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## The devil's in the detail: The hidden costs of private retirement incomes policy

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Australian governments have shifted the focus of public policy onto the private sector in recent decades. Retirement incomes policy offers an important case study of this shift as a major target of efforts to privatise social provision. Rather than involving cutbacks to public provision, the privatisation of retirement incomes has extended occupational welfare offered as a condition of employment and fiscal welfare delivered via the tax system (Titmuss 1958, p. 42). In fact, the introduction of compulsory occupational superannuation represents the largest transfer of social provision to the private sector in recent memory. This scheme has established private super as a secondary source of retirement savings for most Australians and channelled record investments into private super funds.

The unprecedented growth of private super has stimulated debate about the economic and distributive impacts of private retirement incomes policy. This policy shift continues to be justified as a means to promote the key economic objectives of containing public expenditure, particularly over the long term as the population ages, and advancing national savings. That said, the capacity of current policy settings

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to meet these goals, although often assumed, has been challenged by recent evidence. At the same time, the distributive effects of private retirement incomes policy have become of mounting concern, with attention focusing on the tax treatment of super and how private super has shifted the risk profile of retirement incomes. This 'risk shift' is particularly concerning because of the financialisation of private super, which has involved super funds reorganising their operations to maximise short-term profit and minimise fund exposure to long-term risk (Cutler & Waine 2001, p. 100). The financialisation of private super reflects a broader institutional reorganisation of the superannuation market, brought about by the demutualisation of several large not-for-profit operators and the growing market share held by for-profit providers including banks and other financial entities.

This chapter explores both the *fiscal impact* and *distributive effects* of private retirement incomes policy to better understand the strengths and limitations of recent developments. The fiscal impact of private retirement incomes policy is gauged by surveying the available evidence on its capacity to meet key policy goals. The distributive effect of private retirement incomes policy is examined by analysing current policy settings and the impact of private super on the risk profile of retirement incomes. After reviewing the evidence, I conclude by canvassing the prospects for reform in this critical policy domain.

### Retirement incomes in Australia: A two-tiered system

The Australian retirement incomes system is a mixed economy that can be understood as a two-tiered system of social risk management (see Stebbing & Spies-Butcher 2010). The first and primary tier collectively pools protection from the social risk of income insecurity in old age. This tier consists of the publicly financed age pension (and related benefits) that excludes the wealthy through means tests. Providing a modest income stream, the age pension's full fortnightly rate was \$776.70 for singles and \$585.50 (each) for couples in January 2015 (Department of Human Services 2015). The pension forms the bedrock of the retirement incomes system, covering 76 percent of the population aged 65 years and over (AIHW 2013, p. 238).

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In contrast, the second-tier individualises protection from income insecurity in retirement, through private investments managed in individual accounts. This tier mainly consists of private superannuation and voluntary savings, both of which are financed by contributions from individuals (or made on their behalf). Lacking the redistributive mechanism typical of European social insurance schemes, private super benefits are predominantly calculated in relation to individual contributions and investment returns. Because the government does not appear to finance the second tier (despite the generous concessions discussed below), retirees who draw retirement incomes from private sources are widely perceived to be self-funded (and are referred to as 'self-funded retirees'). Private super has become an important secondary source of retirement income and is now held by around 90 percent of income earners (Nielsen & Harris 2009, p. 9).

The Commonwealth government supports both tiers of the retirement incomes system. The first tier consists of income transfers directly financed by the Commonwealth, such as the age pension, rent assistance and benefits provided to Concession Card holders (AIHW 2011, p. 11). Accounting for most expenditure on the first tier, the age pension cost \$42.3 billion in 2014–15 (Australian Government 2014). The second-tier is supported via indirect means; this support includes regulations and tax expenditures, which provide tax payers with selective tax breaks. The major regulatory scheme is the Superannuation Guarantee Scheme, which mandates that employers pay nine percent of their employees' wages into private super. As contributions were increased from three to nine percent between 1992 and 2002 and will only increase to 12 percent in 2025, this scheme is not set to mature until at least 2050 (assuming a working life from 18 to 67 years of age). This scheme channels tens of billions of dollars into private super each year, without mandating financial contributions from the government. The super tax concessions discount the tax levied on super at all three stages of the super income stream – when employers make super contributions on their employees' behalf, when individuals earn interest on their super investments and when individuals withdraw benefits. These tax expenditures account for most public spending on the second tier, costing \$32.1 billion of revenue forgone in 2013–14 (Treasury 2014). And, salary-sacrificing arrangements exist for employees who forgo income in return for their employers making additional contributions to super

funds (which have the benefit of being subsidised by the tax expenditures).

### The shift to private retirement incomes: A brief policy history

The two-tiered structure of retirement incomes policy has a long history, with the Commonwealth establishing the foundations of both tiers in the early 20th century. The age pension was the first social program established after Federation and the super tax concessions formed part of the first federal income tax. Despite these early origins, private retirement incomes policy played a minor role for most of the 20th century. The current emphasis of retirement incomes policy on private superannuation is a novel development. This section outlines the major developments in retirement incomes policy and explains how this shift coincided with the financialisation of private super.

#### *The age pension*

At Federation, age pensions received in-principle support from all major political parties and were one of only two social provisions explicitly identified in the Constitution. Political support for a national age pension was buoyed by the pre-existence of colonial and state schemes in NSW and Victoria, as well as concerns about aged poverty following the economic downturn in the 1890s (Dixon 1977, p. 22). Despite featuring on their agendas, early federal parliaments failed to introduce a national age pension because of fiscal constraints that stemmed from unresolved issues with the states about the distribution of taxing responsibilities (Kewley 1973, p. 67). After the Deakin minority government developed a means of skirting these fiscal constraints in 1908, Labor made support for increasing taxes conditional on the establishment of an age pension (Kewley 1973, p. 72). The government proved receptive to this request as it relied on Labor's greater numbers to retain office (Sawer 1956, p. 71). Legislation for the age pension was swiftly introduced to parliament in 1908 and passed into law with support from the major parties.

The age pension marked a watershed in retirement incomes policy, providing a modest income stream for eligible members of the popu-

lation aged 65 years and over. Like earlier state schemes, the pension was financed out of consolidated revenue and means tests established eligibility. The age pension's design reflected a compromise between Deakin's Protectionists and Labor. Labor supported a universal age pension and opposed social insurance (Kewley 1973, p. 83). The Protectionists (and Free Traders) opposed universalism because of its cost (Kewley 1973, p. 83). They also rejected social insurance because of perceptions that it would expand direct taxation and was unsuitable to Australia's English heritage at the time (Kewley 1973, p. 82). Labor agreed to support the means-tested age pension backed by the Protectionists, but indicated the intention to establish a universalist age pension when the Commonwealth's financial position improved (Kewley 1973, p. 82). At its introduction, the age pension covered a small minority of the population since average life expectancy was less than 60 years (AIHW 2009, p. 83). Despite early reforms that reduced the eligibility age for women from 65 to 60 years and exempted the family home from the means test, the age pension was only received by around one-third of the eligible age group by the 1930s (Kewley 1973, p. 22).<sup>1</sup>

Over the following 50 years, the age pension became established as the primary retirement incomes policy. On the one hand, the age pension's role was firmed up by the failure of alternative policy proposals to take hold. After reversing their opposition to social insurance in 1913 (following the establishment of such a scheme in the United Kingdom in 1912), the non-Labor parties introduced several proposals to parliament before the Second World War but were unable to garner the support necessary to implement them (Dixon 1977, p. 43). Labor continued to support a universal pension and remained opposed to social insurance over this period. On the other, the age pension became entrenched as coverage gradually rose with rising life expectancy and the liberalisation of the entitlement criteria. Liberal and Labor gov-

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1 The family home was exempted from the means test of the age pension in 1912 (Nielson & Harris 2009). This critical decision, which was extended later by a similar exemption in the Capital Gains Tax, has become an entrenched feature of the Australian tax and transfer system. These exemptions for owner-occupier housing has created perverse incentives to over-invest in housing, as well as to use super benefits on housing improvements and mortgage payments (for more on housing policy see Groenhart & Gurrán, this volume).

ernments both liberalised the age pension between the 1950s and mid-1970s. This trend culminated in the Whitlam's Labor government abolition of the means test for those aged more than 70 years in 1975 and the move by the Fraser Liberal government to remove assets from the means test in 1979 (Bateman & Piggott 2003, p. 31).

However, the age pension has increasingly been targeted since the late 1970s. Reversing the direction of its earlier policy, the Fraser government froze the non-means-tested component of the age pension for recipients aged more than 70 years to reduce government spending (Daniels 2011, p. 35). The Hawke Labor government re-established both income and assets tests for all recipients in the mid-1980s as part of its efforts to redirect spending to new programs like Medicare (Daniels 2011, p. 35). The Hawke government also announced that it would increase the age pension by indexing it to 25 percent of male full-time average earnings (rather than index it to the Consumer Price Index) (Whiteford 2004, p. 85). Although this goal was mostly achieved from 1990, this reflected a fall in male average earnings and the reform was not legislated at this time (Whiteford 2004, p. 85). The Howard Liberal-National Coalition government largely retained the policy settings that it inherited, but enacted legislation to index the age pension at 25 percent of male full-time average earnings in 1997 and liberalised the means test as compensation for the Goods and Services Tax in 2000 (Daniels 2011, p. 36). And, the Rudd Labor government increased the rate of the pension to 27.7 percent of male average earnings (an increase of \$60 per fortnight for singles), while tightening the means test and lifting the eligibility to those aged 67 years by 2019 (APL 2009, p. 171). Subsequently, the Abbott Coalition government (2013-) proposed raising the eligibility age of the pension to 70 years by 2035 and reducing the payment by indexing it to inflation rather than average male wages (Australian Government 2014). A century after it was introduced, the age pension remains the primary source of retirement income for most retirees despite the recent shifts to targeting and private provision.

### *The rise of compulsory private superannuation and the super tax concessions*

While compulsory superannuation has recent origins, the Fisher Labor government established the super tax concessions when it introduced

the income tax to fund Australia's role in the First World War in 1915 (Harris 2002, p. 180). Applying to the three stages of the super income stream, these tax concessions provided tax discounts that increased with the amount of income earned and super held. But, at the time they were introduced these tax concessions also had a low budgetary cost because income tax was levied on a minority of high-income earners and fewer than five percent of workers held super (Olsberg 1997, p. 58).

As minor provisions of a new income tax system, it is unsurprising that the inequality of the super tax concessions escaped controversy when introduced. Moreover, these tax concessions reflected the practice of not taxing mutual aid organisations, as not-for-profit life insurance funds administered most super schemes at the time (Rafter 1986, p. 232). It also streamlined the Commonwealth income tax with similar provisions for super in the states' schemes (Harris 2002 p. 177). However, even if they had had a larger cost, these tax concessions are still likely to have had a low profile because tax expenditures were not reported in either the Budget or other reports of public finance. In fact, reflecting their low profile, the super tax concessions were not subject to systematic review until the Asprey Tax Review of 1975 – around 60 years after their introduction.

The secondary role of superannuation grew steadily over the mid-20th century and this coincided with a shift in the composition of the super industry. Super came to cover 32 percent of the workforce by 1974, with coverage concentrated amongst men on higher incomes in managerial, professional and public sector roles (ABS 1976). The rising coverage of public sector employees was the result of governments establishing their own super schemes for their employees from the 1920s (Bateman & Piggott 2003, p. 31). The coverage of public sector super funds gradually expanded, with 44 percent of those with super covered by public sector schemes by 1974 (NSCI 1976, p. 11). Life insurance offices continued to play the major role in the private sector, with estimates suggesting that they held more than 60 percent of private super accounts in 1974 (NSCI 1976, p. 11). The remaining private sector employees were largely covered by small private funds overseen by trustees (NSCI 1976, p. 9).

In the mid-1970s, concerns about the pension's adequacy received wide attention, including in academic reports and union campaigns for national superannuation (a super scheme that covered the workforce

and was administered by the state) (Olsberg 1997, p. 76). Both major parties responded to these concerns with proposals to extend state support. Notably, in 1969, Whitlam responded by placing national super on Labor's policy platform (this move was also a tactic to court the middle-class vote). Although not eventuating in reform, this put national super on the agenda and reversed decades of Labor opposition to social insurance.

Meanwhile, union campaigns extended private super to some workers from the mid-1970s. When confronted with a political climate hostile to wage growth, unions pursued private super in award negotiations to improve the lot of workers in lieu of wage increases (Olsberg 1997, pp. 75–76). Viewing award super – that is, super included in industrial awards – as deferred wages, unions perceived these payments as having the benefits of supplementing the age pension and extending the super tax concessions to workers (Combet 2004, p. 17). Unions, such as the Pulp and Paperworkers Federation (PPF) and the Federated Storemen and Packers Union (FSPU), also sought to increase worker control of super investments (and thereby reduce that of employers) by introducing their own super funds (Olsberg 1997, p. 78).

The union campaign experienced some success, with award super a key factor in expanding super coverage to 44 percent of the workforce by 1982 (Olsberg 1997, p. 78; ABS 1982, p. 8). This increase in coverage was not accompanied by a radical overhaul of the super industry. Public sector schemes slightly increased their share of super accounts to 48 percent, while private sector schemes held 52 percent of accounts (Rafter 1986, p. 241). The most significant change to the super industry during this period involved the drop in the share of super accounts administered by life insurance offices, which fell to around 42 percent of private super accounts in 1983, as other financial organisations increased their involvement in super (Rafter 1986, p. 241). But, the share of super accounts remained concentrated within the life insurance industry itself; Klumpes (1992, p. 124) estimates that the then non-profit Australian Mutual Provident (AMP) and National Mutual accounted for about 69 percent of the life insurance industry's superannuation business in the late 1980s.

Award super reached new heights through its inclusion in the Accord Mark II negotiated by the Hawke Labor government and the Australian Council of Trade Unions (ACTU) in 1986 (Olsberg 1997, p.



76, 81). The Accord Mark II gave unions both the capacity to negotiate award super of up to three percent of wages and a role in administering the not-for-profit industry super funds, which were the default funds into which award super was to be paid (for awards that covered multiple employers) (Kingston, Piggott & Bateman 1992, p. 141). Industry super funds, an Australian innovation, have industry-wide coverage and are mostly financed by compulsory employer contributions (Olsberg 1997, p. 81). Managed by a board comprising an equal number of appointees selected by employers and unions, these not-for-profit funds select investment strategies aimed at maximising members' benefits. In addition to increasing super coverage to 51 percent by 1988 (ABS 1988), this campaign gave Labor and the union movement a stake in the success of private super.

In this piecemeal way, private super came to replace a national, public superannuation scheme as Labor's second arm of retirement incomes policy in the late 1980s. A series of official reports dismissed national super as being no longer viable because of its start-up costs (see Foster 1988, p. 190; SSCCHA 1988, p. xlv). At the same time, compulsory private super was presented as a solution to the long-term pressures of population ageing on the federal budget – which had emerged as a major social issue – because it would not increase public expenditure. Both these views were reinforced by neoliberal ideas, which added to perceptions that a public scheme would place undue costs on the Budget and that financial markets allocate resources more efficiently than the state (Quiggin 2011, p. 34). The popularity of these ideas made national super increasingly unpalatable politically because such a scheme would increase the government's stake in the financial sector (Quiggin 2011, p. 34; Sharp 2009, p. 202).

Formally adopting private super in 1989, Labor argued that it would improve the adequacy of retirement incomes and help to increase national savings (Howe 1989, p. 4). After unsuccessfully attempting to increase award super through later Accords, Labor directly extended private super to the workforce by legislating the Superannuation Guarantee Scheme in 1991 (Mann 1993). This scheme requires employers to contribute super contributions on their employees' behalf; the rate of compulsory employer contributions gradually increased from three to nine percent of wages between 1992 and 2002 (Kerin 1991). In 1994, the Keating government announced that it would defer pre-

viously promised tax cuts as a further increase to the Super Guarantee after 2002. But, the Howard government chose to not implement this increase in 1997 (Nielson & Harris 2009). In 2012, the Rudd and Gillard governments announced that the Super Guarantee would be gradually increased to 12 percent of wages between 2013 and 2019 (Australian Government 2012, p. 9).<sup>2</sup> However, in 2014, the Abbott Coalition government delayed the increase in the Super Guarantee, so that it would not reach 12 per cent until 2025 (Martin & Hutchens 2014). The Super Guarantee represents one of the most significant shifts of provision to the private sector; between 1990 and 2012, this scheme contributed to coverage expanding from 64 to 90 percent of the workforce and to super investments ballooning from \$123 billion to \$1.4 trillion (Nielson & Harris 2009; APRA 2013).

The extension of private super to the workforce also extended the super tax concessions from \$5.6 billion of revenue forgone in 1984 to \$32.1 billion in 2013–14 (Treasury 2014, p. 12). Despite their growing significance, the super tax concessions were subject to minor reforms between 1915 and the election of the Hawke government. In 1983, the first reform package reduced the budgetary cost of the super tax concessions by limiting access to superannuation benefits to those aged 55 years or over and increasing the taxes levied on lump-sum super benefits.<sup>3</sup> The government set the tax rates at 15 percent for the first \$50,000 of lump-sum super benefits and at 30 percent for any benefits above this amount (Keating 1983). This reduced the inequality of the super tax concessions by increasing the tax paid on larger super benefits. In 1984, a second reform removed the 30/20 rule that, since 1961, had required super funds to invest 30 percent of their portfolios in government bonds to receive tax discounts (Wallis 1997, p. 572). As a response to recommendations of the Campbell Committee and Martin Report, this reform was one of a suite of measures that deregulated the

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2 Initial increases to the Superannuation Guarantee were legislated by the Gillard government before Labor lost office in September 2013. In Opposition, the Liberal party committed to raising the Super Guarantee to 12 percent of wages, but indicated that it would delay implementation.

3 Until 1983, lump-sum super benefits were taxed at the highly concessional rate of five percent and there was no minimum age at which super benefits could be drawn.

financial sector (Sharp 2009, p. 201).<sup>4</sup> These reforms aimed to minimise state interference in the financial sector because investors operating in competitive markets were perceived to make more efficient decisions that would maximise return (Sharp 2009, p. 201). In 1988, the third set of reforms brought forward revenue by establishing 15 percent tax concessions on employer super contributions, super fund earnings and benefits (Daniels 2011, p. 36). The government argued that this reform was revenue neutral because tax increases at earlier stages of the super income stream (on contributions and investments) would be offset by reducing the tax on super benefits.

Initially, the Howard government reduced the inequality of the super tax concessions and expanded the options workers had available to them in regards to choice of fund. In 1996, the government reduced inequality by introducing the Superannuation Surcharge, which required those earning more than \$75,000 per year to pay an additional 15 percent tax on super contributions (Treasury 2001, p. 87). The government also supported low-income groups by establishing an 18 percent rebate for private super invested on behalf of low-income spouses and the Superannuation Co-contribution Scheme, which matched voluntary private super contributions made by low-income earners dollar-for-dollar up to \$1,000 per year (Warren 2008, p. 18). And, in 2002, the Howard government was able to introduce legislation for Super Choice (first announced in 1997), which gave workers the ability to choose between five funds nominated by their employers rather than the fund nominated in their industrial agreement (Warren 2008, p. 18). Super Choice made super more like a consumer product, giving individuals greater scope to select a fund and assume responsibility for their investments. This reform aimed to marketise super by increasing both competition between funds for customers and the lucrative opportunities available to private providers.

However, toward the end of its term, the government changed its focus by introducing reforms that increased the benefits received by a core constituency of wealthy voters. Arguing that it was reducing complexity, the government decreased the Super Surcharge to 7.5 percent

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4 The Hawke government set up the Martin Committee in 1983 to assess the Campbell Report. The Campbell Committee, which was tabled in 1981, recommended sweeping financial de-regulation (Sharp 2009, p. 201).

in 2004 and then abolished it in 2005 (Warren 2008, p. 19). Then, in 2006, the government announced the Simplified Super package, which made super benefits exempt from tax and halved the taper rate for the age pension (Warren 2008, pp. 21–23). These reforms simplified the taxation of super but increased inequality by reducing the tax paid by those who had large super investments, which assisted a core Coalition constituency of older and wealthy voters – including those nearing retirement (Fraser 2006, p. 7).

Both the Rudd and Gillard Labor governments reformed these concessions. In 2010, the Rudd government announced that those on annual incomes of less than \$37,000 would receive a 15 percent tax rebate on their super contributions from July 2012. Previously, this group of lower income earners had received no tax discount, as the 15 percent concessional tax rate was equal to their marginal tax rate. In 2012, the Gillard government halved the tax discount on super contributions received by the top 1.2 percent of income earners who receive incomes of more than \$300,000 to 15 percent from July 2012 (Australian Government 2012, p. 35). These reforms have not radically reduced the incidence or scale of those concessions. Overall, the rapid expansion of the super tax concessions in the last few decades is clearly the result of the policy shift to private retirement incomes that has extended compulsory private super to the workforce.<sup>5</sup>

### *The 'financialisation' of private superannuation*

The two decades following the establishment of compulsory super have coincided with structural change to the private super industry. Similar to the United States and the United Kingdom, the Australian superannuation industry has been transformed by financialisation. Financialisation refers to the increasing role of financial actors, motives, markets and institutions in organising the economy (Epstein, cited in Martin, Rafferty & Bryan 2008, p. 122). Cutler and Waine (2001, pp. 99–100)

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5 Revenue forgone in super tax concessions accounts for less now than before the Global Financial Crisis. As recently as 2008, the super tax concessions were estimated at \$38.9 billion of revenue forgone (Treasury 2013, p. 4). However they fell to \$24.1 billion in 2009–10 reflecting the lower returns that super funds have received on their investments (Treasury 2013, p. 4).

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usefully distinguish between three features of financialisation: first, it involves the elevation of financial criteria to assess fund performance (and the marginalisation of other criteria); second, super funds are operated to maximise 'shareholder value', rather than value for stakeholders such as account holders; and, third, regulatory frameworks are deregulated to advance the pursuit of profit (Cutler & Waine 2001, p. 100). These features of financialisation are evident in the deregulation of the financial sector, as well as changes to both the composition of the Australian super industry and structure of benefits offered to fund members over recent decades.

The regulatory framework that private super funds operate in was altered by broad-sweeping deregulation to financial markets in the 1980s and 1990s. These reforms aimed to increase the efficiency (and thus profit) of financial markets by opening up the financial sector to competition, reducing the barriers to market entry, and discouraging market segmentation (Keneley 2001, p. 163). The abolition of the 30/20 rule was of particular significance for the super industry because it gave funds the freedom to pursue more profitable ventures than bonds. On a broad level, these reforms resulted in a regulatory framework that gave private super funds, not-for-profit and for-profit alike, greater scope to pursue profits.

Financial deregulation has encouraged life insurance funds to transform their structure and role in the private super industry (Keneley 2001, p. 164). An important development has been that several large life insurance funds – including major players in the private super industry such as National Mutual in 1995 and AMP in 1997 – have responded to deregulation by demutualising their operations (Keneley 2001, p. 164). Demutualisation has financialised the super industry by converting not-for-profit funds into for-profit entities. This replaced an associational logic of risk-sharing among members, dating back to the 19th century in some cases, with a market logic of profit maximisation. It also transformed fund members of NFPs into consumers and shareholders. With key providers now operating on a for-profit basis, the distinction between not-for-profit life insurance funds and other forms of for-profit private super can no longer be sustained. A further significant development was that not-for-profit life insurance funds were under pressure to act as if they were for-profit because they had to compete with banks for capital to expand their business and they ex-

perienced increased competition from industry super funds (Keneley 2001, p. 162). Another major development has been deregulation of (some) restrictions on mergers and acquisitions that has enabled the formation of conglomerates that specialise in multiple financial services (Keneley 2001, p. 163). These financial conglomerates have blurred the distinction between the life insurance industry and other parts of the finance sector (Keneley 2001, p. 164). These three processes have significantly contracted the traditional role of life insurance funds as not-for-profit providers and expanded their involvement in for-profit provision.

The restructuring of the life insurance sector reflects a wider shift in the composition of the private super industry. The Australian Prudential Regulatory Authority (APRA) classifies super funds into five categories: public sector funds; the non-profit industry funds; retail funds privately operated on a commercial basis; corporate funds run by employers for their own employees; and, small (or self-managed) funds with fewer than five members (2013, p. 10). Table 3.1 displays how the overall share of super accounts and assets held by each type of fund changed between 1996 and 2011. The table shows that industry super funds increased their share of super accounts from 33 to 37 percent, while their share of super assets has increased from eight to 19 percent. As the proportion of assets held by these funds is much lower than their share of super accounts, it suggests that those with lower super balances benefit most from the industry funds. It also reveals that the accounts managed by retail super funds have markedly grown from 39 to 48 percent, whereas their assets increased from 24 to 28 percent of the total. And, the table shows that small funds have marginally increased their share of accounts from one to three percent, but had the greatest growth in assets from 12 percent to 32 percent of those held by the super industry. This suggests that small funds are predominately held by the very wealthy. In contrast, corporate and public sector funds decreased their share of both super accounts and assets; public sector funds now account for about 11 percent of super accounts and 14 percent of assets. Although somewhat offset by the growth of not-for-profit industry funds, these figures indicate that for-profit funds (that maximise shareholder value), and self-managed funds favoured by the well-off, have increased their market share since the establishment of the Super Guarantee.

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Table 3.1: Proportion of super accounts and super assets held by the main types of funds, 1996 and 2011

	Super accounts				Super assets			
	1996		2011		1996		2011	
	'000s	%	'000s	%	\$b	%	\$b	%
Corporate	1,300	8	593	3	45.6	19	56.6	5
Industry	5,200	33	11,449	37	20.2	8	226.2	19
Public sector	3,000	19	3,373	11	48.1	20	172.9	14
Retail	6,100	39	15,063	48	59.6	24	339.5	28
Small	200	1	846	3	28.2	12	392.9	32
Total*	15,800	100	31,324	100	202.0	100	1,299.0	100

Source: APRA (2007, 2012) \* Percentages may not sum to 100 due to rounding

While the Super Guarantee does not require compulsory super contributions to be invested in accounts with particular benefit structures, it has nevertheless coincided with a dramatic shift in the structure of the super accounts offered by private super funds from defined benefit schemes to accumulation accounts. Defined benefit schemes provide private pensions that are calculated according to both a member's final salary and the duration of their contributions (APRA 2007, p. 5). In contrast, accumulation accounts manage super in individual savings accounts, providing benefits in relation to the contributions made and interest earned (or loss) from investment (APRA 2007, p. 5). Whereas 82 percent of super accounts had a defined benefit structure in 1982, less than 14 percent of super accounts had this structure by 2000 (Treasury 2001, p. 85). In 2000, accumulation accounts comprised 86 percent of super accounts.

The shift toward accumulation accounts has continued in the last decade. Table 3.2 provides data on the benefit structures of super accounts held by Australians in 2010. In addition to the two types of schemes already discussed, the table includes data on hybrid accounts that combine features of accumulation accounts and defined benefit schemes. The table displays the number of super accounts held with

Table 3.2: Benefit structures of superannuation accounts in Australia, 2010

Benefit structure	Accounts		Assets	
	'000s	%	\$ billion	%
Accumulation account	19,589	60	750.4	63
Defined benefit	645	2	57.9	5
Hybrid account	12,624	38	379.8	32
Total	32,857	100	1,188.1	100

Source: APRA (2011, p. 21)

each benefit structure (like Table 3.1), but does not reveal the portion of Australians with each type of account (as multiple accounts may be held by an individual). Nonetheless, accumulation accounts have spread further, with the table showing that about two percent of super accounts have only a defined benefit structure. Of these defined benefit schemes, 98 percent of accounts are held in public sector funds and have since been replaced with accumulation accounts (APRA 2011, p. 37). Because of this, the number of accounts in the defined benefit category is expected to drop further. Table 3.2 also shows that accumulation accounts hold 63 percent of super assets and hybrid accounts hold a further 32 percent. Taken together, this data confirm that accumulation accounts have become the main form of private super since the advent of award super and the Super Guarantee.

The shift to accumulation accounts reflects broader international trends in other private pension markets, especially those in other English-speaking countries (see Langley 2004; Cutler & Waine 2001). This shift is associated with the financialisation of the private super industry because the risk profile of accumulation accounts is more conducive to maximising shareholder return than defined benefit schemes (Cutler & Waine 2001, p. 108). In defined benefit schemes, the investment risk is borne by the fund and the employer-sponsor, who guarantee account holders a set benefit level at retirement (Davis & Hughes 1992, p. 167). Accumulation accounts, in contrast, leave the account holder responsible for the investment risk, with employers guaranteeing only a set level of contributions and the funds not specify-



ing the level of benefit (if any) that will be received at retirement (Davis & Hughes 1992, p. 168). The shift of investment risk to account holders with accumulation accounts has been appealing to private super funds that aim to maximise shareholder value because they limit the funds' exposure to shortfalls and provide greater certainty of their liabilities by passing losses onto account holders (Cutler & Waine 2001, p. 108).

Financialisation has also coincided with the growth of accumulation accounts through its impact on industry super funds. The growing role of industry super funds has accelerated the uptake of accumulation accounts, with only three of 100 such funds offering defined benefit schemes in 1992 (Kingston, Piggott & Bateman 1992, p. 141). Kingston and associates (1992, p. 141) contend that industry funds seem to have offered accumulation accounts because of issues in securing sponsors that would be legally responsible to guarantee defined benefits (if funds went into deficit) when multiple employers are involved. APRA (2007, p. 5) further argue that this reflected a broader shift in employer preferences for accumulation accounts since they found the high cost of defined benefit schemes and their potential to increase their liabilities unappealing. The provision of accumulation accounts by industry funds reflects financialisation to the extent that employers sought to limit their liability (and maximise profits) and that the state chose not to regulate sponsoring arrangements. In turn, Davis and Hughes (1992, p. 168) claim that the prevalence of accumulation accounts has led industry funds to manage their investments to maximise short-term profit (like retail funds) since their members follow annual performances more closely than those with defined benefits. The overall implication here is that the industry funds are managed in similar ways and offer similar benefits to 'financialised' private super funds despite their not-for-profit status. In fact, Bryan, Ham and Rafferty (2008, p. 44) found that not-for-profit funds – including the industry super funds – outperformed private retail funds between 2004 and 2008. As will be seen in the ensuing discussion, both the financialisation of the private super industry and the rise of accumulation funds have implications for the efficiency and equity of private retirement incomes policy.

## Value for money? Interactions between private super and retirement incomes policy

What to make of this recent shift to private provision? Has privatisation and financialisation made retirement incomes policy more efficient? A useful starting point for assessing the shift to private super is to examine how efficiently it has met the official rationales that governments have offered for recent reforms. As the policy history above shows, the Super Guarantee has been linked to three major policy goals: boosting retirement incomes; advancing national savings; and reducing the fiscal pressure of population ageing on future governments. On a more general level, Labor and the ACTU came to prefer private super over a public scheme because, as in other cases of privatisation, of perceptions that the private sector would more efficiently allocate funds and that expanding the public sector would cost too much. Support for a private scheme from Treasury, the Cass Social Security Review and the financial sector reinforced these perceptions (Sharp 2009; Mann 1993). At first glance, the superannuation guarantee appears to have met these goals with flying colours. Private super offers almost all workers a secondary source of retirement income and seems to have contributed \$1.4 trillion to national savings and reduced future fiscal pressures – all without seeming to expand public spending. However, a closer look at the interactions between private super and other second-tier policies casts doubt on the efficiency of current retirement income policy.

### *Boosting retirement incomes?*

The superannuation guarantee's contribution to increasing retirement incomes might seem to be its most self-evident achievement. The scheme has expanded super coverage and investments to new heights. But, it is one thing for private super to have increased retirement incomes and quite another for it to have done so efficiently. For the Super Guarantee to boost retirement incomes efficiently, retirees would, at the very least, have to use their super investments as income. Both the structure of super benefits and available evidence on how super is spent by retirees suggest that this link is more tenuous than generally assumed.

### 3 The devil's in the detail

Superannuation is available to those aged 55 years or older who retire and to those who continue to work past the age of 65 years. Nevertheless, the structure of super benefits is a key factor in whether funds are used as retirement income. Defined benefit schemes, as well as the defined benefit component of hybrid schemes, are most likely to be used as retirement income because they are receivable only as a private pension that provides a regular income to beneficiaries once they reach a certain age. Benefits from accumulation accounts or components can be used as retirement income or potentially put to other uses as they are mostly received as lump-sum payments. As Disney points out, super benefits from accumulation accounts can 'be expended at the onset of retirement, or passed on to relatives for tax avoidance purposes, rather than used as retirement income' (2007, p. 3). The potential for super benefits to be put to other uses is exacerbated by the tax exemption of super benefits received after age 60 years – five years before retirees are eligible for the age pension, provided they meet its eligibility criteria. Because of the prevalence of accumulation accounts and the relatively low level of super held by most current retirees, there is no guarantee that private super is drawn on as retirement income (even though people receive it at retirement age).

In fact, the available evidence suggests that lump-sum private super tends to be used to pay off household debt rather than used as retirement income. Kelly and associates (2004) compare household debt and the super held at retirement with the amounts of each held in the years leading up to it. They note that in households with at least one person aged 50–69 years in the workforce, the average super balance was \$170,000 and mean household debt was \$85,500 in 2002 (Kelly, Farbotko & Harding 2004, p. 8). For households where people aged 50–69 years had retired, the average super balance was \$93,000 and household debt was \$22,700 in 2002 (Kelly et al. 2004, p. 8). Because of these different levels of debt and higher home ownership among retired people, Kelly and colleagues (2004) argue that super appears to be used to pay off debt accrued when in the labour force. This is consistent with more recent data that show 69 percent of individual retirees who received lump-sum super between 2003 and 2007 did not use their benefits primarily for retirement income (ABS 2011, p. 92). These 'other' uses of private super undermine the compulsory nature of super to the extent

that individuals use their benefits to bring forward consumption and accrue debt before retirement.

Retirees' use of lump-sum super to pay off mortgages or reduce debt from housing upgrades is unsurprising, considering the incentives for investing in owner-occupier housing. The favourable tax treatment of owner-occupier provides incentives to individuals from all age groups to invest in housing over other investments. Owner-occupier housing is exempt from capital gains tax and imputed rent is not taxed (Smith 2004, p. 194; Yates 2010, p. 32). Retirees have a further incentive to invest in their primary residence, since owner-occupier housing has long been excluded from the assets test of the age pension (as noted above). Taken together, these policies offer retirees incentives to invest their super in owner-occupier housing (potentially to over-invest) and to claim the age pension as their retirement income (also see Spies-Butcher & Stebbing 2011).

Although spending lump-sum super on housing or servicing debt may increase household wealth, it does not, in itself, boost retirement income. It could be argued that this does not prevent private super spent from contributing to retirement income through reverse equity mortgages, which allow retirees to access income or lump-sum from housing assets that they own. However, this industry is in its infancy in Australia, with only 1.4 percent of individuals aged more than 60 years holding a reverse mortgage in 2007 (Henry 2008, p. 28). The evidence thus casts doubt on the significance of the direct, or indirect, contribution made by lump-sum super benefits from accumulation accounts to retirement income.

### *Reducing the pressures of population ageing?*

The capacity of private retirement incomes policy to offset the public costs of the age pension over the long term as the population ages also seems straightforward. The Super Guarantee and other second-tier policies relating to private super are widely assumed to reduce budgetary costs by directing funds into private super that will then be used as retirement income instead of the age pension. As the assumption that private super provides retirement income has already been shown to be suspect, the focus here is on the projected impact of the super tax con-

cessions on the efficiency of private retirement incomes policy as the population ages.

Like other affluent societies, Australia's population is projected to age in coming decades because of declining fertility and rising life expectancy. Fertility rates have fallen from 3.5 to two births per woman between 1961 and 2008 (Treasury 2010, p. 7). Average life expectancy has also risen by (at least) 24 years for men and women since 1901, reaching 79.2 years for men and 83.7 years for women in 2006–7 (Treasury 2010, p. 6). Table 3.3 displays projections from the third *Intergenerational report* on the impact that these trends are expected to have on the age structure of Australia's population. These official projections show that the proportion of the population aged over 65 years is expected to grow from 13.5 to 22.7 percent between 2010 and 2050 – projected growth of almost 70 percent. Population ageing will increase outlays on the age pension, but care has to be taken to avoid overstating by how much for two reasons. First, these projections are likely to over-estimate the scale of the problem because they are based on conservative assumptions and are sensitive to small changes due to their long-term nature (Dowrick & McDonald 2002, pp. 9–10).<sup>6</sup> Evidence of this is that the third *Intergenerational report* has scaled down the projected costs of population ageing found in the first two reports (released in 2001 and 2007). Second, Australia has a 'favourable demographic profile' compared to many similar countries (OECD 2009, p. 150). Both these considerations suggest that the budgetary impact of population ageing will be modest in Australia.

However, in the event that population ageing were to considerably add to fiscal pressures, the evidence suggests that the current policy settings for private super are not particularly efficient. This is because private super has limited capacity to act as a substitute for the age pension and thereby reduce public spending. The *Intergenerational report*

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6 Dowrick and McDonald (2002, p. 10) argue that the projections in the *Intergenerational report* are pessimistic because they underestimate the potential for: the participation rate to increase; low unemployment to stimulate the economy; and, healthier lifestyle choices to counterbalance the cost of health and aged care. Moreover, they argue that the report does not give due attention to the projected growth of real after tax incomes because of its focus on the state of public finances (Dowrick & McDonald 2002, pp. 10–11).

Table 3.3: Age structure of the Australian population, 1970–2050

	1970 (% of population)	2010 (% of population)	2050 (Projected % of population)
0–14 years	28.8	19.1	17.2
15–64 years	62.8	67.4	60.2
65–84 years	7.8	11.7	17.6
85+ years	0.5	1.8	5.1

Source: Treasury intergenerational report (2010, p. 10)

projects that the pension's cost will rise from 2.7 to 3.9 percent of GDP in 2049–50 (Treasury 2010, p. 47). But the Treasury estimates that private super will only reduce public spending on the age pension by six percent in 2050 when the Super Guarantee matures (Harmer 2009). Extrapolating from this, private super is subsidised by \$30 billion of super tax concessions, which amounts to 2.1 percent of GDP, and is projected to reduce spending on the age pension by less than 0.2 percent of GDP in 2050.<sup>7</sup> As super is projected to save less than 10 percent of what the super tax concessions currently cost as a proportion of GDP, it is difficult to avoid the conclusion that private super provides an expensive and inefficient means to combat any fiscal pressures associated with population ageing.

The high cost and inefficiency of the super tax concessions often escapes attention because their tax expenditure design has afforded them a low profile. These concessions are still excluded from official reports such as the Budget and *Intergenerational reports*. The omission from the latter is particularly concerning, since these reports represent official projections of population ageing and the super tax concessions are one of the more expensive social policies associated with this demographic trend, currently costing just less than the age pension itself. This omis-

<sup>7</sup> This figure is calculated as six percent of 3.9 percent of GDP. The latter figure is what the age pension is projected to cost in 2050. Moreover, in 2010, the super tax concessions were lower than they previously had been because super funds made few returns in volatile global markets. This suggests that the potential saving is likely to be even less when global financial conditions improve.

sion considerably reduces the usefulness of the *Intergenerational reports* and makes private super seem to appear more efficient and cost-effective than it is. Despite these data limitations, it is clear that the high cost of the super tax concessions is a major source of inefficiency that thwarts the long-term sustainability of current policies for private super.

#### *Increasing national savings?*

At first glance, the trillion dollars invested in private super appears to have made progress on the economic goal of boosting national savings. Both Labor and Coalition governments have promoted national savings because of concerns that dwindling local savings would leave the economy reliant on global financial markets for investment funds and exposed to shocks (such as the Global Financial Crisis of 2008). This, in turn, would lead to lower economic growth and employment (FitzGerald 1993, p. 5). As private super is preserved until retirement, governments have argued private retirement incomes policy promotes national savings by channelling funds into more productive capital investments than housing (Edey & Gower 2000, pp. 277, 288).

The link between super and national savings has, however, proven difficult to establish in practice, because it is difficult to calculate the extent to which compulsory super contributions replace other forms of household savings that would have been made in their absence (FitzGerald et al. 2007, p. 6). Projections calculated by researchers complicate this further, with estimates of compulsory super's contribution to new household saving ranging from 37 to 75 percent (Edey & Gower 2000, p. 297). A further reason for this difficulty is that record household debt has offset increases to national saving from private super (FitzGerald et al. 2007, p. iii). On the one hand, households have limited savings capacity because they are, on average, servicing high mortgage and credit card debt. On the other hand, the potential of private super to increase national savings is undermined by retirees' use of lump-sum super benefits to service household debts.

But, more fundamentally, Coates (2004) contends that national saving is an abstract concept with increasingly limited practical use. National saving has become difficult to separate from foreign savings because of the global integration of finance and capital markets (Coates

2004, p. 83). This means that a national savings pool cannot be presumed and its definition and size are arbitrary to some extent (Coates 2004, p. 90). For example, it is difficult to calculate how much owner-occupied housing contributes to national savings because its roles as a vehicle of household savings and source of household debt are not easily separated (Coates 2004, p. 91). At the same time, housing values are inflated by tax and pension asset test exemptions. Just as importantly, Coates (2004, p. 93) argues that economic globalisation challenges the concept of national saving by implicating household assets and mortgages, as well as private super funds and their portfolios, in international processes. Since the national element of these savings cannot always be easily separated, Coates claims that private super provides 'savings for investment ... not national savings for domestic investment' (2004, p. 97). This is borne out by recent evidence, which suggests that only 39 percent of super assets actually are held in Australia, with 29 percent of these assets held in Australian shares and 10 percent in Australian fixed interest accounts (APRA 2011, p. 40).

In sum, the economic benefits of private super are more often asserted than defended by evidence. The analysis presented here casts doubt on the efficiency of private retirement incomes policy as a means of boosting retirement income, offsetting future fiscal pressures from population ageing and increasing national savings. It also reveals that the super tax concessions undermine the efficiency of private super because of their immense budgetary cost.

### The hidden inequalities of private super: Shining light on regressive super tax concessions

As retirement incomes policy is a major area of social provision, the distributive effects of the shift to private super are not incidental. The capacity of social provision to address inequalities is important because material differences impact on the distribution of individual opportunities and societal wellbeing (Wilkinson & Pickett 2009). In contrast to the redistributive impact of the first tier of retirement incomes policy, recent reform to private retirement incomes policy has reinforced inequality by individualising risk and expanding the cost of the inequitable super tax concessions.



#### *Reinforcing inequality by individualising risk*

The Super Guarantee has reinforced labour market inequalities between high- and low-income earners, especially as it has coincided with the financialisation of the private super industry. The spread of accumulation accounts, which has been promoted through financialisation, has served to individualise the social risk of income insecurity in retirement (Cutler & Waine 2001). This risk shift is particularly obvious when accumulation accounts are contrasted with their alternatives. Accumulation accounts involve neither the redistributive mechanisms of state-administered social insurance schemes, nor the commitments from employers and financial markets to guarantee a certain benefit in retirement typical of defined benefit schemes. The spread of accumulation accounts has thus shifted risk onto individuals and away from the state, employers and financial institutions (see Cutler & Waine 2001; Langley 2004). Accordingly, the benefits retirees can draw from their super in accumulation accounts are vulnerable to downturns in unpredictable global financial markets – such as the Global Financial Crisis and its unfolding aftermath – but the financial institutions that manage private super funds and the state are largely insulated from liability.

Although retirees with defined benefit schemes tend to receive more benefits and experience less risk than other retirees, the inequalities between those who hold accumulation accounts are the focus here because the latter are the predominant form of private super and most defined benefit schemes have been closed to new members. Accumulation schemes provide individuals with benefits in relation to the rate and length of individual contributions, as well as the earnings from their investments. The advent of compulsory superannuation at a time when accumulation accounts became the norm has provided high-income earners with a cumulative advantage since their contributions are larger and they have the potential to earn more interest than low-income earners. The upshot of this is that second-tier retirement incomes policy mainly benefits those employed full time, while offering little to low-income earners, casual and part-time workers, or those who have extended absences from paid employment (such as the long-term unemployed and full-time carers). Indeed, low-income earners are likely to be adversely affected by the requirement that they defer nine percent of their income via super that could be put to other uses. This has

particular implications for gender inequality because gender pay gaps persist; women perform most casual and part-time work; and, they still undertake the bulk of care work (see Sharp & Austen 2006; also see Spies-Butcher & Stebbing 2011, p. 53).

The next two tables confirm that private super reinforces these inequalities. Again, these tables show the percentage of super accounts (again, individuals may hold multiple accounts). Table 3.4 compares super benefits with the gender, gross weekly income and labour force status of those who held them in 2007. The table shows that women tend to hold less private super than men, lower income earners tend to hold less than higher income earners, and unemployed people hold less than those in paid employment. Table 3.5 compares the median and mean of the super benefits held by the gender, gross weekly income and labour force status of account holders. The mean shows how much super each account would hold if super assets were evenly spread, while the median is the mid-point for each grouping if super assets were ranked by how much super they hold. For example, half of the accounts held by women have \$18,489 or less, but these accounts would each hold \$52,272 if super was spread evenly. Table 3.5 also reveals that median super benefits for each gender, income and labour force grouping is proportionately much lower than the respective mean (or average) – thus the top half of the super accounts in each category hold much more than the bottom half. Although not conclusive, this provides further evidence suggesting that super assets are concentrated among employed men with the highest incomes.

### *Hidden and inequitable: the super tax concessions*

The super tax concessions are, however, the major source of inequality in second-tier retirement incomes. Although the evidence supports this conclusion, the hidden nature of these concessions makes it difficult to ascertain their distributive effects. These policies remain hidden because of limits to existing sources of information about them and their low profile. The *Tax Expenditures Statement*, which remains the most reliable source on the super tax concessions, provides only aggregate estimates. Long-term projections, such as the aforementioned *Intergenerational reports*, do not estimate the revenue forgone from super tax concessions. And, existing research tends to be hypothetical, often us-

### 3 The devil's in the detail

Table 3.4: Super benefits by gender, gross income, and labour force status in 2007, percent

	Current account balance/withdrawal benefit					Total
	\$1–\$9,999	\$10,000– \$24,999	\$25,000– \$49,999	\$50,000– \$99,999	\$100,000+	
<b>Gender</b>						
Male	46	44	53	58	66	52
Female	54	56	47	42	34	48
<b>Gross income**</b>						
\$1–\$299	23	12	8	6	8	13
\$300–\$599	28	19	13	8	7	17
\$600–\$999	27	36	34	26	16	27
\$1,000–\$1,499	6	16	23	29	25	17
\$1,500–\$1,999	2	3	6	11	15	6
\$2,000+	1	2	4	10	18	6
<b>Labour force***</b>						
Employed	79	89	90	92	87	86
Unemployed	5	2	2	1*	1	3
<b>Total</b>	100	100	100	100	100	100

\* High standard error of estimate. \*\* Gross weekly individual income; column totals do not add to 100 as data for nil, negative and unknown income have been excluded. \*\*\* Those not in labour force excluded from analysis as it is difficult to calculate this data due to the inclusion of retirees. Source: ABS (2011, p. 81)

ing estimates based on the policy design of the super tax concessions rather than actual data (for example, see Denniss 2007 and Ingles 2009). Moreover, it is difficult to estimate the distributive effects of these policies because the Super Guarantee will not mature for at least three decades. Before this time, it is difficult to estimate the extent to which salary-sacrificing provisions have been used, how these tax concessions impact on final super balances and financial market returns over the

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Table 3.5: Comparison of mean and median superannuation balances, 2007

	Median (\$)	Mean (\$)	Median as a proportion of Mean (%)
<b>Sex</b>			
Male	31,252	87,589	36
Female	18,489	52,272	35
<b>Gross income*</b>			
\$1–\$299	6,719	41,498	16
\$300–\$599	8,787	33,246	26
\$600–\$999	20,000	44,672	45
\$1,000–\$1,499	47,591	89,884	53
\$1,500–\$1,999	70,851	135,375	52
\$2,000+	108,558	220,774	49
<b>Labour force</b>			
Employed	25,084	69,193	36
Unemployed	3,500	30,556	11
<b>Total</b>	<b>23,698</b>	<b>70,670</b>	<b>33</b>

\* Gross weekly individual income; data for nil, negative and unknown income excluded. Source: ABS (2011, pp. 82–83)

longer term. Nevertheless, given that the concessions reduce tax revenue by around \$30 billion, it is surprising that *so little* is known about their distributive implications.

The super tax concessions may appear to treat taxpayers equally, but the flat tax rates they levy on super deliver inequitable benefits because of how they interact with the progressive income tax scales. As Table 3.6 shows, these tax concessions provide inequitable benefits at each stage of the super income stream. The tax discount received on super contributions depends on the amount of income earned. Super contributions made by those who earn incomes less than \$37,000 per year are subject to a 15 percent tax rebate. The 15 percent concessional tax rate that applies to contributions made by those who earn above

\$37,000 but less than \$300,000 delivers a tax discount between 15 and 30 percent. And, the 30 percent tax concession for contributions made by those who earn over \$300,000 provides a tax discount of 15 percent. Annual limits currently apply to the amount of super contributions that can be taxed at these concessional rates; for those under 50 years, the annual limit is \$25,000, while it is \$50,000 for those aged 50 years and above (ATO 2012). The flat rate 15 percent concessional tax rates on super earnings offers no benefit to income earners with incomes below \$37,000, but delivers a 30 percent tax discount on investment returns for those earning \$180,000 or more each year (up to annual limits). The tax exemption of super benefits is more inequitable, providing the biggest tax discounts to those receiving the largest super benefits (see Table 3.6).

Clearly, these tax concessions grant the largest reductions to those who have income and/or super assets that are sufficient for them to pay the highest marginal tax rates. Moreover, higher income earners are more likely to be able to take advantage of the salary-sacrificing provisions and benefit further from these concessions. Compared to both the equitable age pension and the Super Guarantee that merely reinforces labour market inequalities, the super tax concessions actively extend them. Extrapolating from the above, the evidence suggests that employed men with the highest incomes benefit most from these concessions.

In claiming that second-tier retirement incomes policy is inequitable, I am not arguing that the Australian retirement incomes system is more inequitable overall than those in other countries. This is not only beyond the scope of this chapter, but is unclear because the Super Guarantee has not matured. Rather, my intention is to display how the privatisation of retirement incomes policy has entrenched, and even extended, inequality. It is clear that the super tax concessions are difficult to justify in light of their \$30 billion cost and inequity. It also follows from the earlier policy history that the tax concessions that currently subsidise the operations of for-profit super funds were intended to support the not-for-profit sector and that their current scale was inconceivable at their introduction.

Table 3.6: Tax benefits provided by the super tax concessions in 2012–13, percent

Income range (\$)	Marginal tax rate (%)	Tax paid on super contributions (%)	Tax discount on super contributions (%)	Tax discount from 15 percent flat rate tax on fund earnings (%)	Tax discount from exemption on super benefits (%)
0–18,000	Nil	0	0	0	0
18,001–37,000	15	0	15	0	15
37,001–80,000	30	15	15	15	30
80,001–180,000	37	15	18	17	38
180,000–300,000	45	15	30	30	45
300,001+	45	30	15	30	45

The challenge for reform: A case of politics before policy?

The analysis presented in this chapter calls into question the benefits of privatisation of retirement incomes. Evidence suggests that the recent shift onto second-tier retirement incomes policy, which culminated in the Super Guarantee, has increased inequality – and gender inequality in particular – without efficiently meeting its policy goals. This is not to argue that the Super Guarantee should be abolished, or that private super is not an important source of secondary household savings. Rather, it is to highlight the need for further reform. Importantly, the ability of private super to increase retirement income, reduce public spending and boost national savings are much more tenuous than often assumed. This, in turn, makes it more difficult to justify the large and inequitable subsidies that the super tax concessions provide to private super funds and the well-off. The clear implications of these findings are that reform to the super tax concessions and Super Guarantee could simultaneously improve efficiency and reduce inequality. So, what prospects are there for reform?

Reform to the super tax concessions is a top priority because they are costly policies that deliver most benefit to those who need it least.

However, the major political parties do not currently prioritise reform to these tax concessions. Admittedly, this is less of an issue for the Coalition parties, which extended the benefits these concessions granted to key well-off constituencies at the end of their last term in office. The Rudd and Gillard governments introduced limited reforms that have reduced the inequality of the concessions. Remarkably, even their minor reforms have had an impact because of the immense scale of these concessions; the Gillard government's decision to halve the tax discount on super contributions received by those earning more than \$300,000 per year was projected to raise revenue by around \$1 billion over the 2012–13 Budget's forward estimates (Australian Government 2012, p. 41). Labor may have been expected to propose more ambitious reform, considering that during their period in office, the super tax concessions were the focus of a series of reports that highlighted their inefficiency and inequality (for example, see Davidson 2012; Dennis 2007; Henry 2009; Ingles 2009; Spies-Butcher & Stebbing 2009). Most notably, the Henry Tax Review – which Labor framed as a blueprint for future tax reform – proposed that the tax concession for super contributions be converted into a flat rate tax offset for up to \$25,000 of annual contributions (Henry 2009, p. 100). Nevertheless, there is little to suggest that Labor supports more systematic reform beyond that delivered by the Rudd–Gillard government.

Labor's lack of appetite for reform seems to stem from the fact that the super tax concessions are established policies that have a low profile and receive support from well-resourced interests. As tax expenditures, the inequity of these concessions is concealed and they tend to be viewed as tax cuts for 'self-funded retirees' (Henman & Marston 2008, p. 192). The low profile of the super tax concessions has not been redressed by the annual publication of the *Tax Expenditures Statement* since 1986 as it provides limited information and does not report distributive effects (see Burton 2005). At the same time, these tax concessions enjoy quasi-legitimacy due to their long history. As Pierson (1993) argues, policies that operate over the long term tend to become resistant to reform as they come to inform the expectations of beneficiaries. Reform that reduced the inequity of the super tax concessions could be expected to be unpopular among financial entities that may expect to receive fewer deposits and those voters that would, or expect to, pay more tax. It is thus unsurprising that key representatives of pri-

vate super funds and the finance industry – including the Association of Super Funds of Australia (ASFA), the Self-Managed Superannuation Professionals Association and the Financial Services Council – have recently reaffirmed their support for these concessions (Hepworth 2012; Korporaal 2012). Focusing on benefits received by self-funded retirees rather than the finance industry, these associations framed the concessions as vital to reducing dependence on the age pension and advocated their extension (Korporaal 2012). Against this backdrop, the prospect of reform to the super tax concessions appears very limited indeed.

Another priority for reform that would increase income security in retirement is to amend the Super Guarantee to reduce both gender inequality and the extent of the investment risks borne by individuals. However, the major political parties have not proposed policies to address these inequalities that are reinforced by the current private super arrangements. The Rudd and Gillard governments focused their superannuation policy on increasing the Super Guarantee contribution rate to 12 percent of employees' wages, which has been a long-term Labor goal that was first flagged by the Keating government. The Coalition parties have largely supported this reform; although the Coalition did not vote to increase the Super Guarantee, Prime Minister Tony Abbott promised to retain the reform when Opposition leader (Franklin & Hepworth 2012). In office, the Abbott government has delayed the increase to the Super Guarantee to beyond its first term, but claims to still support the policy (Martin & Hutchens 2014). Ironically, considering it was used to justify the increase by the Rudd government, the Henry Review explicitly advised against raising the contributions level of the Super Guarantee because it was likely to disadvantage low-income earners (Henry 2009, p. 109). In fact, Labor's move to raise the Super Guarantee is likely to exacerbate gender inequality, as well as the inequalities between low-and high-income earners discussed previously. At the same time, this reform has also increased the investment risks borne by the majority of Australians who hold super in accumulation accounts and does not prevent super from being used for purposes other than retirement income. This implies that recent reform to the Super Guarantee has not just failed to address shortcomings of current policy, but has actually reinforced them.

So, will future reform address the major issues with private retirement incomes policy? On balance, it does not seem likely, but time will



ultimately tell. What is clear, however, is that the current scale and inequality of the super tax concessions is a largely unnoticed by-product of the privatisation of retirement incomes policy. It is also clear that it is premature, as the government proposes, to increase the Super Guarantee to 12 percent of wages when the inequalities of private super have not been addressed. From a policy perspective, reform to these concessions could do so much to enhance the efficiency of retirement incomes policy, while simultaneously reducing budgetary pressures and improving equity.

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