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CONTEMPORARY ISSUES IN AUSTRALIAN SUPERANNUATION - A CONFERENCE SUMMARY

by

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1: Background

The first annual Colloquium of Superannuation Researchers was held at The University of Melbourne in July this year. The Colloquium attracted about 50 participants drawn from academia, the public service and the superannuation industry in equal numbers. The diverse backgrounds of those attending was an important feature of the two day meeting and generated a rewarding cross fertilisation of ideas and thoughts.

This paper presents a summary of the papers given at the Colloquium. It should be noted that we do not necessarily agree with all the ideas presented here but have attempted to summarise the issues contained within the colloquium papers to further the discussion of the future development of Australian superannuation. John Piggott summarised the first five papers; David Knox summarised the rest.

The complete set of colloquium papers will be published by Longmans and should be available before the end of 1993.

The second annual Colloquium of Superannuation Researchers will be held in July 1994 and inquiries should be directed to the Centre for Actuarial Studies at the University of Melbourne ph (03) 344 7418. Numbers will be limited to ensure that those attending represent a broad spectrum of individuals and organisations with an interest in superannuation.

2: The Papers

Much of the first day of the conference was devoted to policy analysis. Current and projected policy initiatives, measurement issues, and the economic impacts of the superannuation guarantee were the main topics treated.

Opening Address, Brian Scullin, Executive Director, ASFA

Brian Scullin's opening address focused heavily on the Superannuation Industry (Supervision) legislation (SIS). One could sum up his talk by saying it was a harbinger of the theme of the present conference. ASFA saw SIS as both desirable and inevitable. In support of this position, he made the following points:

- SIS is a response to the need for the Commonwealth to be able to directly regulate the superannuation industry instead of having to rely upon the threat of withdrawing tax concessions. While it would be preferable for the Commonwealth to have a specific Superannuation power, using the corporations and pensions powers is probably the next best solution;
- ASFA supports the move to a strong regulatory regime in Australia which it sees as inevitable. Despite there having been no major fund collapses in Australia, an efficient regulatory regime is necessary in the "post-Maxwell" environment, particularly as there is no Government guarantee of benefits accrued under the system;
- ASFA welcomes the commitment to representative trusteeship under SIS because they see trustee representatives of employees and employers as being in the best position to oversee fund operations. In this regard, ASFA supports the requirements for full disclosure and supports the threat of intervention where funds breach the rules.

ASFA saw the key pillars of SIS as being full disclosure plus the threat of intervention. The main problem is the increasing number of specialists such as superannuation lawyers etc who are made necessary by the increasing complexity of the legislation. This complexity increases costs because it make it harder for funds to rely upon non-specialists, a problem which is compounded by the numerous other developments which are occurring simultaneously. ASFA is worried about the capacity of the industry to keep up with the pace of change currently under way.

The paper concluded by appealing for greater simplicity and indicated that simplification is an important equity consideration. It is the less well off members of funds who are least able to cope with complex provisions and who may face the greatest relative costs. To illustrate, he pointed out that ASFA was compiling a dictionary of superannuation terminology for use by the industry and specialists which would contain up to 50,000 terms.

Superannuation and National Saving: Much Ado About Nothing or All's Well that Ends Well?

Dr Vince FitzGerald of the Allen Consulting Group Pty Ltd.

Vince FitzGerald presented a paper summarising the superannuation aspects of his National Savings Report. The essential point of the paper was that the national savings objectives of retirement income policies are not just incidental but, rather, are a central element of a long term retirement income policy. This is because of implications of the prospective demographic changes and the need to ensure productive investment is undertaken in order to maintain living standards in the face of a declining proportion of people of working age.

The paper suggests that retirement incomes policy has to be based on funded arrangements. Unfunded systems can only work equitably where the demographic structure of the population does not vary much. The demographic transition which is embodied in the aging of the baby boomers will lead to dramatic demographic change.

This has implications for the pattern of age pension payments over time. In the absence of the superannuation guarantee, age pension outlays were projected to rise from their present level of around 3.2% of GDP to 5.7% of GDP in 2031.

The paper, drawing on Retirement Income Modelling Task Force estimates, reports that the superannuation guarantee should increase superannuation saving by 1.4% of GDP within 10 years. Although little impact on age pension outlays in anticipated until after 2010, eventually such outlays will decrease- by as much as 0.5% of GDP by the middle of next century. National saving is estimated to go up by about 0.75% of GDP over the next decade.

The paper argued that the modelling probably erred on the conservative side in estimating the national savings impact because the 50% savings offset factor (ie the extent to which superannuation savings are assumed to displace other, non-concessional, savings) used is most likely too high.

Expansion of the coverage of the superannuation guarantee to the self employed would add a further 0.3% of GDP to national saving within the next decade. As well, if the currently envisaged (9% + 3%) steady state requirement for superannuation guarantee contributions were increased, saving would further increase.

The paper argued for the maintenance of the current 15% tax on superannuation fund earnings as a reasonable proxy for a system of expenditure taxation but noted the scope for shifting the concessions for contributions to the margins of discretional behaviour by increasing the tax on compulsory contributions in order to pay for lower tax on discretionary contributions.

Tax Expenditures and Measuring the Long Term Costs and Benefits of Retirement Incomes Policy

Colin Brown, Retirement Income Modelling Task Force

In the debate over the appropriate tax treatment of superannuation saving, there is perhaps no issue which generates more confusion than that of revenue costs. This confusion arises in the first instance from the inherent difficulty of satisfactorily specifying a counterfactual economy in which such concessions are not available. Actual argument, however, more usually takes the form of a wrangle over the plausibility of some particular estimate, rather than of the (usually ill-specified) counterfactual.

The revenue costs of superannuation tax concessions are conventionally measured by comparing the revenue collected from superannuation contributions, or superannuation earnings, with an estimate of the revenues which would have been collected had the personal income tax been applied to these bases in a non-concessional way. This methodology was first laid out in Surrey (1973), and is used in the Tax Expenditure Statement produced annually by the Treasury. This procedure thus attempts to measure the cost of departing from the traditional definition of the income tax base. There are several well known methodological difficulties with applying this approach to superannuation tax concessions. They have been enumerated and commented on by, among others, Knox (1987) and Bateman and Piggott (1992), who also provide a numerical example.

The importance of the present paper is twofold. First it specifies alternative and more appropriate procedures for calculating the tax expenditures, the result of which is likely to be a dramatic reduction in its size. Second, it reports a much more comprehensive range of tax expenditure estimates for superannuation tax concessions than has previously been available.

If the TES estimates of superannuation tax expenditure are used as a time series of the ongoing cost of the superannuation tax concessions, and the time series is projected forward, the recurring revenue gains from removing the superannuation tax concessions will be overstated.[1] Therefore, simple projections of the annual superannuation tax expenditures cannot be interpreted as an estimate of the ongoing cost of the superannuation tax concessions. These must be estimated by comparing the tax revenue obtained from a concessionally taxed accumulation with that obtained from a separate non-concessionally taxed accumulation. Furthermore, the assessment of the total costs of a retirement incomes policy must take into account the age pension entitlements and the tax payable under both the concessionally taxed and non-concessionally taxed benchmarks for each year of retirement for each person. The individual annual tax expenditures can then be aggregated to obtain a time series estimate of the aggregate cost to Government of a retirement incomes policy.

The paper concluded that the most appropriate basis for estimating the costs and benefits of the superannuation tax concessions is a comparison against an income tax benchmark which takes account of the likely savings offset factors that will apply to the various classes of person modelled, the likely tax rate on alternative saving and the impact of superannuation savings on the age pension and taxes paid in retirement. Establishing the value of the concession requires a modelling approach that accrues benefits separately under a concessional and non-

1. This and the following paragraph draw heavily on James Satrapa's summary.

concessional benchmark regime. The modelling results were reported to be sensitive to a number of assumptions. Considerable research needs to be done to develop reasonable assumptions concerning the values that should be used in modelling the costs and benefits of retirement incomes policies.

However, it was notable that under some not unreasonable sets of assumptions, the net cost of superannuation tax concessions to the government were actually negative. In particular, if it was assumed that tax preferred superannuation saving would, in the absence of tax concessions, not be saved at all, then it actually pays the government to offer the tax concession.

(This contrasts sharply with the current official calculation of superannuation tax expenditures, which account for some 40% of identified tax expenditures.

If the approach discussed in this paper is adopted - and there is a good chance that eventually it will be, given that it originated with the RIM Task Force - then it will be that much easier to argue for superannuation tax concessions as policy evolves over the next period, since the overestimation of the revenue cost of such concessions implicit in current tax expenditure estimates will be ameliorated or eliminated. At the least, however, the traditional tax expenditure estimate will lose some of its traditional authority as a measure of revenue cost).[2]

Notes on the Equity Implications of Mandated Funded Pension Schemes

Hazel Bateman, Geoffrey Kingston and John Piggott, School of Economics, University of New South Wales.[3]

The authors attempt to come to grips with the largely unexplored equity implications of such schemes as the Australian superannuation guarantee, which they call "mandated funded pension schemes". A mandated funded pension scheme is defined as a policy where some proportion of earnings are required to be put aside and preserved for retirement. The authors report that as the 'baby boom' generation ages, national retirement income plans of the mandated funded variety

2. These observations are personal comments by the authors.

3. This summary is reproduced, with minor amendments, from James Satrapa's summary.

are beginning to be introduced in countries which have previously relied on electorally popular unfunded social security.

They note that the reason for the introduction of mandated funded schemes arises out of the concern expressed by policy makers at the escalating cost of unfunded paygo schemes that is projected to occur as a result of the rise in the aged dependency ratio (ie: the ratio of the number of persons aged over 65 to the number of people in the 15 to 65 age group). In other words, it is a question of inter-generational equity because in an unfunded national scheme, the rise in the aged dependency ratio places a proportionately greater burden upon the working population which is paying for the retired population out of current tax outlays.

Mandated schemes have in their favour a comparative immunity from various potential avenues for generational exploitation. What one gets out of such a scheme is directly linked to what one puts in to it.

The main concern about mandated funded schemes is expressed within the context of intra-generational equity. In particular:

- if the cost of contributions is largely paid for through slower real wage growth, then the working poor may suffer more through denied access to consumption today than they gain through increased retirement resources;
- certain groups in the workforce, especially those with broken work histories (predominantly women), and women in general, will tend to experience inadequate retirement income replacement in this type of scheme.

The authors focus on each of these points with special reference to the Australian superannuation guarantee.

If the working poor are defined as those employees who have no discretionary income, that is, they must spend all of their available income to survive, they may rationally view the age pension as providing adequate income replacement in retirement, and have their welfare worsened by forced life cycle saving - they may well prefer higher wages now to higher retirement income. However, no evidence exists about the magnitude of this effect.

The main impact of SGC upon the working poor may well be in housing. This could manifest as a reduction of their housing repayments and therefore the value of their housing services. There may also be cases where the lower wage growth likely to be imposed by the introduction of the SGC will force some people out of home purchase altogether. Because owner-occupied housing is not taxed in Australia (except for municipal rates), whereas earnings in SGC accumulations are taxed at a statutory rate of 15%, some poor people will be driven out of an untaxed asset into a taxed one.

To the extent that women are put at a relative disadvantage by the structure of occupational superannuation, they are likely to be disadvantaged by a compulsory scheme with the same features, although the authors noted that the age pension acts as a cushion for people on low incomes. Women's relative deprivation will be substantially reduced by the way in which the SGC interacts with the age pension.

While the authors are under no illusion that gender related issues can be addressed by superannuation reform alone, they recommend that from the equity rather than efficiency viewpoint, certain steps can be taken, such as:

a. the establishment of shared SGC superannuation property rights;
b. a requirement that annuities purchased with SGC accumulations be joint with the retiree's spouse and should have a reversion clause;
c. for first home buyers, the establishment of a tax free savings scheme unrelated to superannuation, rather than access to superannuation accumulations for home purchase.

Broadly, the paper gave the impression that equity issues were probably not a critical negative in assessing the superannuation guarantee, and that specific policies may well be available to address specific categories of disadvantage flowing from the scheme. However, it also emphasised that there had been little research on the topic, and that more detailed work was required.

A Critique of the Direction of Current Superannuation Developments Using a Simulation Approach

David Knox, Centre for Actuarial Studies, Department of Economics and Commerce, University of Melbourne.

This paper examines the Government's announced long term objectives of a total SGC contribution rate of 12%. It asks two questions:

a. Is a 12% contribution rate sufficient?
b. What are the major risks involved and who bears them?

Numerical insights into these questions were derived from a simulation model generating stochastic estimates for investment returns and the inflation rate.

On the first question, the author concludes that a superannuation contribution rate of 12% of salary provides, *on average*, a reasonable retirement income in terms of final salary for a single male age 65 assuming that the contributions have been paid for at least 40 years. It is important to stress that this result is an average result and that some individuals who have saved for 40 or 45 years will receive an inadequate retirement income due to the variability of the investment returns during the pre-retirement period.

However, even if we concentrate on the average result (which does not represent the total story), a 12% contribution rate is not sufficient for most individuals. Some of the circumstances where a higher contribution rate is needed include:

- females who have long life expectancy
- members with dependent spouses
- individuals who choose or are forced to take early retirement
- individuals who enter the workforce later due to early periods of unemployment or increased education
- individuals who do not work full time throughout their career.

In many cases, an individual may be subject to a number of these factors (eg a female with some part time work experience who retires at age 60) which would result in the need for a very high contribution rate if a reasonable retirement income benefit is to be provided.

Because of the enormous variety of individual circumstances, it is impossible to select a long term contribution rate that will be satisfactory to everyone. However, the paper suggests that a total contribution rate in the order of 15-18% of salary should become a long term objective to provide greater financial security to a much higher proportion of retirees.

On the second question, the paper identifies and focuses on two risks - annuity rate risk, and investment risk. Whether these are borne by the employer or the member depends on the style of superannuation scheme being considered. The following matrix lays out the relevant combinations:

Type of Fund	Investment Risk	Annuity Rate Risk
Defined contribution	Member	Member
Defined benefit-lump sum	Employer	Member
Defined benefit-pension	Employer	Employer

Perhaps the most important result of the paper relates to investment risk. Using the base assumptions (single male participating full time in the workforce continuously from age 20 to age 65 etc), the average retirement income arising from a contribution of 12% of salary for 45 years is an indexed lifetime annuity equivalent to 61.15% of the person's final salary. Although this constitutes, on average, a reasonable retirement income in terms of final salary, the uncertainty of investment returns achieved each year produces a considerable spread of results: the level of retirement income is equally likely to be 35% or 96% of final salary. This variability can be reduced by assuming a more conservative investment strategy, either throughout the contribution period or in the final few years prior to retirement.

On annuity rate risk,, the paper points out that the annuity rates offered at retirement to convert the accumulated benefit to a lifetime annuity can have a significant impact on the ultimate level of retirement income. In particular, if the underlying interest rate used to determine the indexed annuity rate increases from 1% above the inflation figure in the year preceding retirement to 2% above this inflation rate, the expected level of the annuity increases by 21.4%. The author emphasises the importance of this result in the Australian context because the Australian superannuation system is based around the provision of a lump sum benefit at retirement, both for defined contribution and defined benefit funds. Even if the Government succeeds in persuading a higher proportion of retirees to take their retirement benefit as an annuity, the actual level of any lifetime annuity will depend on the annuity rates available at the date of conversion.

In the author's judgement, a more efficacious system of retirement income would exist if the risks were shared between the employee, the employer (beyond a certain size) and the Government.

Personal Comment

Implicit in much of the first day's proceedings was an issue which was not addressed as a central theme in any of the papers, but was alluded to by almost all of them - retirement benefit design. The FitzGerald estimates of the contribution of the superannuation guarantee to national saving are highly sensitive to the "dissipation rate" - the proportion of retirement benefit which is used for purposes other than the acquisition of a lifetime retirement income product. The paper by Colin Brown also relies on the assumption that an appropriate annuity or pension will be taken with superannuation accumulations. Bateman et al refer to the importance of reversion features of retirement income products in their appraisal of the equity implications of the superannuation guarantee. And David Knox's treatment of annuity rate risk assumes that annuities will be bought.

Many of the questions raised by the papers would have better answers and more satisfactory resolutions if appropriate retirement income streams were mandated. This is recognised by policy makers, and continuing policy change, edging toward compulsory annuity purchase or pension provision, must be expected over the next period.

The characteristics of an "appropriate" retirement income product which might become mandatory are still being debated. But whatever the exact path of evolution towards compulsory retirement income streams, this new policy frontier presents challenges and opportunities to the superannuation industry. Retirement income products which are innovative in minimising retiree risk while providing adequate return, in an environment where there is no government guaranteed national earnings related retirement income scheme, must be designed and marketed. This will remain for the foreseeable future an area where industry innovators can make a major contribution to the social efficacy of Australian retirement income policy.

Australia's Retirement Incomes System: Interactions and Attitudes

David W Kalisch and Nigel Patterson, Department of Social Security

Introduction

This paper commences by noting that the Government has twin objectives in terms of retirement incomes: namely poverty alleviation (which is carried out through the age pension provisions) and income maintenance (which is primarily conducted through superannuation and, more recently, the SGC requirements).

The authors note that the age pension is the predominant source of income for most aged Australians and that about two-thirds of age pensioners receive the full rate of pension (ie it is not reduced by the means tests). They also note that 70% of pensioners are female, which is not surprising given their longer life expectancy and earlier pension starting age.

Following this general review, the authors consider the interaction between the two systems of retirement income (ie the age pension and superannuation).

Interaction between the age pension and superannuation

An important issue in this interaction is the extent of "double dipping". Kalisch (1992) has defined double dipping as "the practice of dissipating rapidly at or before age pension age a superannuation lump sum which has received significant tax concessions, ... , with the express intention to receive a greater age pension."

Using this definition, they note that the incidence of double dipping critically depends on the size of the superannuation benefit received. They also claim that a married couple could use a lump sum of around $100,000 to purchase an indexed annuity equal to the age pension income test free area. Although I believe that this amount may be a little high, their conclusion is interesting. That is, as most current superannuation beneficiaries receive lump sum benefits less than $100,000, they cannot be accused of double dipping as the income equivalent of their lump sum would not affect their age pension entitlement. It seems to me that this conclusion highlights the need for a better interaction between the two systems.

They also note that if the Government wishes to 'claw back' some of the tax support provided to superannuation, the amount clawed back will depend on:

- the size of the benefits received;
- the thresholds (or trigger levels) used for the introduction of claw back;
- the rate at which the claw back operates (eg 50%); and
- the form of benefit paid.

The authors also investigated the investments that arose from these lump sum benefits and noted that most recipients invested in income generating assets, property (normally their home) and the repayment of debts. They concluded that "the vast majority of recipients of large lump sums invested them wisely and did not demonstrate any widespread desire to dissipate them quickly." However, later in the paper, they noted that "With the anticipated growth in the average level of superannuation end benefits, ... , there may be a greater likelihood of double-dipping activity in the future than appears evident now."

The Sweeney Report

The paper also discussed the findings of the 1992 Sweeney Report into the intentions and attitudes of Australians towards superannuation. In brief, it found that Australians were confused about superannuation (which should not surprise us!) and that there was still considerable support for an age pension as a reward for paying a life time of taxes.

Key issues highlighted in this Report included:

1. the general confusion about superannuation due to the large number of changes. It noted that if the confusion level was lower and the confidence and understanding level higher, individuals may be willing to contribute a greater amount;
2. the vast majority of individuals have no idea of the level of superannuation contributions that are required to provide a reasonable level of retirement income;
3. there is a strong belief that employer contributions will be sufficient to ensure maintenance of a comfortable standard of living in retirement; and
4. most self employed individuals are contributing 5% or less to superannuation.

In general, these issues highlight the need for greater stability in the system and an increased level of education so that, over time, we all begin to realise that the required level of superannuation contributions is much higher than even the Government's aim of 12%.

Conclusion

This paper confirmed the impression gained from the earlier papers that the Australian retirement income system needs further change. There is limited interaction between the two systems and most Australians are unwilling to voluntarily contribute at the required rate due to the rapid rate of change that we have experienced and which has affected the confidence in the system.

Allocated Pensions: A Technical Overview

Cary Helenius, J B Were & Son

Introduction

This paper compares the investment of a lump sum superannuation benefit into an allocated pension product with investing the same benefit into alternative investment schemes, namely a unit trust or direct investment. In most cases, the allocated pension provides the same level of indexed income for a longer period of time than the unit trust but for a shorter period of time than the direct investment alternative.

The model

The model used requires a number of assumptions including age, sex, the size of the benefit, the benefit components, the investment mix chosen, characteristics of the investments, inflation, tax, expenses and the required income stream.

The methodology chosen is that a level of after tax income is chosen and the model then calculates the number of years that this income can be maintained. Alternatively, it calculates the residual asset values after a set period of time.

Helenius notes that the three most critical factors in the effectiveness of an allocated pension as an efficient method for obtaining an income stream are:

- the appropriateness of the underlying investment mix;
- the tax effectiveness of the income stream;
- the cost efficiency of the investment process.

The investment mix

The results of the projections vary significantly by altering the investment return and CPI assumptions. The author notes that:

a. the ability of retail allocated pensions to effectively utilise the franking credits is important;
b. when franking credits are unable to be utilised by the allocated pension fund, fixed interest investments become the most efficient form of investments for the allocated pension; and
c. when the equity exposure is increased in the retail allocated pension, a longer period of income is produced. However, the annual performance becomes more volatile.

Tax efficiency

In respect of taxation, the author notes:

- the ability to split income is an important consideration in the comparisons
- the ability to use franking credits lowers the average tax rate for the unit trust and direct investment alternatives but actually increases the average tax rate for the allocated pension due to the higher pension paid and the effect of bracket creep;
- higher levels of lump sum tax increase the effectiveness of allocated pensions as this tax is deferred;
- the level of the deductible amount is an issue; and
- indexation of the capital cost base for investments outside an allocated pension is a valuable tax benefit.

However, he notes that the overall impact of tax is small when compared to the impact of charges. This is an important conclusion as many decisions are tax driven and do not take full account of the expenses.

Cost efficiency

The author notes that costs are the most important consideration when comparing alternative investment strategies. He suggests that "if an assumption is made that the same gross return can be achieved from holding direct investments, ... which is not an unreasonable assumption given the existence of listed investment companies and given that some retail managers attempt to merely replicate the market indices, then cost is the single most important factor."

This conclusion may appear obvious but is crucial. I believe that increased pressure will be applied to the existing margins in the years ahead and that consumer pressure will force some managers to cut the existing administration and investment charges. This pressure is especially evident within a low inflation environment.

Problems

Finally, Helenius notes that 50% of individuals will run out of money if the existing minimum age related factors are used. The alternative for these individuals, who represent those who live longer than the average, is to accept a declining level of real income in their later years.

He also identifies an apparent anomaly in the logic of the proposed Social Security treatment of allocated pensions.

Conclusion

This paper highlights the fact that the 'best' investment to produce an income stream in the post-retirement years depends on a large number of factors. These include the investment mix chosen, the taxation treatment of the individual and the investments but, most importantly, the expenses and charges applied by the manager.

Determinants of Financial Disclosure Practices by Australian Publicly Offered Superannuation Funds
Paul J M Klumpes, Australian National University

Introduction

As suggested by the title of the paper, Mr Klumpes researched the issues that affect the information disclosed by superannuation funds that are offered to the public. He commences by suggesting that the promoters of these funds will act to maximise their own self-interests. He then investigates a number of hypotheses linked to the financial disclosure decision.

The hypotheses

The six hypotheses postulated in the paper have been developed from previous research and are presented with some supporting discussion.

They are that the propensity of publicly offered superannuation fund promoters to voluntarily disclose financial information in promotional brochures increase where:

i. the administration/management fee is relatively lower;
ii. they manage a relatively large total investment portfolio;
iii. there are lower realised gains or losses on the disposal of their total managed investment portfolio of assets;
iv. marketing relationships with banks are established;
v. the degree of their regulatory supervision and monitoring mechanism increases; and
vi. the unrealised net investment return earned on their total investment portfolio is relatively high.

The results

Data was acquired from a sample of 94 brochures issued to the public offering superannuation funds during 1990-93. These included products offered by life insurance companies, friendly societies and other promoters subject to the Corporations Law prospectus requirement.

Klumpes used an index to weight the relative importance of each identified piece of financial disclosure. It is interesting to note that the disclosure points for an index out of 30 ranged from 0.5 to 18.0 with an average of 7.90.

This index was then used to perform a regression analysis with variables representing each of the above six hypotheses.

The regression results supported the first five hypotheses in both the suggested direction and at a significant level. However there was no relationship between the level of financial disclosure and the level of unrealised net investment returns. He suggests that the absence of this relationship may be due to heavy competition in the investment management area. Personally, I was not convinced about this hypothesis in the first place!

Conclusion

Klumpes has suggested that there exist a number of factors that influence the level of financial disclosure in brochures and prospectuses prepared for publicly offered superannuation funds. Whilst some of these factors may remain, I believe that we must see an increasing level of financial disclosure and that the significance of some of these factors may decline in the future.

The identification and classification of the attributes and benefits of Personal Superannuation in Australia

Tony Ward, University of Central Queensland

Introduction

This paper reviewed 37 sales brochures produced by 33 registered life offices in respect of personal superannuation products. Rather than researching the financial information disclosed (as in Klumpes' paper), the objective of this paper was to identify the different product attributes and benefits of ownership used in the marketing of personal superannuation products.

An 'attribute' is defined as a piece of information or fact presented in the brochure. The definition used was "a fundamental, characteristic quality of the product." In contrast, a 'benefit' is a gain that arises to the consumer on the purchase of the product. The definition used was "an advantageous effect of product purchase accruing to the buyer."

Naturally, a degree of interpretation is required to determine the difference between an attribute and a benefit in some cases. However, in most cases, it was reasonably clear. In the low number of cases where there was an unclear differentiation, they were deleted from the study.

The results

As mentioned above, 37 brochures were investigated. The following table highlights the major results, including the average and range recorded in respect of a number of the investigations carried out in each case.

Characteristic	*Average*	*Minimum*	*Maximum*
Number of different attributes	46	14	94
Total number of attributes (including repetitions)	84	16	220
Number of different benefits	20	7	36
Total number of benefits (including repetitions)	33	7	69
Ratio of total attributes : total benefits	2.53	0.59	10.53

The range, as shown by the minima and maxima, clearly indicate different emphasis adopted by various offices in the marketing of their personal superannuation products. In particular, the large range in the ratio of total attributes to total benefits highlights a different marketing philosophies and approaches. A low ratio suggests the philosophy of selling on the basis of the benefits of the product whereas a high ratio occurs where the office is relying on a more factual product description.

Ward comments that "The reason for this vast disparity (in the ratios) requires further research, in order to identify the apparently different underlying market philosophies." He also suggests that the methodology used in this paper could be used for any service product.

Conclusion

The marketing of personal superannuation products represents a wide range of products targeted at a number of different markets. It should be apparent that the same brochure (or even the same philosophy) is not suitable for all markets and that variations will occur. Nevertheless, as the marketing of superannuation products affects a larger proportion of the Australian population, analyses of this type will be undertaken to improve the effectiveness of various marketing strategies.

Women in Education and Early Retirement

Margaret Patrickson, Linley Hartmann and Leonie McCarron, University of South Australia

Introduction and Background

This study reports on interviews conducted with a small sample (96 in total) of females, aged 50 and over, employed by the Education Department in South Australia. The research was concerned with the longer term consequences of the changing financial status of women. It noted that many of the recent improvements, linked to greater employment opportunity, have arrived too late to provide significant help for these women near retirement.

The paper also highlighted the great changes that have occurred during the last three decades in respect of women employees. Prior to 1966 only single females were eligible to join the superannuation scheme and part time employment was unavailable until 1979. However, part time employees had no superannuation until 1989. As pointed out by the authors, these past conditions of employment must have consequences for the financial decisions made by these employees now approaching retirement.

Results

Less than 20% of the sample have a continuous employment history since they first entered the workforce while the most common period out of the workforce was 6-10 years. In terms of superannuation, 78% of support staff and 46% of teaching staff have been contributors to superannuation for less than 5 years. In addition, 20% of the sample are members of a personal superannuation fund.

The authors note that the options, in terms of early retirement and financial planning, available to these women are generally more complex than those considered by their male counterparts. The reasons for this include the fact that:

- few have reached a period of 30 years service which is required to receive maximum benefits under the superannuation plan. This means that each extra year of service is very valuable in terms of superannuation;

- many of these women are working for personal reasons and these are not primarily financial. Hence there is little interest in early retirement and a strong commitment to working.

It is also interesting to note that these women do not have an "ideal retirement age" which is in contrast to an earlier study with a male sample where the ideal retirement age was approximately three years earlier than their expected retirement age.

Conclusion

The authors conclude that women's view of early retirement is very different from the generally accepted male view. The reasons are likely to include past financial discrepancies (e.g. in the superannuation area) and the fact that some women perceive early retirement as a return to domesticity, which they do not consider to be an advantage. With increasing superannuation coverage, the difference between men and women will decrease in the future. Nevertheless, contrasting perceptions and desires between male and female employees will probably remain.

Superannuation and the Small Business

Rebecca Benedict, Griffith University and Tapen Sinha, Bond University

Introduction

This paper commences by noting that there are at least 800,000 small businesses in Australia who employ 25% of the workforce. In terms of superannuation, these employees have tended not to be covered in the past. Furthermore, small business are being treated differently under the SGC with the commencing minimum contribution rate at 3%.

This research reports on the results of two surveys sent to small businesses. The first was before the introduction of the SGC (ie prior to July 1992) whilst the second one was in January 1993. For both surveys, about 75% of the respondents employed between 3 and 10 employees on a full time basis.

The results

From the results of the first survey, the authors noted that the respondents had the following concerns about superannuation for small business:

- the safety of superannuation money;
- the possibility that the fund's administration costs may exceed the investment earnings;
- the additional administrative burden of the SGC;
- the problem of labour turnover and their superannuation entitlements;
- the extra costs that may lead to retrenchments or even closure of the firm; and
- the fact that assets are being tied up in a superannuation fund and not in the family business.

It is interesting to note that 83% of the respondents were already contributing 3% into superannuation prior to July 1992 with 42% contributing to an employer fund and 36% to an industry fund.

When they were asked about their future actions in respect of the forthcoming SGC, their answers were:

- 15% were planning to reduce employees;
- 13% would raise prices;
- 11% were planning to cut costs; and
- 17% were planning no action.

The second smaller survey was conducted in January 1993 after the introduction of the SGC. The authors suggest that the most important results from this survey were that 43% of respondents were not aware of the future changes to the SGC and that 81% were not planning to take any action to meet these future increases.

It is also worth noting that when asked about the actions that the employer has so far taken to meet the costs of mandatory superannuation, the responses were that

- 61% had reduced profit margins;
- 26% had raised prices;
- 21% were using more casuals and part-time employees
- 15% had lowered wages; and
- 15% had reduced the total number of employees.

Conclusion

Although the results of the second survey come from a pilot study, and further work is needed, there is no doubt that the introduction of the SGC has had an impact on smaller businesses. It is also clear, and not at all surprising, that a number of smaller employers have major concerns about the introduction of compulsory superannuation. These include the extra costs and the burden of additional paperwork.

Earnings Replacement Programs: Are they a policy initiative and regulatory model in the public interest?

Sue Taylor and Peter Little, Queensland.University of Technology

Introduction

This paper discusses the reasons for the introduction of Australia's compulsory superannuation system, with the help of several theories of regulation. It then goes on to raise five important issues which will influence the future direction of Australian superannuation. As noted in the paper's abstract, the underlying purpose of the paper is to investigate major conceptual weaknesses in the regulatory framework of occupational superannuation and concludes that superannuation investors do not have the same power as corporate shareholders.

The Theories of Regulation

The authors discuss the following three theories which seek to both explain and predict regulatory activity.

The first is the public interest theory. There are various forms of this theory including:

i) the consumer protection concept in cases of market failure;

ii) the balancing of national interests between competing interest groups; and

iii) a national interest objective which overrides private interests.

The authors conclude that the development of compulsory superannuation indicates that it was introduced in the 'national interest' with national economic goals far outweighing the attention paid to the rights of individual superannuation consumers.

The second theory of regulation is the regulatory capture view. Under this approach, it is suggested that the regulators have been "captured" by the industry or other agencies so that the effectiveness of the regulation is weak. The authors conclude that while the implementation and administration procedures of the ISC may have the characteristics of being captured, this is not an accurate interpretation of events. Rather, the policy initiatives had their origins in the government's need to alleviate future budgetary pressures (ie a narrow public interest objective).

The third theory of regulation is known as the private interest theory where governments react to public demands. In effect, industries or firms wield political influences and responses from the government are sought by the 'producer' private-interest groups for whose benefit the regulation is primarily designed. The authors note that while the producer groups within the superannuation industry will benefit from the introduction of compulsory superannuation, this development was in response to demands from the providers.

Having reviewed the introduction of the SGC in terms of the three major theories of regulation, the authors then raise five critical issues.

1. What were the factors that led to the demands for, and the adoption of, the compulsory earnings replacement programs and their associated regulations?

The authors suggest that two of the major reasons for the introduction of compulsory superannuation was a coalition between the ACTU and the government together with the public interest policy to ensure the provision of adequate and secure levels of retirement income through the superannuation system.

In addition, the demand for compulsory superannuation appears to have originated as a response to alleviate the increasing demands on budgetary resources for pension benefits. In terms of the theories outlined above, this objective is consistent with the 'public interest' approach.

2. Why was the original trust law basis of the superannuation industry retained as the primary protection mechanism for beneficiaries in these programs?

The authors, in quoting Lord Browne-Wilkinson, highlight the differences between a traditional trust structure and a superannuation trust. These differences include:

- the members are beneficiaries not volunteers;
- there is an underlying contract of employment;
- the size of the trust fund is variable;
- the employer continues to have a financial interest; and
- the trustees have power to amend the scheme.

They also note the First Report from the Senate Select Committee on Superannuation which argued that "there was a strong preference for retaining both the trust structure and trust law foundations of superannuation." The difference between the trust *structure* and the trust *law* used to manage the structure is an important issue. Indeed the authors note that in the United Kingdom there is a preferred alternative, after a decade of debate, to retain the trust structure but to replace the trust law as the primary protection mechanism for members.

They conclude that "the maintenance of the 'paternalistic' trust basis which was originally developed to protect individuals who were deemed to be incapable of protecting their own interests, has apparently been assumed necessary to achieve the (Government's) economic objective."

3. What was the original position of fund beneficiaries in the superannuation industry under trust law before the introduction of compulsory earnings replacement programs?

In this section of the paper, Taylor and Little are concerned with the position of the fund member prior to the introduction of the SGC. In particular, they consider the member's position in respect of **exit** (ie the option to leave) and **voice** (ie the option to protest or complain).

They find that there existed barriers to both the options of exit and voice for members of superannuation funds. The reasons include the costs involved of any action, the availability of limited information (particularly prior to OSSA), barriers within trust law and the absence of market pressures on fund trustees and some producers.

As these problems existed before the introduction of compulsory superannuation, it was natural for the authors to investigate the effect of recent changes.

4. What are the effects of the government's current and proposed regulatory models on this original position of fund beneficiaries?

The authors discussed the problems raised above in terms of barriers to Exit and Voice by members in terms of the original OSSA, the 1992 amendments to this Act and the recently introduced SIS Bill.

In terms of the cost-based barriers to action, the authors suggest that these barriers appear to have intensified due to:

- the introduction of national award-based or industry-based schemes which have located the administration of the fund in a single capital city away from many members;

- the complex governing structure of many industry funds; and
- the role of the ISC which has tended to establish relationships with the providers and funds but not the beneficiaries.

They note that the SIS Bill attempts to partially remove these costs and that the new powers given to the ISC should enable it to act more as a protectors of member's interest. However the authors conclude that much is left to common law and the enforcement framework cannot be favourably compared to the Corporations Law.

In terms of access to information, the authors note that OSSA required members to receive personal statements but that the onus was left with the member. The subsequent OSSA amendments and the SIS Bill provide for better information but the authors suggest that the absence of an accurate public data base means that this information must be judged in a vacuum and not in the general market place.

In general, the authors believe that the introduction of the SGC and the associated regulations have not been primarily designed to protect and further individual rights. "Rather, the functions of the regulatory models have the priority of ensuring that superannuation both contributes to the government's broader economic goals ... and to require people to provide for their own retirement - a national interest objective." This conclusion of national interest and limited rights to the member led the authors to their final issue.

<u>5. How do the rights of occupational superannuation fund beneficiaries compare with the rights enjoyed by corporate shareholders?</u>

The authors note that there are important differences between superannuation trust beneficiaries and corporate shareholders. These include:

- they are all small investors;
- they are often required to invest in certain superannuation funds and therefore cannot leave;
- they are required, by law, to invest for long periods and in larger amounts than is normal;
- they are not able to access a national public data base; and

- their superannuation represents a significant proportion of their lifetime's savings.

The paper notes that the Corporations Law attempts to balance national economic interest and investor protection. It is also suggested that the proposed superannuation regulations do not meet this balancing role to the same extent as the Corporations Law.

Conclusion

This paper set out to establish the underlying reasons for the recent introduction of compulsory superannuation in Australia. It found that the SGC was introduced with a narrow 'national interest' objective but that within this context individual investors "remain embedded in a fundamentally inappropriate framework, characterised by such barriers to the right of exit and voice as would be unacceptable to any other investor. ... Indeed the present disparity between corporate shareholders and superannuation beneficiaries is fundamentally inequitable."

The authors suggest that there is a likelihood of substantial problems for investors in a system where there is limited protection and an inactive market for corporate control. Their final conclusion is that "the government has a responsibility to ensure that investors in superannuation products have equivalent rights and protections to those which are taken for granted by other investors and consumers."

A personal comment

I believe that Sue Taylor and Peter Little have raised issues which represent an important challenge for the superannuation industry and the government. We may not agree with all their conclusions but there is no doubt that the era of consumerism is upon us. The right of exit and voice, within certain limits, must be the other side of individuals being given greater individual responsibility to provide for their own retirement. An increased level of personal choice is an *essential part of our trend towards greater individualism which is now prevalent in many aspects of our society. We may not all support the trend, but I believe that it will take a major 'event' to reverse this societal trend.*

Financial Reporting by Superannuation Funds: Contracting and Political Costs of Accounting Regulation

Natalie Gallery, Griffith University

Introduction

The superannuation industry is well aware of the introduction of AAS 25 which requires each superannuation fund to prepare a general purpose financial statement. Although the superannuation industry responded in a strongly negative manner prior to its introduction, it is now a fact of life.

However, even with the introduction of this accounting standard, superannuation fund trustees have a number of accounting policy choices, including when to adopt AAS 25. The research proposal outlined in this paper suggested several hypotheses relating to the timing of the introduction of the standard. At the time of the colloquium, the research into the hypotheses had begun, but the results were not available.

The suggested hypotheses

The hypotheses suggested by the author, together a brief rationale for them, are as follows:

- Superannuation fund governing boards with an equal number or majority of employee representatives (will) adopt AAS 25 earlier than boards with a majority of employer representatives.

  The author suggested that employee representatives are expected to minimise the costs incurred by members obtaining financial information and therefore will be willing to adopt the standard early.

- Defined benefit funds (will) adopt AAS 25 later than defined contribution funds.

  The reason for this suggested result is that decision making for defined benefit funds are dominated by employer representatives. Personally, I remain to be convinced of this rationale.

- Superannuation funds governed by a corporate trustee (will) adopt AAS 25 earlier than funds with other types of governance structures.

  The author suggests that as corporate trustees are already preparing reports in accordance with mandatory accounting rules, it is likely to be efficient to also prepare the fund reports in accordance with these rules.

- The investment portfolios of defined contribution funds (will) have higher risk after adopting AAS 25 than before adopting the standard.

  The suggestion is that the reporting standards will encourage DC funds to improve investment returns by investing in higher risk strategies.

- The investment portfolios of defined benefit funds (will) have lower risk after adopting AAS 25 than before adopting the standard.

  The author suggests that DB funds are under pressure to decrease their investment return volatility and will therefore adopt a lower level of risk. Personally, I believe that if the investment policies of superannuation funds are found to be driven by accounting standards and not by the needs of the member and/or the liabilities of the fund, then we are most certainly going down the wrong road.

- More funds restructure in the same accounting period that AAS 25 is adopted than in prior periods.

  The author suggests that an incentive for restructuring is to streamline reporting requirements and that, in terms of efficiency, it is reasonable to adopt AAS 25 at the same time.

- Superannuation funds which have an income reserve account (will) adopt AAS 25 later than funds with no reserving policy.

  This hypothesis is due to the fact that AAS 25 does not permit an income reserve account to be presented in the financial statements.

- Large superannuation funds (will) report higher effective tax rates than small funds.

  The logic proposed to support this hypothesis is that larger funds are subject to greater public scrutiny and that if low rates of tax are reported, there will be greater political pressure to increase these tax rates. Although theoretically plausible, I wonder how much time trustees give to the tax rate declared.

- Large superannuation funds (will) report higher effective tax rates after adopting AAS 25.

  In following on from the previous logic, the author suggests that funds will adopt accounting policies which inflate the reported tax rate.

- Defined benefit funds report lower effective tax rates than defined contribution funds.

  The author suggests that employers with DB funds have an incentive to maximise reported earnings and thereby minimise employer costs. This result may occur but I believe that the major reason would be the difference in asset allocation between DB and DC funds.

Conclusion

Although I have some doubts about several of the hypotheses suggested in this paper, it will be interesting to see if there are any fund specific factors which influence the timing of the adoption of AAS 25. If Gallery finds some of her hypotheses proven, it may be evidence of how behaviour in the industry responds to external forces. Of course, whether that response is beneficial to anyone (and, if so, to whom), remains an open question.

A discussion of some issues in relation to the taxation of excess benefits paid from a superannuation fund - post *Platell v FCT 92 ATC 2018*

Jocelyne Boujos, Philips Fox and University of Western Australia

Background

This paper was based on the decision in the above case which meant that 190 ex-members of the West Australian Newspapers Pension Fund did not pay tax at the top marginal tax rate on the portion of their benefits which exceeded the Reasonable Benefits Limit at the time.

The reason for this decision by the AAT is that the circumstances which applied to this case were similar to those outlined in tax ruling *IT2274*. In particular, paragraph 5 of that ruling suggests that the Commissioner may exercise his discretion (ie not subject the excess benefit to maximum tax rates) 'where the excessive benefit arose fortuitously or in other circumstances beyond the effective control of the recipient or the employer'. This occurred in this case where the rate of return declared in 1986-87 was 72%!

Consequences of the decision

The author then considers the situation under the existing rules, and in particular S15R of OSSA which contains a discretion for the Commissioner to treat the whole or part of the payment as if it were within the reasonable benefit limits "because of the special circumstances of the case." Of course, the key question is, what are special circumstances?

The author concludes that the Insurance and Superannuation Commissioner ought to exercise his discretion in respect of excessive benefits on in the same basis as used by the Commissioner of Taxation when applying his discretion under S26AFA of the Tax Act.

In order to make an application to the ISC to seek an exercise of this discretion under S15R of OSSA, she suggests that it is essential to establish

- the position of the fund's investments prior to any unexpected gains;
- the source of the unexpected gains;
- an estimate of the gain due to these unexpected events;
- details of any subsequent gains; and
- details of the fund's balances and the level of contributions in the relevant years.

Concluding remarks

Superannuation in Australia affects all Australians, either directly or indirectly. These effects will increase as the superannuation guarantee continues to rise and the level of assets held in superannuation and rollover funds become an increasing proportion of our total financial assets.

This collection of research papers highlight the breadth of topics that are being, and need to be, investigated. Whilst some of the papers addressed important macro economic and policy issues, others concentrated on smaller components within the big picture. Both are important. We need to get the right long term policy in place but we also need appropriate and cost efficient regulations and standards. In addition, we must not forget that the final beneficiaries are individuals in a wide range of personal circumstances. Much work remains to be done.

The first Colloquium of Superannuation Researchers confirmed the multi disciplinary nature of superannuation. It is also essential that all parties and professions who have an interest in superannuation keep communicating, contributing and learning from each other. The topic of the development of superannuation is too important for Australia to be driven by one set of interests or from one perspective.

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