COTA
For older Australians

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Ms Serena Wilson
Deputy Secretary
Department of Social Services
GPO Box 9820
Canberra ACT 2601

Dear Serena,

Social Security Means Testing of Retirement Income Streams

Thank you for the invitation to comment on the "Discussion Paper: Social security means testing of retirement income streams".

It is unfortunate that the timeframe for comment on the paper was essentially January, as it was only released on the eve of Xmas and responses have a deadline of today. Like most organisations COTA's very limited number of relevant personnel were on leave up to 16 January. In addition, many of the people who we sought to consult on the issues, within the COTA network and in the industry, were also on leave.

These comments therefore carry the caveat that COTA's position may further develop as we have time for further discussions within and outside the organisation.

Purpose of new retirement income stream products

From COTA's perspective the development of a strong market in Comprehensive Income Products for Retirement (CIPRs) is vitally important for a range of reasons, including:

1. The public policy need to reinforce that superannuation is designed to assist people achieve a higher level of income across their retirement to enable them to have a better standard of living than if they were on the age pension;

2. Following on from point 1, the need to encourage more people to primarily utilise their superannuation as retirement income and not retain substantial portions of it as capital right through to their death;

3. The public policy interest in a larger portion of people in retirement / later years being able to meet a higher proportion of their aged care costs in a more robust user contributions regime;

4. The public policy interest in retirees having a higher income across their retirement years and therefore drawing less income from the age pension;

5. The public policy interest and personal value inherent in superannuation enabling people to have more choice and control during their retirement over matters such as their health services, aged care and housing, which a higher income makes more possible.

Means Testing Treatment of CIPRs

CIPR's are designed to increase retirement income above what people who don't know when they are going to die are prepared to take from their allocated pensions or by taking their superannuation as a lump sum and self-managing it as an investment.

CIPR's achieve this not by dint of their issuers being better fund managers than those who manage allocated pensions; nor by any mysterious form of financial magic. CIPR's achieve this by being a different kind of retirement living product than allocated pensions or passive investments like term deposits.

CIPRs achieve a higher income because they utilise one or more forms of annuity that are in whole or part a form of risk pooling based around actuarial calculations of life expectancy which mean that a proportion of retirees will "win" and a proportion will "lose" but both "winners" and "losers" will be able to take higher incomes while they are alive than if they were not using a CIPR.

CIPRs operate on a similar principle to all other forms of insurance – individual risks are pooled.

Right now many current and future retirees will find this form of retirement income provision unusual and somewhat challenging. If they could be guaranteed to be a "winner" they would be more enthusiastic about them, but the idea of being a "loser" does not sit well. Yet we insure our homes, cars, holidays and our lives and hope we will not need to claim.

To encourage the take up of CIPRs it will be essential that they are not treated in the same way as current conventional retirement income products, because very few people will take them up if that happens.

For example, the suggestion in the Discussion Paper that people using an annuity who exceed life expectancy would receive concessional means testing treatment fails to understand the nature of risk pooling. If they are to be means tested on the same basis as account based pensions, then are people who die early going to get a refund to their estate?

COTA is concerned about the options proposed in the Discussion Paper based on our limited (due to time constraints) discussions with the industry. As the department knows well COTA often takes industry views sceptically (e.g. with regard to the proposed statutory objective of superannuation) but on this occasion we are inclined to the view that the more modest industry views are correct and the options proposed in the Discussion Paper will effectively kill off CIPRs before they get going. For the reasons we set out earlier this would be a great pity.

It is critical that there be a whole of government perspective on the means testing of CIPRs that takes into account the goals of an overarching retirement incomes policy, not just a perspective based on one siloed area of public policy.

I have not commented in this letter on the detailed technical aspects of the Discussion Paper. Some of these are outside COTA's internal expertise and we rely on advice from technical experts. Nevertheless, we do have views on some of the matters discussed in the paper and their implications - for example, the differential impact on different wealth cohorts over time of different treatments of deferred products.

However, we have not gone into any technical matters in this letter because they really are subsidiary to the question of the basic approach to means testing of CIPRs which we have tried to address and which if not resolved leaves the technical questions moot, as there will not be a CIPR market to means test.

I would be happy to discuss this response with you and your colleagues. I am also happy for COTA’s position to be disclosed publicly.

With best regards,

Yours sincerely,

Ian Yates AM
Chief Executive

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