouse contributions for a spouse aged 70 and over; or
> (d) make contributions for a spouse aged 65 but under 70 unless the spouse meets a work test.
> What effect do these restrictions have on mature age participation in the workforce?
> What changes, if any, should be made to these regulations to remove barriers to work for mature age persons?

Splitting contributions, particularly where one person has been the key income generator, acts as a disincentive because the amount that can be contributed is limited by concessional and non-concessional caps. The inability to split contributions makes little sense, has negligible taxation revenue consequences from aged pensioners and low-wealth self-funded retirees (See the definition in the Question 11 response), and does not meet the principle of self-agency — the right to make decisions about matters affecting them — or the principle of system coherency. The decision to make a split or a contribution to a spouse is often determined by the circumstances of the relationship, including the degree of independence, between the partners.

Removal of the disincentive of ‘gainful employment’ discussed in Question 11 applies also to the need for a spouse aged between 65 and 70 to meet the work test.

Recommendation:
• That the regulations set out in Question 12 should be removed.

Question 20. What other changes, if any, should be made to superannuation laws, including tax laws, to remove barriers to mature age participation in the workforce?

A superannuation fund is identified in the Act S.10 as being (a) in the accumulation phase, where capital is being accumulated for the future payment of a retirement pension, or (b) in the pension or drawdown phase where the capital is being used for the purpose of paying a pension, or (c) a combination of the two. A retiree taking a pension may make additional contributions from working or from assets accumulated outside superannuation within limits specified under the Superannuation Industry (Supervision) Act.

After a person retires, the separation of assets into those which are used to pay a pension or pensions and those which are still interpreted as being in the accumulation phase arises because of the different tax treatment applying to each. Earnings from funds used to support a pension or pensions are tax free, whereas the earnings from those not used for that purpose are taxed at 15%. A retired person may nominate the proportion in each category.

The simple decision, particularly for retirees with low assets, is to nominate all funds as being used for pension purposes.
However, age-related minimum drawdown conditions are specified which apply only to the pension proportion of the assets. The balance between the minimum amount of pension to be taken from the fund and the amount of assets that will incur tax on the earnings at 15% becomes a decision for the retired person in terms of their retirement priorities and assets.

The definition of a pension

Meaning of pension (Act, s 10): A benefit is taken to be a pension for the purposes of the Act if (a) it is provided under rules of a superannuation fund that (i) meet the standards of subregulation (9A); and (ii) do not permit the capital supporting the pension to be added to by way of contribution or rollover after the pension has commenced.

prevents the capital supporting a pension being increased after the pension has commenced. A retiree with a pension, who wishes to make further contributions whether from working or otherwise, has three options:
• Commence an additional pension immediately following the contribution;
• Roll back the original pension and commence a new pension with the total amount;
• Have the contribution placed into an accumulation account (existing or new) in the fund.

The component of the regulation prohibiting addition of contributions to a pension was made in 1994 before the extensive use of account-based pensions. The Association has been unable to obtain any reason from the Taxation Office for retention of the component.

For a person with a pension from a public superannuation fund and making a contribution, the fund has to keep either an accumulation account in addition to a pension account for the person, or establish a number of pension accounts, or carry out a complex accounting procedure to commute the pension, add the contribution, and commence a new pension. Superannuation funds generally try to force members to add all contributions from paid work into an accumulation fund for that financial year for simplicity in administration. This leads to a) the contributions not being available till the end of the financial year, b) the 15% tax on employee contributions not being recoverable until after the end of the financial year when the employee pays no tax (a common situation), and c) the earnings on the contributions being taxed at 15% — in many cases, the administrative fee removes most, if not all, of these earnings. Draft tax ruling TR 2011/D3 issued on 13 July 2011 will increase the complexity further. It proposes that cessation of a pension during a financial year should be interpreted to be that the pension did not commence on 1 July of that year but that the assets should be considered to be in the accumulation phase during that financial year. A consequence of this ruling if accepted is that a person will only be able to commute an existing pension on 30 June in any financial year further blocking access to funds earned during that year. The administrative process in SMSFs is complex: minutes are required, notes to the accounts have to be properly prepared, and contributions may need to be segregated from other investments.

Each of the three options not only adds to complexity but adds to fees charged and costs of administration. Where a retired person undertakes part-time work it is quite likely that the fees charged will be a very high proportion of the SG contribution more than offsetting the benefit of the contribution.

Retirees with an account-based pension, working to supplement their income or for a retirement activity, and having SG contributions made to the superannuation fund, would expect to be simply able to add the contribution to the assets supporting the existing pension and draw these down when and as required without the complexity consequent on the regulations. The minimum withdrawal requirements can be readily adjusted if necessary.

The regulation is an example of third-party stakeholder pressure from the dominant industry in the name of the principle of ‘system stability’ at the expense of the flexibility needed to encourage participation in work. It is a major disincentive to undertaking more formally structured paid work and does not meet the principle of ‘coherence’. It is in the interests of the industry to deliberately withhold information on the options available to retirees. It should be removed or extensively modified.

Recommendations:

- That the Act (S10), Regulation 1.06 covering the definition of a pension should be modified to remove the restriction on adding to an existing pension.
- That legislation and regulations relating to the retirement phase should be separated from the accumulation phase of superannuation.
- That regulation of the retirement phase of superannuation has become so complex that a major review and new approach is required to legislation for the retirement phase.