AMERICAN ACADEMY *of* ACTUARIES

Retirement for the AGES Assessment

Retirement System Assessment and Policy Committee

Australian Superannuation Guarantee Program[1]

Grade: B

The Australian Superannuation Guarantee Program (Super) is a savings scheme[2] where employers set aside contributions on behalf of their workers to provide for their retirement. Employers are required by law to make at least minimum Super contributions, referred to as Super Guarantee (SG), for all eligible workers. The payments are tax-deductible, unless the employer fails to meet the SG obligation, in which case they are also subject to a non-deductible Super Guarantee Charge (SGC). In addition, employers could be subject to additional penalties for failure to properly offer a choice of Super Funds, for directors who fail to meet an SGC liability, and for other administrative violations. Employees can also make voluntary contributions.

All employers who employ one or more people for wages or salary in exchange for work must contribute to a Super Fund (or another retirement savings account which satisfies the rules under the program) for all employees who are 18 years old or older and paid AUD[3] 450 or more (before tax) in a calendar month, or if younger or a private or domestic worker who receive at least this amount and also work 30 hours or more a week ("eligible employees"). The SG rate is 9.5 percent of ordinary time earnings (OTE) up to AUD 228,360 for 2020/2021 which includes commissions but not overtime earnings. Effective January 1, 2020, OTE includes any sacrificed OTE amounts described below. The SG rate is scheduled to increase to 12 percent by July 1, 2025. Self-employed individuals may contribute tax-deductible amounts on their own behalf.

Eligible employees, depending on industry agreements under the Australian Fair Work laws, may be eligible to choose a Super Fund for their and their employer contributions. If employees are not eligible to choose a Super Fund or if they don't make a choice, employers must pay their contributions into an employer-nominated or default fund and advise employees of the details of the fund. Small employers can contribute through a clearinghouse. After January 1, 2014 all employer default contributions are required to be paid into a registered MySuper product. MySuper products must offer specific product features and investment offerings and meet fee standards. As of July1, 2017, default balances, except for some legacy products, were required to be transferred into a MySuper product. Employees wishing to make other choices still can opt for an alternative product or a self-managed fund. Super Funds are subject to the Australian Tax Office (ATO) and must be registered with the Australian Prudential Regulatory Authority (APRA) to offer MySuper products.

[1] Based on legislation in effect as of January 2020.

[2] There are also pension schemes where employers make contributions to fund to a target minimum level of benefit instead of funding a specific contribution percentage.

[3] Australian dollars. As of <date of publication>, 1 AUD = X USD.

There are two types of contributions individuals can make to the Super Funds: concessional (pre-tax, and also called "salary sacrificed contributions") and non-concessional (after tax). Concessional contributions include the employer's SG contributions as well as salary sacrifice contributions[4], which are employee contributions arranged through the employer. Concessional contributions are not subject to income tax but are subject to a 15 percent tax on the contribution by the Super Fund. Investment earnings in the fund generally also are subject to a 15 percent tax until funds are in the decumulation phase. There are limits to concessional contributions so that amounts over the limit are subject to income tax plus an excess concessional contributions charge. Other contributions made as an individual are considered non-concessional contributions and are also subject to limits. Certain low- and middle-income earners who make non-concessional Super contributions are eligible for additional contributions called co-contributions from the government. Effective July 1, 2020, funds are allowed to accept the voluntary contributions for individuals: (1) aged 65 and 66 – without meeting the work test, and people aged 70 to 74 to receive spouse contributions and (2) for individuals under age 75 receiving contributions made by another person on their behalf if they meet the work test.

Employees can access their Super account when they reach their preservation age (which is increasing from 55 to 60 between July 2015 and July 2024) and retire or when they turn 65, even if they are not retired. They also may be able to access a limited amount each year under transition to retirement rules. Earlier access is limited to certain medical and hardship conditions. Benefits are payable as a lump sum or by investing in a retirement income stream, which means transferring the fund to a pension phase Super account. Income streams include both account-based streams and annuities; however, annuity options are rarely used.

In most circumstances, Super Funds also must offer some level of death and total/permanent disability benefits. Death benefits are paid to dependents and permanent disability benefits can be paid as a lump sum or income stream. Temporary disability benefits are payable in an income stream. Complex tax rules apply depending on the age at death or disability, the age of dependent at employee's death, type of fund used, and the form of the payment (lump sum or income stream).

The Superannuation Industry (Supervision) Act of 1993 (SIS) made provisions for the prudent management of certain superannuation funds and supervision by APRA, the Australian Securities and Investments Commission, and the Commissioner of Taxation. The SIS sets the rules that a superannuation fund must follow, such as the requirements for the trustees and operation of the fund, including the investments, management (including fund accounts), and administration. It also sets the penalties for trustees if the rules are not followed. Since 2004, a trustee must be a Registrable Superannuation Entity Licensee, and each fund the trustee operates also must be registered. Trustees must demonstrate to APRA that they have resources, risk management systems, skills, and expertise to manage a fund.

---

[4] These contributions are referred to as salary sacrifice contributions because the employee elects to have the employer make the additional contribution in lieu of direct salary.

Source Material

Australian Taxation Office (ATO) overview of Super for employers. Information available at:

https://www.ato.gov.au/Business/Super-for-employers/

https://www.ato.gov.au/Individuals/Super/Growing-your-super/Adding-to-your-super/Tax-on-contributions/

https://www.ato.gov.au/Individuals/Super/Getting-your-super-started/Employees/

https://www.ato.gov.au/uploadedFiles/Content/IND/Downloads/Changes_Impacting_the_Superannuation_Industry_Dec_2019.pdf

The Australian Prudential Regulation Authority (APRA) is an independent statutory authority responsible for the prudential supervision of financial institutions and for promoting financial system stability in Australia. Information available at:

https://www.apra.gov.au/about-apra

https://www.apra.gov.au/industries/superannuation

Australian Treasury overview of MySuper and recent changes available at:

https://treasury.gov.au/superannuation-reforms

https://treasury.gov.au/superannuation-reforms#improving

Government communication, tools and distribution choices for Individuals are found at:

https://moneysmart.gov.au/about-us

https://moneysmart.gov.au/grow-your-super/super-contributions#listo

https://moneysmart.gov.au/how-super-works/getting-your-super

Alignment

B+

Description

- Aligns each stakeholder's role with their skills.
- Redefines employer's role by placing responsibility for important roles with those appropriate entities.
- Helps individuals by structuring their choices to be well-defined and to enhance good decision making.
- Develops systemic ways to enhance financial security through appropriate levels of laws and regulations.

Application of Principles

+ Employer responsibility is minimal—limited to distribution of information packets provided by the government and Super Fund, withholding and transmitting employer and any employee contributions as required by the law, and selecting a default fund if the employee fails to elect one.

+ Administration and investment handled by separate trustees and entities, registered with APRA.

+ Individuals may use their Super account to purchase an annuity plan or to receive income through an income stream where investment earnings are tax-free.

+ Actual fund selection and fund requirements are well defined in the law and operations are subject to policies, guidelines, and supervision.

+ Online Communication materials for the participants are thorough and understandable

+ Employer contributions are mandated at 9.5 percent of pay (increasing to 12 percent over time) for broad coverage of employees.

+ Employees can also opt to contribute.

* Employees are allowed to set up self-managed Super Funds and direct contributions to them.

- In many cases, employees may select a Super Fund from among a very large number of options and notify their employer of their selection. Employees may or may not have the expertise to make the selection since available investments, associated fees, etc. may vary.

- The benefits may be paid out as a lump sum and employee may not understand how to manage their savings to produce retirement income.

- The average participant may not understand the benefit that will be provided by the program or what contribution level would be needed to meet their retirement objectives.

Legend
(+) feature meets principles
(-) feature does not meet principles
(*) feature where there is not enough information to determine impact

Governance

C

Description

- Clearly defines roles and responsibilities and acts in accordance with them.
- Reduces real and potential conflicts of interest.
- Recognizes and manages competing needs.
- Staffs boards with financial and other professionals who possess relevant expertise.

Application of Principles

+ Registered Super Funds are subject to extensive guidance and requirements covering fiduciary responsibilities, registration requirements to receive beneficial tax treatment, fund policies, guidance requirements, and operational oversight under ATO and APRA purview.

+ Recent statutory changes aim to improve the quality of financial advice and enhance retail investor protection.

* Self-managed funds are subject to separate oversight and guidelines set by the ATO.

- The governance laws are extremely complex, with many different categories and standard requirements, possibly confusing employers and employees.

- The retail nature of some funds' offerings presents potential conflicts of interest.

- There are some non-complying funds available in the marketplace. Unlike complying funds, contributions to these funds do not count toward the SG obligation, are not tax-deductible, and may incur a fringe benefit tax liability. However, these are rarely used.

- The process and guidance to help employees access lifetime annuities appears to be scant and cumbersome. Employees are directed to their Super Fund, a Financial Advisor, or the Government Financial Information Services to explore this option. This may directly explain why few employees elect a lifetime annuity. The perceived lack of value (i.e., high price) is also a major factor in the lack of take-up of annuities.

Legend
(+) feature meets principles
(-) feature does not meet principles
(*) feature where there is not enough information to determine impact

Efficiency

B+

Description

- Allows smaller plans to group together, with standard and transparent fees to lower plan costs.
- Provides consistent opportunities to accumulate assets during working lifetime to enhance participation and coverage.
- Minimizes leakage for non-retirement benefits during accumulation and payout phases.
- Encourages pooling and effective risk sharing so funds can provide lifetime income.
- Incents narrowing the variability of benefits by fostering risk hedging and allowing for pricing benefits and guarantees.

Application of Principles

+ A mandatory employer program, with automatic enrollment, provides consistent savings for employees and opportunity to save more for retirement.

+ Program minimizes pre-retirement leakage by allowing only tax-favored distributions for retirement, death, and disability.

+ Most assets are managed professionally, so should provide overall better results than individually managed accounts.

+ Large Super Funds hold and manage most of the money, thereby affording economies of scale.

+ Super Funds are required to offer benefit payments in the form of super income streams (payable over an identifiable period of time or meeting annual minimum distribution requirements), or if the Super provider allows, to provide super lump sums, or a combination of both.

- Plan allows for lump-sum distributions, which are frequently elected.

- Lack of specific standards for fund expenses may result in high fees, thereby diluting the ultimate accumulations.

Legend
(+) feature meets principles
(-) feature does not meet principles
(*) feature where there is not enough information to determine impact

Sustainability

B

Description

- Promotes intergenerational equity.
- Allocates cost properly among stakeholders.
- Withstands market shocks.
- Maintains balance between sustainability and adequacy.

Application of Principles

+ Employer cost is limited to guaranteed contributions.

+ Various levels of safeguards minimize sustainability risk, including: 1) mandatory coverage; 2) automatic enrollment; 3) establishment of separate funds; 4) use of individual accounts; and 5) ATO and APRA guidelines and oversight.

+ The guidance clearly limits the liability of the employer and the state.

+ 9.5 percent (increasing to 12 percent over time) employer-mandated contribution promotes retirement income adequacy.

- Limited ability for employees to deal with market shocks or changes in interest rates, which affects ultimate retirement income.

- All investment and longevity risks are borne by employees and retirees unless they purchase an annuity from an insurance company post-retirement.

Legend
(+) feature meets principles
(-) feature does not meet principles
(*) feature where there is not enough information to determine impact