

A Plan to Simplify and Streamline Superannuation

ClearView's Submission Paper

Introduction

ClearView Retirement Solutions was established in February 2002 to focus specifically on retirement planning, a move seen as relevant to the needs of Australia's ageing population. ClearView has Financial Advisers throughout NSW & ACT, metro and regional areas. ClearView offers financial advice and investment products for people approaching or already in retirement and is dedicated to the idea that all Australians deserve a clear view how to look after their life savings and enjoy a reliable income in their retirement. As at June 2005 ClearView Retirement Solutions had 37,885 clients with funds under management of \$1.5 billion. ClearView is part of the MBF Group.

We at ClearView Retirement Solutions support the Governments intention to simplify the superannuation system and are grateful for the opportunity to respond. As a consumer-focused, end-to-end advice and funds management business, we are, however, concerned that certain proposals may have unintended consequences. The proposals of key concern have each been analysed with the potential impacts and proposed solutions also identified. The key proposals that have been addressed (in order of our perceived importance as specialists in retirement) are listed below:

1. Removal of end benefit tax for retirees over the age of 60
2. 'Simplification of Superannuation' with message to retirees that they no longer need to seek advice in retirement
3. Cap of \$150,000 on undeducted contributions each year or \$450,000 over a three-year period.
4. Removal of compulsory cashing of benefits delayed to 1 July 2007
5. Removal of Reasonable Benefit Limits from 1 July 2007
6. Taxation of lump sum and pension payments to those under the age of 60 to remain unchanged (as per current rules).
7. Proposed simplification of pension rules
8. Limit of \$50,000 on concessional deductible contributions from 1 July 2007, irrespective of age with transitional period, allowing for \$100,000 pa for those over 50 until July 2012.
9. Increase age for deductible contributions to age 75 (from age 70), however no provision to extend SG to age 75.
10. Lump sums paid to dependants will be tax-free irrespective of the amount and lump sums paid to non-dependants will be taxed at 15%
11. Reduction in asset test taper rate from \$3 to \$1.50 for every \$1,000 of assets in excess of lower asset threshold.
12. Removal of 50% asset test exemption for income streams purchased on or after 20 September 2007.

We also have some alternative suggestions for consideration that could further simplify the system. These are outlined at the end of the document.

Government Proposal	Removal of end benefit tax for retirees over the age of 60.
ClearView Concern	<p>We fear that a large portion of retirees (particularly the less educated) will simply cash out their superannuation benefits once they attain age 60 without adequate consideration being given to wealth preservation and the amount of income they will need over the duration of their retirement. Our reasons for the concern include:</p> <ul style="list-style-type: none"> • The level of education and understanding of the average retiree of their life expectancy, income needs, financial risks and means of funding their retirement is poor. There remains a relatively “live for the moment” attitude, especially within the baby-boomers. There is no longer any end benefit tax and therefore no disincentive from an immediate tax point of view in “cashing in” and relying on the (inadequate) Age Pension. • The tax free earnings environment of income streams will not act as an incentive for the average Australian retiree whose income will likely fall below the level where tax is payable (eg because of SATO). • The general feeling amongst many retirees is an inherent fear and mistrust of the superannuation and pension system, which is fuelled by the constant change.
Potential Individual Impact	<p>An increased number of retirees will run out of money prematurely and therefore will not have funds to sustain a comfortable lifestyle into retirement. This will have a flow on-effect and will mean fewer will be able to afford private health insurance and may find it harder to be accepted into aged care (as there are currently only a limited number of places available to concessional residents).</p>
Potential Government Impact	<p>Increased reliance on the age pension at an earlier age for a larger portion of the population. Furthermore increased reliance on the public health care system.</p>
Potential Industry Impact	<p>The emphasis will move away from pension products in favour of the development and devotion of resources to accumulation style products.</p>

Proposed Solution	<p>To counter the above concerns we believe it is important to limit the amount a retiree can withdraw from the superannuation and or pension environment to a set percentage of their benefits, to be calculated annually based on the individual's age.</p> <p>For example a 60-year old retiree may be able to access up to 20% (in the form of a lump sum and or income stream) of their superannuation benefits in a financial year.</p> <p>An alternative approach may be to rely on the provision of financial advice enabling consumers to make sensible long-term decisions. Even in a more complex environment today, many consumers do not seek advice at retirement and while we support the simplification initiatives, they notionally remove a current trigger for those seeking advice. Incentives or encouragement to seek advice could help to address this. This could be in the form of</p> <ul style="list-style-type: none">• The ability to make withdrawals subject to receipt of financial advice with a Superannuation Fund Trustee approval process; and/or• Financial incentives to obtain and act on advice.
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<p>Government Proposal</p>	<p>'Simplification of Superannuation' with message to retirees that they no longer need to seek advice in retirement.</p>
<p>ClearView Concern</p>	<p>Retirees are being encouraged to go it alone and not seek out financial advice in retirement.</p> <p>Currently, maximising Centrelink benefits and minimising tax through somewhat complex advice and product strategies are tangible benefits that advisers produce. While these services will become less relevant, there are numerous services that a financial adviser provides including:</p> <ol style="list-style-type: none"> 1. Establishing lifestyle and financial goals and objectives in the short, medium and long term including planning for beneficiaries 2. Support with budgeting for expenses and income needs 3. Understanding life expectancy and the need for generating income over the duration of retirement 4. Education on financial risk and trade-offs between investment returns and volatility of investments 5. The benefits of diversification to reduce risk 6. Choosing investments (asset allocation, products and managers or direct investments) 7. Facilitating reporting and consolidation of investments 8. Ongoing adjustment of strategies and plans reflecting changes in circumstances. <p>These services are necessary to ensure the average Australian retirees use their accumulated savings wisely and require specialist skills and training to deliver. There is an ongoing need for professional financial advice.</p>

<p>Potential Individual Impact</p>	<p>Many retirees will resort to the only thing they really understand and trust, property and or a bank account.</p> <p>Consequently they will miss out on the benefits of diversification and the value that a more appropriate approach to investing could afford them in additional earnings over the longer term in retirement.</p> <p>Given poor understanding of how to manage their retirement funds over the long term, there is a significant risk that consumers could spend their money early or on “less necessary” items and not have sufficient funding to meet their income needs throughout their retirement. Alternatively, some may be too conservative with their spending and live an unnecessarily frugal and uncomfortable life, leaving more than intended at death.</p>
<p>Potential Government Impact</p>	<p>With funds being exhausted earlier it is expected that there will be more people on the age pension and more people relying on the public health care system.</p>
<p>Potential Industry Impact</p>	<p>The emphasis will be on cash management accounts and property advice.</p> <p>Invalid dissatisfaction with investment industry driven by inappropriate choices and timing because of a lack of advice, for example moving money out of shares at the bottom of the market and missing out on the long term upside.</p>
<p>Proposed Solution</p>	<p>We propose the leveraging of the Financial Literacy Foundation work on a program to be introduced by the Government (similar in principle to the program introduced for school children) to assist retirees better understand concepts like budgeting, wealth preservation, risk and return and risk profiling.</p> <p>In short the program should equip a retiree with the skills needed to ‘do it your self’ where possible and understand where a professional financial adviser and investment managers can and should help.</p> <p>As described above, incentives or encouragement for retirees to seek and act on professional advice would be relevant.</p>

<p>Government Proposal</p>	<p>Cap of \$150,000 on undeducted contributions each year with the proposal of a transitional period of \$450,000 over a three-year period to apply from budget night. Excess contributions to be returned at taxed at top marginal tax rate.</p>
<p>ClearView Concern</p>	<p>No consideration is given to the 'real' value of the contribution levels over time.</p> <p>No transitional provision has been allowed to assist those close to retirement.</p> <p>It is not clear which fund would be required to refund the excess where the individual has contributed to several funds or how the penalty will be paid where the individual has already commenced a superannuation pension.</p>
<p>Potential Individual Impact</p>	<p>This proposal severely disadvantages those individuals who are close to retirement and have been planning on selling an investment property or downsizing just prior to retirement and investing the proceeds into superannuation for the purpose of commencing an income stream, particularly where they are close to 65 or over and cannot physically continue to work.</p> <p>Furthermore it disadvantages those individuals who were in the process of implementing the recommendations in their Statement of Advice provided by their adviser prior to budget night.</p>
<p>Potential Government Impact</p>	<p>Increased compliance activity required to monitor and control excess contributions being made.</p>
<p>Potential Industry Impact</p>	<p>Administration complexity associated with the refund of excess contributions and any penalty tax applicable.</p> <p>Increased reporting requirements.</p>

Proposed Solution	<p>We recommend indexation be applied to the cap on undeducted contributions as at 1 July each year.</p> <p>In addition we have a number of alternative recommendations to ensure that those who are close to retirement are not disadvantaged by the imposition of the new caps:</p> <ul style="list-style-type: none">• Double the cap on undeducted contributions for those over the age of 50 until 2012 (similar to principle proposed for deductible contributions) or• Remove the cap on undeducted contributions for individuals over the age of 50 until 1 July 2007 or• Allow a lifetime limit (similar in amount in the current pension RBL) to ensure those who receive large lump sum amounts for example inheritances, later in life are able to contribute the proceeds into superannuation. <p>In a bid to reduce the complexity involved in refunding excess contributions and the payment of penalty tax we propose limiting the number of funds to which an individual can make an undeducted contribution in a financial year to just one fund. This will ensure excess contributions can be stopped at entry into the fund (as the fund would have records of undeducted contributions previously made for the financial year).</p>
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Government Proposal	Removal of compulsory cashing of benefits from 1 July 2007
ClearView Concern	<p>Prior to 1 July 2007, the delayed start date may mean a large number of individuals will be required to cash out their superannuation benefits over the course of this coming year as they do not satisfy the work test (240 hours in the previous financial year) even though because of a potentially arbitrary start date, others would not have to.</p> <p>On an ongoing basis, more complexity will be introduced with retirees seeking to maximise any arbitrage opportunities that may exist by switching between the pension and accumulation phase throughout retirement.</p> <p>Finally superannuation will become a vehicle for the wealthy to minimise tax in retirement and in some cases used as a quasi-family trust.</p>
Potential Individual Impact	<p>Inequity between those not meeting the work test prior to 1 July 2007 and those not meeting it after that date.</p> <p>The ongoing arbitrage opportunities and estate planning opportunities will benefit those individuals who can afford the services of an accountant/financial adviser. Moreover there will be greater tax savings available to those with more money available to invest.</p>
Potential Government Impact	Potential loss of tax revenue.
Potential Industry Impact	Increased administration.
Proposed Solution	<p>Remove the compulsory cashing requirement with effect from budget night.</p> <p>An alternative solution would be to remove the work test for individuals over the age of 65 to allow anyone who has recently cashed out or who cashes out over the coming year the opportunity to re-contribute the proceeds to superannuation.</p> <p>We are proposing a simplified 'retiree fund' for those over preservation age and have retired. It would represent a replacement for the currently distinct accumulation and the pension phase. We believe the retiree fund would operate in the same way as the pension phase currently operates, that is no tax on earnings however we do not believe they should be required to draw a minimum pension. Therefore superannuation accounts would not exist for retirees, thereby assisting in the reduction of complexity.</p>

Government Proposal	Removal of Reasonable Benefit Limits from 1 July 2007
ClearView Concern	<p>The delayed removal of RBLs would deter individuals who have excess benefits from retiring until 1 July 2007.</p> <p>In addition it will disadvantage anyone that dies over the course of the next year who has excess benefits, as the payments made to their dependants/non-dependants will be taxed at up to 47%.</p>
Potential Individual Impact	Individuals who have excess benefits and who are required to trigger release of their benefits before 1 July 2007 will be unfairly disadvantaged by being levied with the penalty tax.
Potential Government Impact	The delayed implementation does not reflect positively on the Government for those individuals who trigger excess benefits over the coming 12 months.
Potential Industry Impact	Financial advisers will continue to hold the key for the next 12 months to reducing tax for retirees who have excess benefits. In some cases this may mean using products such as Term Allocated Pensions, which will become irrelevant and legacy products from September 2007.
Proposed Solution	Remove RBLs with effect from budget night.

Government Proposal	Taxation of lump sums and pension payments to those under the age of 60 to be similar to existing arrangements.
ClearView Concern	<p>It is alarming that little has been done to simplify the retirement process for those who have reached their preservation and are ready to retire (that is between 55 and 60 years of age depending on the year they were born).</p> <p>Furthermore the proposals do not appear to simplify the taxation treatment of benefits paid to those under the age of 60 as a result of total and permanent disability.</p>
Potential Individual Impact	<p>Individuals who retire at their preservation age (or may be planning to) will still be confused, perhaps even more so than before the introduction of the proposals and will still require the assistance of a financial adviser to help them organise their finances in retirement.</p>
Potential Government Impact	<p>Minimal potential impact on revenue of the proposed solution.</p>
Potential Industry Impact	<p>The continued complexity for just a small part of the retiree market (that is those between preservation age and age 60) will mean that many will choose to ignore this part of the market all together.</p>
Proposed Solution	<p>The removal of tax on lump sum and pension payments should be broadened to include those over preservation age and retired.</p> <p>In addition the same principles should apply to lump sum and pension payments made to individuals that are made and totally and permanently disabled.</p>

Government Proposal	Proposed simplification of pension rules
ClearView Concern	<p>It may not be sustainable for providers to continue offering the old and the new pensions and as there has been no discussion of whether a 'transfer mechanism' would be made available for the purpose of allowing providers to do bulk transfers to their new product offering. In addition it is not clear whether:</p> <ul style="list-style-type: none"> • Individuals in existing pensions would be able to rollover to these new pensions from 1 July 2007. • Concessional income test treatment will apply to the new pensions or whether extended deeming provisions applies and existing pensions will retain their current concessional treatment for income test purposes. <p>Finally as the proposals do not support a maximum (by way of lump sum or annual payment amount) there is the risk that superannuation/pension benefits will be cashed out prematurely.</p>
Potential Individual Impact	<p>Retirees will still be confused as to the best pension product for them, as different providers will offer different bells and whistles. In addition the investment selection process has not been made any easier. Finally as clients are not restricted by any maximum payment amount it is expected that many will exhaust their savings prematurely.</p>
Potential Government Impact	<p>Increased reliance on age pension as retirees are expected to exhaust their savings prematurely. This in turn could increase the pressure on the public health care system as less are able to afford to continue private health insurance in retirement.</p>
Potential Industry Impact	<p>Increased focus on investment offering of pension products.</p>

Proposed Solution	<p>Individuals in existing pensions (including non-commutable pensions) should be allowed to rollover to the new income stream arrangements from 1 July 2007. This should be facilitated by the introduction of a successor fund transfer mechanism that allows a smooth transition to the new system.</p> <p>We propose that the transition allow for the continuation of Centrelink asset test exemptions that the prior non-commutable products provided to investors on a simplified basis.</p> <p>This proposal would not require another pension product to be developed (in addition to the proposed offering provided by the Government from 1 July 2007) as we believe the underlying pension could be exactly the same as that proposed, the only difference being a non-commutable 'flag' that is attached to the pension.</p> <p>In addition to encourage the use of pensions, it is recommended that a 'deductible' amount for Centrelink purposes be allowed for new pensions to account for the return of capital.</p> <p>It is also proposed that the current concessional income test treatment provided to income streams are retained.</p> <p>Finally we proposed a 'maximum' apply to restrict the amount of benefits that can be withdrawn as a pension and or lump sum in a financial year.</p>
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Government Proposal	Limit of \$50,000 on concessional deductible contributions from 1 July 2007, irrespective of age (transitional period, allowing for \$100,000 pa for those over 50 until July 2012). Excess contributions taxed at the top marginal tax rate and payable by the superannuation fund.
ClearView Concern	<p>The relative limits will reduce in real value quite quickly as no indexation is being provided for.</p> <p>In addition where a client has contributed in excess of the limit to several funds, there will be the issue of which fund the penalty tax should be paid from.</p> <p>Finally we do not believe that levying tax at the top marginal tax rate will be a disincentive for those who are already on the top marginal tax rate from contribution amounts in excess of the limit.</p>
Potential Individual Impact	Individuals who are on the highest marginal tax rate may benefit from making contributions in excess of the limits.
Potential Government Impact	Minimal impact.
Potential Industry Impact	Increased administration issues.
Proposed Solution	<p>We recommend indexation of the proposed \$50,000 contribution level be done at 1 July each year.</p> <p>We also recommend that the client is responsible for paying the penalty tax where they have exceeded the relevant limit and that the penalty tax rate exceeds 45% to reduce the incidence of this situation occurring.</p>

Government Proposal	Increase age for deductible contributions to age 75 (from age 70), however no provision to extend Superannuation Guarantee to age 75.
ClearView Concern	We do not have any issue with the extension of the contribution age, however with the number of individuals continuing to work part or full-time up to the age of 75, it does not seem equitable that they are disadvantaged by not receiving SG between 70 and 75.
Potential Individual Impact	<p>Increased equity for our older workers. Employers are in many cases making this payment already in the form of salary and so there is not expected to be much of an impact on employers.</p> <p>For those employees who are not currently receiving any SG support (as they are over age 70) it may encourage them to stay in the workforce longer. Furthermore it may encourage employers to provide employment opportunities to our grey workers if it is perceived that the working age has unofficially been extended to age 75.</p>
Potential Government Impact	Minimal.
Potential Industry Impact	Minimal.
Proposed Solution	We recommend SG contributions be mandatory to age 75.

Government Proposal	Lump sums paid to dependants will be tax-free irrespective of the amount and lump sums paid to non-dependants will be taxed at 15%.
ClearView Concern	<p>To avoid paying tax on death benefits paid to non-dependants we believe that many retirees (particularly those who seek financial advice) will be encouraged to use a re-contribution strategy each year (between 60 and 65 at least) to convert any taxed component to a non-taxed component.</p> <p>The re-contribution strategy would allow retirees to convert the taxable component (mainly Post-83) of their benefit into exempt components. That is by withdrawing the benefit and contributing back into superannuation as an undeducted contribution. As a result on the death of the retiree the payment would be received by their non-dependant/s tax-free, instead of being subject to tax at 15% (provided all benefits have been converted from taxable to exempt components).</p> <p>We also believe that many will look to cashing out their benefits in their latter years as they feel the end is coming near and do not want their beneficiaries to pay tax at 15% on their benefits.</p> <p>These rules add complexity, as new advice strategies will be created to minimise tax.</p>
Potential Individual Impact	Individuals who will have their superannuation benefits eventually paid to a non-dependant (for example an adult child) will benefit their estate (in tax savings) by having a financial adviser but the process of repeatedly implementing strategies adds complexity and time.
Potential Government Impact	Minimal potential impact on revenue of the proposed solution.
Potential Industry Impact	Financial advisers will continue to hold the key to reducing tax for retirees, even if it is only for their estate.
Proposed Solution	The removal of tax on all death benefits (irrespective of whether paid to a dependant or non-dependant) would reduce the complexity and any arbitrage opportunities that a financial adviser may be able to provide.

Government Proposal	Reduction in asset test taper rate from \$3 to \$1.50 for every \$1,000 of assets in excess of lower asset threshold.
ClearView Concern	<p>We do not understand how lowering asset test taper rate would contribute in a meaningful way to an increased 'participation rate' in retirement. This is partially because it is usually the income test and not the asset test which reduces the age pension received for the average retiree who still working.</p> <p>Furthermore it is usually the retirees who cannot afford to retire (as a result of insufficient assets being saved) that are the ones who continue to work in retirement. With the average investment balance of a large portion of retirees sitting under \$200,000 (for a couple combined) we do not see that this proposal will benefit the average retiree. It should be noted that the current lower threshold for a couple (home-owners) to qualify for the full age pension is currently \$229,000 (1 July 2007).</p> <p>Without having seen any modelling on this proposal, we are concerned that it will effectively increase the number of retirees eligible for a part-age pension and increase the amount of age pension received by those currently receiving a reduced rate of age pension (where currently affected by the asset test) without, we believe, increasing the participation rate.</p>
Potential Individual Impact	Increased age pension entitlements for self funded retirees.
Potential Government Impact	Increased funding required to support the additional payments that will need to be made. Increased administration for Centrelink with a larger volume of recipients.
Potential Industry Impact	Minimal impact.
Proposed Solution	<p>We propose an alternative to reducing the taper rate for asset test purposes. The alternative is to increase the lower income thresholds. This would increase the amount of income that could be earned without having the age pension reduced.</p> <p>It is believed that this would have an increased effect on increasing the work force participation rate of those who have reached age pension age.</p>

Government Proposal	Removal of 50% asset test exemption for income streams purchased on or after 20 September 2007.
ClearView Concern	While at first glance, this appears to be a viable measure, the merits of complying income streams lie in their ability to provide retirees with an income for an extended period of time.
Potential Individual Impact	The removal of complying income streams will mean there is little or no incentive to lock up their funds and increased accessibility to 100% of their funds for consumption.
Potential Government Impact	Minimal in the short-term. In the medium to long term it is believed that there will be increased reliance on the age pension as retirees prematurely exhaust their savings.
Potential Industry Impact	Significant impact on providers offering complying income streams for example term allocated pension.
Proposed Solution	<p>Pensions offered under the new rules should be offered a 50% asset test exemption where the individual agrees to non-commutability of the income stream.</p> <p>We recognise that there has only been limited success to date of these products but believe that this could be a key aspect of the financial literacy programs we have already proposed.</p>

Alternative Solutions

We also believe that there are other initiatives worthy of further exploration as part of a package of reforms. The proposals as they stand create an environment where, depending on the environment that the accumulated assets remain in, the tax on earnings will differ post retirement. For example, income streams will have tax-free investment earnings, superannuation at 15% and assets outside the superannuation or income stream system at the retiree's tax rate based on income tax thresholds and the variety of offsets and other factors. Unfortunately the differential in tax environments will lead to continued complexity for retirees.

Furthermore it is believed that a variety of strategies will be employed pre and post retirement to minimise the tax paid by retirees in retirement. Once again, benefiting retirees who seek out financial advice as compared to those that do not.

Some potential strategies may include:

1. Using reverse mortgages (pre-retirement) to move equity from the retiree's home or investment properties into superannuation with the intention of repaying the mortgage on sale of the property. While this is likely to be an effective financial strategy given the proposed environment, it really just introduces another product and cost to the retiree as well as a requirement for financial advice to move assets already owned by an individual into a different taxation environment.
2. Using the income generated from income streams to replace the income earned from employment that has been salary sacrificed into superannuation (for the over 60's). As an example this would provide an effective tax rate of just 13.75%* for a 60-year old worker earning \$120,000 who chooses to salary sacrifice \$100,000 into superannuation. Again this strategy will benefit those who seek tax advice and earn well in excess of the average weekly earnings.
*15% contribution tax applied on \$100,000 contribution to superannuation and \$1,500 tax applied to \$20,000 of income earned (\$600 low income tax offset included).
3. Using removal of 'compulsory cashing' as an estate-planning vehicle. The removal allows the retention of assets in the superannuation environment so that they can be passed to the next generation in the same way that many family trusts are currently used. This provides the retiree with a maximum tax rate of just 15% as compared to their marginal tax rate.

We believe that further simplicity could be achieved by trying to eliminate some of the tax differences in one or more of the following ways:

1. Introducing a new form of tax threshold for those over preservation age such as nil tax rate on assessable income for income from any source up to a level of say \$150,000 pa per couple (indexed) and then the top marginal tax rate thereafter. Potentially SATO provisions could be removed as part of this proposal.
2. Removing the 15% tax rate on earnings in superannuation for those post preservation age or providing for a rebate on tax paid for those individuals allowing a single, tax free product for those post preservation age that allows retention of superannuation assets as well as facilitating income streams, that is the introduction of the 'retiree fund'.

Modelling of the tax revenue impacts of these suggestions clearly is required but the negative impact should be considered in the light of the potential cost savings to consumers and the government intention to drive simplicity into the retirement system.

Conclusion

In conclusion we at ClearView commend the Government on its initiative to simplify the superannuation system. We are enthusiastic about the future of our Superannuation system and are excited about the forthcoming changes.

We look forward to continuing to support the Government on the road to simplification. If we could be of further assistance or should you require further clarification on any of the issues identified or solutions proposed please contact:

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