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Treasury Discussion Paper – Review of the provision of pensions in small superannuation funds

The Strategist Group seeks to make a submission in relation to the Treasury Discussion Paper on the provision of pensions in self managed and other small superannuation funds ("SMSFs").

By way of background The Strategist Group ("TSG") is an independent company established in 1996 that provides advice, training and compliance to accountants and financial planners who deal in SMSFs. Since establishment the company has trained or advised on SMSF issues to more than 20,000 accountants and financial planners. Subscribers to the company's core SMSF publication "The Strategist" look after more than 90,000 SMSFs in one way shape or form. In addition the CEO of the company Grant Abbott has authored the "Guide to SMSFs" published by CCH and used as the text book for SMSF professionals.

1. Government Retirement Incomes Policy

The purpose of the government's retirement incomes policy as stated in the Treasury discussion paper is as follows:

> "The Government is committed to a retirement income policy that provides encouragement for individuals to provide a higher standard of living than would be possible from the Age Pension alone, but also ensures all Australians have security and dignity in retirement. This will be achieved by:
>
> - encouraging people who are able to save for their retirement to do so, particularly through superannuation;
> - ensuring the provision of an adequate public safety net in the form of an Age Pension for Australians who are unable to support themselves in their retirement years;
> - ensuring the system is predictable, but facilitates choice and is equitable; and

- ensuring the system is fiscally sustainable and delivers an increase in national saving.

The Government believes these objectives can be met by the current three pillared retirement income system comprising:

- voluntary superannuation and other private savings;

- compulsory superannuation savings through the Superannuation Guarantee contributions; and

- a means tested Age Pension and associated social security arrangements."

It is recognised that in making any submission and as well as any change to the current superannuation pension system the retirement income principles considered above should be taken into account.

2. The Current Retirement Income System

Prior to making any submission we provide a brief background on SMSFs paying defined benefit pensions.

i) Security of retirement income for retirees is important

As noted above, one of the key planks in the government's retirement income policy is to "*ensure all Australians have security and dignity in retirement.*" TSG submits that security in retirement means security of income for life and hence the guarantee of a lifetime income independent of any government safety net. From research we have conducted with more than 1,000 retiree members of a SMSF – security of income for life is one of the most important things in their life.

In that regard, defined benefit pensions currently used in SMSFs are lifetime not life expectancy pensions. These pensions have become popular since the defined benefit pension rules for SMSFs were introduced in 1999 – the basis of their popularity has been that they provide a secure income stream for the life of the member and that on death any surplus stays in the fund rather than going to a life insurance company.

In contrast allocated pensions last until the capital runs out and the market linked pension has a term equal to at best life expectancy plus five years. From a retiree's perspective it is impossible to guarantee with both of these products that they will run for the life of the member.

Although life insurance companies offer similar types of lifetime income streams, control is also another important thing for many retirees – control of investments, control of income and control of any surplus left in the fund on death. That is why they naturally turn to a lifetime income via a SMSF rather than acquire a similar product from a life insurance company.

ii) Defined Benefit Pensions have strict actuarial guidelines

The object of the Superannuation Industry Supervision Act 1993, according to section 3(1) of the Act, "is to make provision for the prudent management of regulated superannuation funds." In terms of a lifetime pension there is a vast array of conditions laid down in the Act and regulations that must be adhered to. One of these is actuarial certification that the relevant fund paying the lifetime pension has sufficient resources to pay these pensions. In terms of most superannuation funds the actuarial certification standard in regulation 9.29 is required every three years. For SMSFs a *far higher and more costly standard* is prescribed in regulation 9.29A requiring the trustee of the fund to obtain actuarial certification **every year** that "there is a high degree of probability that the fund will be able to pay the pension as required."

Failure to adhere to the reporting requirements and the numerous other conditions laid down in the Act in respect of the payment of a lifetime pension may result in the trustee being fined and at the same time the fund losing its concessional taxation status. In terms of the actuary and auditor - failure to monitor the solvency of the fund on an annual basis may result in them being fined and also subject to a recovery action for any loss by the trustee and members of the fund. Such is the purpose of an Act dealing with the prudent management.

Given the potential litigation exposures for actuaries, as a profession they are generally extremely conservative in relation to setting aside reserves in the fund – including investment, mortality and liquidity reserves to ensure the lifetime pension is that – a pension paid for life. As these reserves – which can make up 30% of the purchase price of the pension, do not form part of the income determination, any lifetime income stream sourced from pension assets (ex reserves) is lower than may be the case if no reserves were applied. Many retirees would prefer their income to be much higher however actuaries hold the upper hand in the debate due to the prudential certification standards for lifetime pensions.

For example, using the cameos in the Treasury discussion paper provided by the Australian Government Actuary – an underlying rate of return of 7% has been set yet the rate of pension payment withdrawal is set at 4%. This conservative methodology guarantees a build up of surplus assets in the fund over time thereby ensuring that the trustee of the fund is able to pay the pension for the life of the member.

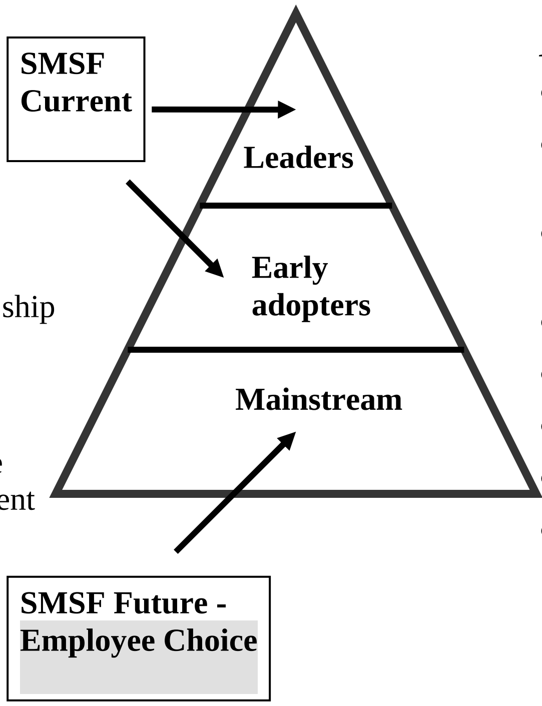
iii) SMSFs are the fund of choice for many retirees

In the Australian superannuation industry there are more than 3,000 retail, employer and industry based funds. Yet over the past five years many retirees have been switching to SMSFs to take control of their superannuation with current figures published by APRA for the September 2004 quarter showing just under 300,000 small and SMSF funds in existence. The diagram below is taken from a market research study undertaken by the ASX as to attitudes of trustees and the market in relation to their preference in choosing SMSFs:

Diagram One – SMSF Choice Characteristics

Mindset:

- control
- responsibility
- interest
- effort
- captain of own ship
- can do better
- satisfaction
- need to provide for own retirement



Marketplace:

- poor performance + fees
- scattered super – consolidation
- accountant advice – business
- choice & flexibility
- tax efficacy
- pensions in doubt
- bull markets late 90's
- media/awareness

★The spread of SMSFs into the mainstream working population is expected to continue once employee choice commences on 1 July 2005.

iv) SMSFs are the only real choice for lifetime pensions

The table of the types of superannuation funds that offer lifetime pensions can be seen below:

Table One – Lifetime pension choices

Type of Super Fund	% of total Super Fund assets	Lifetime pensions offered	Actuarial standards
Employer	10	**Yes**	three years
Industry	11	**No***	three years
Public sector	20	**Yes**	three years
Retail	34	**No***	three years
Life office	2	**Yes**	three years
SMSFs	23	**Yes**	every year

** Lifetime pensions are defined benefit pensions and are generally not offered by retail and industry based funds that are essentially accumulation style plans. As such retail clients, who are not able to access employer or public sector superannuation funds, must choose between a lifetime annuity from a life insurance company or a lifetime pension from a SMSF.*

The market perception regarding lifetime annuities is low as the retiree does not have control over the investment process and generally returns on these pensions are exceedingly low. SMSFs allow the trustee to be less conservative than their larger brothers through investing in growth assets rather than fixed interest style of investments commonplace for non-SMSF providing lifetime pensions. This means more income – subject to the strict actuarial constraints discussed above.

Moreover until recently when a person lived beyond ten years and then died any surplus funds would be left for the benefit of other policy holders and shareholders of the life insurance company. Even with changes to the death benefit commutation period for complying lifetime annuities, there is still the concern that any monies left in the account are lost forever to the insurance company. In contrast any surplus assets in a SMSF are left for other fund members. Although the preference for most members would be to pay the benefits out as a commutation payment from the pension on death (not allowed under the SIS Act), it is better that it ends up with members of a fund that you do know rather than policy holders that you don't.

v) Strict estate planning requirements

Unlike allocated and market linked pensions where the remaining accumulated benefits in a deceased member's account may be paid to the member's estate or dependants – the prudential standards in the Superannuation Industry Supervision Act 1993 limit the amount that may be paid out to the deceased member's estate for a lifetime pension.

As noted above, members would prefer the opportunity to pay out any remaining amounts in their pension account – including any residual reserves, to their estate. As of late the death benefit payout under a lifetime complying pension has been extended to life expectancy or a maximum of twenty years where life expectancy exceeds twenty years at the commencement of the pension. However in any case this may not prove sufficient such that some part of any remaining lifetime pension on a member's death to be left in the superannuation fund.

From a taxation point of view any surplus will generally find its way into a miscellaneous reserve. Should the trustee of the fund allocate an amount from this reserve to a member's account then any such allocation may be treated as an "allocated surplus amount" under SCT Regulation 2G and included in the member's surcharge determination. When the member ultimately takes this benefit as a lump sum or pension it is to be tested again under their reasonable benefit limits. Accordingly the surplus left over from an amount held in a lifetime pension of a deceased member is effectively double counted for RBLs when passed through to remaining members via a reserve. This may be contrasted to the payment of any commutation component of an allocated or market linked pension where such a double counting of RBLs does not occur.

vi) Pension design flaws

There are numerous pension options available under the SIS Act however each has its own design flaws. These flaws have been expertly highlighted in the Treasury

Discussion Paper and result from legislation made more than a decade ago and not being amended to keep up with the government's retirement incomes policy. As such it is opportune time to review all of the pension rules to simplify but at the same time ensure that they allow a member of a superannuation fund – whether retail, industry or SMSF to access a pension that is a lifetime or as close to a lifetime pension as is possible. It is not equitable that only public sector and some corporate employees have the opportunity of security of income for life and that of their spouse.

vii) Defined benefit pensions for children

An important part of any superannuation account for a member, irrespective of whether it is in a SMSF or non-SMSF, is what to do with any benefits on the death of the member. Where an individual seeks to pay a benefit on their death to their children, in many instances the desire is to pay a pension. The reason for this is that the child may end up becoming divorced, may be in business or may not be able to handle a lump sum (particularly if the child is under age 25).

Defined benefit pensions for a term with a residual capital value ("RCV") provide an effective tool to allow a deceased member to look after their child until they come of age and are in a position of being able to handle a lump sum. This may be contrasted with the allocated pension that, if not set for a term must continue on until the capital runs out. The discussions so far have been in relation to the use of defined benefit pensions for retirement income purposes and not focused on their practical use for looking after child beneficiaries in the event of the death of the member. In any pension review consideration as to the estate planning and also disability aspects of any pension choice is important.

viii) Government changes

One of the planks of the government's retirement incomes policy is to encourage people to save for their retirement. Over the last three years more than $18 billion of undeducted contributions have been made by members of a SMSF – showing that the current system of encouraging self fund retirees is working. Government must be careful in keeping the superannuation system stable and practical – too many changes to the system, particularly without industry consultation will knock the confidence out of superannuation thereby impacting the retirement incomes policy.

An example of uncertainty can be found under the current transitional laws for defined benefit pensions where we find that the trustee of a SMSF can only offer a defined benefit pension to a person who was:

i) a member of the fund at 12 May 2004;

ii) was aged 55 and retired or aged 65 when the pension commenced; and

iii) the pension was paid prior to 30 June 2005.

Unfortunately these provisions appear to not consider the position of including a reversionary pensioner – such as a spouse who does not meet the conditions laid down in i) and ii) should the pension revert to them on the death of the member. This was probably not the intention of Treasury in drafting the transitional provisions however the end result has been uncertainty in the market. It is submitted that clarification of this position be released immediately.

3. Scope of Treasury Review

The scope of the Treasury review of pensions in small and self managed superannuation funds is noted in the terms of reference of the Treasury Discussion Paper to be:

> "The Government has been advised, including by the Government Actuary, of a number of concerns with the provision of defined benefit pensions in small superannuation funds, namely:
>
> • access to unintended tax and social security benefits, particularly from the use of 'RBL compression';
>
> • their use for estate planning purposes in the superannuation system outside what was intended and not available to other superannuation fund members; and
>
> • whether a small number of members can effectively pool risk and guarantee income payments over the term of the pension.
>
> The review will examine options for small superannuation funds to provide pensions to their members, including consideration of:
>
> • design features of prospective pensions that address the Government's concerns and that could attract complying status for taxation and social security purposes;
>
> • management of investment, liquidity and mortality risks; and
>
> • likely future demand for pensions with defined benefit characteristics."

4. TSG Submissions

First off Treasury is to be commended for not only considering the issue of defined benefit pensions in small and SMSFs but also looking at pensions across the entire superannuation industry through their review of market linked and allocated pensions. In this way there is no perceived bias in the system and ensures that all potential retirees – irrespective of where they choose to house their superannuation and retirement income benefits, are treated equally.

In terms of the Treasury Discussion Paper TSG makes the following submissions.

A. CHANGES TO THE CURRENT RULES

a) RBL Compression

The mischief noted in the Treasury Discussion Paper as *RBL compression* comes about from the use of the formula in section 140ZO(1) of the Income Tax Assessment Act 1936 in relation to the determination of the RBL amount for a lifetime pension. For example consider the cameo in the Treasury paper of the SMSF member with $5M in benefits including $2.5M in undeducted contributions.

According to the figures in the cameo provided by the Australian Government Actuary – a pension of $200,000 indexed to 3% may be paid to the 65 year old member with a full reversionary to his 60 year old spouse.

Using the formula in section 140ZO(1) where:

RBL Amount = [annual value x PVF] – UPP + RCV

RBL Amount = [$200,000 x 9] - $2,500,000 + 0 = -$700,000 = 0

As can be seen from this example the formula can provide an absurd negative result, particularly where there is a large undeducted contributions component. Although using actuarial software provided by Bendzulla Actuarial Services we find a higher amount as the annual value of the pension - $223,000 – see below:

Table Two - Treasury discussion paper Cameo – Bendzulla Actuarial Software

DATA INPUT:

Name of Potential Pensioner:	Carlos	
Date of Birth (dd/mm/yyyy)	9/10/1939	
Sex (M or F)	M	
Spouse Date of Birth (dd/mm/yyyy)	1/08/1944	
Assets Available for Complying Pension	5000000	
Commencement Date of Pension (dd/mm/yyyy)	01/06/2005	
Pension $pa	223000	
Pension indexation (%pa)	3.00%	For CPI use 2.5%
Social Security Interest Rate (if applicable)	5.70%	The 10 year Bond Rate
Investment Strategy	Balanced: 40-60% Shares/Property	

RESULTS:

Best Estimate ie amount of capital expected to be used and part of the tax exemption percentage calculation.	$3,910,324.89
The Valuation of Pension Assets for Adequacy:	
Best Estimate of Liability	$3,910,324.89
Investment Reserve	$447,839.63
Mortality Reserve	$359,407.95
Liability plus Reserves	$4,717,572.47
Less Net Value of Assets	$5,000,000.00
SURPLUS/(DEFICIT)	$282,427.53

Level of surplus is adequate.

Under the above Bendzulla actuarial calculation, we still find a negative result:

RBL Amount = [$230,000 x 9] - $2,500,000 + 0 = -$493,000 = 0

RBL compression comments

There are several comments that may be made in terms of the above RBL compression cameo including:

- The cameo used is at the extreme end of the spectrum - $5M with a $2.5M undeducted contribution. There would not be many Australian retirees with the capacity to have accrued such large amounts in superannuation and also at the same time being able to contribute a large undeducted contribution. As such the cameo – although interesting for discussion purposes, may or may not be reflective of widespread abuse. To determine the extent of any such abuse regard should be had to the ATO RBL figures for members with $1.5M or more in benefits (less any undeducted contributions) who have taken lifetime pensions over the past five years. This will provide accurate figures as to the amount of potential RBL compression that may have taken place and hence whether defined benefit pensions should be outlawed from SMSFs;

- The figures used by the Australian Government Actuary are low in terms of income produced. For example the Bendzulla figures with more than 20% in reserves provide an annual pension payment 10% higher using the same figures. Other actuaries TSG has consulted provide even higher incomes which have the effect of dampening the impact of any RBL compression using the Australian Government Actuary figures. It is surprising in all of the discussions that there is no suggestion of standards being set for lifetime pensions by the Australian Institute of Actuaries;

- The use of a large undeducted contribution – the same size as the superannuation amount in the cameo has had a significant impact on the member's RBL amount. Without the undeducted contribution and with Carlos having $2.5M in benefits in the fund the RBL amount increases significantly:

    RBL amount = [$100,000 x 9] = $900,000

- The formula – as pointed out in the Treasury discussion paper, is filled with anomalies including - deducting any undeducted contributions as a lump sum rather than factoring them into reduction of the annual value - the use of out of date pension valuation factors and pension valuation factors that don't really change even when a young reversionary beneficiary or beneficiaries are introduced into the mix.

RBL compression submission

To ensure the system is predictable, but facilitates choice and is equitable, TSG submits that the formula in section 140ZO(1) be repealed for all taxpayers and that section 140ZO(2) – which provides the Commissioner of Taxation with power to determine the RBL amount of a pension, be used as the sole determinant of assessing pensions for RBL purposes.

In terms of pensions sourced from public sector and corporate superannuation funds where the purchase price cannot be referenced to an accumulation account it is submitted that a "purchase price equivalent" test be used. In that regard the Commissioner, in making his determination may:

- lay down guidelines with the Australian Government Actuary to determine a "purchase price equivalent"; or,

- require the trustee of the fund at the time of paying a defined benefit pension to obtain a purchase price equivalent for the terms and conditions of the pension.

The benefit of leaving the determination in the hands of the Commissioner of Taxation is that if there are any RBL pension valuation issues then he may move quickly to address the issue rather than require legislative measures that may come too late

b) Estate Planning

The cameos produced by the Australian Government Actuary show a significant growth in surplus over a twenty year period with a member ending up with more in their account than when they started. This is not surprising given the use of a 7% rate of investment return and a 4% pension income payout. Even with less conservative actuaries there is a chance due to the expert investment skills of their trustees and investment managers that the fund will move into surplus at times. Likewise it should be considered that in times of poor investment returns, the fund will need sufficient reserves to draw upon to ensure that the fund does not go insolvent under the weight of its pension liabilities.

The concerns of Treasury in relation to the build up of reserves are also a concern for members of SMSFs who are not allowed to access these reserves due to the design flaws inherent in defined benefit pensions – the reserves are forced to build up and cannot be paid out as extra pension payments of by way of commutation.

It is submitted that any surplus that is built up in the fund be able to be commuted by the pension member during the life of the pension and also that it must be commuted upon the death of the member. The taxation of the surplus would follow section 140R(1A) of the Income Tax Assessment Act 1936 which has reference to the pension's rebatable amount such that if the pension has a nil rebatable proportion then any commutation amount is excessive. Any such surplus payout – which could be known as a "surplus commutation amount" would not be classified as a death benefit under section 27AAA.

This ensures the following:

- the payout and taxation of all benefits in the fund that have received concessional taxation treatment;

- certainty of what is to happen to surplus for the pension member and trustee;

- taxation of any surplus commutation amount in the member at the underlying RBL rates as determined by the Commissioner with no ability to access a tax free death benefit for the member's dependants.

If Treasury are concerned as to the deferment to death of any "surplus commutation amount", rules may be enacted that require the commutation of any "surplus commutation amount" at the time that the reserves exceed a surplus threshold based upon a percentage of assets required to fund the pension. The amount of the commutation would equal the amount of the excess.

A word of concern: The use of the special income provisions is not appropriate in any discussion of defined benefit pensions irrespective of the type of fund. They are there to prevent non-super income being diverted to a concessionally taxed environment. In the case of pensions any income generated on assets held for pension purposes is not taxed in the trustee's hands but at the level of the member. If the pension does not have a rebatable proportion then any commutation payment will be excessive – irrespective of when it is received. The RBL rules will ensure that and should remain consistent across all pensions.

c) Managing Risk

A key plank of the review is the management of the investment, mortality and liquidity risks. There are some broad suggestions outlined in the Treasury Discussion Paper of prescribing investment rules as well as enhancing actuarial guidelines.

Currently there are a number of methodologies adopted by actuaries across Australia that use different calculations to manage the above risks. As such there is no consistency or certainty in the market – which has led some trustees to go actuary shopping to find the best deal given their desired circumstances. This variability leads to taxation and social security consequences as highlighted in the discussion paper.

It is submitted that the Australian Government Actuary along with the Institute of Actuaries produce guidelines for actuaries in terms of managing investment, liquidity and mortality risks for defined benefit pensions in small and self managed superannuation funds. These guidelines – if tightly prescribed will ensure consistency of approach to managing the relevant risks.

Key questions on the strategy to develop new rules for defined benefit pensions

• *Defined benefit pensions in non-arm's length funds can be structured to provide a residual capital value. What role do residual capital pensions and annuities have in providing retirement income?*

Residual capital value pensions – for example a lifetime with 100% RCV are not a popular option for retirees in SMSFs for three reasons:

- the formula in section 140ZO(1) requires the net present value of the RCV to be added back to determine the RBL amount of the pension;

- from a taxation perspective where a pension has an RCV and has been funded with undeducted contributions, they are deemed to be built into the RCV thereby losing any tax breaks from the use of undeducted contributions;

- a review of actuarial calculations shows that building an RCV into the pension does not have a substantial impact on the underlying pension amount unless the member is close to their life expectancy.

Accordingly, were defined benefit pensions to remain, it is submitted that provisions may be adopted to limit the trustee from providing such a pension with an RCV where the pension is paid to a person over age 65. As noted above, the use of a defined benefit pensions with an RCV is an effective tool where the deceased member of the fund seeks to provide an income stream for a child who may not be responsible with money, not of age or subject to a possible divorce.

• *What would be the likely demand for defined benefit pensions in small funds if the above measures to develop new rules were implemented?*

The demand for lifetime pensions is a demand for security of income and peace of mind in retirement. The changes suggested above will correct the design flaws of defined benefit pensions and at the same time protect government revenue. It is submitted that lifetime pensions in a SMSF will continue to be popular provided the government provides certainty as to the treatment of the pensions for tax, RBL, actuarial and social security purposes.

B. MODIFY EXISTING PENSION PRODUCTS

There is a great opportunity for the complexity of the current pension system to be addressed by modifying the design flaws in the allocated and market linked pension products.

i) Market Linked Pension

The market linked pension is designed to run for a member's life expectancy plus five years at maximum duration. Where a reversionary spouse is used then their life expectancy plus five years may be used. Either way there remains a strong possibility that the pension will run out should the member of the fund and their spouse well outlive their life expectancies.

As has been expressed in this submission on a number of occasions, for many retirees it is important that they have a secure income stream for life. This allows them dignity and peace of mind knowing that they do not have to fall back onto the government's safety net except in the worst possible scenarios.

It is submitted that the market linked pension may be used to approximate a lifetime pension by allowing the member to the option to choose a term at the time of establishment of the pension for a period from life expectancy to a maximum of 95 years or if a reversion to the spouse was part of the pension then to their life expectancy or when they reach 95 years of age.

The benefits of making such a change are as follows:

- although not a guaranteed lifetime product, it is as close as can be achieved with an account based product and still remain easy to understand;
- from a legislative perspective, the changes needed to Superannuation Industry Supervision Regulation 1.06(8) dealing with market linked pensions are simple and easy to enact;
- mortality, investment and liquidity risks are removed as the product is account based;
- RBLs are to be determined by the Commissioner of Taxation according to section 140ZO(2);
- the changes can be made across the board for all superannuation funds thereby enhancing the market linked product;

- ➢ there is no need to be concerned about providing deferred annuities to kick in at the time the market linked pension ceases.

Apart from the duration, all other rules for the market linked pension would continue as required under the current laws.

ii) Allocated Pension

The allocated pension is a pension that is well known and easy to understand. As is stated in the Treasury Discussion Paper:

> "The minimum payment factors for this pension are designed so the pension payment in any one year is similar to that from a reversionary, CPI-linked lifetime pension purchased with the account balance at the start of the year. The maximum pension factors are based on a reasonable income stream being paid to age 80. These factors have not been updated since the product commenced in 1992.
>
> Updating of the minimum payment factors to reflect current economic and mortality assumptions would allow lower annual payments in initial years. This would lead to higher levels of income being paid in later years than at present because of larger account balances in these years."

Any review of the allocated pension is welcome and it is submitted should ensure that the minimum payment factors are set to replicate a reversionary, CPI linked lifetime pension to age 95 in tandem with the market linked pension allowing the member flexibility for both types of income streams to provide a look alike lifetime pension.

iii) Allocated Complying Pension

At this time the market linked pension is the only account based complying pension. As an alternative the introduction of a complying allocated pension should be considered if a full review of all pension products is being undertaken. The complying allocated pension would be the same as the allocated pension – with relevant minimum and maximums, must last until age 95 or until the capital runs out but is non-commutable.

The benefits of a complying allocated pension are:

- ☑ allocated pensions are easily understood by the market and a complying version would be well received and simplify superannuation and SMSF pensions;

- ☑ the member can maximise the duration of their combined income streams by managing the income draw down – something not able to be down with a market linked pension;

- ☑ it would provide the member with flexibility in terms of where the income stream is to be drawn down from and how much subject to the minimum and maximum rules;

☑ on death the remainder left in the account would pass to the deceased member's dependant beneficiaries or their estate as is the case with the allocated pension;

☑ would allow the government to simplify the system into a complying and a non-complying allocated pension and at the same time get rid of the market linked pension rather than trying to fix it up.

Key questions on the strategy to modify existing products

• *Would there be a demand for the above modified products?*

As noted above, any change to existing pensions to allow them to meet the needs by retirees for security of income for life will create a demand as this feature is important to most retirees. At this stage the market linked pension provides no security and an amendment to age 95 – at the option of the member would provide welcome relief and demand. Alternatively a complying allocated pension – as detailed above would stimulate demand.

• *Would the industry be willing to offer such products? For example, is it feasible to develop longevity insurance products that could be provided to small superannuation funds?*

SMSFs would undoubtedly offer modified allocated and market linked pension products as would non-SMSFs. In terms of longevity insurance to cover the fundamental flaw in the market linked pension, this issue falls away if a term to age 95 is used. There are serious doubts whether any insurance company would offer such insurance and more importantly whether the trustee of a SMSF would take up any such product.

C. INTRODUCE NEW PENSION PRODUCTS

Two new pension products have been raised – both of which are accounts based and designed to last as close to lifetime as is possible. At this stage with the recent introduction of the market linked account it will create confusion in the marketplace to introduce more pensions when it would be that much easier to address the fundamental problems inherent in the market linked pension as noted above.

Key questions on the strategy to introduce new products

• *Should new products be introduced or should modifications be made to existing account based products?*

There is no need to introduce new pension products in the market if the existing pension products can be modified to take into account the desire by retirees for a secure income stream that lasts for life or as far into the future as can be imagined – say age 95.

• *Would the industry be willing to offer such products? For example, would annuity providers be willing to offer lifetime annuities at an advanced age, and if so, from what age?*

This issue does not need to be addressed.

* * * * *

TSG thanks Treasury for the opportunity to make the above submissions and awaits the outcome of the review of pensions in small and self managed superannuation funds. Should you have any queries regarding the above please do not hesitate to contact me on 02 9938 8588.

Yours sincerely

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