…practical solutions for the financial services industry…

Removing the Superannuation Employment Nexus

Final Report
July 2002

Kieren Dell
Stuart Milne

Greek doing, action

Modern 1. the exercise of an art, skill or science. 2. The exemplary joining of theory and action into practice

Praxis Partners Pty Limited (acn 091 159 330)

Contents

1 Introduction 2
1.1 Brief 2
1.1.1 Overview/Background 2
1.1.2 IFSA's Objectives 2

2 Executive summary 3

3 Current environment 5
3.1 Who can contribute 5
3.1.1 Those that can contribute themselves 7
3.1.2 Those that can have contributions made on their behalf 7
3.2 Who cannot contribute 7
3.3 ABS Statistics 8
3.3.1 Superannuation Contribution Coverage 9
3.3.2 Voluntary contribution rates 11

4 Benefits of removal 13
4.1 Participation 13
4.2 Compliance costs 14

5 Breaking the employment nexus for voluntary contributions 17
5.1 What needs changing (policy/legislation) 17
5.2 What new policies would be required? 18
5.2.1 Reasonable Benefit Limits 18
5.2.2 Retirement ages 19

6 Summary 20

1 Introduction

Praxis Partners has been engaged by IFSA to prepare this report on the superannuation contribution and employment nexus. This report aims to identify those areas of superannuation regulation, specifically the employment test in the contribution standards, which are no longer appropriate or relevant given the relatively wide variety of situations under which superannuation contributions can now be made.

1.1 Brief

1.1.1 Overview/Background

Removal of the remaining general restrictions on superannuation contributions based on the employment nexus is a logical extension of recent initiatives and proposals.

- Legislation still generally prevents superannuation funds accepting contributions unless the member is employed. There are now numerous exceptions to this general rule, with a number of significant new exceptions to commence under commitments made in the 2001 election.

- The situation after 1 July 2002 will be that so little of the general restriction will actually have effect as to call into question its continued relevance (and more so after 1 July 2003).

- The general restriction will continue to place a significant cost burden on superannuation funds, and this burden is ultimately borne by Australians savings for their retirement.

Consequently, the employment nexus appears to impose cost on the system for little or no continuing benefit.

1.1.2 IFSA's Objectives

IFSA would like to make an initial exploration of the process required to remove the remaining general restrictions arising from the employment nexus, and identify some of the costs and benefits of doing so.

The report of this project will be used to assess the desirability of a larger scale project on the long-term costs and benefits of removing the 'nexus', and may well be used to advocate for further examination of the issue by government.

2 Executive summary

Rules surrounding a person's eligibility to make voluntary personal contributions to a superannuation fund have, over the years, been amended and enhanced to allow more and more individuals the ability to contribute. There is still, however, at the heart of the contribution rules a general requirement that a person be gainfully employed in order to make a superannuation contribution. This requirement now prohibits only a relatively small section of the community from making personal voluntary superannuation contributions.

Removing this nexus would provide a number of benefits to both the Australian population and the superannuation system in general. Two of the main benefits are:-

- Participation – people that are currently excluded from making a contribution would be able to access the superannuation system. An example of these types of people include divorcees who are not employed.

- Simplicity – superannuation in Australia is a complex system. Part of the complexity arises from the number of contribution options available to participants and under what circumstances a person may make certain types of contribution. Removing the employment test would effectively leave the system with three different types of contribution:-

    - Employer contributions (deductible)

    - Self-employed contributions (deductible)

    - Voluntary personal contributions (non-deductible)

The range of people currently excluded from making superannuation contributions is relatively small. Those unable to make a contribution include the long-term unemployed and long-term welfare recipients, non-employed divorcees, those never employed and never married, people who may have become disabled after leaving employment and people who "work" but cannot meet the gainful employment test requirements.

All of this complexity surrounding whether or not a person is eligible to make a superannuation contribution, and whether a superannuation fund can accept a contribution from these people, excludes such a limited number of people that there seems to be little benefit to the rules as they currently stand.

Relatively simple legislative changes would be required to break the employment and superannuation nexus. Firstly, those parts of the Superannuation Industry (Supervision) Regulations 1994 which combine the gainful employment test with certain age-based criteria would need to be removed. This would leave age as the basic criteria.

Secondly, some changes surrounding the conditions of release and the nexus between retirement and employment would be required to ensure that the superannuation system

continued to prevent people from accessing a benefit prior to “retirement” whilst allowing those who may not be employed to access their superannuation when eligible.

Removal of the nexus would not appear to pose any significant costs to government in the operation of the superannuation system nor in terms of revenue. For superannuation fund trustees and administrators there do seem to be avenues by which cost savings could be achieved. Conceivably, these would be achieved in the areas of compliance, administration and systems cost.

3 Current environment

Restrictions on eligibility to contribute to superannuation are contained in the Superannuation Industry (Supervision) Regulations 1994 (SIS). When first introduced, this legislation restricted who was able to make contributions to superannuation. Effectively, contributions could only be made where a person:

- was gainfully employed or had been gainfully employed in the past two years;
- had ceased work due to invalidity
- had temporarily ceased work for the purposes of raising children (for up to seven years)

Over the ensuing years a number of changes, additions and relaxations have been made to these restrictions. These include permitting contributions on behalf of non-working spouses, and most recently, permitting contributions:

- on behalf of children
- to be split between spouses (including non-working spouses)

Additionally, amendments to Family Law will permit accumulated superannuation balances to be split between divorcing couples effectively meaning that a spouse who has never been employed may ultimately be the beneficiary of a superannuation fund to which they cannot continue to contribute.

3.1 Who can contribute

Employed persons	• Covered by the Superannuation Guarantee. **Aged under 65** • Are able to make personal contributions provided they are working at least 10 hours per week in the last two years. **Aged between 65 and 75** • Are able to make personal contributions provided they are currently working at least 10 hours per week (changes to legislation increasing this to age 75 have been passed and applies from July 1st, 2002).
Self employed persons	• As above (except they are not covered by the SG).

Ill-health	• Ceased employment due to ill-health (and under age 65).
Parental leave	• Are on authorised parental leave for up to seven years (and under age 65).
Previously employed persons	• Have a two year window in which they can continue to contribute to superannuation • It could be argued that the trustee discretion for accepting contributions under SIS [SIS Reg 7.04(2)] allows contributions outside of this two year window
Married people & non-working spouses	• Spouse contributions provided the spouse is under age 65 irrespective of the employment status of either party (the contributor must however be a "taxpayer"). • Splitting of contributions by working spouse between them and their spouse (in accumulation funds only). This is expected to apply from July 1st, 2003 however no legislation has yet been introduced.
Non-employed persons starting families	• Recipients of the First Child Tax Offset (Baby Bonus) will be able to contribute this amount to a superannuation fund. Additionally, the Minister for Revenue and Assistant Treasurer's Press Release announcing this initiative states that *"Recipients of the Baby Bonus will be able to contribute the Baby Bonus, **as well as any other amount**, to superannuation, even if they have never worked before"* (changes to regulations have been made for this and are currently in force). Applies from July 1st, 2002.
Children	• Up to $3,000 over a three year period can be contributed per child (who must be under the age of 18) by anyone – this was originally announced to be parents, grand-parents, other relations and friends (changes to regulations have been made for this and are currently in force). Applies from July 1st, 2002.

Effectively, there are two broad categories of people who can make, or have made, superannuation contributions.

- Those that can contribute themselves.
- Those that can have contributions made on their behalf.

3.1.1 Those that can contribute themselves

- Employed persons.
- Self-employed persons.
- Previously employed persons
- Those that have left employment due to ill-health or to raise children.
- Recipients of the Baby Bonus.

3.1.2 Those that can have contributions made on their behalf

- Employed persons (under the SG regime).
- Spouses.
- Children.

3.2 Who cannot contribute

Given the wide range of people who are now eligible for superannuation coverage there appear to be only a small number of groups of people who cannot effectively make a superannuation contribution.

These generally include:

- People who have never been employed and are not eligible to receive, or have made, spouse contributions (those not married and never employed) or who have not received the First Child Tax Offset (one might expect that these people would need to be long-term-unemployed spinsters or bachelors).
- Certain people who can't meet the requirements of the gainful employment test, that is, those people who are under age 75, not employees and are not in gainful employment for more than 10 hours per week. This, for example, may include people in certain "employment" type roles such as investors, those individuals managing personal property portfolios and people in unpaid work such as charity work if their work is not for gain or reward.
- Divorcees who are not employed. These include would women (and men) who may receive part of a superannuation balance as part of a divorce settlement but may then be unable to further contribute to the fund due to their employment status.
- The long-term unemployed and other long-term recipients of welfare benefits (for longer than two years if they had previously been employed) such as carers allowances and sickness benefits.

- People over the age of 75 (even if they are employed/working).

- People who have left employment and then become disabled (via such things as a car accident after ceasing work for example) as distinct from those that become disabled whilst in work.

It should be recognised that many people in some of these categories may not have the ability (such as those on unemployment benefits), due to the difficulty they may have in meeting their day-to-day expenses from their limited income, to make voluntary contributions to superannuation. Many of these however, do recognise the need to save for retirement.

Conversely, many people in categories who are ineligible to contribute are in a financial position which would allow them to contribute to superannuation. Allowing these people access to the superannuation environment would not only put them on an equal footing with regards to retirement savings as those that are able to contribute but would also, as is Government policy, properly facilitate (and regulate) the orderly drawdown of income and capital upon retirement. A good example of the category of people who would benefit from this are divorced people who may have received a share of a superannuation account balance on divorce but are excluded from making further contributions due to their non-employed status.

Anecdotal evidence indicates that those "retirees" who are funding their retirement outside of the superannuation system, that is, people who do not have access to an allocated pension, tend to have a more conservative drawdown of income and capital than those required by the minimum and maximum limits imposed on allocated products. This would suggest that some of these people may have lower than ideal retirement incomes that could be enhanced by utilising the superannuation system.

Additionally, many investors funding their retirement outside of superannuation retirement income streams do not have the benefit of gaining access to a product that provides them with an income which is relatively worry free and administratively simple for the investor.

3.3 ABS Statistics

Statistics produced by the Australian Bureau of Statistics[1] show that, as at June 2000, there were some 13,388,800 people in the 15 to 69 age bracket.

Of these, 1,920,400 (14%) were retired and 131,100 (1%) have never been employed and were not intending to become employed.

The balance (11,337,300, 85% of total) were in the pre-retired phase. Of this 85%:

- 40% had employer or business superannuation contributions currently made (34% of total)

[1] ABS Superannuation Coverage and Financial Characteristics, April to June 2000 – 6360.0

- 17% had employer or business and personal contributions made (15%)
- 4% had only personal or spouse contributions made (3%)
- 14% had superannuation but no contributions were currently being made (12%)
- 25% had no superannuation (21%)

Those with no superannuation included 55% of unemployed people, 70% of people not in the labour force (but not retired) and 48% of people aged between 15 and 24.

These statistics do not, unfortunately, tell us the number of people who cannot specifically contribute to superannuation rather than those that can, but do not contribute (of those who currently have no superannuation or for whom no contributions were being made). The statistics in the following section, however, do provide some further information.

3.3.1 Superannuation Contribution Coverage

These statistics are based on the number of persons aged between 15 and 69 which includes retirees and those that have never been employed and were not intending to become employed.

	Employer/business contributions only	Personal/spouse and employer/business contributions	Personal/spouse contributions only	No contributions currently being made	No superannuation
Employed	**51.4%**	**22.4%**	**4.1%**	**8.8%**	**13.3%**
• *Males*	*47.6%*	*24.7%*	*5.8%*	*8.8%*	*8.8%*
• *Females*	*56.3%*	*19.4%*	*2.3%*	*7.4%*	*14.6%*
Unemployed	**1.8%**	**0.3%**	**1.4%**	**41.9%**	**54.6%**
• *Males*	*1.2%*	*0.4%*	*1.0%*	*45.4%*	*52.0%*
• *Females*	*2.6%*	*0.2%*	*0.7%*	*13.6%*	*31.7%*
Not in labour force[2]	**1.0%**	**0.2%**	**0.7%**	**12.3%**	**32.9%**
• *Males*	*0.6%*	*0.2%*	*0.8%*	*10.0%*	*35.3%*
• *Females*	*1.3%*	*0.2%*	*0.7%*	*13.6%*	*31.7%*

In addition to the above, of those not in the labour force (as they were retired) an additional 28.2% of males and 13.4% of females (18.6% of the combined) had received a lump sum or income from superannuation already and an additional 22.9% of males and 35.1% of females (30.8% of the combined) had not received a superannuation lump sum and were not receiving income from superannuation.

Of these statistics, the figures relating to people "unemployed" and "not in labour force" are the most telling. 54.6% of unemployed people and 32.9% of people not in the labour force have no superannuation.

Of the same sample, some 47.1% of people between the ages of 15 to 24 had no superannuation and of those with "nil or negative income", 57.1% had no superannuation. Additionally, for those with incomes between $1 and $19,999 31.9% had no superannuation.

For those that had income between $1 and $19,999 we can assume that some of these people will be employed but may not meet the gainful employment test and some may fall under the SG income threshold. Additionally some of these may be people living off non-superannuation investment income.

[2] figures do not add to 100% due to the % of people who are not in the labour force but are retired

For those in the "nil or negative income" category it can be assumed that these people may be non-working spouses, invalids, itinerants, those people not on welfare and not employed (possibly those people living off their assets which produce no income such as lottery winners) and even possibly bankrupts.

3.3.2 Voluntary contribution rates

3.3.2.1 Personal (voluntary) contribution rates

Of the 8,727,600 jobholders in the ABS survey some 30.4% of males and 21.4% of females were making personal superannuation contributions.

By age, the highest incidence of contributors were found in the 45-54 age group.

	Age 15-24	Age 25-23	Age 35-44	Age 45-54	Age 55-69
% making personal voluntary contributions	7.4%	20.9%	32.4%	38.5%	32.4%
Total people in survey	1,563,200	2,128,600	2,257,000	1,937,900	840,900

Of those not making personal contributions the following reasons were given:

	Age 15-24	Age 25-23	Age 35-44	Age 45-54	Age 55-69
• Cost/cannot afford to	37.2%	36.9%	40.5%	36.8%	30.6%
• Have not bothered	24.5%	20.2%	12.7%	12.9%	10.9%
• Not eligible to make personal contributions	8.6%	6.6%	6.8%	8.9%	8.1%
• Has other investments	1.8%	5.4%	7.1%	8.8%	12.0%

These statistics show that the number of people who were ineligible to make contributions were not a huge number by percentage, largely one assumes, due to the large range of contribution options that are now available. Of the total, 7.7% of people were ineligible to make a superannuation contribution.

For those that were making contributions the main driver of the amount of contribution was income based.

		Contribution Level per week				
		% making contributions	Under $20	$20 to $39	$40 to $59	$60 and above
Annual Income	$1 to $19,999	8.6%	35.7%	21.7%	10.0%	11.5%
	$20,000 to $39,999	23.7%	28.3%	35.1%	12.7%	8.4%
	$40,000 to $59,999	43.9%	13.2%	25.9%	26.8%	21.3%
	$60,000 to $79,999	48.5%	7.6%	12.4%	23.6%	43.4%
	$80,000 to $99,999	44.0%	8.4%	10.1%	16.8%	51.3%
	$100,000 and above	39.5%	6.5%	10.0%	9.6%	61.1%

3.3.2.2 Spouse participation

Many spouses, particularly non-working spouses, were for a long time excluded from the superannuation system resulting in superannuation savings for many couple being concentrated in the name of the working spouse.

Spouse contributions and the splitting of contributions between spouses (for those in accumulation funds) has, and will go some way, to alleviating this issue. However, there are still quite a the number of spouses who do not have access to superannuation or have an accumulated superannuation balance.

ABS statistics show that, of males with superannuation some 9.7% of them have spouses with no superannuation. For females with superannuation, some 4.2% of their spouses do not have superannuation.

For males who have no superannuation the percentage whose spouses do not have superannuation is somewhat higher at 14.5% (11.6% for spouses of females that do not have superannuation). This means that neither party has any superannuation at all. The incidence of spouses who do have superannuation where their partner did not was 13.2% for males and 27.9% for females.

Whilst anecdotal evidence would suggest that these rates have been declining over recent years due to the incidence in modern society of both parties in a marriage being employed, the amount of contribution (and tax incentive provided to make the contribution) that can be made on behalf of a spouse under the spouse contribution rules has also increased coverage (although the account balances of these spouses would tend to be relatively low).

4 Benefits of removal

4.1 Participation

Much has been written over the last ten years since the introduction of the Superannuation Guarantee system on the level of superannuation coverage now enjoyed by the Australian workforce.

As can be seen from ABS figures noted previously there are still a great number of the Australian population that does not have superannuation coverage at all. Some 21% of people aged between 15 and 69, at June 2000, had no superannuation at all, some 12% had some superannuation but no contributions were currently being made. Whilst some 92% of full time employed persons had superannuation only 72% of those employed part time did. These figures indicate that whilst penetration of superannuation is relatively high amongst employed people, there are a large group of people who do not currently have any superannuation (including those not in the labour market).

Recent changes to contribution eligibility and the addition of other "types" of contribution have widened the superannuation net further than ever before.

The prime benefit of removing the employment nexus would be to allow all of these people access to the superannuation system providing increased coverage across the Australian population as well as ensuring that these people who currently do not have the ability to make contributions have access to a retirement income system that ensures the efficient and orderly drawdown of a retirement income stream (at present they have access only to non-superannuation annuities which are seldom used).

Whilst providing all people with the ability to make superannuation contributions will not eliminate the need of many people to rely on Government funded pensions in retirement, it will provide those with some ability to save to ensure that any saving for retirement is done on a equal footing, in the concessionally taxed superannuation environment, as those who are currently able to contribute. It also ensures that these people will be saving (specifically) for their retirement in an efficient and regulated savings environment.

Nor will the removal of the employment test necessarily mean that those previously "locked-out" will definitively use the superannuation environment simply because they now can. The use of incentives encouraging people to use the superannuation environment is more likely to prompt them to use superannuation. Whilst the current (personal) tax deductibility of contributions is limited to the self-employed, the Government's introduction of co-contribution measures and the existing spouse contribution rebate system increases the chance that these people will utilise the superannuation system.

It should be noted that allowing those that currently cannot make personal voluntary contributions to superannuation to contribute, should not pose a threat to Government revenue due to the fact that these contributions would generally be made from an individual's after-tax income. In fact, it could can expected that these contributions will contribute further to

Government revenue though the payment of the fund earnings tax whilst in the accumulation phase of superannuation and possibly, on withdrawal from the superannuation environment upon retirement.

4.2 Compliance costs

The removal of the employment test would also benefit superannuation fund trustees. Considerable time is currently spent by trustees on validating a person's eligibility to make voluntary personal contributions to a fund.

Whilst it is difficult to pin down costs relating specifically to this exercise which fund trustees bear, anecdotal evidence from a number of fund trustees, administrators and fund managers indicate that up to one-third of their "processing" cost is made up of compliance activities and checking required by superannuation legislation. Whilst there are a number of facets to this checking, the verification of employment status or eligibility to contribute upon receipt of a contribution poses a significant cost on fund trustees both in terms of employee cost and administration systems cost.

In some cases this verification may be easily achieved if the personal contribution is being made to an employee's employer sponsored fund (as the trustee merely must check whether an employer contribution has been received within the last two years). However, in the case of a contribution made to a different fund altogether the fund trustee must verify a persons eligibility independently (the ABS statistics show that some 22.4% of people with a superannuation balance have two accounts/funds and 8.8% have three or more).

For those non-employed who are making a contribution a trustee's compliance checking gets more difficult. As an example, from July 1st this year how will fund trustees determine whether a contribution made on behalf of a child is acceptable and that the child does not have any employer (or other) superannuation support if that child performed some casual work or was employed as an apprentice?

The removal of the employment test has been advocated in a number of forums of late. Most recently many submissions made by industry bodies, fund trustees and reputable commentators to the Senate Select Committee on Superannuation's inquiry into "Superannuation and standards of living in retirement" have advocated the removal of the employment test citing compliance costs and the limited number of people who are now ineligible to contribute to superannuation as major points. AMP, for example, submitted that…

> *"… that anyone between the age of 18 and 75 be able to make personal undeducted superannuation contributions, regardless or their employment status. This will enable those outside of the workforce (especially women) to voluntarily save through super while reducing the administrative complexity of checking eligibility"*[3]

[3] AMP, "Can you afford to retire" submission to Senate Select Commission, p5

Additionally, the Productivity Commission, in its final report *"Review of the Superannuation Industry (Supervision) Act 1993 and Certain Other Superannuation Legislation"* dated December 18th, 2001 have stated and recommend[4] that:

> *"The Commission has identified a number of provisions under review which impose significant compliance costs on fund trustees. These include:*
>
> - *procedures for verifying the age and employment status of members in relation to contributions and benefit payments;…"*
>
> *"Age and employment requirements governing contributor status and compulsory cashing of benefits should be simplified. The most effective means of doing so would be removal of the employment tests, while limiting any adverse implications for taxation revenue by measures such as reasonable benefit limits and age-based deductible limits. Considerations should also be given to raising the age at which benefits must be compulsorily cashed."*

In response to the Productivity Commission's report Senator Coonan, the Minister for Revenue and Assistant Treasurer, have noted the recommendation (5.1) above and stated that:

> *"At the 2001 election the Government committed to allowing those aged up to 75 to make voluntary contributions to superannuation. The Government continues to monitor the operation of Australia's retirement income system with a view to ensuring that it efficiently provides positive outcomes for all Australians.*
>
> *In this context, the Government has asked Treasury to review the monitoring requirements for superannuation funds in respect of the 10 hours per week part-time gainful employment test for persons aged between 65 and 70 years."*

This, unfortunately, appears to be committed to reviewing the test for a limited number of people and seems to be limited to reviewing the process of fund trustees obligation to ensure that those aged between 65 and 70 are maintaining their gainfully employed status in relation to remaining within the system not their ability to make superannuation contributions.

The removal of the nexus would also potentially provide fund trustees with considerable cost savings in the preparation of offer documents (which contain eligibility requirements and "category or contribution" questions on application forms). Additionally the removal would present fund trustees with the opportunity to make cost savings in the maintenance of their computer systems by reducing the number of inter-related checks carried out by these systems on receipt of a contribution and removing a layer of system testing which is required when other system amendments are carried out.

It could also be expected that costs incurred by regulatory bodies, such as APRA and the ATO, in auditing superannuation funds could be saved by them not having to check the

[4] Productivity Commission Inquiry Report pages XXIII & XXXVII, December 18th, 2001

validity of these items during audit. Whilst unquantifiable, the same could be said for costs incurred by internal audit teams in fund trustees' offices.

It is therefore conceivable that removing this layer of compliance checking at the time contributions are made would reduce the costs borne by fund trustees (and hence the funds and superannuants themselves). Any savings could be passed on to fund members by way of lower management fees making superannuation cheaper for the consumer which, over the longer term, will increase the balance of accumulated superannuation held by members.

5 Breaking the employment nexus for voluntary contributions

5.1 What needs changing (policy/legislation)

In order to provide greater equality and access to superannuation for all, a number of changes are required to break the employment and superannuation nexus.

These changes are required to both give greater access to superannuation contributions and to reduce the possibility/potential for individuals to make excessive contributions and abuse the superannuation system.

In the first instance, regulations in SIS [SIS Reg 7.04 & 7.05] which combine aged-based tests with the definition of gainful employment should have those parts which rely on gainful employment tests removed.

Consequentially , the requirements surrounding authorised leave relating to the raising of children could then be removed as they would be superfluous.

These (relatively) simple changes would leave, predominantly, age as a criteria for various types of contribution.

The current age limit on acceptance of contributions (and compulsory cashing of benefits) effectively provides a mechanism for ensuring that people older than 75 (previously 70) do not use the superannuation system simply as a tax effective investment vehicle or estate planning mechanism. For this reason it would be generally acceptable to retain a single upper age limit on the making of contributions. It is suggested that this age should be the same as the maximum age at which contributions can be accepted. Hence, one age limit on the ability to contribute to superannuation could be implemented.

An alternative to the removal of the employment test, which has been suggested, would be to allow any recipient of taxable or assessable income to make a superannuation contribution. Whilst this would allow more people to make a superannuation contribution than the current rules permit, it would merely impose an alternative test on superannuation fund trustees which would require a level of checking to be conducted. Additionally, the imposition of this test could easily be circumvented simply by opening an interest bearing bank account in order to generate a minimal amount of taxable income.

This proposal therefore, simplistically, would seem to replace the current test with another, different, test and would not necessarily reduce the compliance burden currently borne by fund trustees.

5.2 *What new policies would be required?*

Allowing people to make superannuation contributions regardless of their employment status may, to protect the integrity of the superannuation system, require a number of additional measures to be introduced.

Importantly, the system may need to be structured so that overuse of voluntary superannuation contributions does not permit individuals to abuse the system. Predominantly this would occur where large or excessive contributions could be made to superannuation to take advantage of the tax advantaged regime. It should be recognised that this is currently an issue in some parts of the superannuation landscape and these avenues are no worse than for those currently able to make personal superannuation contributions.

5.2.1 Reasonable Benefit Limits

The system currently has in place, via reasonable benefit limits and the age-based contribution limits, mechanisms for dealing with this problem. It does so by limiting both the amount of superannuation benefit that can be received on retirement from the concessionally taxed superannuation environment and by limiting the amount superannuation contribution which can be claimed as a tax deduction in any given financial year.

Effectively, this system provides the Government with double protection from abuse – at the time of contribution and at the time of retirement. Additionally, the RBL system, to large degree, covers a greater area of superannuation as it covers most contributions to the fund as well as any fund earnings.

There is currently no limit on the amount of contribution an individual can make to a superannuation fund (if eligible to contribute) – the current age-based limits simply restrict the tax deductibility of the contribution. It is therefore currently possible for an individual to make large contributions to a fund (for which no tax deduction is being claimed) and for those contributions to not form part of the individual's RBL assessment. Whilst these contributions have not provided any specific tax benefit for the individual at the time of contribution, these contributions make use of the concessionally taxed superannuation environment whilst invested (any fund earnings or gains on these contributions are however subject to the individual's RBL).

Additionally, it is unclear to what extent undeducted superannuation contributions would be made in excess of these deductible limits given that there is no immediate incentive for people to exceed these limits. In fact, it could be argued that there is a disincentive to exceed these limits as the contributions made are protected and must be retained in the superannuation system under preservation rules.

From an RBL point of view, if the Government were concerned that voluntary contributions could be abused to defer or avoid tax, the system could be further protected from abuse by ensuring that voluntary contributions, specifically non-deductible contributions (undeducted contributions), are dealt with and accounted for adequately. However, the abuse risk here is no bigger than currently exists.

5.2.2 Retirement ages

Currently, superannuation benefits may be withdrawn from the superannuation environment on:

- Retirement
- Death
- Permanent or temporary disablement
- Termination of employment (restricted access)
- Severe financial hardship

The definition of retirement, as with the current contribution rules, are heavily reliant on the definition of gainful employment. Additionally, the age at which people may access their superannuation is dependent upon their date of birth.

Currently, those born prior to July 1st, 1960 are able to access their superannuation from age 55. This age increases to age 60 for those born on or after July 1st, 1964. Generally speaking, once a superannuant has reached their preservation age and ceased employment they may access their superannuation.

In order for the employment nexus on contributions to be removed some tweaking of the employment nexus on retirement will be required. As an example, if someone who has never been employed is permitted to make contributions to a superannuation fund – at what point can they be considered to have "retired"?

For this reason the "conditions of release" [SIS Reg Part 6] could be slightly amended. Currently, to access superannuation benefits (under the retirement category) a person must not be gainfully employed (although the regulations refer to the "ceasing of a gainful employment relationship") and must have reached their preservation age.

Whilst this system will work for those that may ever have been employed (by virtue of them not being gainfully employed when they reach their preservation age) the regulations could be drafted in a slightly different manner to ensure consistency with contribution standards.

Additionally, the regulations allow those not gainfully employed to leave their superannuation in the accumulation stage of a fund until age limits have been reached (currently 65 but being increased in line with the allowance of personal contribution by those up to age 70). Upon turning 65, benefits currently must be paid out to those not gainfully employed.

Effectively, this system would continue to prevent people accessing their superannuation prior to reaching their preservation age whilst allowing those without the need to access their superannuation upon reaching their preservation age to maintain their investment until age 65 (proposed to be age 70).

6 Summary

Given the (now) wide range of circumstances in which many people can make, or have made, superannuation contributions the employment test contained in superannuation legislation does not serve a tremendously useful purpose. Additionally, it imposes costs on fund trustees, and hence members of superannuation funds, which could be avoided.

The employment test system, fundamentally, imposes restrictions on such a limited number of people that it has become inefficient to the industry, government and its appointed regulators and the Australian public.

The removal of the test, allowing anyone to make voluntary personal superannuation contributions will provide greater access to both the accumulation of superannuation benefits and to the retirement income system encouraging the orderly drawdown of capital in retirement. Greater access to the accumulation phase of superannuation ensures that, through the preservation requirements, retirement savings can be used (generally) only when a person is deemed to have retired or has retired thereby ensuring the integrity of the system and facilitating the self-funding of some, if not all, of a persons retirement decreasing the reliance on Government funded pensions.

Effectively, by removing the nexus between employment and the ability to make a superannuation contribution many of the same people who cannot make a contribution still may be unable to make a contribution (due to personal financial circumstances). However, many who need to be able to accumulate more superannuation who currently cannot and have the financial resources to do so will gain access to the system.