

Moving the goalposts

May 16, 2009

Page 1 of 4 [Single page view](#)

Superannuation changes mean that baby boomers shooting for wealthy, healthy retirement may miss the mark, writes Annette Sampson.

AUSTRALIA has a problem and it is growing more wrinkly by the day. Even if we're all botoxed and collagen-pumped to within an inch of our lives, the population is getting older. More than 1 million Australians are set to retire in the next 10 years, and if that's not scary enough, another 3 million will retire in the 10 years after that. By 2047, about 7.2 million people, or a quarter of the expected population, will be over 65. That's almost double the current level of 13 per cent. And the proportion of us who are very old — 85 or older — will more than triple to 5.6 per cent of the population, or a staggering 1.6 million people.

Baby boomers have no intention of growing old quietly. This is the generation that claimed 40 was the new 30. Then, that 50 was the new 40. With many now approaching 60, the years that previous generations had set aside for a quiet cup of tea and maybe a caravan trip up the coast are being viewed as a chance to have it all — leisure, part-time work, and a healthy income to fund it all.

Or that's the dream. The reality is that the global financial crisis has savaged the wealth of pre-retirees and few will have the savings needed to pay for their aspirations.

Yes, we're living healthier and longer lives on average, but that presents its own problems. Instead of retiring at 65 and living for another five or 10 years, we're likely to spend longer in retirement. That increases the odds of seeing our savings run out before we do, and the likely cost of our old age on the public purse.

The challenges of an ageing population have been brought back into the spotlight by this week's federal budget, particularly the controversial decision to give existing pensioners a pay rise but increase the pension age for those further down the chain from 65 to 67 by 2023. Anyone aged 57 or less will have their pension age increased from 2017 and everyone born after January 1, 1957 can forget claiming their pension until they turn 67.

Future retirees will also be hit by savings measures to help fund the cost of the increased pension payments. Giving pensioners a much-needed pay rise might make political and common sense, but it is not cheap. The Government budgeted an extra \$14.2 billion over the next five years to deliver a \$32.49 increase a week to single pensioners and \$10.14 a week (combined) for couples. About \$4.2 billion of the cost will come from reduced superannuation tax concessions for both higher and lower-income earners.

Baby boomers hoping to play catch-up by making big super contributions in their pre-retirement years will have their maximum tax-deductible contribution limits slashed by more than half — to \$25,000 for the under-50s and \$50,000 for those aged 50 or more. From 2012, the limit for the over-50s will also be cut to \$25,000 — though it will be indexed. Lower-income earners will get a reduced benefit from the popular co-contribution where the Government kicks in \$1.50 for each after-tax dollar you contribute to super, up to a maximum government contribution of \$1500. That will be cut to \$1000 for the next three years, then \$1250 for a further two years.

The proposed measures have thrown the retirement plans of many older workers into disarray. While the Government says the new limits on concessional contributions are merely removing some of the obscenities from superannuation tax concessions, those in the super industry say it will hamper the ability of the baby boomers to provide for their retirement, potentially generating higher pension costs later on. [Continued...](#)

"Certainly if you have more than \$25,000 to put into super you would need to be reasonably well-off," says the head of Ernst & Young's asset management practice, Graeme McKenzie. "But people close to retirement age were making significant contributions because it was the lifeblood for their future. They don't think it's obscene to be saving for their retirement."

Mercer (Australia) chief executive Peter Promnitz says the new limits will also disadvantage people who have been out of the workforce for extended periods, such as women, and the self-employed who may simply not have been in a position to make big contributions earlier.

IPAC Securities manager for advice development John Dani says many self-employed people are also looking to make higher contributions now to try to recoup the hit their savings have taken, due to investment losses in the financial downturn.

Watson Wyatt managing director Andrew Boal says many baby boomers will be disappointed by their retirement. While they have received some of the benefits of compulsory super, the system won't be fully mature until 2047. Unless they have saved extra, most will still be forced to rely on the age pension for at least part of their retirement. He says many baby boomers intended to top up their retirement savings after paying off their mortgage and educating their children. The new contribution limits will make this more difficult and some who intended to be self-reliant may now claim the age pension. Others will look to save outside the super system, raising fears that they may opt for riskier strategies of building wealth such as gearing.

Baby boomers will also be the most immediate victims of the increased pension age and new taper rates, which make it harder to get the pension. While handing out more money to existing pensioners, Treasurer Wayne Swan increased the rate at which new pensioners would lose their pension entitlements under the income means test. The measure will apply from September 20, but only to new pensioners.

McKenzie is concerned the people will lose confidence in the super system because of the changes. "Confidence has already been rattled by the investment markets downturn," he says. "(Super) is a long-term savings plan but every year they change the rules."

McKenzie says legislative risk has always been a concern for people investing in super, but concerns have now heightened, particularly with the Government considering a recommendation by the Henry review into the tax system for the superannuation preservation age — that magic date when you can access your super — to be increased to 67 in line with the proposed new pension age.

Institute of Actuaries of Australia chief executive John Maroney says this will have a much bigger impact than increasing the pension age because it will force people to hold onto their super for a further seven years. The super preservation age is currently in the process of being raised from 55 to 60. He says the pension age is also elastic in terms of government revenues because a large proportion of people stop working before 65 and claim other government benefits — such as disability or carers benefits — until they get the pension. So the full impact of a higher pension age may not be reflected in lower costs.

But it is also likely to encounter stiff opposition.

"The two key problems people currently have with super are that their money is locked up until at least age 55 years and that the rules are constantly subject to change," says David Moss, a director of super specialist Moss Munro Hunt. "Knowing the Government will be contemplating locking up superannuation benefits for an additional 12 years will give many of our clients a huge scare." [Continued](#)

The Government says the changes are all about sustainability. The Henry review says the same. But what they're really grappling with is a tug of war between current and future retirement needs that will only intensify as the population ages.

As more workers retire, the drain on working taxpayers will inevitably rise. Currently there are about five people of working age to support every person aged 65 or more. But by 2047, this will halve to just 2.4 workers for every oldie.

Expecting them to shoulder double the current burden is clearly untenable, but how much should current taxpayers chip in to lessen the future burden?

The initial report into retirement incomes by the Henry review, released with this week's budget, draws a line in the sand between the old view that government should do all it can to encourage people to save for better retirement outcomes and the new focus on costs.

In addition to recommending the preservation age be lifted, the report effectively quashed long-standing arguments — including those from the architect of compulsory super, former prime minister Paul Keating — that the current compulsory super contributions of 9 per cent should be lifted to at least 12 per cent.

The review also recommends a further review in 2020 to consider whether retirement ages should be increased even further, that means tests for the pension be simplified and better targeted, and that super tax concessions be distributed more equally between high and lower-income earners — including limiting salary sacrifice concessions.

The Government has said it won't consider the proposals until the full tax review is delivered at the end of the year, but it is clear investors have reason to be uncertain.

The problem is that even with compulsory super, most Australians will continue to rely on the age pension. Treasury modelling shows that almost 30 per cent of over-65s would still be receiving a full pension in 2050 and 45 per cent would be receiving a part-pension.

So even a modest pension rise now sets up a financial time bomb for future taxpayers. The Government says the cost of any pension increase now will almost double as a share of GDP by 2050, purely due to demographic change.

The Government has made much of the fact that when the pension age was originally set in 1909, only half the male population even reached retirement age. Those lucky enough to crack the pension jackpot typically had 11 years to enjoy the spoils.

Now more than 85 per cent of males reach 65 and they can expect to live another 19 years on average. Boal says life expectancies have been increasing by one year every six years. If this continues, by 2023, many retirees will be living into their 90s and someone will have to fund those extra years. And while many will expect to live at least part of this additional life expectancy in good health, the Henry review points out that health expectancies have increased at a lower rate than life expectancies, setting future taxpayers up for increased health and aged care costs.

In his pension review, Dr Jeff Harmer said it was estimated social spending was set to increase from 13.1 per cent of GDP in 2006-07 to 18.2 per cent in 2046-07 with increased spending on the age pension and related payments for the aged contributing 1.9 percentage points (or 37 per cent) of that 5.1 percentage point rise.

Even bigger was the projected rise in health costs, where the costs of an ageing population are compounded by the costs of new drugs and technologies. Costs here are projected to rise from 3.8 per cent of GDP to 7.3 per cent between 2006-07 and 2046-07. Harmer says that while there are offsetting savings, funding the increases in social spending would require an increase on government receipts — that's mostly taxes — of more than 23 per cent. [Continued...](#)

In its take on the numbers, the Henry review points out that the projected 3.7 per cent of GDP projected increase in health, aged care, and the age pension due to the ageing population would be equivalent to the entire GST revenue, the entire federal health budget, or a third of the money raised from personal income tax. In order to ensure long-term fiscal sustainability, it said, governments need to look at a combination of higher workforce participation, higher productivity growth, reduced spending or increased taxes.

To some extent, retirement incomes are the lesser problem. Boal says super savings are already projected to rise to \$3.5 trillion by 2023 and once we start to see workers retiring who have had the benefit of a full working life with compulsory super, people on average incomes should be getting a retirement income including a part pension of close to two thirds of their pre-retirement income.

Boal says health and aged care costs are the big sleepers in terms of costs, but it is not as if they operate in isolation. Rising costs there increase the need for savings in other areas.

"One of the concerns will be that if future governments need to save cash, tinkering with the pension means tests will be a temptation," he says. "It's very difficult for people to plan if things are going to change.

"(Ageing and longevity) are issues we have to get on the table. we have to understand exactly what we can afford.

- [Single page view](#)
 - - [Prev](#)
 - [1](#)
 - [2](#)
 - [3](#)
 - 4