

Age and Work barriers to superannuation contributions

NOTE: A first round of submissions was called following an Issues Paper. This has led to a Discussion Paper and call for further submissions on a series of specific questions. AIR does not have problems with questions other than the ones related to superannuation. They generally call for uniform age barriers across States in matters such as insurance, workers' compensation, safety, etc.

The Government has legislated to remove the 75 year barrier to making contributions to superannuation. The Australian Law Reform Commission propose removal of all age barriers BUT propose extending the work test to all people over 65 years; they also propose making the spouse contribution arrangements consistent across all ages but require spouses to meet the work test.

This submission is therefore focused on the work test. The question implies that they are considering making the work test more difficult.

This gives a background to the approach.

Submissions are required by the ALRC no later than 23 November. Barry Ritchie seeks comments from members which can be forwarded to him at britchi1@bigpond.net.au by 17 November. Please note that references and other details will be added after he has received your comments. Also note that there is an electronic format to be used and that is why there is no Introduction, etc.

DRAFT ALRC Second submission prepared by Barry Ritchie 15 October 2012

Age and work barriers to superannuation contributions

This submission is an expansion of the previous AIR submission related to barriers to employment of people over the age of 65 arising from superannuation and relates to the following proposals and question in the Discussion Paper.

Proposal 8-1 Regulation 7.04(1) of the *Superannuation Industry (Supervision) Regulations 1994* (Cth) restricts superannuation funds from accepting voluntary contributions for members of superannuation funds:

(a) aged 75 years and over; and

(b) aged 65 years until 75 years, unless they meet a work test, that is, where they are gainfully employed on at least a part-time basis during the financial year.

The Australian Government should amend reg 7.04(1) to remove the restriction on voluntary contributions for members aged 75 years and over, and to extend the work test to these members.

Proposal 8-6 Section 6(1)(e) of the *Superannuation (Government Co-contribution for Low Income Earners) Act 2003* (Cth) provides that government co-contributions are payable only for persons aged under 71 years. *The Australian Government should repeal this restriction.*

Question 8-1 Regulations 7.04(1) and 7.01(3) of the *Superannuation Industry (Supervision) Regulations 1994* (Cth) stipulate a work test for members of superannuation funds aged 65 years and over who wish to make voluntary superannuation contributions. Members must be gainfully employed on at least a part-time basis during the financial year, that is, for a minimum of 40 hours over a consecutive 30-day period. *What changes, if any, should be made*

to the work test? For example, should the minimum hours of work be increased and, if so, over what period?

General

The Discussion Paper acknowledged that “a person’s workforce participation, and the kinds of choices he or she will make about participation, vary within the wide age range covered by this Inquiry—‘from 45 through 65 into retirement’” (Para 1.43). It quoted the AIR statement that:

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

The importance of the role of paid work in contributing to an active retirement for people over 65 is widely acknowledged (Ref Brotherhood of St Laurence).

Structure of work and superannuation for people over the age of 65

ABS Statistics show that only about 12% (354,700) of the 3 million people age 65 and above were employed in paid work in November 2011. They show that a major change in work participation occurred from age 55-59 to age 65 and above:

- Most (87.5% or 105,000) Other Business Operators (farmers and small businesses) maintained participation in work beyond age 65.
- Few (25% or 181,000) Employees maintained participation in work beyond age 65. Of these over 43,000 were casual (defined as those without leave entitlements).
- Approximately 60% (69,000) of Independent Contractors maintained participation in work beyond age 65.
- Almost half of those maintaining participation in work (Other Business Operators and Independent Contractors) would have interest in maintaining participation and would have the administrative ability to readily meet the work test.
- The number of employees may be understated and the number of independent contractors may be overstated because some employees may establish consultancy or part time contracting on retiring from work as an employee.

The maximum number of people age 65 and above who might be encouraged to increase participation in work can be gauged from the fall in participation in work from age 55-59 of 275,000 suggesting that 20% of the age cohort at best might be encouraged to participate in work.

Superannuation factors encouraging this age cohort to undertake paid work include:

1. Superannuation pension income is not included in taxable income. Therefore, tax payable on paid work or other income is not affected by any accumulated superannuation assets;
2. Earnings from voluntary concessional contributions and non-concessional contributions to superannuation may attract the 15% tax concession;
3. The SG contribution payable by an employer to an employee of any age can be added to superannuation, taken as a lump sum, or used to take an additional superannuation pension;

Superannuation regulations inhibiting this age cohort from undertaking paid work include:

1. There is no taxation advantage in contributing concessional or non-concessional amounts to superannuation assets where income from superannuation assets used to pay a pension is less than the upper limit of the 15% marginal tax rate. This applies to most people in this age cohort;

2. There is no concessional advantage to employers of employing older age employees against younger persons; the SG contribution is the same for all ages;
3. The gainful employment test restricts the type of work opportunities available;
4. Obtaining access to the SG contribution is complicated and the amount can be reduced by fees charged;

ATO statistics show that in the 2009/2010 financial year about 10% (300,000) paid tax above the 15% marginal tax rate (about 100,000 paid tax at the 15% marginal tax rate). Apart from people who might be affected by increasing income, this is the only group who gain some tax benefit or concessions from having or contributing to superannuation.

Earnings from individual average superannuation assets held at age 65 and above are unknown but most are less than the taxable income tax-free threshold or the taxable income corresponding to the top of the 15% marginal tax rate. Therefore, for most of the 3 million people in the age cohort, there is little advantage in working to contribute to superannuation as any income earned from investing the funds will be tax free in the personal tax system. This is likely to be an explanation for the reason people in this group take all or a large proportion of their superannuation as a lump sum on retirement. The only reason for keeping some accumulated funds in superannuation is to avoid the need to manage the investment of retained retirement assets. The superannuation fund simply becomes a convenient provider of retirement investment products for this very large group.

Summary Building individual superannuation assets adds little or no value for most of the 3 million people age 65 and above. Superannuation regulations provide little encouragement for people in the age cohort to increase their participation in work.

Work Test

The work test is based on the definition of 'gainful employment' as undertaking paid work for a minimum of 40 hours in a thirty day period.

The ABS statistics do not provide a breakdown of type of work or frequency for the over 65 age cohort. However, they do provide statistics for 'non-traditional' work patterns across all employees. The percentage of casual workers working only one day per week was 2.4%; 6.2% worked 1 hour or less per day. These groups would not meet the work test. Further, 6.4% worked less than 3 months with one employer; the number of days worked in any one week varied between weeks in 16.7% of cases; and 26% reported that they did not work the same number of hours each week. A large percentage of people age 65 and over would be expected to be represented in these work patterns. These work patterns will have difficulty meeting the work test of 40 hours in any one thirty day period.

Examples of retirees using flexible work patterns were quoted in AIRs previous submission to include 'non-traditional' types of work such as working at polling booths during elections, emergency work in teaching or nursing, or standing in for a family member (supporting family members is recognised as a major unpaid work role of retired people (Para)). Many casual consulting contracts, which are often for significant amounts of work, are drawn up on the basis of a financial return for delivering a specified outcome within an agreed timeframe; the method of arriving at the specified outcome is not defined, nor is the work pattern. A common example in universities is in supervision of a research student. The supervision pattern cannot be defined as 40 hours in any one thirty day period.

The percentage of employee females fell 80% (to 72,000) from age 55-59 to age 65 and above. This compares with the percentage fall for males of 69% (to 109,000). Although females make up about 46% of total employed persons in all age groups, they make up only 33% of employed persons in the age 65 and above cohort. Females are significantly more disadvantaged by the work test and are more likely to require greater flexibility.

The work test does not take account of the amount of the retirement asset held by an individual in superannuation. Individuals unable to participate in paid work for whatever reason, and with low asset balances that allow access to the age pension, are denied the ability to add to those assets through non-concessional contributions. In contrast, those with the ability to undertake paid work, no matter what their asset balance is, can make non-concessional contributions in addition to voluntary concessional contributions irrespective of the size of their superannuation asset balance.

There are more appropriate methods of measuring gainful employment that allow for the flexibility required by the age 65 and above age cohort. These methods are generally monetary value based. For example, Centrelink allows a pensioner to estimate average weekly earnings to determine whether allowable fortnightly income is in excess of allowable income of \$152 per fortnight or \$329 per month (effective 20 September to 31 December 2012). Employers are exempted from paying the SG contribution for low income employees where the SG contribution is less than \$450 per month. The 40 hour test corresponds to an amount of \$624 per month at the minimum wage (as at 1 October 2012). A common value should be determined and applied to all cases.

Summary Of those participating in paid work, of the order of 5% are unlikely to meet the gainful employment test because of their pattern of work, despite the fact that their work is clearly gainful employment. Of those eligible to access the work test only 33% are females. A common monetary value applicable to all measures of minimum employment should be established across Centrelink and the superannuation system.

Equity in Retirement Income

AIR's policy is that people over the age of 60 without superannuation should have access to the same concessions as those with superannuation. It does not agree with the concept of a device that denies a major section of the community, who have used their own initiative to establish their retirement assets without support from government, the right to access benefits and concessions available to those with superannuation.

The Discussion Paper quotes the Cooper Review three component model for superannuation. However, the three component model does not recognise the importance of private assets accumulated outside superannuation as a retirement vehicle. Private assets accumulated while participating in and investing the proceeds of paid work form a retirement vehicle at least as significant as superannuation; accumulation of these assets has received no concessions. The argument that concessions should be granted because of compulsion is not accepted. People accumulating private assets have had to make more arduous decisions to accumulate rather than spend to protect their future and should be at least as favourably treated.

Summary. AIR does not support a work test in any form on equity grounds.

Obtaining Access to the SG Contribution

People age 60 and above and contributing to superannuation may nominate the use to which those funds are to be put; to be accumulated, to be taken as a lump sum, or to be used for the purpose of taking a pension. 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%. 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 person in terms of their retirement priorities and assets.

The definition of a pension prevents the capital supporting a pension being increased after the pension has commenced.

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.

People age 60 and above who participate in work and meet the work test have the SG contribution paid into their nominated superannuation fund. In addition to nominating the superannuation fund, they need to nominate whether:

1. The contribution is to be taken as a lump sum. The employer is required to pay the SG contribution into a fund and then the fund is required to pay the amount to the person.
2. The contribution is to be used to commence a new pension. It cannot be used to add to an existing pension.
3. To have the contribution placed into an accumulation account (existing or new) in the fund.

Another option available to the person is to request the fund to commute any existing pension, add the SG contribution and commence a new pension with the total proceeds.

Many persons in this age cohort wish to undertake paid work to supplement their income. They do not wish to have to cope with detailed, cumbersome and complex administrative processes to earn relatively small amounts of additional income. The fact that many people use default funds to accumulate their SG contribution is evidence of their unwillingness to become involved in complex administrative processes.

For people in the age 60 and above age cohort the following situation applies:

- If they meet the means test, they need to apply for the co-contribution to offset the 15% tax their employer paid on their behalf;
- If they wish to take the SG contribution as a lump sum and to avoid the 15% tax on the income from the contribution, they need to notify the nominated fund that they wish to take this option; the amount of the contribution may be reduced by a fee charged by the fund;
- If they wish to have it used to support a pension, they need to notify the fund accordingly, have the contribution reduced by any fee charged by the fund to administer the pension, and end up with multiple pensions paying small amounts.

These processes are cumbersome, complex and cause delays in receiving the funds

AIR argues that no case has been put by the ATO that justifies retention of clause (ii) of the definition of pension. It recommends that this clause be removed from the definition. AIR stated in its previous submission that this regulation is the most significant of all disincentives discouraging people in this cohort from participating in paid work. Yet it was not addressed in the Discussion paper.

Summary Complexity in the administrative process for dealing with the SG contribution and its use for people age 60 and above is the most significant disincentive to participate in paid work for people in this age cohort. There has been no case put to justify retention of the restriction to add to an existing pension. The co-contribution is a clumsy way of dealing with the cancellation of tax paid for those who do not have to pay tax for people in this age cohort because of their need for flexibility in managing their retirement income.

Data Collection

The extent to which the work test meets its objective is far from clear. For example, the Income Tax statistics do not indicate any significant non-concessional inflow to superannuation from

persons age 65 and above who work. Tax revenue from this cohort has reduced from \$8.17billion in 2007, the financial year before the introduction of Simpler Super to \$6.65billion in 2010, a fall of 18.6%. The number paying tax has decreased from 544,749 in 2007 to 393,875 in 2010, a fall of 28% suggesting that the fall in revenue has come from people at the lower end of the marginal tax rate structure. These figures include the fall in revenue from the ability to add \$1million to a super fund in the 2007/2008 financial year as well as the effect of the work test. Research should be carried out to determine the extent that people who meet the existing work test do contribute non-concessional contributions and its impact on Government tax revenue.

Recognising the increase in longevity and to aid in research on retirement incomes, the ABS and ATO should be asked to present the relevant statistics for five year cohorts from age 65 to age 90.

Response to Question 8-1.

AIR recommends that:

1. If the government insists on retaining discriminatory limitations on contributions to superannuation for people over the age of 65, then the gainful employment test:
 - should be redesigned to provide consistency between the private income allowed under the full-age pension, that allowed from participation in work under the gainful employment test, and that exempt from SG contributions and at a level equal to the existing minimum allowable income for the full age pension;
 - should be modified to include all formally established casual employment/consulting contracts;
2. People aged 65 or above with retirement asset levels below a defined level (for example, \$500,000 has been defined for increasing the concessional cap for people over age 50) should not be subject to a gainful employment work test;
3. The limitation on adding assets to existing pensions should be removed;
4. Independent research should be carried out to determine the cost to Government of inflows into superannuation from removing the work test;
5. Relevant statistics from the ABS and ATO should be modified to provide five-year statistics for ages above 65 up to age 90.