1. OUTLINE OF AUSTRALIA'S RETIREMENT INCOME SYSTEM

Outline of this chapter

This chapter provides background to the retirement income system and introduces key concepts relied on in this report. The chapter is organised in four parts:

First, it examines how the concept of retirement has changed over time, explores historical trends in when people retire, and defines what is meant by 'retirement' for the purposes of this report.

Second, it outlines the design of Australia's retirement income system and how different parts of the system interact. It includes background on the history of the system and current system settings, as well as an overview of the sources of income for recent retirees and a brief international comparison.

Third, it suggests an objective for Australia's retirement income system and considers the roles of system participants and pillars.

Finally, it identifies the broad demographic and economic factors that could affect the retirement income system.

Section 1A. What is retirement?

Box 1A-1 Section summary

- **People have diverse timings for and pathways to retirement.** Many work part time as they transition to retirement. Not all choose when they retire (involuntary retirement). Some retire multiple times.
- **For most workers there is not a mandatory 'retirement age'.** Retirement can be triggered by the main ages in the retirement income system, which are when people can access their superannuation (the preservation age) and when they are eligible to apply for the Age Pension.
- **The average age of retirement for both men and women has increased over the past two decades.** On average, people currently retire around ages 62-65, with women tending to retire one to three years earlier than men.
- **The average age of retirement is expected to rise.** Legislated increases to the preservation and Age Pension eligibility ages, as well as improved health and higher average levels of educational attainment, are expected to continue to support higher average retirement ages. However, the economic and financial consequences of the COVID-19 Pandemic may have mixed effects on when people retire, particularly in the short term. Falls in the value of retirement savings may influence some people to work longer, while higher unemployment rates may result in some people retiring earlier than they had planned.
- **For the purposes of defining 'early retirement' and 'late retirement', the review uses the Age Pension eligibility age as the 'standard' retirement age.** This reference point was selected as more people withdraw from the labour force at this age than any other age.

Box 1A-2 Stakeholder views on the concept of retirement

Many submissions referred to the Age Pension eligibility age as the retirement age. No submissions defined any other age as the retirement age. However, a few submissions recognised the changing nature of retirement and that expectations of retirement age can vary between certain occupations and industries. One submission noted:

> *'Retirement is now a continuum between reduced participation in the paid workforce … and leaving it altogether.' (Australian Council of Social Service, 2020, p. 12)*

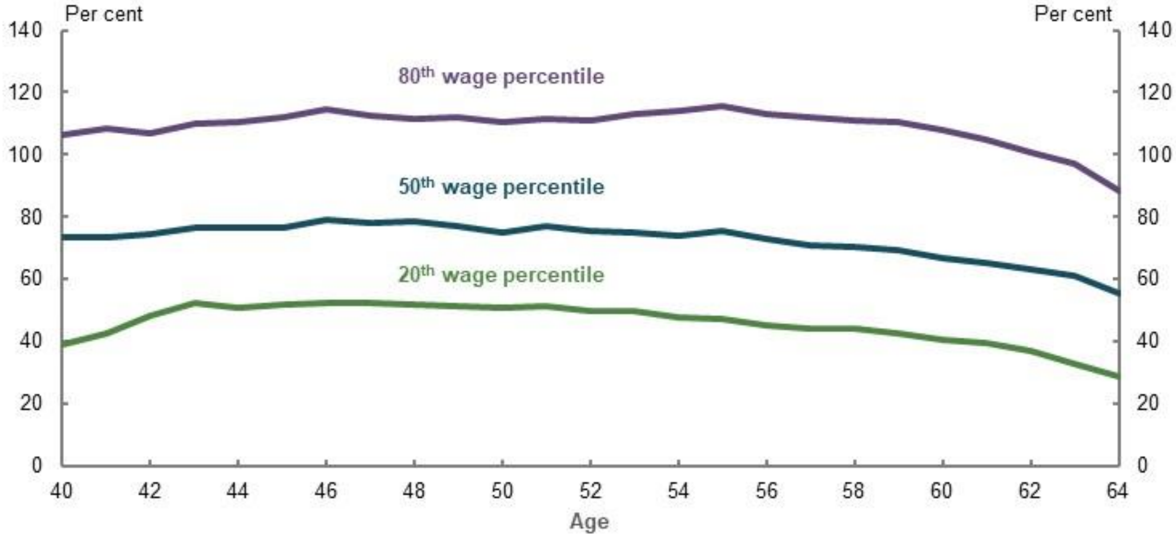
One submission suggested participation in work is an important part of the retirement income system:

> *'… if the primary objective or purpose of the retirement income system is to "generate income to support consumption in retirement", then considerations of the role of work (both pre and post retirement age) should be included as part of the retirement income system.' (National Seniors Australia, 2020, p. 13)*

Diverse pathways to retirement

The concept of retirement has changed over time. In the past, retirement was viewed as an abrupt change from a full-time job to permanently leaving the workforce. Today, switching to part-time employment as people transition to retirement is becoming more common. In 2018-19, 39 per cent of retired Australians stated their last job before retirement was part time (ABS, 2020n). Supporting this, longitudinal analysis shows that, on average, wage income declines after age 55 (Chart 1A-1), partly due to part-time employment.

Chart 1A-1 Weekly wage as a per cent of average weekly ordinary time earnings, by age



Note: Follows the same cohort from ages 40-64. This cohort was aged 64 in 2017. Uses the June value of average weekly ordinary time earnings in the relevant year (e.g. average weekly ordinary time earnings at age 50 is average weekly ordinary time earnings at June 2003). Uses median wage of the wage percentile. Wage percentiles are calculated using the sum of wages over 2008 to 2017. Source: ATO analysis of ATO Longitudinal Information Files (ALife).

Retirement is not always a single event. A significant number of people who retire re-enter the labour force and potentially retire several times. In 2018-19, 169,000 people aged 45 and over who had previously retired were, at the time of the survey, either in the labour force or were planning to look for, or take up, work in the future. The most common reasons people re-entered or planned to re-enter the labour force after retiring were financial need and boredom/needed something to do (ABS, 2020n).

Few workers have a mandatory retirement age.[2] The main ages in the retirement income system are when people can access their superannuation (preservation age) and when they are eligible to apply for the Age Pension.

Changing careers can be used by people to prolong their working life, pursue an interest or change their work conditions. This practice has always been common in some professions (e.g. professional sports, military personnel), but it is now becoming increasingly common for many older workers (both professional and non-professional) (Shultz & Wang, 2011, p. 2).

Some people also never leave the paid workforce. Around 2 per cent of people aged 70 and over never intend to retire from the paid workforce (ABS, 2020n).

The reasons for entering retirement vary considerably. Common reasons include reaching preservation age or Age Pension eligibility age, the desire to have more leisure time, their own or someone else's ill health, and difficulties finding appropriate work. The prevalence of, and reasons for, involuntary and voluntary retirement are explored in *3E. Age of retirement*.

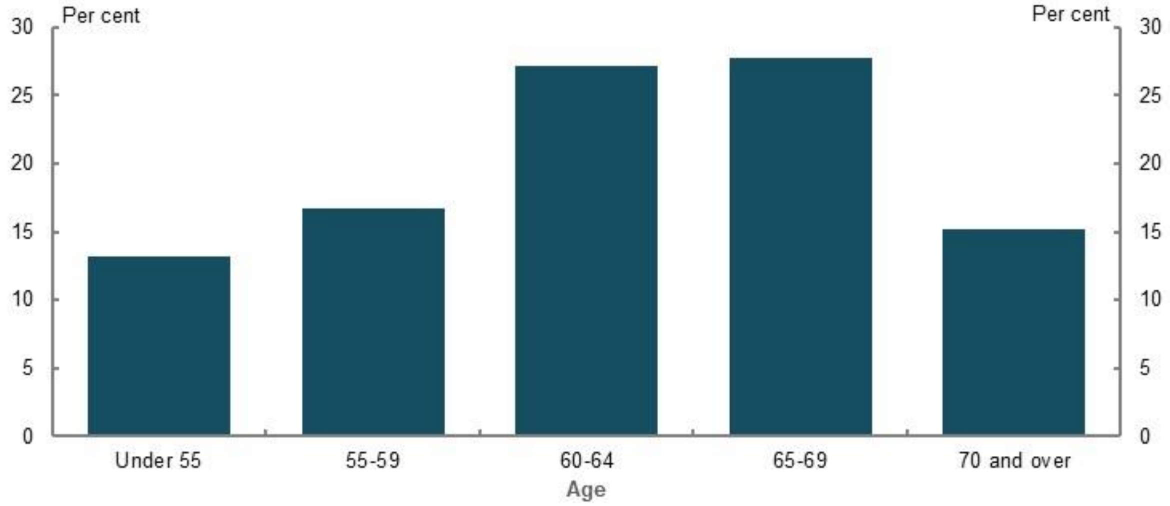
Trends in the average age of retirement

Although the retirement income system does not mandate retirement at a particular age, retirement broadly takes place between the ages of 50 and 80 (ABS, 2016a). Of those who retired between

[2] There is an exception for a small number of people for whom retirement is mandated at a particular age. For example, Australian Defence Force personnel must retire at age 65 and judges and magistrates must retire at age 70 (Equal Opportunity Commission, 2020).

July 2013 and June 2019, 13 per cent were younger than age 55 and another 15 per cent were aged 70 and over (Chart 1A-2).

Chart 1A-2 Proportion of people retiring at particular ages



Note: Includes people who retired between July 2013 and June 2019. Assumes the age of retirement is equal to the age of ceasing last job. Source: Analysis of (ABS, 2020p).

While the average age of retirement varies across surveys, it tends to be around ages 62-65, near the Age Pension eligibility age.[3] Women tend to retire one to three years earlier than men, on average.[4] The variability in data is because the definition of retirement is not always consistent across surveys and some people come out of retirement and return to work.

The average age of retirement in Australia has been relatively similar to the OECD average over the past decade (Chart 1A-3).

The average age of retirement changes in response to a wide range of economic conditions and policy influences. For example, Australia saw a trend towards earlier retirement in the 1970s and 1980s, partly due to more people having the financial means to retire earlier and increased retrenchment of older workers in some industries (Productivity Commission, 2015b, p. 56).

More recently, the average retirement age has gradually increased for both men and women (Chart 1A-3). The participation rate of people aged 60-64 rose by 22 percentage points between April 2000 and April 2020. The participation rate for people aged 65 and over also increased by more than 7 percentage points during this period (ABS, 2020j).

Over the past two decades, multiple labour market supply and demand side factors have led people to remain in the workforce longer on average. On the supply side, increased longevity, improved health and growth in average levels of educational attainment[5] are facilitating people to work longer to ensure they have adequate savings for retirement (see *1D. The changing Australian landscape*). On the demand side, people are encouraged to remain in the workforce by growth in more flexible and less physically demanding jobs (Debelle, 2019), and employers becoming more willing to employ

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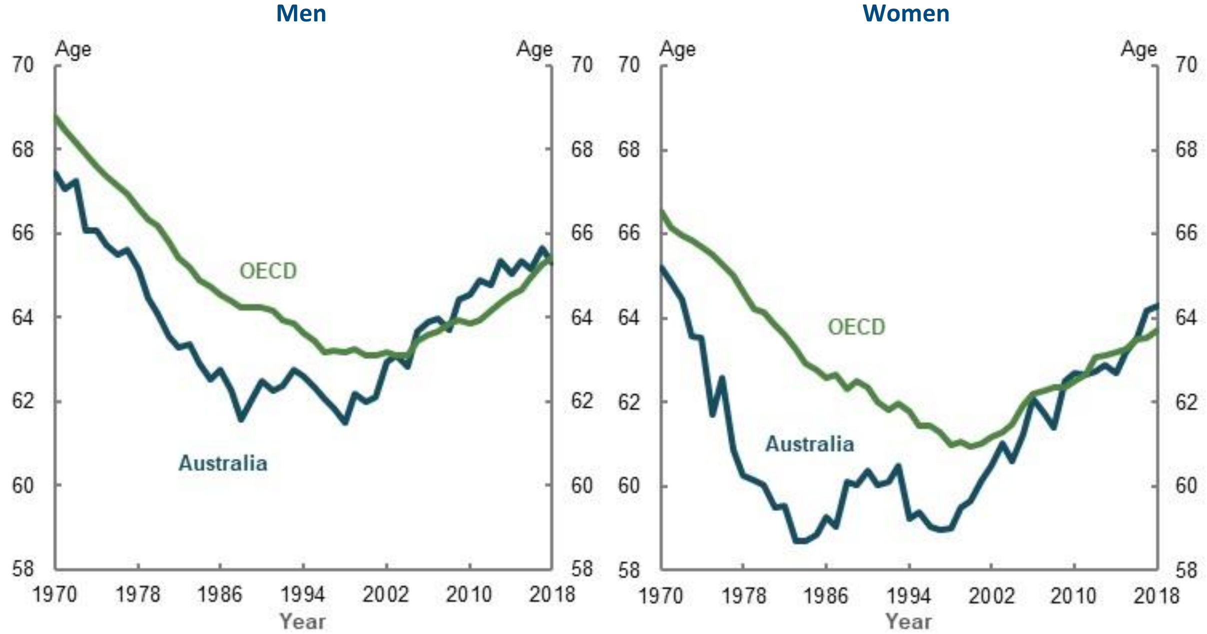
[3] Calculations using (OECD, 2019a), HILDA Survey data (Waves 16-17) and data provided by the ABS for the review. For females, the Age Pension eligibility age increased from 60 years in 1995 to 65 years in 2013. For males, the Age Pension eligibility age has been 65 years since the inception of the Age Pension in 1909 (ABS, 1998). For all persons, the Age Pension eligibility age increased to 65 years and six months on 1 July 2017 and to 66 years on 1 July 2019.

[4] Calculations using (OECD, 2019a) and data provided by the ABS for the review.

[5] Higher levels of educational attainment are associated with a later average age of retirement (see *3E. Age of retirement*).

older workers. Certain policy changes, such as increasing preservation and Age Pension eligibility ages have also encouraged later retirement (see *5A. Cohesion*).

Chart 1A-3 Average age of retirement, by gender



Note: 'OECD' includes the average of all members of the OECD in the year. For example, in 2018 there were 36 members of the OECD. The average age of retirement is the average age of all persons withdrawing from the labour force in a given period.
Source: (OECD, 2019a).

The economic and financial consequences of the COVID-19 Pandemic are likely to have mixed effects on when people retire, at least in the short term. The impact on retirement savings and income may lead some workers to remain in the workforce for longer than they had originally planned. This occurred after the GFC, with a 2008 survey showing many Australians aged 50-64 planned to postpone retirement (Kendig, et al., 2013). A higher unemployment rate may also increase involuntary retirement as people who lose their job and cannot find another one in a more competitive environment retire earlier than planned. HILDA Survey data from 2001-18 shows people aged 55 and over are three times more likely than those in their 20s to become discouraged and leave the labour force following one year of unemployment (Chomik, R, 2020, p. 4).

Although forecasting is difficult, over the medium term the average age of retirement is expected to continue to increase, for three reasons:

1. **The average person is expected to be healthier for longer.** People born in 2015 could expect to live disability-free for more years than people born in 2003 (Australian Institute of Health and Welfare, 2017). Older people who report themselves as in good health are around twice as likely to participate in the labour force as those in poor health (RBA, 2018).
2. **Education levels are rising.** Between 2006 and 2016, the proportion of Australians holding a post-school qualification increased by 10 percentage points, particularly for women (ABS, 2017a). This trend is likely to continue as the Commonwealth and state and territory governments have set targets to increase the average level of educational attainment (Department of Skills, Education and Employment, 2019). People with higher education levels remain in the labour force until later ages, on average (see *3E. Age of retirement*).
3. **Preservation and Age Pension eligibility ages are increasing to 60 and 67 years, respectively.** Evidence suggests that retirement decisions are influenced by changes to the Age Pension eligibility age (see *5A. Cohesion*).

Retirement timing expectations

On average, current working-age Australians expect to retire at later ages than current retirees. The average age of intended retirement increased from 62.3 to 65.5 years based on surveys conducted in 2004-05 and 2018-19 of people aged 45 and over (ABS, 2020n; ABS, 2006b).[6]

However, people's actual retirement age and pathway to retirement can often differ from their expectations. Many people who intend to gradually transition to retirement do not do so (Warren, 2015). One survey indicated 50 per cent of people retired from full-time employment at an earlier age than planned, primarily due to ill health, job-related issues and caring responsibilities. In contrast, 12 per cent of people retired from full-time employment at a later age than they had planned, most commonly driven by the need to boost financial security in retirement or the desire to keep working.[7]

Definition of 'early retirement' and 'late retirement'

In the absence of a mandated retirement age, the Age Pension eligibility age has been used as the reference point for the retirement age since more people withdraw from the labour force at this age than any other age (see *5A. Cohesion*).[8] As such, in this report, 'early retirement' means retiring before Age Pension eligibility age, and 'late retirement' means retiring after Age Pension eligibility age.

For discussion of the outcomes of retiring at different ages, see *3E. Age of retirement*.

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[6] This may understate the expected age, as it does not include people who indicated they do not intend to retire from the workforce in the future.
[7] Investment Trends October 2019 Retirement Income Report.
[8] Calculations using (ABS, 2016a).

Section 1B. Design of Australia's retirement income system

Box 1B-1 Section summary

- **Australia's retirement income system is unique and complex.** Its main components are a publicly funded Age Pension, a privately managed superannuation system and voluntary savings.
- **The Age Pension is means tested and provides a minimum standard of living in retirement for Australians with limited financial means. The Age Pension also supplements the retirement income of middle-income earners.** Age pensioners can currently receive up to $24,552 a year for singles, and $37,014 a year for couples combined, subject to a means test.
- **The superannuation system includes both a compulsory element and voluntary contributions.** The Superannuation Guarantee (SG) currently requires employers to pay 9.5 per cent of certain wages and salaries into a superannuation fund. The SG rate is legislated to increase by increments until reaching 12 per cent in 2024-25. Voluntary superannuation provides the flexibility for people not covered by the SG to contribute, for people to make catch-up contributions after periods out of the workforce, and for people to make additional contributions.
- **Many Australians provide for their retirement through voluntary savings separate to superannuation.** Most household wealth for people aged 65 and over is held outside the superannuation system, with owner-occupied housing the largest asset for most retirees. Home ownership supports retirement income by reducing housing expenses and acts as a store of wealth that can be accessed in retirement.
- **Free or subsidised health and aged care services support Australian retirees.** Retirees also receive a range of other concessions.
- **Australia's three-pillar retirement income system compares favourably in international comparisons.** Australia's Age Pension, compulsory superannuation and private savings, including voluntary superannuation and a high level of home ownership, gives Australians flexibility to achieve retirement incomes that suit their circumstances. Many overseas systems do not perform to a similar standard.

Outline of this section

This section outlines the main elements of Australia's retirement income system and the interactions between these elements. It also provides an overview of the sources of income for recent retirees and an international comparison of the Australian system.

Box 1B-2 Stakeholder views on the design of the retirement income system

Submissions generally supported the current design of the retirement income system, with most focusing on changes to settings within the existing framework.

Most submissions discussed the system in terms of three pillars: the Age Pension, compulsory superannuation and voluntary savings. A number of submissions referred to additional pillars, such as the JobSeeker Payment (formerly Newstart Allowance) for involuntary retirees, and health and aged care services available to retirees. Some suggested housing should be treated as a separate pillar.

Submissions noted that the system's multi-tiered structure was directed at alleviating poverty in retirement and allowing retirees to supplement the Age Pension with other savings.

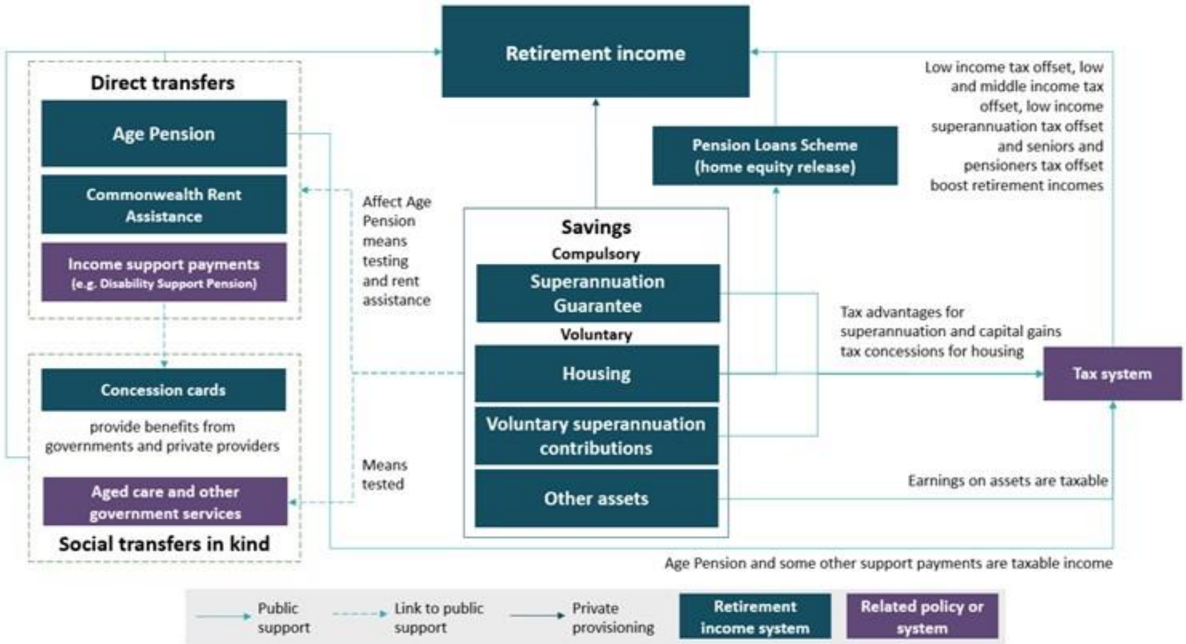
System interactions

The main components of Australia's retirement income system are the Age Pension, compulsory superannuation and voluntary savings. These income sources are complemented by other systems that support retirees' living standards (Figure 1B-1).

The interaction between the tax system and the retirement income system is important in determining retirement income outcomes.

Social transfers in kind, which include free or subsidised health and aged care services, are also key to retirement outcomes. They are an important source of support for lower-income retirees but are received across the income distribution, including by higher-income retirees. See Chart 1B-5 for details of the value of social transfers in kind to people of different age groups.

Figure 1B-1 Key retirement income system interactions



Overview of the Age Pension

The Age Pension is a means-tested payment for older Australians. The Age Pension is not based on past income or contributions, or taxes paid during a person's working life. When introduced in 1909, the purpose of the Age Pension was to provide a 'safety net' of income support, targeted to those most in need, determined by a means test (Groom, 1908; Parliamentary Library, 2011). Its primary function was poverty alleviation.

The Age Pension is the main source of retirement income for people who were lower- to middle-income earners during their working lives. Particularly for middle-income earners, it supplements superannuation and other savings (see Chart 1B-4).

Eligibility

To receive the Age Pension, a person must meet age, residency and means-testing requirements (Table 1B-1).[9]

Table 1B-1 Age Pension eligibility criteria

Criteria type	Eligibility rule
Age	Age pensioners must be over Age Pension eligibility age. From 1 July 2019, the Age Pension eligibility age is 66 years.
Residency	Age pensioners must be Australian permanent residents for 10 years, with at least 5 years being continuous.[10]
Means test	Age pensioners must meet both the income test and the assets test.

Source: (Department of Social Services, 2020e).

Age Pension eligibility age

In 1909, the Commonwealth Government introduced a national 'old age' pension age from age 65 for both men and women, before later reducing it to age 60 for women. The eligibility age for women remained at 60 until 1 July 1995, when it started increasing by 6 months every two years, until reaching 65 on 1 July 2013.

Based on legislation passed in 2009, the Age Pension eligibility age for men and women was increased to 65 and 6 months on 1 July 2017. It is scheduled to increase by six months every two years until it reaches 67 years on 1 July 2023.

Age Pension payment rates

The maximum rate of the Age Pension includes the base pension rate, the Pension Supplement and the Energy Supplement (Table 1B-2). Almost all age pensioners receive the Pension Supplement and the Energy Supplement.

Table 1B-2 Maximum Age Pension rates, as at 1 May 2020

Status	Maximum rate of Age Pension
Single, and illness-separated couples	$944.30 per fortnight ($24,551.80 a year)
Member of a couple (each)	$711.80 per fortnight ($18,506.80 a year)

Note: These rates apply for age pensioners, Carer Payment recipients and adult Disability Support Pensioners. Rates are for non-transitional Australian residents and include the Pension Supplement and Energy Supplement. Maximum rates do not include Commonwealth Rent Assistance. Source: (Services Australia, 2019).

[9] Those who do not qualify for the Age Pension but are over Age Pension eligibility age may qualify for other income support, such as the Disability Support Pension, Carer Payment or Special Benefit.

[10] Pending the passage of legislation, to qualify for the Age Pension or Disability Support Pension a person will be required to have 10 years continuous Australian residence, with either five years of this residence being during their working life (16 years of age to Age Pension eligibility age), or not have been in receipt of an activity-tested income support payment for a cumulative period of greater than five years. In circumstances where the person does not meet the requirements set out above, they will be required to have 15 years' continuous Australian residence before being eligible to receive the Age Pension or Disability Support Pension. Some age pensioners meet the residency requirements under the terms of international social security agreements.

Indexation

Age Pension rates (and other adult pensions) are indexed every March and September.

Base pension rates are indexed according to the higher of the six-month growth in the consumer price index (CPI) or the pensioner and beneficiary living cost index. After price indexation, base pension rates are then compared to male total average weekly earnings and are increased if below a set benchmark.

From September 1997, the single base rate of the Age Pension was benchmarked to 25 per cent of male total average weekly earnings (Harmer, 2009, p. 65). From 20 March 2010, the male total average weekly earnings benchmark was revised, effectively benchmarking the single base rate of the Age Pension to 27.7 per cent of male total average weekly earnings (Parliament of Australia, 2009, p. 10).[11]

The Pension Supplement is indexed to CPI growth every March and September. The Energy Supplement is not indexed.

Other components of the Age Pension

Age pensioners can also receive other supplementary payments, such as:

- Commonwealth Rent Assistance
- Carer Allowance and Carer Supplement
- Mobility Allowance
- Pensioner Education Supplement
- Family Tax Benefit (FTB), if they have dependent children in their care

Housing tenure and Commonwealth Rent Assistance

The majority of Age Pension recipients are home owners. In June 2019, 73 per of age pensioners owned their own home, while 14 per cent received Commonwealth Rent Assistance for private rental costs.[12] Five per cent lived in residential aged care and 4 per cent in public housing.[13]

Once a recipient's rent is above a threshold, Commonwealth Rent Assistance pays 75 per cent of their rent up to a cap. For a single person without dependent children, the threshold is currently $124.60 per fortnight. The maximum Commonwealth Rent Assistance payment is capped at $139.60 per fortnight for rents of $310.73 or more per fortnight. Different rates and thresholds apply to couples, those sharing accommodation or those with dependent children. The maximum payment amounts and rent thresholds are indexed by CPI in March and September each year.

Over time, an increasing proportion of age pensioners have received the maximum rate of Commonwealth Rent Assistance. Single age pensioners receiving Commonwealth Rent Assistance in 2019 received, on average, 85 per cent of the maximum rate; couples received 90 per cent of the maximum. This compares with 70 per cent for singles and 79 per cent for couples in 2001.[14]

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[11] The combined couple base rate of Age Pension is benchmarked to 41.76 per cent of male total average weekly earnings. The single base rate of Age Pension is 66.33 per cent of the couple combined rate.

[12] Age pensioners must pay enough rent to reach the minimum rent threshold to receive Commonwealth Rent Assistance. As a result, there may be more age pensioners who live in private rentals that are not counted by this proportion, if they do not pay enough rent to receive Commonwealth Rent Assistance.

[13] Department of Social Services payment data, June 2019.

[14] Department of Social Services payment data, 28 June 2019. Calculation uses the maximum rate for those without dependent children.

In June 2019, around 133,800 single women, 86,800 single men and 79,500 couples received Commonwealth Rent Assistance on top of their Age Pension.[15]

Means testing

Means testing is used to target payments to those in need. All income support payments, apart from pensions paid to people who are blind, are subject to means testing.

The Age Pension has two means tests: an income test and an assets test. A person's entitlement to the Age Pension is assessed under both tests, with the lower result determining how much they receive.

The income and assets tests assess means in different ways:

- The **income test** assesses the income a person has from employment, overseas pensions and other sources, including 'deemed' returns on financial assets, such as superannuation and bank accounts.
- The **assets test** assesses financial and non-financial wealth. The assets test recognises that people with significant assets have the capacity to draw down on those assets to support themselves in retirement.

The income and assets tests have two elements:

1. **A free area**, which allows people to have certain levels of income or assets without affecting their Age Pension rate.
2. **A taper rate**, which progressively reduces the Age Pension for people with higher levels of assessable means. Box 1B-3 details the operation of the means tests.

Employment earnings

Few retirees on the Age Pension earn income from employment. The proportion of retirees with employment income has remained steady at around 4 per cent since 2012.[16] This contrasts with the proportion of the wider population of older Australians with earnings, which has been steadily increasing over the same period (see *1D. The changing Australian landscape*).

Box 1B-3 Age Pension income and assets testing

Income test

The Age Pension income test provides different free areas based on whether an age pensioner is single or partnered. For each dollar of income over the income test free area in a given fortnight, the single rate of Age Pension is reduced by 50 cents (the taper rate). For couples, their combined rate of Age Pension is reduced by 50 cents.

Table 1B-3 Income test free areas and cut-offs, as at 1 May 2020

Status	Free area ($, per fortnight)	Cut-off ($, per fortnight)
Single	174	2,062.60
Couple, combined	308	3,155.20

Note: 'Cut-off' refers to the point at which the Age Pension is no longer payable. Cut-offs may be higher if the age pensioner receives Commonwealth Rent Assistance. The deeming rules and the Work Bonus (see below) mean that some pensioners have private income above the cut-off. Source: (Services Australia, 2019).

[15] Department of Social Services payment data, 28 June 2019. Couples includes all couples with at least one person on the Age Pension.
[16] Department of Social Services payment data, June 2019.

Age pensioners may also access the Work Bonus. Under the Work Bonus, the first $300 of work income per fortnight is not counted in the Age Pension income test. Any unused amounts of the $300 fortnightly exemption can be built up to a total of $7,800, which can be used to exempt future earnings from the Age Pension income test.

Deeming

Deeming is a set of rules used to assess income from financial investments for social security purposes. Deeming assumes financial investments earn a certain rate of income, regardless of the amount actually earned.[17] The Government periodically adjusts deeming rates to reflect the returns available from financial investments.

Before the deeming rules, many income support recipients maximised their income support payment, instead of their total disposable income, by investing in low interest accounts (Harmer, 2009, p. 137). Deeming was introduced in 1991 to encourage income support recipients to choose investments based on their merit. The aim was to encourage people to seek better returns to maximise their overall income before turning to the community for support. Deeming also increases the predictability in income support payments by reducing payments fluctuations.

Assets test

The Age Pension assets test provides different free areas based on whether an age pensioner is single or partnered and their home ownership status. The value of a person's assets above the assets test free area reduces their Age Pension by $3 per fortnight for each additional $1,000 in assets.

Table 1B-4 Assets test free areas and cut-offs, as at 1 May 2020

Status	Free area ($)	Cut-off ($)
Single home owner	263,250	578,250
Single non-home owner	473,750	869,500
Couple home owners, combined	394,500	788,750
Couple non-home owners, combined	605,000	1,080,000

Note: 'Cut-off' refers to the point at which the Age Pension is no longer payable. Cut-offs may be higher if the age pensioner receives Commonwealth Rent Assistance. Source: (Services Australia, 2019).

Most people with assets above these thresholds are assets tested as a result of deeming, unless they have significant income from other sources.

The principal home and some adjacent land have been exempt from the assets test since it was introduced in 1985.

Indexation

The income and assets test free areas are indexed to the CPI every 1 July.

[17] Financial assets include: cash, bank accounts, term deposits, shares, managed investments, loans, superannuation accounts and some income stream products. Most non-financial assets are not subject to deeming. For example, investment properties are not deemed; the actual income is used instead. To calculate the income assessed under deeming, deeming rates are applied to the total market value of an income support recipient's financial assets. Deeming has upper and lower rates. Effective from 1 May 2020, the first $51,800 of a person's financial assets (for an age pensioner couple combined, the first $86,200; and for each member of a couple receiving an allowance payment, the first $43,100) is assumed to earn a return of 0.25 per cent. For amounts above these thresholds, the assumed rate of return is 2.25 per cent. The thresholds are indexed in line with the CPI every July. The deeming rates are set by the Minister for Social Services.

Taxation of the Age Pension

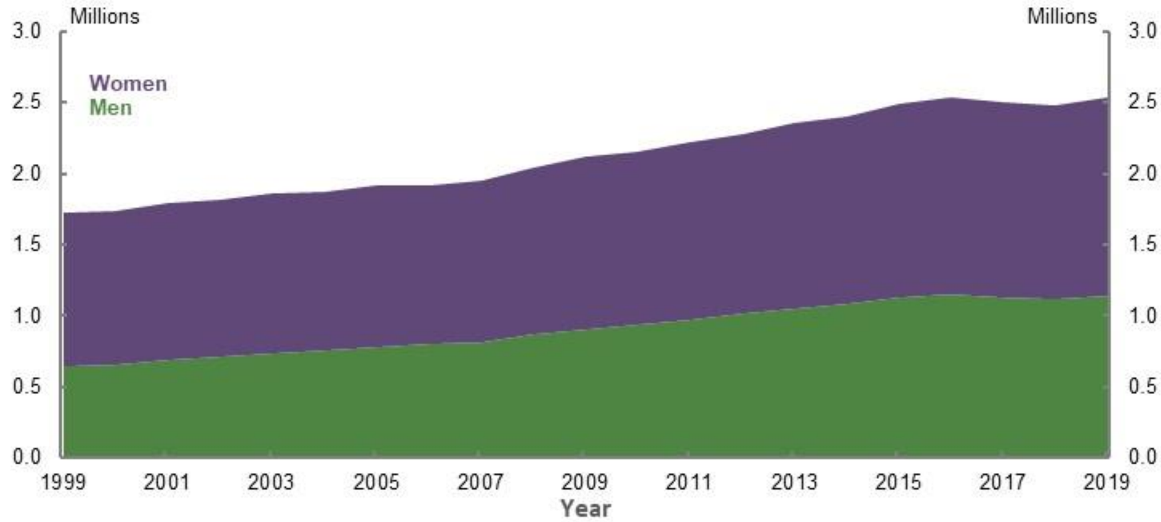
Age Pension payments form part of a person's taxable income. This is consistent with most working-age income support payments, including the JobSeeker Payment and Parenting Payment. Commonwealth Rent Assistance payments are not taxable.

By accessing various tax offsets, including the seniors and pensioners tax offset, the low income tax offset, and the low and middle income tax offset, age pensioners with incomes up to $33,088 (or $29,783 for each member of a couple) pay no income tax. For singles, the seniors and pensioners tax offset begins to phase out at incomes above $33,088 and is fully phased out at an income of $50,928.

Age Pension coverage and expenditure

In June 2019, around 2,533,000 people, or 65 per cent of people over Age Pension eligibility age received the Age Pension.[18] This compares with around 1,725,000, or 67 per cent, in 1999 (Chart 1B-1).

Chart 1B-1 Number of Age Pension recipients



Note: 1999-2013 data includes Age Pension recipients paid by the Department of Veterans' Affairs. 2014-2019 data does not include recipients paid by the Department of Veterans' Affairs. Source: Department of Social Services payment data 1999-2019.

The proportion of older Australians receiving the Age Pension increases with age. At 30 June 2019, 42 per cent of people aged 66 received the Age Pension, compared with 80 per cent of people aged 80.[19]

At June 2019, 3 per cent of people over Age Pension eligibility age received a payment similar to the Age Pension from the Department of Veterans' Affairs. A further 3 per cent received some other income support payment, such as the Disability Support Pension, Carer Payment or Special Benefit.[20] In total, around 71 per cent of people over Age Pension eligibility age receive some kind of income support payment.

Age Pension expenditure has increased in real terms from $24 billion in 2000-01 to $46 billion in 2018-19. It has remained relatively stable as a proportion of GDP (2.4 per cent in 2018-19) and as a proportion of the Federal Budget (9.7 per cent in 2018-19) (see *4. Sustainability*).

[18] Review calculation using Department of Social Services Payment data, 30 June 2019; (ABS, 2018g).
[19] Review calculation using Department of Social Services Payment data, 30 June 2019; (ABS, 2018g).
[20] Department of Social Services Payment data, 30 June 2019.

Concessions

The Australian Government provides concessions to income support recipients and lower-income earners. State and territory governments also provide concessions and subsidised services to older Australians. Subsidised aged care and health services are of particular significance to improving retirement outcomes (see *2A. Achieving a minimum standard of living in retirement*).

Pensioner Concession Card

The Pensioner Concession Card is automatically issued to recipients of the Age Pension, Parenting Payment Single, Disability Support Pension and Carer Payment.

People aged over 60 who have been continuously receiving one (or a combination) of the following payments for more than 39 weeks can also receive the Pensioner Concession Card: JobSeeker Payment (formerly Newstart Allowance), Sickness Allowance, Widow Allowance, Partner Allowance, Parenting Payment Partnered or Special Benefit.

People holding a Pensioner Concession Card and their dependants can access:

- Cheaper Pharmaceutical Benefits Scheme-listed medicines
- Reduced out-of-hospital medical expenses after reaching the Concessional Extended Medicare Safety Net threshold
- Bulk-billed general practitioner appointments at the discretion of the doctor
- Free hearing assessments and hearing rehabilitation, including supplying and fitting hearing aids

In December 2019, around 2,649,000 people aged 65 and over held Pensioner Concession Cards (Department of Social Services, 2020b).

Commonwealth Seniors Health Card

The Commonwealth Seniors Health Card gives eligible Australians above Age Pension eligibility age who do not receive an income support payment access to Australian Government health concessions.

The Commonwealth Seniors Health Card is not an automatically issued concession card. A person must claim for the card and must meet the eligibility criteria, including an income test of $55,808 per year for singles and $89,290 per year for couples, with additional allowances for each child recipients have in their care. These thresholds are indexed in September each year in line with the CPI. The Commonwealth Seniors Health Card is not subject to an assets test.

People holding a Commonwealth Seniors Health Card have access to the same Australian Government concessions as those holding Pensioner Concession Cards, except for hearing services.

In December 2019, 386,690 people held a Commonwealth Seniors Concession Card (Department of Social Services, 2020b).

Pension Loans Scheme

The Pension Loans Scheme was established in 1985 to allow eligible age pensioners to receive a fortnightly payment, drawn against real assets, to support their living standards in retirement.

The Government introduced major reforms to the Pension Loans Scheme on 1 July 2019, expanding the scheme to include self-funded retirees. Under these changes, the amount a person could access under the scheme was increased. A pensioner (or their partner) can now top up their pension so their pension plus loan amount can be up to 150 per cent of the maximum fortnightly rate of

Age Pension. Self-funded retirees can receive the entire 150 per cent amount as a loan. Pension Loans Scheme payments are not taxable.

Under the scheme, the additional payments above any Age Pension entitlement accrue as a debt secured against real estate the person owns. The interest rate on the debt is currently 4.5 per cent.[21] Safeguards limit the maximum loan that can accrue. The Government generally recovers the debt when the property securing the loan is sold, or from the person's estate after the person has died. The scheme is voluntary and people can withdraw at any time.

Overview of compulsory superannuation

The Superannuation Guarantee

Employers must pay the SG for eligible employees on a quarterly basis. Generally, the SG must be paid into a superannuation fund the employee chooses. Currently the SG rate is 9.5 per cent, calculated on the employee's ordinary time earnings. Ordinary time earnings are the amounts earned for ordinary hours of work, not including overtime payments or parental leave. SG contributions are a deductible expense for employers. Compulsory contributions are generally taxed at a rate of 15 per cent, which for most people is a concessional rate compared to how their regular income is taxed (see *Regulation and taxation of superannuation*, below).

Some Australians are not covered by the SG. Self-employed people, employees who earn less than $450 per month, employees who are under 18 and work less than 30 hours per week, and people who do work of a private or domestic nature for less than 30 hours per week are not covered (see *3D. SG coverage*). Higher-income Australians' earnings are covered by the SG up to a threshold (currently $55,270 of income per quarter) beyond which the SG is not payable.

The SG rate has incrementally increased since its introduction at 3 per cent in 1992. It is legislated to rise in increments from its current rate of 9.5 per cent to 12 per cent by 1 July 2025. While the minimum is 9.5 per cent, some employees receive higher superannuation contributions from their employers, such as those negotiated through enterprise agreements.

Preservation

Superannuation savings cannot generally be accessed until a person reaches their 'preservation age' and they meet a condition of release. This is usually on retirement, or in some very limited other circumstances. In line with longer life expectancies, the preservation age is slowly increasing from 55 to 60. The preservation age is 55 for those born before 1 July 1960. It increases to 60 for those born after 1 July 1964.

The role of defaults for compulsory superannuation

Default settings are important in the retirement income system as people generally do not engage with their superannuation. Defaults also assist those with limited knowledge of money management, removing their need to make investment decisions. Defaults, particularly those dealing with contribution levels, are important in the pre-retirement phase as the further people are from retiring, the less they engage.

Most employees can choose the superannuation fund into which their SG is paid. If an employee does not choose a superannuation fund, they are defaulted into a 'MySuper' product. Since 1 January 2014, only funds offering a MySuper product have been eligible to receive default superannuation contributions for new employees. MySuper products provide a simple,

[21] As at 1 May 2020. The Pension Loans Scheme interest rate is set by the Minister for Social Services.

cost-effective, balanced product[22] for the vast majority of people who are invested in the default option of their current fund.

Another default setting is the provision of insurance. Superannuation fund members receive death and permanent disability insurance by default. Premiums for this insurance are deducted from the member's superannuation balance. Changes legislated in 2019 mean that only opt-in insurance can be offered where a member is under 25 years of age or their account is less than $6,000, unless that member is in a high-risk occupation. The changes also prevent insurance premiums from being deducted from accounts that are inactive.

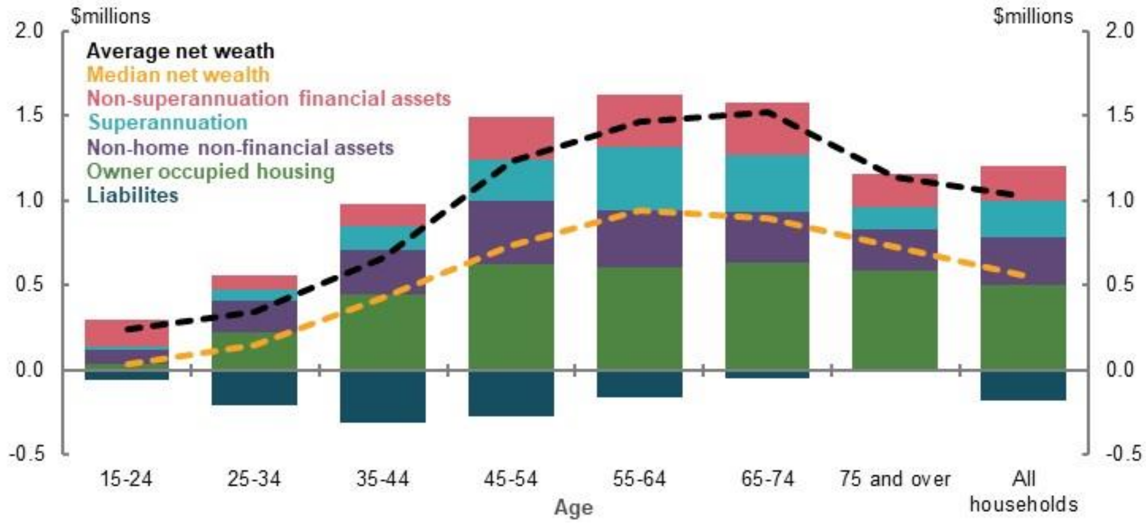
Overview of voluntary savings

Voluntary savings make an important contribution to people's retirement incomes. For those who are not covered by compulsory superannuation for a significant portion of their working lives, such as sole traders and small business owners, or those with extended career breaks, voluntary superannuation contributions provide the necessary flexibility to contribute to the system. More broadly, voluntary savings allow people to choose how much they save for retirement.

Voluntary savings can include business assets, real estate including owner-occupied dwellings, and other financial and non-financial assets. Although these assets supplement retirement incomes, they are often accumulated for purposes unrelated to saving for retirement. The main way Government policy settings affect voluntary saving for retirement is through concessions for voluntary superannuation contributions.

The family home is an important voluntary savings vehicle for most Australians as it reduces accommodation expenses in retirement. On average, equity in the family home represents the largest share of net wealth for Australians aged 65 and over (Chart 1B-2).

Chart 1B-2 Average net household wealth by age group, 2017-18



Note: A small number of estimates have high standard errors and should be used with caution. Source: (ABS, 2019k).

Voluntary contributions to superannuation

People can make additional contributions to superannuation. In 2017-18, voluntary contributions made up around 40 per cent of the total contributions to superannuation (Table 1B-5). As

[22] While a 'balanced' product suggests a balance between growth and defensive assets, typically 60 per cent growth and 40 per cent defensive assets, there is no standard definition, and the composition of balanced product may vary considerably.

superannuation is concessionally taxed, it can be an attractive savings vehicle. However, caps on superannuation contributions limit access to these concessions. These caps have changed over time (Box 1B-4).

Table 1B-5 Superannuation contributions

Contribution type	Amount ($billion)	Per cent
Employer (excluding salary sacrifice)	62.9	62
Concessional — salary sacrifice	10.9	11
Concessional — personal deductible	5.0	5
Non-concessional	23.1	23
Total	**101.9**	**100**

Note: Does not include those with no member contribution statement. Does not include 'other' superannuation contributions, such as spouse contributions and Government co-contributions. Does not include contributions to defined benefit funds. Source: Analysis of ATO individual income tax returns and member contributions statements, 2017-18.

People make two broad types of voluntary contributions:

- **Concessional contributions** are made from pre-tax income and taxed at 15 per cent in the fund. Employees may salary sacrifice or make tax-deductible contributions to a superannuation fund. SG contributions are generally concessional contributions. People without access to salary sacrifice arrangements (such as self-employed people) generally make concessional contributions by contributing to a superannuation fund and claiming a tax deduction for the contribution.
- **Non-concessional contributions** are made from post-tax income.

Currently, people can make up to $25,000 of **concessional contributions** each year. Since 1 July 2018, people have been able to 'carry forward' some of their unused concessional contributions cap for up to five subsequent years if their superannuation balance is less than $500,000.

People can make up to $100,000 in **non-concessional contributions** each year. People with superannuation fund balances of $1.6 million or more cannot make non-concessional contributions. 'Bring forward' arrangements allow people under 65 to make up to three years' of non-concessional contributions (i.e. $300,000) in one year, provided the contribution does not mean the person's balance breaches the $1.6 million cap.[23]

From 1 July 2017, the **concessional contributions cap** was indexed to average weekly ordinary time earnings. It is increased in increments of $2,500. The non-concessional contributions cap is indexed in line with the concessional contributions cap.

People are also subject to **age-based contribution rules**. From 1 July 2020, those aged 67 and over can only contribute if they meet the 'work test' by working more than 40 hours in a 30-day period at some point in the relevant year.[24] Those aged 75 and over cannot make voluntary contributions to superannuation.

People can also contribute to superannuation in a number of **specific circumstances**. For example, specific rules apply to personal injury payments, proceeds from downsizing a home, and proceeds from selling a small business.

Downsizer contributions allow a person aged 65 or over to make a contribution of up to $300,000 from the proceeds of the sale of their home. Certain conditions apply, including that the home has been held for at least 10 years prior to the sale.

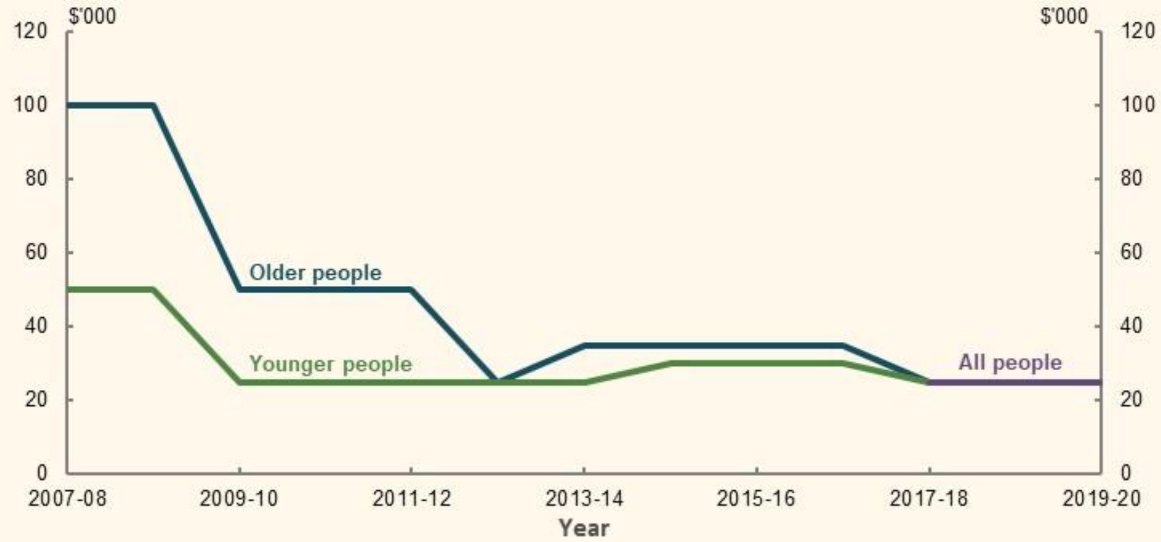
[23] A change to allow people aged 65 and 66 to access the bring-forward arrangements was announced in the 2019-20 Budget, but at July 2020 is yet to be legislated.
[24] A change to the work test allowing those aged 65 and 66 to make voluntary superannuation contributions without meeting the test commenced from 1 July 2020.

Box 1B-4 Historic changes to contribution rules

Non-concessional contributions were uncapped before May 2006, limited to $1 million between 10 May 2006 and June 2007,[25] $150,000 from 2007-08 to 2013-14, $180,000 for 2014-15 to 2016-17, and $100,000 from 1 July 2017 onwards.

Similarly, concessional contributions caps have changed over time, typically to make them less generous (Chart 1B-3).

Chart 1B-3 Changes in superannuation concessional contributions caps



Note: 'Older people' are people aged 50 and over in 2007-08 to 2011-12, people aged 59 and over in 2013-14 and people aged 49 and over in 2014-15 to 2016-17. 'Younger people' are people younger than 50 in 2007-08 to 2011-12, people younger than 59 in 2013-14 and people younger than 49 in 2014-15 to 2016-17. 'All people' are the contributions caps that apply to people of all ages. Source (CEPAR, 2018b).

Prior to 2007, self-employed people received a 100 per cent tax deduction for only the first $5,000 of a contribution (increased from $3,000 in 2002) and 75 per cent of any subsequent contributions. They were also not eligible for the Government co-contribution scheme available to employees. From 1 July 2007, self-employed people under age 75 were able to claim all personal superannuation contributions as a tax deduction, but they were required to earn less than 10 per cent of their income as an employee to make a contribution. From 1 July 2017, the 10 per cent restriction was removed. Today, anyone can make deductible superannuation contributions (both the self-employed and employees who do not have access to salary sacrificing arrangements).

Reforms that took effect from 1 July 2017 generally prevent people with a total superannuation balance above $1.6 million from making post-tax voluntary contributions.[26] Since these reforms, voluntary contributions have declined from 33 per cent of all superannuation contributions in 2015-16, to 25 per cent in 2018-19 (see *1D. The changing Australian landscape*).

Small businesses may contribute the capital proceeds of the sale of certain small business assets, subject to certain conditions. This allows small business owners to contribute the assets they have accumulated through their business to their retirement savings. The total lifetime contributions must

[25] *The Tax Laws Amendment (Simplified Superannuation) Act 2007* introduced a permanent cap of $150,000 on non-concessional contributions and the temporary cap of $1 million.

[26] Non-concessional contributions made by a person with a total superannuation balance above $1.6 million are classified as excess contributions, which are taxed at the top marginal tax rate unless they are withdrawn from the superannuation system. However, under the downsizer and small business CGT concession measures, such non-concessional contributions are not treated as excess contributions.

not exceed $1.565 million in 2020-21. This cap is indexed annually. These contributions do not count for other contributions caps and can be made even if the person has a balance exceeding the transfer balance cap of $1.6 million.

Government contributions and offsets

The Government provides certain contributions and offsets to eligible people, usually those with lower-to-medium incomes. Government contributions and offsets are generally aimed at improving equity for people who would otherwise receive smaller benefits from superannuation tax concessions. They include the low income superannuation tax offset, Government co-contributions for certain lower-income earners and spouse tax offsets.

The **low income superannuation tax offset** refunds the 15 per cent tax incurred on concessional superannuation contributions to people with a taxable income of less than $37,000. In 2018-19, almost 3 million people benefited from the low income superannuation tax offset, 60 per cent of whom were women.[27] In practice, the offset removes a tax penalty by refunding tax paid on superannuation contributions to ensure lower-income earners pay no more tax than they would if receiving contributions as income.

The **Government co-contribution** provides up to $500 per year as a 50 per cent matching contribution for any personal non-concessional contributions made by people aged under 71. The rate of co-contribution decreases where a person's income is above the low-income threshold ($39,837 for 2020-21) to the point where no contribution is payable for those with income above the high-income threshold ($54,837 for 2020-21). In 2018-19, around 376,000 people received co-contributions, 65 per cent of whom were women.[28]

The **spouse tax offset** provides a tax offset of up to $540 to people who contribute to their low-income spouse's superannuation.[29] The maximum offset reduces as the spouse's income exceeds $37,000 and phases out at $40,000.

Using superannuation to fund retirement

Retirees generally have two choices for using their superannuation to fund their retirement:

1. **Lump sums**. Traditionally, the superannuation system paid out lump sums at retirement age. This was influenced by historical features of the retirement income system, such as tax settings that favoured lump sums in the 1970s and 1980s, and the former predominance of employer-based defined benefit schemes that paid entitlements as lump sums.

2. **Income streams**. Current policy settings favour income streams over lump sums, as earnings on funds supporting income streams are tax-free in the retirement phase. Superannuation income streams provide a retiree with a regular payment. This comes in the form of an allocated or account-based pension purchased from the fund when the member's balance is rolled into a pension account at the point of retirement.

   Around 83 per cent of income streams are account-based (Australian Prudential Regulation Authority, 2020a). Account-based income streams offer the benefit of a regular income and the flexibility of access to lump sums of money held in an account where funds can be withdrawn at any time.

[27] Data provided to the review by the ATO.
[28] Data provided to the review by the ATO.
[29] The offset is 18 per cent of the value of contributions, up to a total of $3,000 in contributions.

People have significant flexibility in how they use their superannuation. Minimum drawdown rates limit the ability of retirees to retain funds in the retirement phase indefinitely in order to remain exempt from tax on investment earnings. Minimum drawdown rates increase with age, from 4 per cent for a person under 65, to 14 per cent for a person over 95.[30] These rates have temporarily been halved for the 2019-20 and 2020-21 income years to allow for reduced superannuation balances following the COVID-19 Pandemic.

Regulation and taxation of superannuation

Regulation

Compulsory superannuation contributions were extended to nearly all employees in 1992. The following year, a regulatory framework was introduced to ensure superannuation funds were managed prudently and in the best interests of their members.

Superannuation funds operate under a trustee model derived from the general law of equity and legislated in the *Superannuation Industry (Supervision) Act 1993* (SIS Act). A corporate trustee, or a group of individual trustees, controls the fund's assets and operates it solely for the benefit of its members and beneficiaries. The trustee has a fiduciary obligation to the members and beneficiaries. The trustee has ultimate responsibility for the entity and an obligation to manage the assets of the entity with competence, diligence, prudence and honesty.

Unlike many other jurisdictions and earlier iterations of the Australian system, most members are now in defined contribution arrangements rather than defined benefit arrangements.

The mandating of contributions and the provision of taxation incentives to encourage superannuation saving necessitates prudential regulation of superannuation entities, which is conducted by APRA.

Trustees of APRA-regulated funds must, among other things, demonstrate that they meet minimum standards of fitness and propriety; possess adequate human, technical and financial resources to meet their trustee responsibilities; and have appropriate risk management arrangements in place.

Prudential regulation does not guarantee that a superannuation entity will not fail, or that superannuation fund members will not suffer investment losses. Rather, it aims to ensure the prudent management of superannuation entities, so they can meet their financial promises to their members and beneficiaries. ASIC regulates the conduct and disclosure obligations of superannuation trustees.

Around two-thirds of the system (in terms of total value of assets) is APRA-regulated. The remainder is held by self-managed superannuation funds (SMSFs), balance of life office statutory funds or exempt public sector superannuation schemes.[31] SMSFs may include up to four members, all of whom must be trustees or directors of the corporate trustee. These funds are exempt from prudential regulation on the basis that there is no difference in interests between trustees and members. The ATO is responsible for regulating SMSFs.

[30] The minimum drawdown rates are found in Schedule 7 of the *Superannuation Industry (Supervision) Regulations 1994*.

[31] Balance of life office statutory funds are assets held for superannuation or retirement purposes in statutory funds of life insurance companies, regulated under the *Life Insurance Act 1995*. Exempt Public Sector Superannuation Schemes provide defined benefit pensions and abide by the relevant provisions of the SIS Act.

Taxation

Contributions tax applies to superannuation contributions that have not otherwise been taxed. These 'pre-tax' or concessional contributions are generally taxed at the flat rate of 15 per cent in the superannuation fund.

Division 293 tax requires people with an adjusted income of $250,000 and over to pay 30 per cent tax, instead of 15 per cent, on concessional contributions.[32] Division 293 tax ensures people with annual incomes of $250,000 and over receive only a 17 per cent tax saving on superannuation contributions above this threshold. This tax advantage is lower than most other income levels. In 2018-19, around 230,000 people paid tax under Division 293, 77 per cent of whom were men.

Earnings tax is paid when superannuation assets grow in value. Earnings on superannuation assets are taxed in the superannuation fund at 15 per cent in the accumulation phase and are tax-free when the assets are in the retirement phase (i.e. they are providing a pension). Capital gains are also taxed at 15 per cent, with a one-third discount for assets held for more than one year.

The effective earnings tax rate may be lower than 15 per cent in the accumulation phase. This is because superannuation assets are eligible for franking credit tax offsets and a one-third capital gains discount if the assets have been owned for at least 12 months. As a result, the effective tax rate in the accumulation phase averages around 7 per cent.

To limit the total value of assets subject to earnings tax exemptions in the retirement phase, people are limited to the amount they can transfer to the tax-free retirement phase by the transfer balance cap. The transfer balance cap is currently $1.6 million. It is indexed each July in line with CPI, in $100,000 increments.

Overview of sources of income for recent retirees

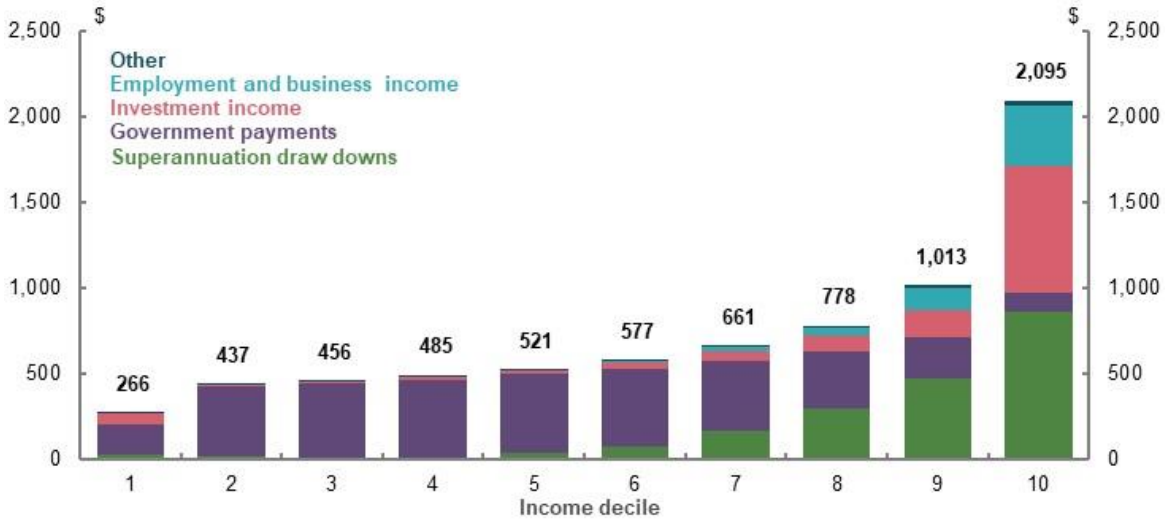
Half of retirees rely on the Age Pension for at least 80 per cent of their income. At June 2019, almost 62 per cent of age pensioners received the maximum rate of pension, with the remaining 38 per cent receiving a part-rate pension.[33]

In 2017-18, the median retiree household had equivalised[34] income of $521 per week, primarily from the Age Pension, with a small supplemental income from superannuation and investments (Chart 1B-4).

Retiree households in the top two income deciles rely more on income from superannuation and investments than Government payments. Higher-income households are also more likely to be earning business or employment income.

[32] Adjusted income for Division 293 tax purposes is similar to the income used for Medicare Levy surcharge purposes.
[33] Department of Social Services payment data, 30 June 2019.
[34] Equivalisation is a way to compare households of differences sizes and compositions. Further information explaining how the review has defined equivalisation can be found in the Glossary.

Chart 1B-4 Equivalised retiree household weekly disposable income, by source and income decile

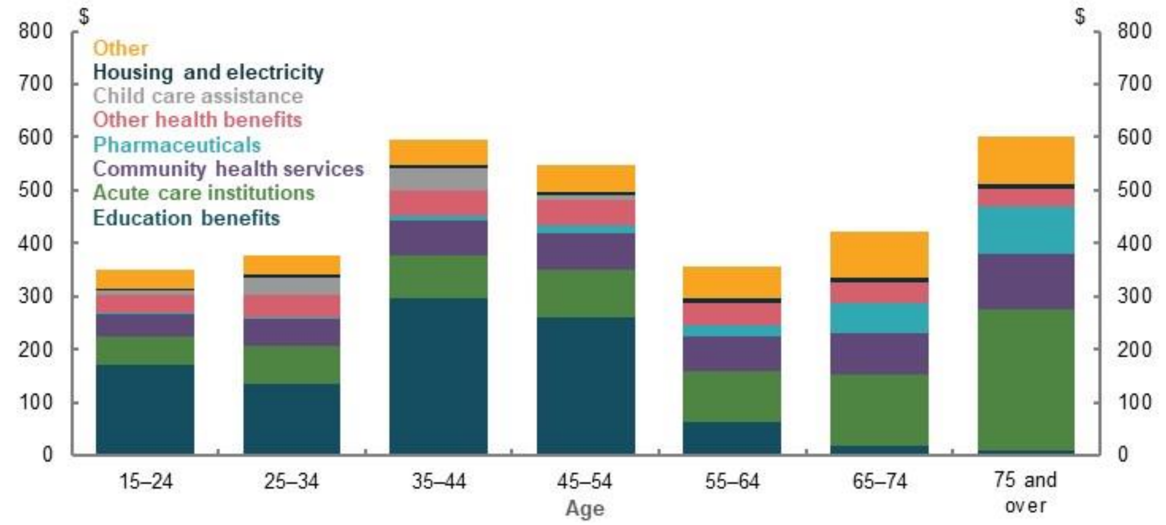


Note: Numbers above the column are total equivalised weekly income for each decile. Government payments include social security payments administered by Services Australia and the Department of Veterans' Affairs, including compensation payments and family payments. Other includes income such as child support, income from non-superannuation annuities or financial support received from family members. Retirees are defined as households where the reference person is aged 65 or older and is no longer in the labour force. Household wealth has been equivalised using the OECD equivalence scale in order to take account of differences in a household's size and composition. Low government income at decile one is influenced by households with assets in excess of the Age Pension assets test minimum threshold who may be drawing on assets not well captured in ABS income survey methodology. Average equivalised net wealth for the first income decile is over $900,000. Values are in 2017-18 dollars. Source: Analysis of (ABS, 2019s).

The value of government services for retirees

All Australian households receive support in the form of government-provided services, also referred to as social transfers in kind. The type of service, and degree to which it is used, changes as households age. Younger households receive significant in-kind support through benefits associated with primary, secondary and tertiary education. Older households receive significant social transfers through health services (Chart 1B-5), which are higher as a proportion of their income than other age groups (ABS, 2019k).

Chart 1B-5 Average weekly value of social transfers in kind, by age group



Note: Social transfers in kind are goods and services provided free or at subsidised prices by the Government. Education benefits includes school, tertiary and other education benefits. 'Other health benefits' includes private health insurance rebate and other health benefits. 'Other' is the residual of total selected social transfers in kind not covered. Values are in 2017-18 dollars. Source: (ABS, 2019k).

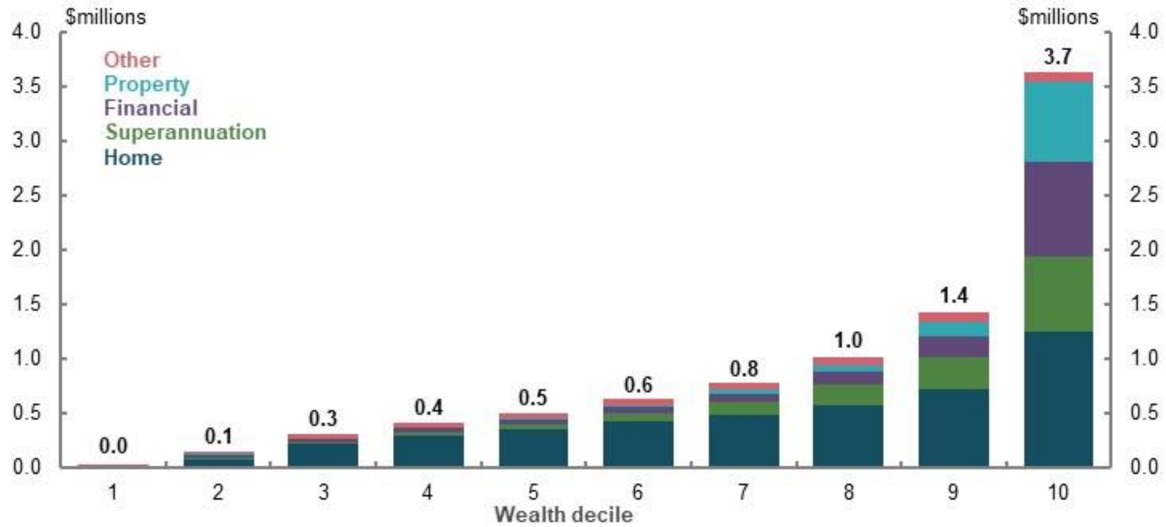
Assets of retirees

For most households aged 65 and over, the family home is their largest asset (Chart 1B-6). The home makes up 60-72 per cent of net wealth for households in the 40th to 70th percentile of the wealth distribution.

Excluding the family home, the median retiree household has around $165,000 in net wealth. For most households in retirement in 2017-18, superannuation makes up a relatively small share of net wealth.

Households in the top 20 per cent by wealth have on average more than $500,000 in equivalised wealth outside the home. Their wealth is held across financial, property and superannuation assets.

Chart 1B-6 Equivalised household wealth by asset type, for retirees



Note: Retirees are defined as households where the reference person is aged 65 or older and is no longer in the labour force. Household wealth has been equivalised using the OECD equivalence scale in order to take account of differences in a household's size and composition. Values in 2017-18 dollars. Source: Analysis of (ABS, 2019s).

Superannuation wealth for people in or near retirement

While superannuation is a minor source of wealth for most current retirees, it will be an increasingly important asset as the system matures.

Currently, most people approaching retirement have some superannuation. However, they will have received the SG for only part of their working lives, and at a relatively low rate for some of this time. Superannuation balances for people approaching retirement are skewed towards higher-wealth households (Chart 1B-7 and Chart 1B-8). For people approaching retirement in 2017-18, the average superannuation balance for those at the fifth decile of the household wealth distribution was close to $140,000 compared with more than $1 million for the top decile.

Chart 1B-7 Equivalised superannuation balances of households aged 60-64

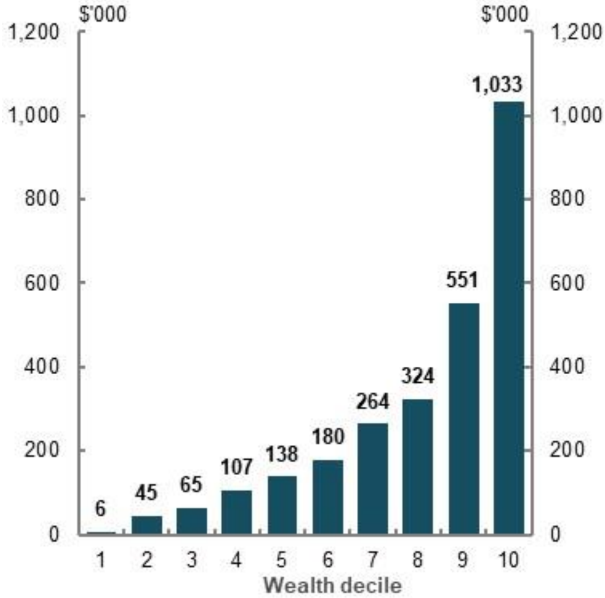
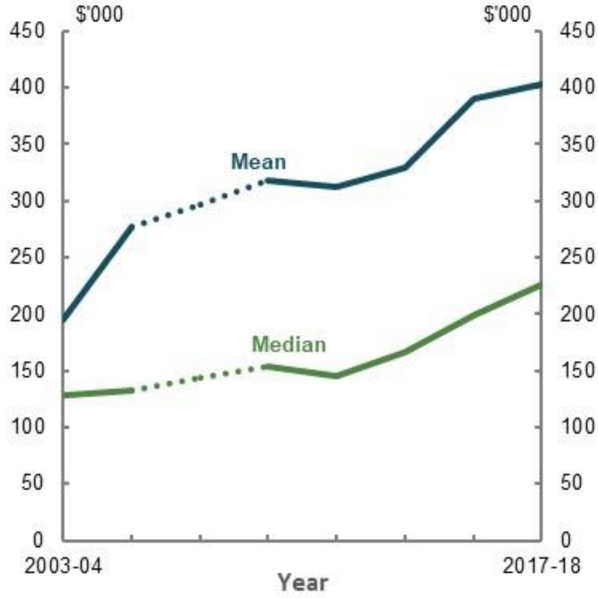


Chart 1B-8 Superannuation balances of people aged 65-74



Note: All values are in 2017-18 dollars. Household wealth has been equivalised using the OECD equivalence scale in order to take account of differences in a household's size and composition. Superannuation balances presented in Chart 1B-8 are on an individual rather than household basis. Data on superannuation was not collected in 2007-08. Source Analysis of (ABS, 2019s); (ABS, 2019k).

International comparison of Australia's retirement income system

Australia's retirement income system generally ranks highly in international comparisons of retirement income systems. For example, the Melbourne Mercer Global Pension Index ranked the Australian system third of 37 countries in 2019, behind the Netherlands and Denmark (Mercer, 2019b). It ranks highly on both adequacy and sustainability compared to others as it is more fully funded than most through superannuation contributions. It is also rated highly on integrity, as a result of the regulatory and governance requirements for superannuation funds operating in Australia.

Australia was one of the first countries to adopt a retirement income system with three pillars, comprising a means-tested Age Pension, compulsory superannuation and tax incentives to encourage voluntary contributions to superannuation. The Australian approach has been endorsed by the World Bank as international best practice (Nielson & Harris, 2010).

Australia's Age Pension is unique. Some countries, mostly those in Scandinavia and Southern Europe, have a basic pension for poverty alleviation that covers a much smaller range of people. Around 71 per cent of Australians over Age Pension eligibility age receive an income support payment. According to CEPAR, Australian pensions involve higher payments and slower rates of withdrawal than most other countries (CEPAR, 2020, p. 4). However, most other countries have publicly funded contributory social security systems that provide benefits higher than basic pensions.

A key consideration in Australia's retirement income support is housing. Australian levels of home ownership are high by international standards, particularly compared with Europe, where lifelong residence in 'public housing' is common for a significant percentage of lower-income earners. For many Australians, the family home is their most significant form of voluntary savings. Home ownership is important in determining the adequacy of retirement income, because most home owners have significantly lower housing costs than a retiree renting on the private market.

Internationally, the two most common retirement income schemes are:

1. **Government social insurance schemes** are operated by many European governments. They involve an extra tax paid every year from employment income, with the promise of a regular payment in retirement. For example, the current rate of National Insurance in the UK for most employees is 12 per cent. Social security contributions are 18.6 per cent in Germany and 9.2 per cent in France. These schemes are often unfunded, meaning the additional tax paid is not separated or quarantined from other government funds to pay for pensions in the future.
2. **Employer-based defined benefit schemes** involve employers providing retirement incomes to their employees. These schemes were the most common type of retirement income system internationally until the early 1990s, and were designed to retain employees. They typically paid a multiple of an employee's final average salary based on their number of years of service. These schemes placed investment risk on the employer, meaning the employee received the same benefit irrespective of market returns. Following many companies struggling to meet these liabilities, particularly in the UK and US, defined benefit schemes are now less common.

Australia's compulsory, privately managed superannuation system is unique. The most closely comparable schemes in the US or Canada are not compulsory. Instead, they encourage participation through tax incentives or behavioural 'nudges', such as automatic enrolment when starting a new job.

Private management of a pool of funds collected from member contributions places investment risk on the employee and retiree. This differs from employer defined benefit schemes or government social security schemes, and can expose retirees to lower incomes if market returns are low during retirement. However, experience with employer schemes demonstrated that employers do not always manage this risk effectively. Insolvency of some large US and UK firms has led to employees losing both employment and retirement savings. Unfunded government schemes carry a risk of governments reducing benefits in the future if the scheme becomes difficult to afford. This is particularly a risk for countries with ageing populations.

Preservation of retirement savings until retirement age is strictly enforced in Australia. With some small exceptions for 'early release', in circumstances of severe financial hardship or on compassionate grounds, superannuation can only be accessed after reaching preservation age. In contrast, overseas systems, for example funds established under section 401K of the US Internal Revenue Code, sometimes allow access to retirement savings earlier in life, but with a tax penalty (10 per cent in the US system).

Australia's superannuation system provides more flexibility in retirement than most schemes. Retirees can access lump sums to pay for large one-off expenses (e.g. to finalise a mortgage or buy a car) or access an income stream over the longer term. European pension schemes typically provide an income stream, but do not offer access to a lump sum.

Section 1C. The objective of the system and the roles of the pillars

Box 1C-1 Section summary

- **The retirement income system needs a clear objective** to:
  - Anchor the policy direction of the system
  - Ensure the community understands the role and purpose of the system
  - Provide a framework for assessing the system's performance
- The Australian community will ultimately have to endorse the system's objective through the Government**.** To that end, the following broad objective for the system is suggested:

  The retirement income system should deliver adequate standards of living in retirement in an equitable, sustainable and cohesive way
- **To expand on this broad objective, the following elements are suggested**:
  1. The system should ensure a minimum standard of living for retirees with limited financial means that is consistent with prevailing community standards.
  2. The system should facilitate people to reasonably maintain their standard of living in retirement.
  3. The system should target Government support to those in need.
  4. The system should provide similar outcomes for people in similar circumstances.
  5. The system should be cost-effective for taxpayers in achieving adequate outcomes.
  6. The system should be sustainable and robust to demographic, economic and social change.
  7. The system should have effective incentives to smooth consumption and support people in taking personal responsibility for their retirement incomes.
  8. The system should interact effectively with other systems.
  9. The system should not be unnecessarily complex for consumers.
- **The roles of the Government, individuals, the private sector and the three pillars will be influenced by the system's objective**. The role of the pillars will depend on their effectiveness, including cost-effectiveness, in achieving the system's objective. All support for retirees — such as social transfers in-kind — need to be considered.

Outline of this section

This section suggests an objective for the retirement income system and considers the roles of system participants and pillars.

The objective of the retirement income system is ultimately a decision for the community (Box 1C-2). This section suggests issues to consider in deciding on the objective. The roles of system participants and pillars will stem from the objective the community endorses through the Government.

Box 1C-2 The system's objective and community endorsement

The retirement income system's objective should be established and endorsed by the Australian community through the Government. To help determine what this objective should be, and to facilitate this review, the panel has identified a possible objective and nine supporting elements for the system. The roles of system pillars should be determined by the objective, taking into account each pillar's effectiveness in achieving that objective.

The system objective and roles of the pillars should be endorsed by the community to ensure public support for the system's purpose and operation. It would be preferable if the objective of the retirement income system was legislated and not subject to frequent change.

The retirement income system and its component parts (the pillars) currently lack a stated objective. A clearly articulated objective is essential for anchoring the system's policy direction, ensuring the community understands its purpose, and providing a framework to measure system performance. Many submissions endorsed the need to clearly establish the objective of the retirement income system and roles of the pillars (Box 1C-3).

Box 1C-3 Stakeholder input on the importance of the objective for the system

Stakeholders strongly agreed on the need for well-defined system objective. Stakeholders observed the lack of an objective has led to poor public understanding of the retirement income system and a lack of clear policy direction. Stakeholders also suggested that a formal objective would help in assessing the system's performance.

- A wide range of stakeholders noted the public lacks a common understanding of the system's objective, at least partly because the Government has not defined one (Committee for Sustainable Retirement Incomes; AMP; Challenger; Financial Planning Association of Australia; National Seniors; Rice Warner).
- Some suggested that a lack of clear roles for each pillar is a key reason people do not understand the overall system's objective (Actuaries Institute). Others similarly observed that more clearly defining what each pillar is trying to achieve would assist public understanding of an overall system objective (Australian Super). Many submissions singled out the lack of a clear purpose for superannuation as being harmful in assisting public understanding (AIA Australia; AIST; Centre for Law, Markets and Regulation).
- Some noted that a system objective is needed to guide the review's performance assessment (ASFA; AIST; Business Council of Australia).
- One view was that an objective would guide more coherent policy change, and this would reduce complexity and improve confidence (Business Council of Australia). Similar views were expressed that a clear system objective would help steer policy around pillar roles (Financial Planning Association of Australia).
- Many stakeholders held the general view that the system lacked a clear objective and establishing an objective is an important step (Alliance for a Fairer Retirement System; IOOF; Australian Unity; Dr Gaurav Khemka and Associate Professor Geoff Warren; Grattan Institute).

The principles of the retirement income system

The consultation paper released in November 2019 suggested that the principles for the retirement income system should be adequacy, equity, sustainability and cohesion.

Stakeholders largely endorsed these principles. Several additional principles were suggested, but these are generally captured by the principles outlined in the consultation paper.

- Some stakeholders suggested efficiency, competition or innovation.[35] These can be interpreted as part of the principle of sustainability.
- Several stakeholders suggested certainty and integrity.[36] These can be seen as being part of public confidence under the principle of sustainability.
- A number of stakeholders suggested simplicity.[37] This is covered as part of the principle of cohesion.
- One stakeholder suggested fairness.[38] This is covered under the principle of equity.
- Other stakeholders suggested personal responsibility.[39] This is incorporated in the principle of cohesion.

A number of studies and reviews have previously proposed principles for the system. These previous suggestions are broadly consistent with the principles outlined in the *review's* consultation paper, albeit with differences in emphasis.

- A*ustralia's Future Tax System Review* (2009) (the Henry Review) proposed that the system should be broad and adequate, simple and approachable, acceptable (which includes equity), robust and sustainable.
- The *Super System Review* (2010) (the Cooper Review) contained 10 principles for the superannuation system. These principles mostly pertained to the internal operation of the superannuation system, rather than the outcomes the broader retirement income system produces.
- The Superannuation Charter Group (2013) proposed adequacy, sustainability, certainty and fairness as principles to guide superannuation policy.
- The *Financial System Inquiry* (2014) (the Murray Inquiry) proposed that superannuation policy should ensure retirement income is the ultimate goal. It also argued that choice, freedom, competition and innovation are important, but behavioural biases must be recognised and accounted for.
- The Productivity Commission (2016) developed a framework of objectives to assess the efficiency and competitiveness of the superannuation system. These objectives spoke to the performance of the superannuation system as a market that sells products and services to consumers, rather than the broader consideration of retirement outcomes.
- The OECD (2018a) emphasised poverty relief, redistribution, sustainability and consumption smoothing.
- The World Bank (2008) proposed that retirement income systems should be adequate, affordable, sustainable and robust.

Some submissions queried whether it was constructive for this review to put forward yet another set of principles. This is a valid point. Rather than successive reviews of the retirement income system proposing a new version of principles for the system, these should be decided by the Government, endorsed by the community and incorporated in the agreed objective of the system.

[35] (Mercer, 2020; Actuaries Institute, 2020).
[36] (AustralianSuper, 2020; Australian Institute of Superannuation Trustees, 2020; COTA, 2020; National Seniors Australia, 2020).
[37] (Mercer, 2020; AustralianSuper, 2020; Business Council of Australia, 2020; AIA Australia, 2020; First State Super, 2020b; Cbus, 2020; COTA, 2020; Actuaries Institute, 2020).
[38] (COTA, 2020; National Seniors Australia, 2020; Actuaries Institute, 2019).
[39] (Bunbury Branch of the Association of Independent Retirees, 2020; Save Our Super, 2020).

The retirement income system's objective

Suggested objective for the system

To deliver adequate standards of living in retirement in an equitable, sustainable and cohesive way.

For this objective to serve as a guide for policy setting and a basis for assessing system performance, it needs to be expressed as clearly as possible. For example, what constitutes 'adequacy, equity, sustainability and cohesion' will need to be clarified. A vague, ambiguous objective that is open to interpretation will not provide the guidance required.

A single sentence that attempts to cover the objective for the retirement system cannot encompass all the aspects and goals with the clarity required. The following nine elements provide additional detail on how the broad system objective could be clarified.

Adequacy

Two elements are suggested to meet the objective of an adequate retirement income. Stakeholders broadly agree on the first element but differ as to how the second element should be expressed.[40]

Element 1

The system should ensure a minimum standard of living for retirees with limited financial means that is consistent with prevailing community standards.

Australia's retirement income system aims to ensure retirees have a minimum standard of living in retirement in line with prevailing community standards and, in particular, to ensure that no older Australian should live in poverty.[41] Broadly, this is consistent with the current settings of the Age Pension, which ensure the maximum rate of the Age Pension moves with the higher of wages or living costs (see *2A. Achieving a minimum standard of living in retirement*). Older Australians also receive substantial in-kind support in addition to the Age Pension.

There are trade-offs between the generosity of the minimum standard and the:

- Sustainability of the system
- Incentives for people to take a more active role in funding their own retirement

The Age Pension provides more than a safety net for older Australians who do not have a sufficient level of financial resources to achieve a minimum standard of living. It supplements the savings of lower- to middle-income people and households to maintain their standard of living in retirement. This is the second suggested element of the objective of achieving an adequate retirement income.

[40] (Fitzgerald, 1993; World Bank, 2008; OECD, 2018a; Actuaries Institute, 2019; Mercer, 2020; Committee for Sustainable Retirement Incomes, 2020; Grattan Institute, 2020).
[41] (Harmer, 2009).

Element 2

The system should facilitate people to reasonably maintain their standard of living in retirement.

Stakeholders differ as to whether element 2 should be expressed in aspirational terms or if the aim should be, as stated, for retirees to maintain their living standards into retirement.[42] As outlined subsequently, the weight of evidence supports the second approach. This is often referred to as 'consumption smoothing', which balances the trade-off between consumption in working years and consumption in retirement.

For most individuals or households, maintaining living standards in retirement requires them to save while working, so they can draw on those savings in retirement. A tendency to undersave means some intervention (such as from the Government) is needed to encourage retirement saving and therefore maximise lifetime wellbeing.

The amount of income that retirees need to maintain a similar standard of living in retirement as in their working life is generally lower than their pre-retirement income. This is because:

- Expenses typically fall in retirement, increasingly so as individuals and households age. For example, children move out and mortgages are often extinguished
- People no longer need to save for retirement
- In-kind support from the Government subsidises living costs for most retirees

Consumption smoothing is most relevant for middle-income households. This is why the objective of maintaining living standards in retirement is qualified with the word 'reasonably'. For many lower-income individuals or households, the Age Pension represents an increase in their income in retirement (see *2C. Maintaining standards of living in retirement)*. In these cases, achieving a minimum standard of adequacy is more relevant than consumption smoothing.

Higher-income earners have additional wealth to draw on and capacity for voluntary saving. There is less of a rationale for policy based on compulsory superannuation contributions to target consumption smoothing for higher-income earners in the same way it would for others.

Some stakeholders proposed that risk management (against longevity, market or inflation risk) should be an explicit goal of the system.[43] Risk management is clearly important. However, it is arguably covered in the adequacy elements. A minimum standard provides some degree of insurance against these risks by providing an income level that retirees do not fall below. A system that enables people to efficiently maintain their living standard throughout retirement also manages longevity risk.

Equity

Retirement outcomes will inevitably be different across the population because they reflect differences in pre-retirement income and wealth, and individual circumstances. Although stakeholders agreed that equity was an objective of the retirement income system, a range of views were offered regarding what constitutes equity. Many submissions focused on whether particular cohorts of the population (such as women, Aboriginal and Torres Strait Islander people, renters, the

[42] (Australian Council of Trade Unions, 2020; Australian Institute of Superannuation Trustees, 2020; Australian Council of Social Service, 2020; ASFA, 2020a; Financial Services Council, 2020; Grattan Institute, 2020; CEPAR, 2020).
[43] (Committee for Sustainable Retirement Incomes, 2020; Grattan Institute, 2020).

self-employed, and involuntary retirees) were achieving equitable outcomes in retirement.[44] The retirement outcomes of these groups of people and for people across the income and wealth distribution are considered in *3. Equity*.

A key aspect of the objective of equitable retirement outcomes is that Government support is targeted to those in need.

Element 3

The system should target Government support to those in need.

Targeting Government support to those in need is consistent with the broader community consensus on the design of Australia's transfer system, which is one of the most targeted in the OECD (Whiteford, 2015). Targeted support should not discourage people from saving for their retirement if they can.

The largest and most important elements of Government support are the Age Pension and superannuation tax concessions. But other interventions, such as social transfers in-kind, also affect retirement outcomes (discussed more below).

There is a trade-off between targeting and complexity. Universal Government support would be simpler to administer but would be inconsistent with community preferences. Therefore, targeted support should be designed without unnecessary complexity.

Element 4

The system should provide similar outcomes for people in similar circumstances.

Targeting should ensure that people in similar circumstances receive similar levels of support. Similar circumstances can include similarities in income and wealth levels, and household composition.

Sustainability

Sustainability, which focuses on the costs of the system, has two elements. First, whether the system is cost-effective in achieving adequate outcomes (element 5). Second, whether the system can continue to deliver adequate outcomes in the future (element 6). In both cases, the potential impacts on public confidence and community support are important.

Element 5

The system should be cost-effective for taxpayers in achieving adequate outcomes.

The retirement income system contains a wide range of costs for different parties:

- Government. The Age Pension, superannuation tax concessions and in-kind support for retirees.
- Individuals. The cost of the fees charged by the superannuation industry.

From both a community support and a general cost sustainability perspective, this money should be efficiently directed towards achieving adequate retirement outcomes.

[44] (Australian Institute of Superannuation Trustees, 2020; Australian Council of Trade Unions, 2020; ASFA, 2020a; Women in Super, 2020).

This does not mean solely focusing on identifying 'waste' and reducing the overall cost of the system, but identifying whether existing resources could be redeployed to achieve better adequacy outcomes.

This is an important relationship between sustainability, equity and adequacy. If there is scope to reallocate resources to better achieve adequacy objectives, this may imply that Government support could be better targeted.

Element 6

The system cost should be sustainable and robust to demographic, economic and social change.

The first part of element 6 (the system should be sustainable) considers all the different costs of the system. Costs that grow faster than the nation's ability to pay may lead to public perceptions that the Government is making unrealistic promises. This may undermine public confidence that the system is sustainable. Conversely, public confidence can be enhanced by ensuring people have a personal stake in the system and are supported in taking personal responsibility for their retirement.

The second part of element 6 (robustness to change) considers how achieving the system's objective might be affected by adverse external forces, such as lower wage growth or reduced investment returns. The system cannot be impervious to broader forces; the examples listed above will naturally affect the adequacy of retirement incomes. Rather, the system needs to be able to weather such forces and, to some extent, offset their impacts.

Cohesion

Cohesion considers whether the processes, mechanisms and incentives that contribute to retirement outcomes are achieving the system's objective in a well-integrated way. This includes whether the incentives in the system are effective and complementary, whether the system interacts effectively with other systems and whether the system's processes are easy to engage with, or if they are too complex.

The retirement income system is not a discrete entity. It comprises multiple components that have evolved over a century. Considering whether these components operate in a cohesive fashion is important.

Element 7

The system should have effective incentives to smooth consumption and support people in taking personal responsibility for their retirement incomes.

For the system to help people reasonably maintain their living standards in retirement (element 2), all policy settings should encourage optimal consumption smoothing. In practice, this means incentives must balance a person's working, saving, investing and spending across their lifetime.

Incentives should encourage and enable people to take responsibility for their retirement incomes. Having people contribute to their retirement income is central to the objective of people maintaining their living standards.

For many people, this encouragement is in the form of compulsory superannuation. But there also need to be incentives for those who are not covered by compulsory superannuation. People should not only be encouraged to take responsibility for saving for their retirement, they should also be encouraged to use their savings to support their living standards in retirement as effectively as possible.

Incentives operate in a complex policy environment, including:

- In accumulation, the tax incentives associated with voluntary savings; in particular, purchasing housing and making voluntary superannuation contributions
- Approaching retirement, the preservation and Age Pension eligibility ages, and also the incentives stemming from the interaction of private savings and the Age Pension means test
- In retirement, the incentives to drawdown savings to finance living standards

These incentives create many trade-offs against other objectives. For example, tax incentives come at a cost to the system. Hence, it is important that the incentives are 'effective' (shifting behaviour in the intended direction) rather than just rewarding behaviour that would occur regardless.

The intent of incentives to support personal responsibility is to contribute to retirement incomes, rather than boosting savings in their own right. This is particularly relevant where savings go beyond what is needed for generating retirement incomes that maintain people's living standards. It is also relevant when people do not effectively draw on their savings to maintain their living standards in retirement and leave the bulk of their wealth as a bequest.

Element 8

The system should interact effectively with other systems.

Many other factors outside the retirement income system influence people's retirement outcomes. For example, the need to address health issues and to plan for aged care influences people's savings and spending behaviour in retirement. Wherever possible, these interactions should be effective and not undermine either system's objectives.

Element 9

The system should not be unnecessary complex for consumers.

Ideally, the retirement income system should be as simple to navigate as possible. Simpler systems are easier to understand and are more likely to lead to good decisions.

However, producing adequate retirement outcomes in an equitable, sustainable and cohesive way requires input from Government, individuals and the private sector; pillars that span income support and the funds management industry; social transfers in kind that draw together services from across different systems; the tax system; and a multitude of trade-offs.

Inevitably, the system will be complex. The issue is not whether the system itself is complex, but rather:

- Whether the system is unnecessarily complex
- Whether effective steps, including regulation, are taken to help people navigate the system to achieve good retirement outcomes

Complexity can arise slowly and unexpectedly, so regular stocktakes as to whether it is necessary are important. Government and the private sector have a role in developing tools or interfaces that bypass complexity and make it easier for individuals and households to engage with the system (see *5A. Cohesion*).

Key considerations in approaching the elements

The elements are interrelated. For example, achieving adequate standards of living in retirement is inherently related to equity; namely, do all people have an equal opportunity to obtain adequate standards of living in retirement? Similarly, the standard of living being sought in retirement is closely connected to whether the system is sustainable.

The elements should clearly focus on supporting a standard of living in retirement rather than on wealth accumulation in and of itself. Stakeholders and previous studies overwhelmingly agree that the retirement income system should aim to produce income for consumption in retirement, and not be used as a vehicle for estate planning.

Opinions differ over whether the adequacy elements of the system should be aspirational. Some stakeholders recommended objectives such as achieving a 'comfortable retirement', a 'dignified retirement' and a '…retirement [people] want and deserve'.[45] Often these suggested objectives result in target budget standards comprising a basket of goods and services (rather than replacement rates that compare income in working life with income in retirement). Other stakeholders pointed out that such aspirational objectives would involve many people having a higher income in retirement than they have in their working years, which may reduce their standard of living before retirement.[46]

The degree to which an increase in the SG is considered to affect wages growth is critical to this issue. If the SG is not considered to reduce wages growth pre-retirement, then the impact of aspirational retirement income objectives on pre-retirement income is not an issue.

The report examines this issue in detail, concluding that the weight of evidence suggests increases in the SG have an impact on wages growth. Budget standards do not measure the trade-off between retirement and working-life living standards. While a person can choose how much consumption to forgo to save for retirement, in a system based on compulsory superannuation, it would not be optimal to set a retirement objective that requires inappropriate sacrifices during working life (see *2C. Maintaining standards of living in retirement*).

The system should be centred on achieving the best outcomes for individuals. Some stakeholders proposed that the retirement income system should explicitly aim to reduce the share of retirees drawing on the Age Pension.[47] This should not be an aim in itself. The system should prioritise individual outcomes above Government outcomes. If the system specifically aimed to reduce the share of retirees drawing on the Age Pension, optimal retirement outcomes would not necessarily be achieved. For example, such an objective could imply the Age Pension means tests be set so that as few people as possible would qualify. Government costs are best assessed by looking at the fiscal impact of the whole retirement income system. The proportion of the population receiving the Age Pension is only a proxy for the cost of one element of the system. While Government costs are an important consideration, they need to be considered holistically and in the context of the retirement outcomes they produce for individuals.

[45] (Australian Institute of Superannuation Trustees, 2020; AustralianSuper, 2020; First State Super, 2020b; ASFA, 2020a).
[46] (Grattan Institute, 2020).
[47] (Save Our Super, 2020; Business Council of Australia, 2020; AMP, 2020).

The roles of the Government, individuals and the private sector

Achieving the objective of the retirement income system requires involvement by the Government, individuals and the private sector. This shared responsibility is reflected in the structure of the system.

The Government

The Government has the foundational role in the system of setting retirement income policy.

The Government guarantees a minimum standard of living in the form of the Age Pension, which also helps many low- and middle-income people maintain their standard of living in retirement. In addition, the Age Pension helps insure against longevity, inflation and market risk. For many age pensioners who do not own their own home, Commonwealth Rent Assistance assists with their retirement outcomes. The Government also provides support via superannuation tax concessions.

The Government compels employees to save a portion of their income via compulsory superannuation. Some stakeholders argue this compulsion implies the Government should take primary responsibility for appropriate default settings for the disengaged and regulating superannuation savings once invested (Productivity Commission, 2018a; Minifie, et al., 2014; 2015; Financial System Inquiry, 2014).

As the custodian of policy, the Government is also responsible for ensuring retirement income policies are sustainable and cohesive.

Individuals

The Government's role (providing the Age Pension and compelling superannuation payments through the SG) could be seen to suggest that the role for individuals is limited to making voluntary savings for retirement. However, the individual's role is more substantial than this for several reasons.

Not everyone is covered by the SG. For example, self-employed people need to take a more active role in making retirement savings, particularly if they want to maintain their living standards at a level beyond what the Age Pension provides.

Individuals bear the risks of adverse market outcomes or poor investment performance. Ideally, people should take an active interest in ensuring their finances are well-positioned to manage these risks. Knowledge of the relative performance of their investments or the value of diversification can help people to achieve good retirement outcomes.

Some stakeholders argued individuals have a responsibility to take an active role in managing their superannuation in the accumulation phase, whether compulsory or voluntary.[48] Although this is desirable, it comes with many obstacles. The system is inherently complex and not all working Australians can understand complex financial products. The Productivity Commission (2018a) found a significant share of Australians either cannot or will not actively manage their superannuation. This underlines the importance of strong default settings that protect those who are unable or unwilling to engage.

Defaults can, however, encourage disengagement. Improving financial literacy and understanding of superannuation is important to allow people to take an active and informed interest in their

[48] (Business Council of Australia, 2020; Chartered Accountants Australia and New Zealand, 2020).

retirement savings. The Productivity Commission (2018a) suggested default settings be set to encourage people to make active choices while also protecting those who do not.

Individuals need to take a more active role when they retire, in particular, using accumulated superannuation balances and other savings to support their standard of living in retirement. This means people need to have the confidence to draw down their savings in retirement. In doing so, they will have to assess products that will help manage market and longevity risks. Here, the private sector plays an important role, particularly in providing financial advice, guidance and information.

The private sector

Private sector participants in the retirement income system include, most notably, employers, superannuation funds and financial advisers.

Employers are required to fulfil their obligations under the *Superannuation Guarantee (Administration) Act 1992* (or under industrial agreements in many cases) to make superannuation contributions on behalf of their employees. Some employers are also required to select a default fund for their employees. It has been recommended that this decision should rest elsewhere as employers are not optimally positioned for this role (Productivity Commission, 2018a).

Broadly, the role for **superannuation funds** is codified in legislation as acting in their members' best interests with the sole purpose of providing retirement benefits. What this means in practice has been interpreted differently by different parties (Productivity Commission, 2018a; Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry, 2019). Changes stemming from the *Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry* aim to ensure these obligations are consistently enforced by regulators.

The private sector also helps to manage risks for individuals and households. With balances at retirement continuing to grow as the superannuation system matures, greater innovation is needed to deliver retirement incomes that meet retirees' needs. The proposed Retirement Income Covenant would require **superannuation funds** to play a larger role in longevity and market risk management for members in retirement. The role of quality advice and guidance in helping individuals manage these risks will become increasing important (see *5A. Cohesion*).

The roles of the pillars

Views differ as to what constitutes the retirement income system. The terms of reference for the review refer to its three pillars: the Age Pension; compulsory superannuation; and voluntary savings, including voluntary superannuation contributions and home ownership. Several submissions suggested more pillars, ranging from work in retirement,[49] non-financial arrangements,[50] Jobseeker Allowance (formerly Newstart) for the involuntarily retired,[51] private intergenerational transfers[52] and health and long-term care.[53]

The World Bank (2008) proposes a five-pillar framework that includes social transfers in kind outside the formal pension system. Social transfers in kind are a significant factor influencing retirement outcomes. All sources of income and support that people can draw on to support their standard of living in retirement are important and should be considered.

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[49] (COTA, 2020; National Seniors Australia, 2020; Chartered Accountants Australia and New Zealand, 2020).
[50] (Chartered Accountants Australia and New Zealand, 2020).
[51] (Australian Council of Social Service, 2020).
[52] (Chartered Accountants Australia and New Zealand, 2020).
[53] (COTA, 2020; Australian Council of Social Service, 2020).

The review focused on the three pillars identified in its terms of reference. These pillars involve measures by the Government specifically aimed at supporting incomes in retirement by:

- Directly funding eligible people through the Age Pension
- Requiring people to contribute a proportion of their wages to superannuation
- Providing tax advantages to encourage voluntary contributions to superannuation

Owner-occupied housing is an important component of voluntary savings. It is supported by a range of government policies, including exemptions from much taxation and means testing. Home ownership reduces housing costs for most retirees and creates an asset that can be drawn on to supplement retirement income. For most retirees, the home is their largest form of saving (see *1B. Design of Australia's retirement income system*).

Regardless of their number, the retirement income system pillars should be well-integrated and operating coherently as a 'system'. Therefore, pillar roles are best thought of as partial and may not be clearly distinct from one another. They should not be considered in isolation. Several stakeholders echoed this sentiment.[54]

Following is an assessment of some of the factors to consider when determining each pillar's role. As mentioned above, the exact role that each pillar should play is a function of the system objective, which is ultimately for the community to endorse through the Government.

The Age Pension

The Age Pension serves two key roles:

1. Providing a safety net for those Australians who do not have the financial means to support a minimum standard of living in retirement.
2. Supplementing the retirement incomes of a large proportion of low- and middle-income retirees.

In both these roles, the Age Pension reduces income inequality in retirement (see *3A. Income and wealth distribution*). Balancing these roles revolves around the targeting of the Age Pension. Targeting could primarily aim to provide a safety net or aim to play an expanded role in supplementing the income of low- to middle-income people and help them maintain their living standards in retirement.

Determining this balance will depend on the relative effectiveness, including cost-effectiveness, of the Age Pension and the other pillars.

A safety net level of income

Stakeholders had diverse views about the level of income the Age Pension should provide. Many stakeholders suggested the Age Pension's role is poverty alleviation.[55] However, using poverty alleviation as the basis for the Age Pension is complicated by the various poverty definitions available: some are absolute budget measures, and some are relative to prevailing living standards (see *2A. Achieving a minimum standard of living in retirement*).

Previous work has suggested the safety net role of the Age Pension is *at least* poverty alleviation by some relative measure, if not to provide a standard of living somewhere above this. *The Pension Review* (2009) (the Harmer Review) suggested the role of the Age Pension is to provide a basic,

[54] (Australian Council of Trade Unions, 2020; Business Council of Australia, 2020; Ralston & Feng, 2016).
[55] (Australian Council of Social Service, 2020; AustralianSuper, 2020; COTA, 2020; Actuaries Institute, 2020).

acceptable standard of living, accounting for prevailing living standards. The Henry Review (2009) suggested the Age Pension be enough to provide a reasonable minimum standard of living.

The maximum rate of the Age Pension has been benchmarked to a given portion of different measures of wages since the early 1970s (Yeend, 2009). Ensuring the Age Pension's safety net level of income takes account of prevailing living standards is likely to be consistent with the broader community consensus.

However, there are trade-offs with the degree to which the Age Pension takes account of prevailing living standards. Set too generously, the incentives to save for retirement may be muted, and the Age Pension could jeopardise the sustainability of the system, particularly in the face of an ageing population.

The safety net has traditionally been set with reference to the needs of retirees who own their homes. Commonwealth Rent Assistance acts as a supplement to the Age Pension to improve the living standards of those who pay rent.[56]

Supplementing income

Several submissions raised the role of the Age Pension in supplementing the retirement income of lower- to middle-income earners.[57] For many lower- to middle-income Australians, their retirement income is the combination of a part Age Pension and other income sources, particularly superannuation. The Age Pension component tends to take on more importance as people age and other income sources deplete.

Many stakeholders acknowledged a role for the Age Pension in longevity and/or market risk protection.[58] This role was reaffirmed in previous reviews (Australia's Future Tax System Review, 2009; Harmer, 2009). The Age Pension provides a degree of protection against these risks. If someone lives longer than their private savings last, they will be supported by the Age Pension's safety net level of income. If someone's private assets or income are reduced, such as with a market downturn, their income will be supplemented by the Age Pension. The community may not sufficiently recognise this role of the Age Pension.

Compulsory superannuation

Stakeholders had diverse views as to the role of compulsory superannuation in the retirement income system, particularly around whether its role is to replace or supplement the Age Pension. Previous studies came to different conclusions.[59] However, there is general agreement about the need for compulsion per se.

Clarity on the role of compulsory superannuation is important so as to provide guidance for a range of policy variables, including the SG rate, the coverage of individuals who are compelled to save, the extent of tax concessions and the targeting of the Age Pension.

Important trade-offs must be managed across these policy variables. For example, the SG compels people to trade off future and current consumption (see *2C. Maintaining standards of living in retirement*), and the extent of tax concessions has sustainability implications.

[56] Age Pension supplements such as Commonwealth Rent Assistance are considered part of Pillar 1.
[57] (Australian Institute of Superannuation Trustees, 2020; Grattan Institute, 2020).
[58] (Australian Institute of Superannuation Trustees, 2020; Business Council of Australia, 2020; First State Super, 2020b; Grattan Institute, 2020; Mercer, 2020).
[59] A lot of input on the role of superannuation is about the superannuation system as a whole (the compulsory and voluntary components), whereas this discussion pertains to the role of only the compulsory component. That said, these contributions can still provide relevant insights.

Previously suggested roles of compulsory superannuation have centred on its effect on the Commonwealth Government budget (reducing Age Pension expenditure), boosting national savings and providing retirement income. Another rationale when compulsory superannuation was introduced was to reduce inflationary wage pressure present at that time.

Broadly, compulsion is typically justified on the basis that individuals or households would 'undersave' in its absence. When compulsory superannuation was introduced, it was noted that people tended to be short-sighted about providing for their own long-term needs (Fitzgerald, 1993). This behavioural, bias-based reasoning is consistent with international guidance (World Bank, 1994; 2008; OECD, 2018a).

The Government budget

When compulsory superannuation was introduced, one of its intended roles was to ease pressure on the budget in the face of an ageing population (Senate Select Committee on Superannuation, 1992; House of Representatives, 1992; The Treasury, 1991; Fitzgerald, 1993). The goal of easing pressure on Age Pension expenditure has been supported more recently by the Superannuation Charter Group (2013) and the Murray Inquiry (2014). These reports did not anticipate replacing the Age Pension.

The underlying intent of this goal relates to how the retirement income system affects the Government's overall fiscal position over time. As such, the budgetary impact of the SG is best considered not by looking at the impact of the SG on Age Pension costs alone, but at the costs across the entire system, including the cost to the budget of superannuation tax concessions.

National savings

When compulsory superannuation was introduced, increased national savings was one of the policy's explicit goals (Keating, 1991; Dawkins, 1992). Fitzgerald (1993) predicted the SG would increase annual national savings by almost 0.75 per cent of GDP over the following decade. Gruen and Soding (2011) found compulsory superannuation led to a net increase in the national private savings rate of around 1.5 per cent of GDP. Stakeholders did not suggest increased national savings currently constitutes an explicit role of compulsory superannuation.

Some submissions said that the broader economic benefits of the SG system should be recognised.

Retirement income

Providing income in retirement is the fundamental role of compulsory superannuation.

The Murray Inquiry (2014) recommended that the objective of the superannuation system should be to 'provide income in retirement to substitute or supplement the Age Pension'. This recommendation was subject to consultation and drafted into Bill form but remains unlegislated. A number of submissions on the Bill raised problems with how the objective was specified, pointing out the significant differences between 'replacing' and 'supplementing' the Age Pension. Some noted it was unrealistic to expect superannuation income to replace Age Pension income for most people (Australian Council of Social Service, 2016).

At its inception, compulsory superannuation was generally described as offering income *additional* to the Age Pension, rather than replacing it (Fitzgerald, 1993; House of Representatives, 1992; Keating, 1991; The Treasury, 1991; Dawkins, 1992). At the time, the Age Pension was expected to remain the foundation of equity and adequacy in the system (Keating, 1991). If the role of the SG is to replace the Age Pension for most people, its rate would have to be higher than if its role was to supplement the Age Pension. Fitzgerald (1993) estimated that a rate of 18 per cent would be necessary to meet this goal.

Many submissions highlighted that compulsory superannuation should not aim to be the single source of adequacy for most individuals or households,[60] and that the Age Pension will inevitably play an important role for most individuals or households. However, there were different points of emphasis, with some stakeholders suggesting:

- Compulsory superannuation, combined with the Age Pension, should provide no more income than the average standard of living during working life
- Compulsory superannuation and the Age Pension should work together to ensure a 'comfortable' standard of living

The Henry Review (2009) did not explicitly tie the purpose of compulsory superannuation to the Age Pension, instead suggesting the SG be informed by a moderate replacement rate for a typical median-income earner. Some stakeholders suggested a similar approach.[61] However, by targeting the median-income earner's replacement rate, the framing implicitly takes account of the Age Pension income that feeds into that replacement rate.

The use of median or average incomes or living standards in calibrating the role for compulsory superannuation is compelling. The SG mandates the same level of savings across the population, regardless of income, wealth or personal objectives. Studies have found a reasonably wide range of 'optimal' SG rates across the population (Warren, et al., 2020). A system that contains a range of rates depending on the person would be overly complex and almost certainly unworkable. On this basis it is appropriate the SG rate be set with regard to the circumstances of an average or median-income earner with a typical working life.

Preservation of superannuation means the SG provides only upward flexibility in personal saving rates (i.e. people can only save more, not less). Therefore, setting the SG rate too high is arguably worse than setting it too low, forcing some individuals and households to save more than would be required in retirement and compromising working-life living standards. According to the World Bank (1994), it is not unreasonable to set mandatory contributions rates slightly below a reasonable replacement rate estimate to allow for individual heterogeneity. Alternatively, loss aversion suggests that underestimating the savings needed for retirement may cause more harm than overestimating.

An individual and household adequacy outcome (one that balances the trade-offs between present and future consumption) supports the historical view of compulsory superannuation being generally supplemental to the Age Pension. In performing this role, as the superannuation system matures, compulsory superannuation will reduce reliance on the Age Pension in supporting retirement outcomes.

Voluntary savings

Voluntary savings are far more expansive than the Age Pension and compulsory superannuation. They incorporate the flexibility offered by voluntary superannuation contributions, as well as owner-occupied housing, and other investments such as property, shares or bank deposits. This diversity makes the role of voluntary savings in the retirement income system less clear.

[60] (Australian Council of Social Service, 2020; Grattan Institute, 2020).
[61] (Australian Council of Social Service, 2020).

Flexibility

Many stakeholders cited individual flexibility as a key role for voluntary savings (in particular, voluntary superannuation contributions).[62]

For those not subject to the SG, such as the self-employed, voluntary savings (and voluntary superannuation contributions in particular) take on a much more important role. When compulsory superannuation was introduced, Fitzgerald (1993) noted the justification for compelling employees to save was likely applicable to the self-employed as well. Many stakeholders suggested SG coverage should be extended to the self-employed.[63]

Flexibility provides the opportunity for some people to save more for retirement than the savings stemming from the SG, including to make 'catch-up' payments following periods out of the workforce. Some stakeholders suggested that the flexibility offered by voluntary superannuation contributions only really applies to higher-income earners.[64]

Voluntary superannuation savings are subject to concessional tax treatment. Voluntary contributions can be made from pre-tax income and are subject to concessional earnings taxation once invested. The role of tax concessions in encouraging voluntary contributions to superannuation is an important consideration, both in terms of their effectiveness (see *5A. Cohesion*) and the trade-offs associated with equity and sustainability (see *3. Equity* and *4. Sustainability*).

Housing

Housing is an important component of voluntary savings and a key determinant of retirement outcomes. Those who enter retirement with owner-occupied housing typically enjoy higher effective living standards by avoiding rental costs (including protection against rent increases) (see *2A. Achieving a minimum standard of living in retirement*). Owner-occupied housing acts as a store of capital security while being mostly exempt from the tax and transfer system (although this is arguably a broader feature of the tax system that goes beyond the retirement income system). Home ownership also serves as a source of emotional security and safety (Australia's Future Tax System Review, 2009). These roles were noted by numerous stakeholders, with some submissions suggesting an explicit objective to ensure retirees have stable and affordable housing, and others arguing owner-occupied housing should be seen as a separate pillar.[65]

Arguably, it is the *service* that owner-occupied housing provides that is most important, rather than the actual savings. If housing were a stand-alone pillar it should constitute housing services, and therefore would include rental accommodation.

Home owners also have the opportunity to access the equity in their home to supplement retirement income and manage longevity risk, although few currently do so. If this potential were realised, housing would take on an even more important role in the retirement income system.

Social transfers in kind

Social transfers in kind are not an explicit pillar of the retirement income system as laid out in the terms of reference. However, they are an important factor in influencing retirement outcomes (see

[62] (Australian Institute of Superannuation Trustees, 2020; Business Council of Australia, 2020; Actuaries Institute, 2020).
[63] (Australian Council of Trade Unions, 2020; Australian Institute of Superannuation Trustees, 2020).
[64] (Committee for Sustainable Retirement Incomes, 2020; IOOF, 2020).
[65] (Australian Institute of Superannuation Trustees, 2020; Chartered Accountants Australia and New Zealand, 2020; Australian Council of Trade Unions, 2020; Australian Housing and Urban Research Institute, 2020; National Seniors Australia, 2020; Combined Pensioners & Superannuants Association, 2020; Grattan Institute, 2020; Association of Independent Retirees, 2020; CEPAR, 2020).

2A. Achieving a minimum standard of living in retirement). All sources of income and support that people can draw on to support their standard of living in retirement are important and should be taken into account.

The World Bank's (2008) five-pillar framework for retirement income systems describes pillar four as access to informal and formal support and social programs. This acknowledges the important role social transfers in kind play in supporting effective living standards for retirees.

Some social transfers in kind are targeted based on needs, while others are universal. Social transfers in kind support adequacy by reducing retiree's living costs, and therefore boosting their effective living standards for a given level of income. The role of social transfers in kind in the retirement income system may not be sufficiently recognised in the community, or by retirees themselves (see *5A. Cohesion*).

Section 1D. The changing Australian landscape

Box 1D-1 Section summary

- **Australia's population is growing and ageing.** As at December 2019, the population was projected to increase from 26 million people in 2020 to 42 million in 2060. Projections indicate that the population aged 65 and over will increase from 16 per cent in 2020 to 22 per cent by 2060. This is a result of lower fertility rates since the 1960s, partly mitigated by net overseas migration, which has slowed population ageing. The COVID-19 Pandemic may accelerate the rate of population ageing**.**
- **Australians are living longer.** Life expectancies across all ages have increased over the past 40 years, particularly for men. Although women continue to have greater life expectancy and longevity than men, the life expectancy gap reduces with age.
- **More Australians, particularly women, are in the labour force today than 40 years ago.** Total labour force participation increased by 5 percentage points from 1980 to 2019. Female participation increased by 16 percentage points over this period, with sustained increases in participation across all ages. This increase in female participation was partly offset by lower participation among men under age 55.
- **Economic conditions have been positive for the past three decades but are uncertain in the short- to medium-term in light of the COVID-19 Pandemic.** The Australian economy has experienced sustained growth since the early 1990s. Unemployment has generally fallen during this time, remaining below its 40-year average since 2002. Real wage growth has been on average positive over the past 20 years.
- **Growth in domestic and international equity markets has been strong over the past 40 years,** although there have been sharp declines during economic shocks. Over the past decade market interest rates have fallen domestically and internationally to historic lows.
- **The superannuation system will fully mature in the 2040s when the workforce will have experienced SG rates of at least 9 per cent for 40 years**. Seven in ten Australians aged 15 and over are now covered by superannuation. Strong investment returns and increasing contributions have nearly doubled assets under management as a per cent of GDP since 2005. Superannuation is now the largest asset held by most households outside the family home.
- **Higher home and superannuation values have increased household wealth over the past 30 years.** Increases in housing wealth have benefited existing home owners. People buying a home have increasingly needed to take on greater household debt and are spending larger proportions of their working-life incomes on housing. Mortgage debt among households aged 55 and over has increased in the past 20 years.
- **Home ownership has fallen for younger and lower- to middle-income Australians over the past 40 years.** Increases in residential property prices, later workforce entry and household formation have delayed and reduced the affordability of home ownership. Ownership rates for households aged 65 and over and higher-income households have remained relatively stable.
- **Older households are increasingly renting through the private market.** Private market rental costs are generally higher than those of public housing. Overall, rates of renting by households aged 65 and over have been stable over the past 10 years. Current trends in home ownership suggest lower-income retiree households may be more likely to rent in future.

Outline of this section

This section identifies the broader demographic and economic trends that could affect the retirement income system and its ability to deliver adequate outcomes:

- Demographic trends
- Labour force trends
- Economic growth and returns on investments
- Maturity of the superannuation system
- Household wealth and debt
- Housing

Trends are generally shown over a historical 10-40-year horizon depending on available data.

Box 1D-2 COVID-19 and economic trends

To improve understanding of how the retirement income system performs over the long term, cameo and population-level modelling was used to project potential future outcomes. Such modelling exercises give a guide to the direction and magnitude of possible outcomes relative to how the system performs today. It does not predict outcomes.

Like most medium- to long-term analysis, including that presented in the Intergenerational Report (Commonwealth of Australia, 2015), the modelling focuses on medium- to long-term trends in the economy rather than short-run fluctuations. A wide range of short-term factors, such as business cycles, and labour market and financial market shocks, will affect the actual path of Australia's economy to 2060.

Short-term factors should not materially affect the analysis of very long-term outcomes. They may, however, result in substantial short-run deviations from the long-term trends. The full extent of COVID-19's effect on the Australian and global economies is not reflected in the long-term trends outlined in this chapter. For example, the COVID-19 Pandemic is expected to result in below-trend economic growth, participation rates, wage growth and population growth in Australia in 2020-21. The OECD has projected a global economic recession (OECD, 2020a). The effects of these deviations may continue to be felt for some time with decreasing severity. Short-term shocks can have large effects on superannuation balances. The short-term effects of market volatility for people in or nearing retirement are explored in *2C. Maintaining standards of living in retirement*.

Economic outcomes over the medium- to long-term are driven by factors such as population growth, labour force participation and productivity. The analysis and long-term projections in this report incorporate assumptions for these variables based on trends over the past 40 years. This incorporates periods of slower and faster economic growth, including the GFC in 2008-09.

The modelling framework underpinning this report (and Intergenerational Reports) takes into account long-run averages of key macroeconomic variables to model long-term changes in the structure of the Australian population and labour force over the coming decades. Although the economic impacts of COVID-19 were beginning to be observed during the course of the review, the full effects and any long-term economic consequences will not be known for some time. Predicting the economic impacts of a pandemic is difficult and outside the scope of this report.

Given this uncertainty, this report includes sensitivity analysis to assess the potential impact of deviations from the assumed long-term trends. For example, *2C. Maintaining standards of living in retirement* and *4. Sustainability* assess the effects of negative short-term shocks to wage growth and investment returns on outcomes for individuals and to the cost and performance of the system.

Modelling has been used to illustrate how policy outcomes over a long period may be affected by policy settings. A range of scenarios was explored and outcomes compared with a modelled baseline (see *2C. Maintaining standards of living in retirement* and *4. Sustainability)*. If the relationships between trends underpinning the modelling framework remain largely unchanged, the effect is not expected to be sensitive to economic shocks. Any short-term shocks would affect both the baseline and the policy lever scenarios.

Details of the models and modelling approaches used in this report are included in *Appendix 6A. Detailed modelling methods and assumptions*.

Box 1D-3 Stakeholder views on broad trends that affect the retirement income system

Stakeholders identified the ageing population as the prominent trend affecting the retirement income system, noting this impact has been moderated due to sustained migration. This places Australia in a better situation than other countries facing the challenges of an ageing population, with improved life expectancy and health outcomes for older people increasing demand for aged care services.

The intersection of the ageing population and the maturing superannuation system was noted. As people live longer and superannuation balances increase, it was emphasised that the system will need to mitigate longevity and sequencing risks.

Stakeholders commented on the impact the ageing population will have on broader economic trends. An ageing population may lead to lower productivity growth and economic growth because older people tend to be more risk-averse and take on less entrepreneurial risks than younger people.

Stakeholders identified a number of trends affecting women and their outcomes under the retirement income system. These included increasing longevity, rates of divorce, homelessness and the prevalence of renting in retirement.

Stakeholders suggested historical trends in home ownership may not continue. Many cited declining ownership among younger Australians, suggesting more retirees will be renting and paying mortgages in future. The insecurity of tenure associated with renting was of concern to stakeholders, who noted lower-income earners and women were at particular risk. Stakeholders noted retirement income system policy settings were often designed on the assumption that a retiree owns their home outright. They cautioned that current policy settings and emerging home ownership trends would lead to future adequacy and equity challenges.

Stakeholders identified significant changes in the labour market affecting the retirement income system's ability to support Australians in retirement, including:

- Improvements in technology and health reducing the physical demands of some positions and allowing people to work longer
- Increases in flexible employment arrangements such as part-time, casual and 'gig economy' workers
- Rising participation rates for the women and those aged 55 and over
- Lower wages growth
- High youth unemployment

Lower SG coverage, barriers to workforce participation and inability to save were some of the concerns raised around these changes.

Climate change was identified as an emerging trend that would affect the retirement income system. Stakeholders suggested climate change would likely increase the cost of living, negatively affecting retirees who were unable to absorb higher costs. However, as these impacts are difficult to quantify, the impacts of climate change have not been assessed.

Demographic trends

Demographic trends affect the sustainability of the retirement income system because they determine the number of people the system needs to support. Australia's ageing population means the retirement income system must support more people for longer periods. This is explored in *4. Sustainability*.

Population size and distribution

The size and age distribution of the population influences the demand for government services and support, and the capacity of the workforce to fund government expenditure through taxation.

Increases in the proportion of the population aged 65 and over may lead to rising government expenditure on the Age Pension, health care and aged care services, despite a possibly shrinking workforce.

As at December 2019, Australia's population was projected to increase from an estimated 25.8 million in 2020 to 42.2 million in 2060.[66] The number and proportion of older Australians to the total population is also projected to increase (Table 1D-1).

Table 1D-1 Actual and projected number of Australians aged 65 and over

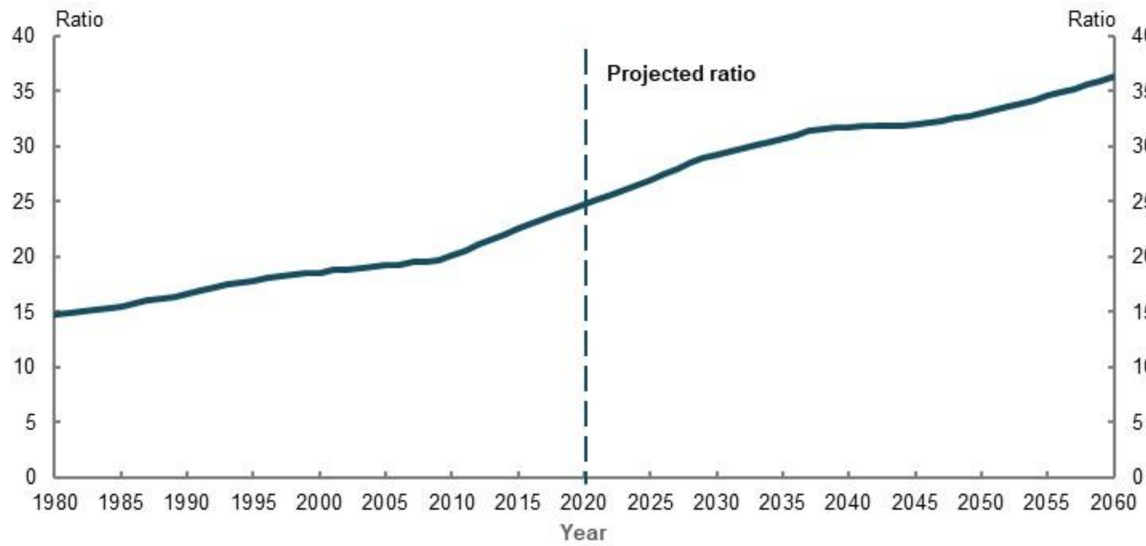
	Number (millions)					Portion of population (per cent)				
	1980	2000	2020	2040	2060	1980	2000	2020	2040	2060
Aged 65 and over	1.4	2.4	4.2	6.7	9.3	9.6	12.4	16.1	19.7	22.0
Aged 75 and over	0.5	1.1	1.8	3.7	5.1	3.4	5.6	7.0	10.8	12.2
Aged 85 and over	0.1	0.3	0.5	1.2	2.1	0.7	1.3	2.0	3.6	4.9

Source: Analysis of (ABS, 2019c), population projections by Centre for Population, The Treasury as at December 2019.

Declining fertility rates have contributed to Australia's ageing population. Since its peak of 3.5 births per woman in 1961, the fertility rate has declined, falling below the replacement rate of 2.1 after 1975 (ABS, 2019c). Fertility rates are projected to continue to stay below the replacement rate (ABS, 2018g). In 2018, the fertility rate was 1.7 (ABS, 2019e). Net overseas migration has helped to offset the growing proportion of older Australians, as migrants are generally of working age (ABS, 2020m).

The generation born while the fertility rate was high represents a larger portion of the population compared with other generations, contributing to the ageing population. From 2010, as this generation started reaching age 65, the old-age dependency ratio began rising steeply (Chart 1D-1). From 2030, the ratio was projected to grow more slowly as subsequent generations are smaller in size.

Chart 1D-1 Actual and projected old-age dependency ratio



Note: The old-age dependency ratio represents the number of people aged 65 and over per 100 working-age (15-64) people.
Source: Analysis of (ABS, 2019c), population projections by Centre for Population, The Treasury as at December 2019.

[66] Population projections by Centre for Population, The Treasury as at December 2019.

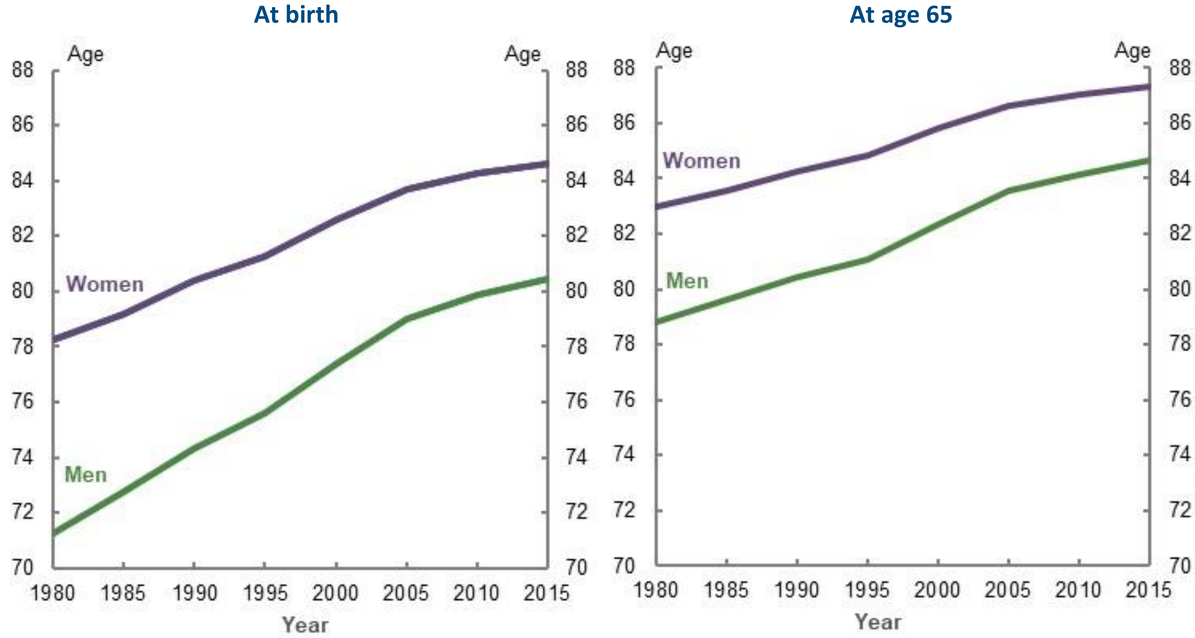
These projections do not account for possible short- to medium-term demographic changes associated with the COVID-19 Pandemic. There may be a significant fall in net overseas migration during 2019-2021 (Prime Minister of Australia, 2020), which could see the old-age dependency ratio increase more sharply over this period. There may also be a further short-term decline in the fertility rate.

Life expectancy and longevity

Improvements in longevity and life expectancy mean people spend more time in retirement if working lives are not similarly extended. As a consequence, retirement incomes need to last longer. *2C. Maintaining standards of living in retirement* and *4. Sustainability* explore these issues.

Over the past 40 years, life expectancy has increased significantly. Women continue to have longer life expectancy than men, despite the gap closing over time and reducing with age (Chart 1D-2).

Chart 1D-2 Life expectancy



Note: Years at age 65 represents total expected years of life, not just expected years remaining. Source: (ABS, 2019c).

Aboriginal and Torres Strait Islander people have lower life expectancies than the total population. This affects their outcomes in the retirement income system. Aboriginal and Torres Strait Islander demographics and outcomes are explored in greater detail in *3F. Aboriginal and Torres Strait Islander people*.

Life expectancies are a measure of the average number of years someone could be expected to live (Australian Government Actuary, 2019, p. 10). They show a simple *probability* of longevity, not *actual* longevity. Projected cohort life expectancies factor in long-term trends in improvements to mortality rates, but they cannot capture unforeseen future changes in living conditions and technology that may extend longevity.

Life expectancies are also unable to provide information on the diversity of longevity outcomes (Australian Government Actuary, 2014, p. 12). Factors such as lifestyle, health and disability status, technology and exposure to hazardous events all affect how long people live. As a result, a significant proportion of the population lives beyond life expectancy (Table 1D-2).

Table 1D-2 Longevity for those born in 1932-34

	Total life expectancy at birth (years)	Total life expectancy at age 65 (years)	Per cent who lived to at least life expectancy at birth	Per cent who lived to at least life expectancy at age 65
Women	68	86	88.8	*
Men	64	82	84.4	56.6

Note: Total life expectancy is rounded up to nearest whole year. *Cohort has not reached life expectancy yet. In 2015-17, 67.1 per cent of these women had reached age 83. Source: Analysis of (ABS, 2019c).

Over the past 40 years, average lifespans have increased, particularly for men as a result of improvements in health outcomes and workplace safety. The proportion of men who live to 65 years increased at more than twice the rate of women from 1980 to 2015. This means men are now more likely to reach retirement age than in the past (ABS, 2019c).

Women still generally live longer than men. In 2015, approximately 61 per cent of women born in 1930 lived to 85 years, compared with 46.5 per cent of men (Australian Government Actuary, 2019). Variances in longevity affect outcomes across genders, as explored in greater detail in *3B. Gender and partnered status*.

Increased life expectancies and longevity are correlated with other lifetime trends. The median age people achieve milestones, such as finishing education, entering and leaving the workforce, home ownership and marriage, is higher than it was 50 years ago (CEPAR, 2019, p. 9).

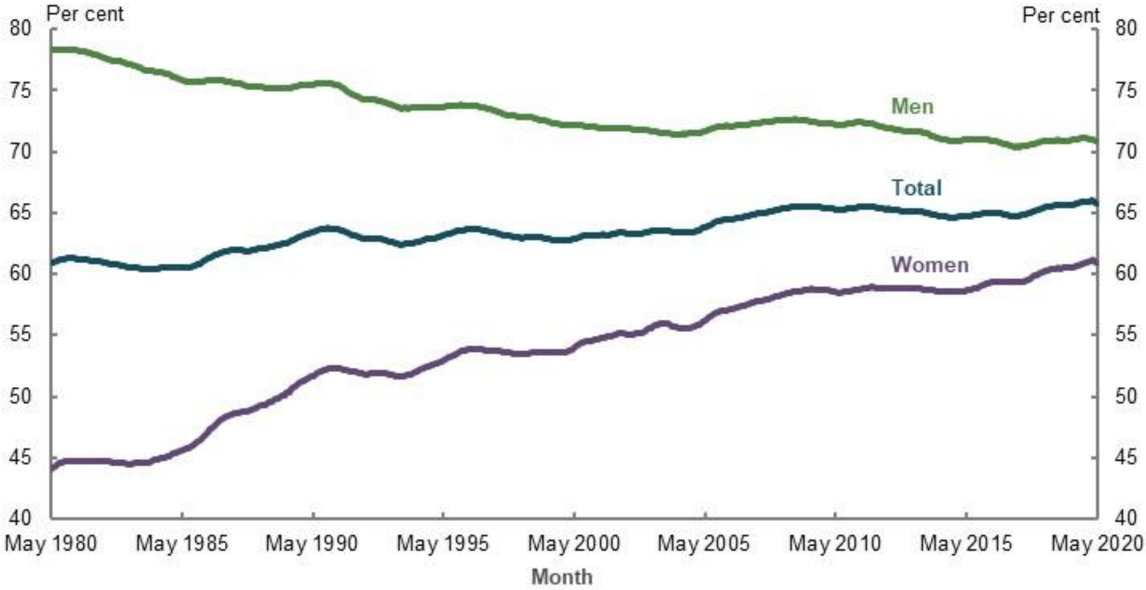
Labour force trends

The retirement income system's performance is directly related to labour force trends. As employers pay the SG, higher levels of workforce participation generally lead to greater superannuation coverage and higher superannuation balances at retirement. Greater superannuation coverage reduces reliance on the Age Pension. This reduces Age Pension expenditure but increases superannuation tax concessions.

General labour force trends

Total labour force participation has increased from around 61 per cent in 1980 to a high of around 66 per cent in early 2020 (ABS, 2020k). The increase is due to greater female participation, partly offset by lower male participation (Chart 1D-3).

Chart 1D-3 Total labour force participation rate, by gender

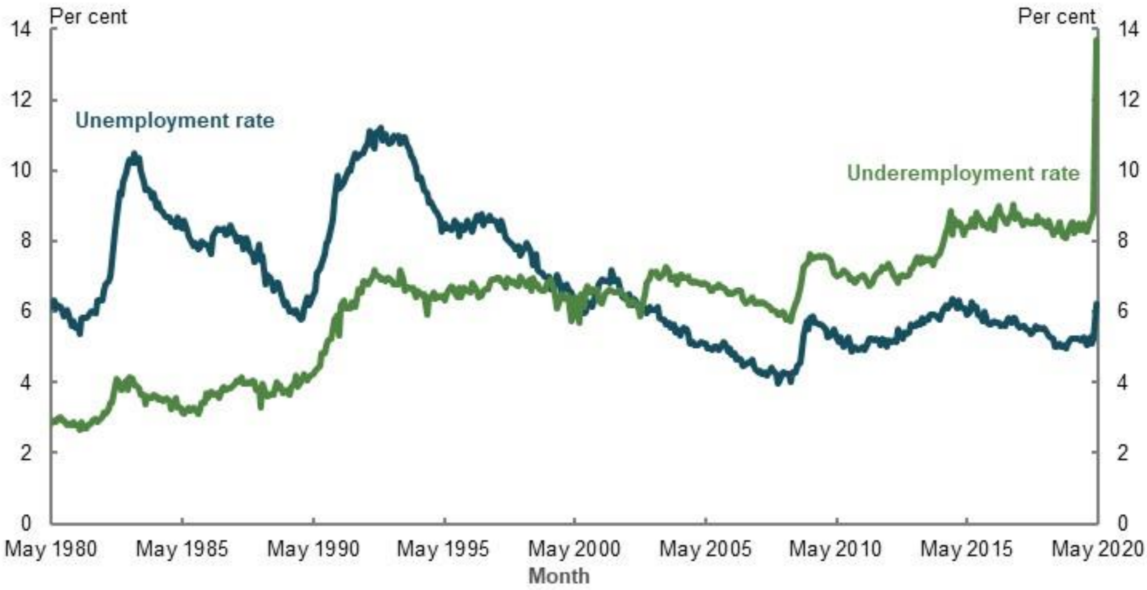


Note: Rolling 12-month average. Source: Analysis of (ABS, 2020k).

Changes to the societal role of women, flexible working arrangements and childcare access have likely contributed to greater female participation. Women are more likely than men to participate in education (ABS, 2019j), suggesting female participation rates may continue to converge on male rates in future. Differences in male and female workforce participation leads to different outcomes during retirement. These effects are explored in more detail in *3B. Gender and partnered status*.

Labour force participation represents the pool of *potential* workers — not the pool of *actual* workers. Employment rates affect the retirement income system's sustainability and outcomes. Over the past 40 years, unemployment has averaged 6.8 per cent (Chart 1D-4). Over the same period, underemployment has averaged 6.2 per cent, despite being persistently above this average since the early 1990s (ABS, 2020k). How long it may take for the unemployment and underemployment rates to fall following the COVID-19 Pandemic is uncertain.

Chart 1D-4 Historical unemployment and underemployment rates



Source: (ABS, 2020k).

Labour force trends across age groups

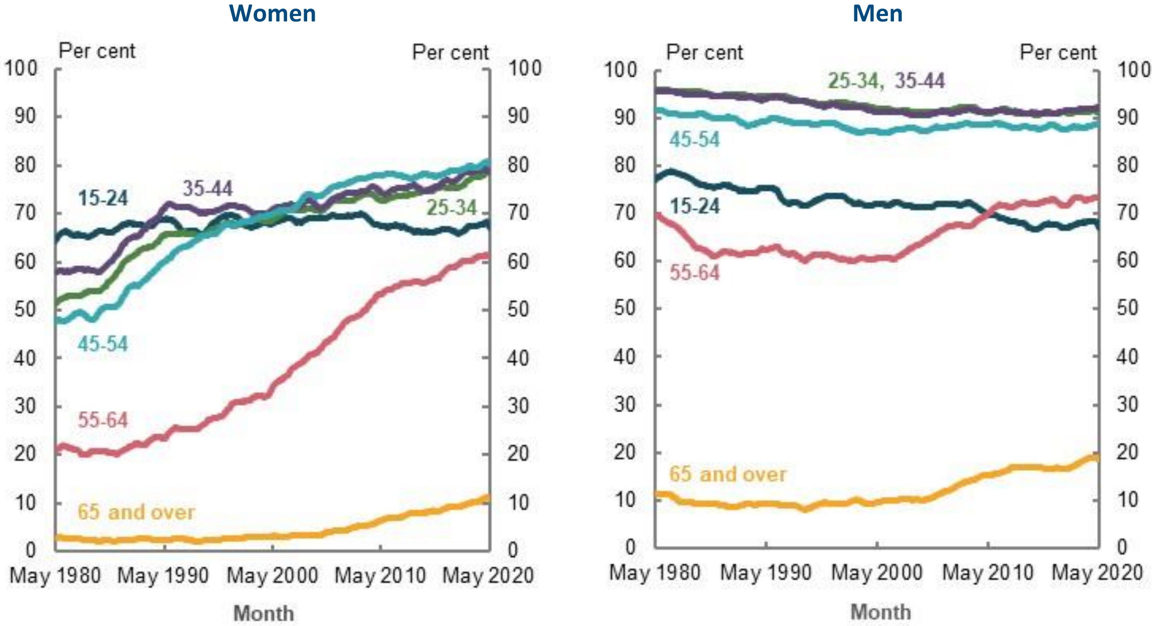
Improved health outcomes, greater flexibility in working arrangements and increasing rates of education, especially for women, have likely increased older people's labour force participation (Chart 1D-5). Increasing household debt and the later age people pay it off may also be behind this increased participation (discussed under *Household wealth and debt*, below).

Retirement income system policy settings are strongly correlated with labour force participation. As the women's Age Pension eligibility age rose from 60 in 1995 to 66 in 2019, the peak age for women leaving the labour force shifted in parallel, from 63 to 65 between 2006 and 2016 (ABS, 2006a; ABS, 2011a). Over the same period, the men's peak was maintained at 65 years — the men's Age Pension eligibility age. Increasing labour force participation among older Australians may continue as the Age Pension eligibility age rises to 67 on 1 July 2023.

Participation rates of men and women aged 15-24 are now similar. As the number of jobs requiring formal qualifications has increased, time spent studying means younger generations are entering the workforce at older ages than in the past. The median age for completing education has increased from 17 in 1981, to 22 in 2016 (CEPAR, 2019, p. 10).

The median age of people entering full-time employment has increased more quickly than the median age of exiting the labour force (CEPAR, 2019, p. 9), reflecting generational differences in working lives. People who have delayed their workforce entry may delay their exit from the workforce in future. However, if they do not, they will spend less time working and more in retirement. How shorter and interrupted working lives affect retirement outcomes is explored in *2C. Maintaining standards of living in retirement* and *3E. Age of retirement*.

Chart 1D-5 Labour force participation, by age



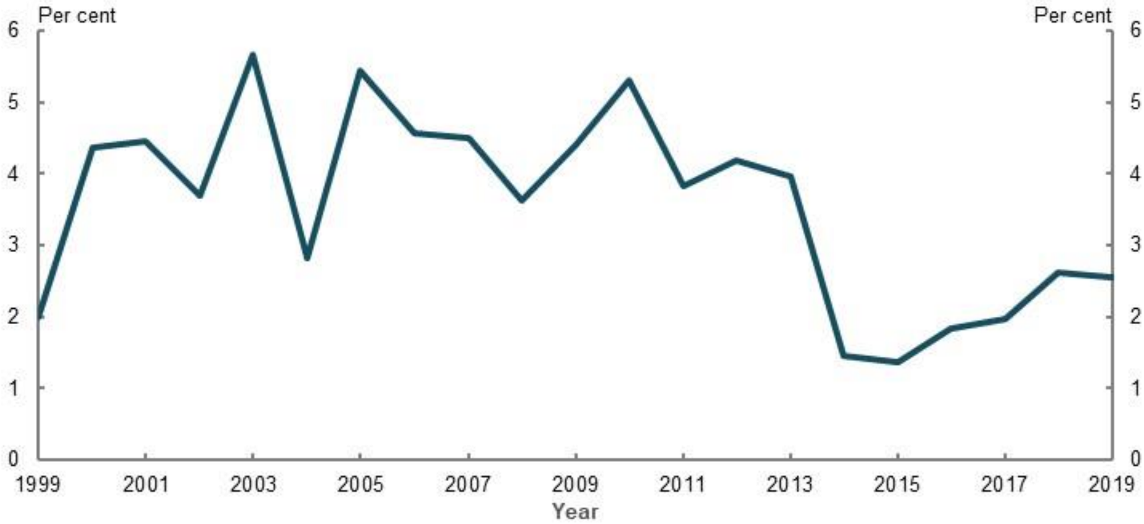
Note: Rolling 12-month average. Source: Analysis of (ABS, 2020k).

Wage growth

Wage growth affects the outcomes and sustainability of the retirement income system. Real wage growth boosts savings capacity and higher superannuation contributions, increasing superannuation balances.

Over the past 20 years, annual nominal growth in average weekly earnings averaged 3.7 per cent (1.0 per cent real) but only 2.8 per cent (0.7 per cent real) over the past ten years since the end of the GFC (Chart 1D-6). A number of factors have weighed on wage growth, with possible causes including reduced rates of job switching and changing market conditions, with lower growth noted in other developed economies (Andrews, et al., 2019).

Chart 1D-6 Average annual growth in average weekly earnings



Note: Change in nominal average weekly earnings. Source: (ABS, 2020d).

In the long term, real wage growth is driven by productivity. Over the past decade, productivity growth has fallen from its long-term average of 1.7 per cent to an average of 1.2 per cent, partly because of low capital investment (Productivity Commission, 2019a, pp. 3-9).

The possible effects of sustained lower wage growth on the retirement income system and its outcomes are explored in *2C. Maintaining standards of living in retirement* and *4. Sustainability*.

Economic growth and returns on investments

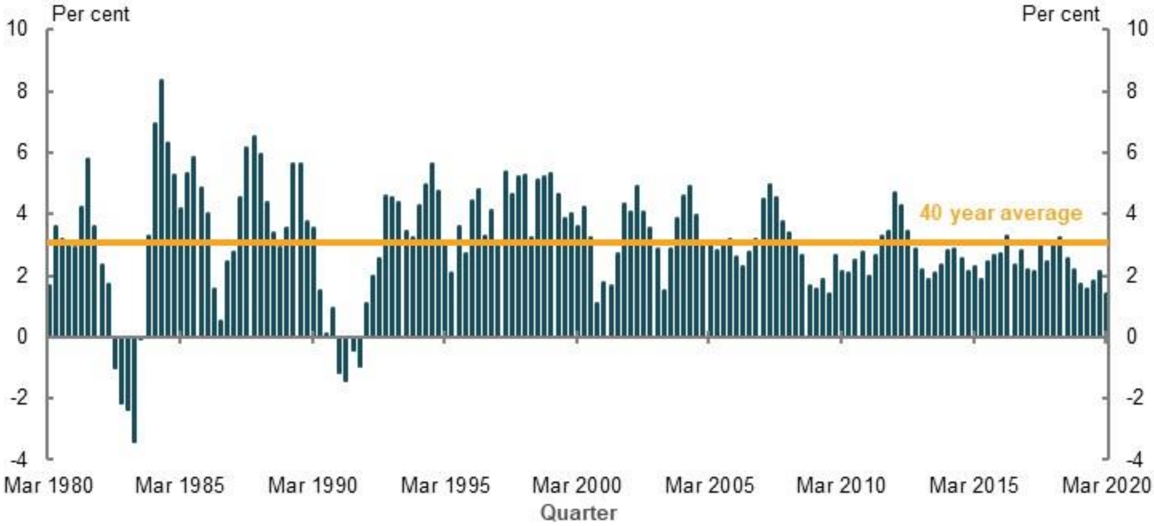
Economic growth and returns on investments heavily influence the retirement income system's sustainability and outcomes.

Economic growth

Economic growth generally leads to higher superannuation coverage through greater employment. It also influences the Government's ability to maintain spending on the Age Pension.

Australia's real GDP growth has averaged 3.1 per cent over the past 40 years (Chart 1D-7). Negative economic growth during the early 1980s and 1990s coincided with global recessions. Since 2010, the economy has been growing below the long-term trend. The effect of the COVID-19 Pandemic on global economic growth remains uncertain, with some suggestions of a global recession (OECD, 2020a).

Chart 1D-7 Annual through the year real GDP growth



Note: Per cent growth rate through the year. Average 40 year growth rate calculated using compound average growth rate.
Source: Analysis of (ABS, 2020b).

Return on investments

Economic growth, market interest rates and movements in equity markets influence investment returns, which affect the value of superannuation and voluntary savings.

Higher investment returns increase the value of superannuation and voluntary savings more quickly. This generally lowers reliance on the Age Pension. Conversely, the value of savings increases more slowly during periods of lower returns, increasing or maintaining reliance on the Age Pension.

Equities have grown strongly over the past 40 years (Chart 1D-8), but experience volatility and potential decline during economic shocks, such as the GFC and the COVID-19 Pandemic. Superannuation funds are heavily invested in equities, holding an estimated 35 per cent of the total market capitalisation of the Australian Stock Exchange (ASX). On current trends, this will increase to more than 60 per cent in 2038 (Deloitte Actuaries & Consultants, 2019, p. 18).

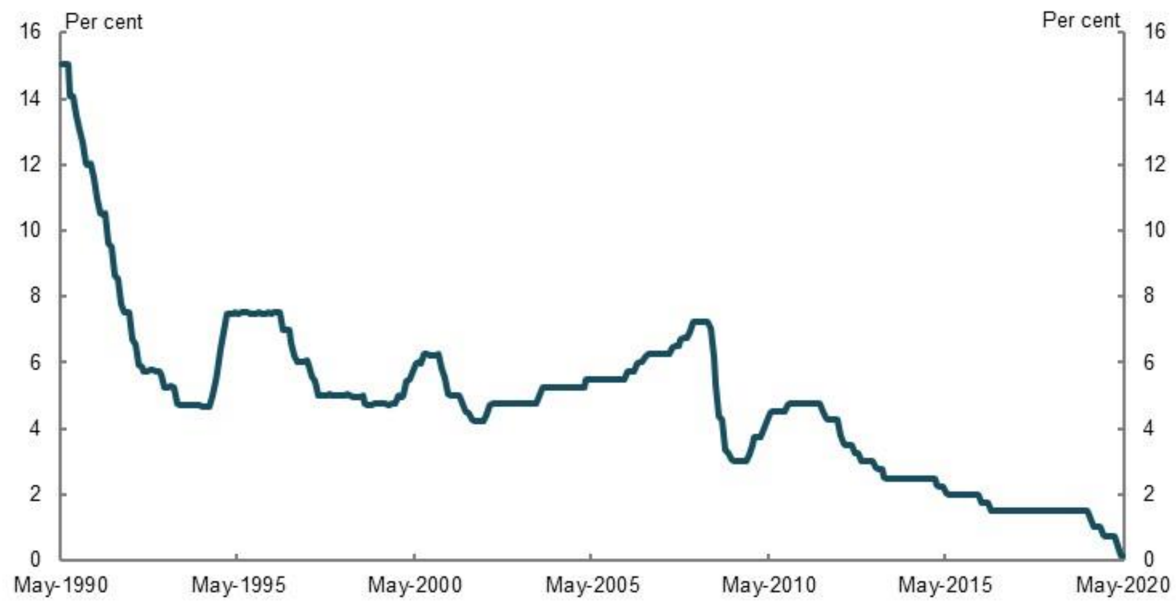
The effect of these investments on the superannuation system is discussed under *Maturity of the superannuation system* below.

Chart 1D-8 Equity market indices

Note: Indices to log scale, end May 1980 = 100. The All Ordinaries Index is made up of the largest 500 companies as measured by market capitalisation that are listed on the ASX. The MSCI World Index represents approximately 85 per cent of the free float-adjusted market capitalisation of 23 developed markets. Source: Analysis of (Bloomberg L.P., 2020).

Market interest rates influence the returns on generally low-risk, fixed-interest investments, such as term deposits. Interest rates are currently at historic lows, both in Australia and globally. The RBA cash rate target has fallen from 4.75 per cent in November 2010 to a record low of 0.25 per cent in March 2020 (Chart 1D-9). As a result, investors holding fixed-interest investments have seen investment returns decline and risk-averse retirees, who rely on these investments for income, have received lower incomes.

Chart 1D-9 Monthly interbank overnight cash rate



Source: (RBA, 2020c).

Interest rates in developed economies have steadily fallen since the 1980s (Negro, et al., 2018). These lower rates are the result of increased global savings brought on by weaker investment, demographic changes and debt repayment (House of Representatives, 2019).

From March 2020, the RBA has begun purchasing government bonds to further reduce market interest rates (RBA, 2020d). This suggests interest rates may remain relatively low for the foreseeable future.

Low interest rates mean lower returns on fixed-interest investments, such as term deposits, but not necessarily lower returns on overall savings. Superannuation funds and people may respond to lower interest rates by investing more in higher yielding assets, such as equities and property.

The effect of persistently lower or negative overall returns on investments on the system and its outcomes are explored further in *2C. Maintaining standards of living in retirement* and *4. Sustainability*.

Maturity of the superannuation system

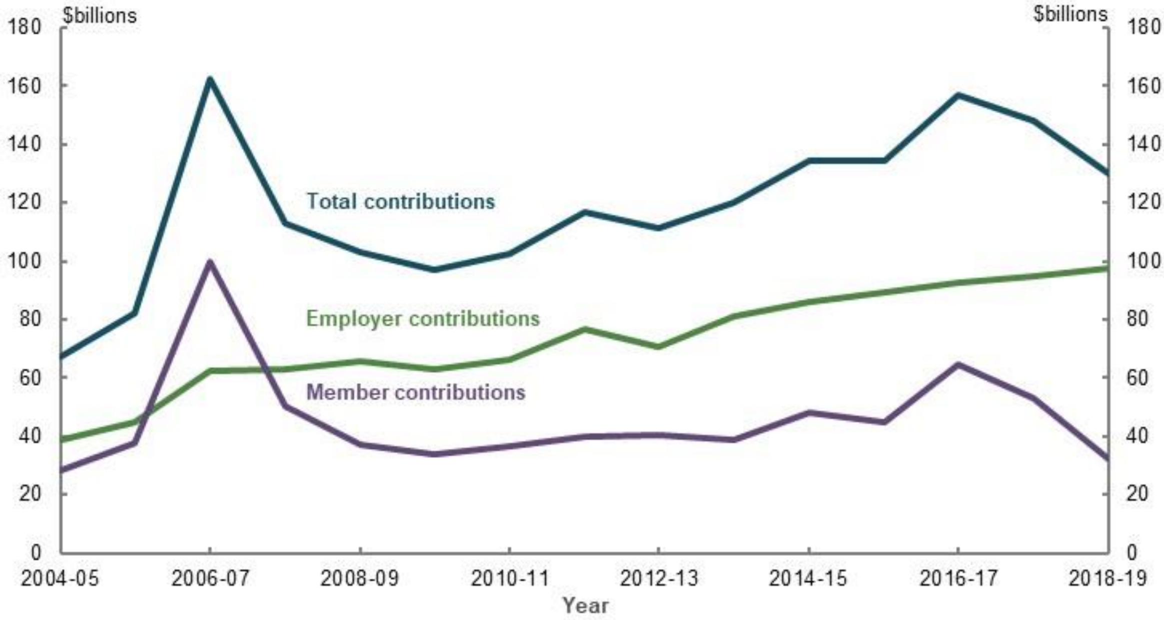
The maturity of the superannuation system influences the level of assets people hold when they reach retirement and how much they rely on the Age Pension. Australia's superannuation system will have matured by the 2040s, when the SG will have been at least 9 per cent for 40 years (the average length of a working life — see *2C. Maintaining standards of living in retirement*). Most people entering retirement over the past five years have only had around 20 years of superannuation accumulating at relatively low rates.

Compulsory superannuation was introduced in 1992 through the SG, expanding superannuation coverage from those working in professional, government and executive positions to a much broader range of employees. Superannuation coverage[67] for those aged 15 and over rose from 63.9 per cent in 2003-04 to 71.9 per cent in 2017-18 (ABS, 2019k). Superannuation coverage is explored further in *3D. SG coverage*.

In 1992, the SG rate was set at 3 per cent, increasing over time to 9.5 per cent from 1 July 2014. Total contributions made to superannuation accounts increased from $67 billion in 2004-05 to $130 billion in 2018-19 (Australian Prudential Regulation Authority, 2020a). Member contributions spiked in 2006-07, coinciding with policy reform announcements, which included a one-off opportunity to contribute up to $1 million to superannuation in some situations (Chart 1D-10). The spike in 2016-17 and subsequent decline reflects the impact of changes to tighten contributions caps that took effect from 1 July 2017. Growth in wages and the SG rate have increased the share of employer contributions relative to total contributions from 58 per cent in 2004-05, to 75 per cent in 2018-19.

[67] Defined as 'having a superannuation balance above zero, receiving regular income from superannuation, or having received a lump-sum superannuation payment in the last two years'.

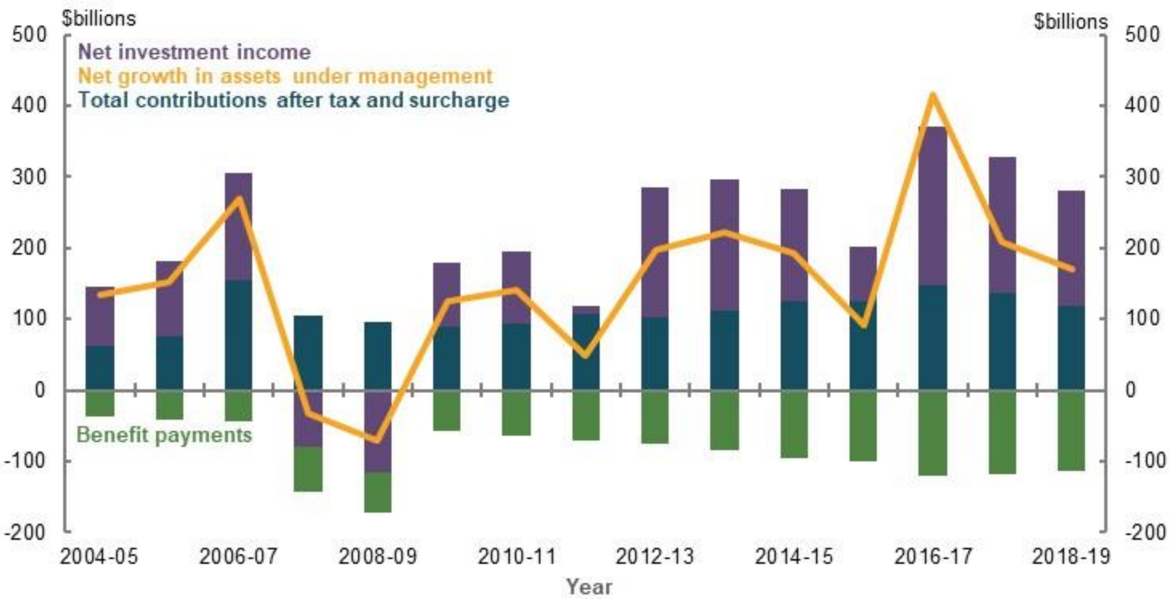
Chart 1D-10 Annual superannuation contributions, by contribution type



Note: Employer contribution represents contributions made by an employer on behalf of the member. Includes SG, award or other obligations; salary sacrifice arrangements; transfers from consolidated revenue funds for exempt public sector superannuation schemes and constitutionally protected funds; and SG charge and the taxable component of any super holding accounts special account amounts that the ATO transferred to the provider on behalf of the member. Member contributions represents contributions made by a member including non-excluded capital gains or capital proceeds and personal injury payments, direct termination payments, other third party contributions (government contributions and other family and friend contributions) and other contributions made by a person other than the employer. Total contributions represents employer and member contributions. Values are in nominal dollars. Source: (Australian Prudential Regulation Authority, 2020a).

Assets under management have grown from $750.5 billion in June 2005 (81 per cent of GDP) to nearly $2.9 trillion in June 2019 (148 per cent of GDP) (Australian Prudential Regulation Authority, 2020a). Strong investment returns and total contributions after tax and surcharge added nearly $3.2 trillion over the period, partially offset by benefit payments (Chart 1D-11).

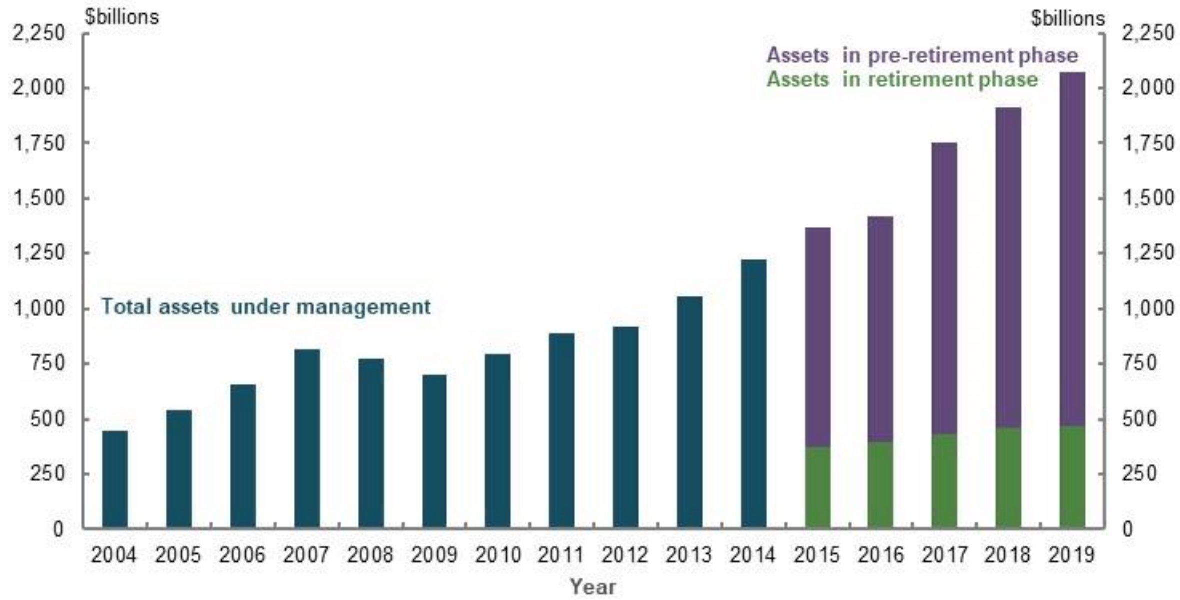
Chart 1D-11 Growth in assets under management, by flow type



Note: Total contributions after tax and surcharge represents total contributions less tax expenses relating to taxable contributions made to the superannuation entity and contributions surcharge tax. See note in Chart 1D-10 for more information on how total contributions is calculated. Net investment income represents gross revenue in the form of income or distributions from investments, including interest, dividends, rental income, trust distributions, less expenses that relate to the investment of the assets of the entity, including expenses for which investment fees are charged and expenses associated with generating income on investments. Benefit payments includes lump-sum benefit payments and pension benefits paid directly to members, but excludes rollovers and successor fund transfers. Net growth in assets under management is the figure published by APRA and may include items and amounts not represented in the other chart series. Values are in nominal dollars. Source: Analysis of (Australian Prudential Regulation Authority, 2020a).

Most of the growth in assets under management occurs in the pre-retirement phase. Assets held in the pre-retirement phase by institutional funds rose from $992 billion in 2015 to $1,600 billion in 2019 (Chart 1D-12). Assets in the retirement phase by institutional funds increased more slowly, from $374 billion in 2015 to $472 billion in 2019.

Chart 1D-12 Allocation of assets under management by institutional funds, at June year-end



Note: Data excludes SMSFs and only includes entities with more than four members. APRA commenced collecting retirement phase data from June year-ending 2015. Values are in nominal dollars. Source: Analysis of (Australian Prudential Regulation Authority, 2020a).

Future projections of the superannuation system and its effects on Age Pension expenditure are explored in *4. Sustainability*.

Household wealth and debt

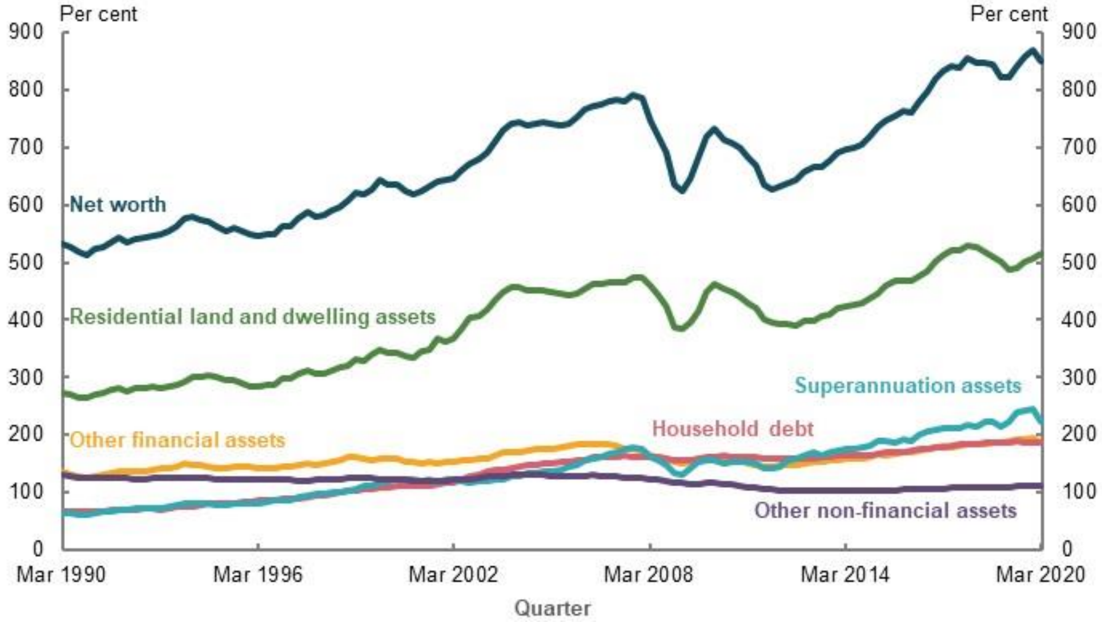
The size and composition of household wealth influences retirement incomes. Households with more financial assets at retirement are generally less likely to rely on the Age Pension for retirement income. Less liquid wealth, such as housing, can also support people in retirement, providing accommodation as well as a potential source of income.

However, if households are diverting their income to pay down large mortgage debts, they could struggle to build retirement savings outside the home. This could delay when some households retire.

Australian household net wealth has increased over the past 30 years (Chart 1D-13). Most of the increase can be attributed to growth in the value of housing and superannuation, with superannuation asset values as a percentage of household disposable income more than tripling over this period. In 2017-18, on average, the family home continued to be a household's largest asset in dollar terms, followed by superannuation (ABS, 2019k).

Growth in the value of these assets is uncertain in the short- to medium-term because of the lower economic and population growth and higher unemployment caused by the COVID-19 Pandemic.

Chart 1D-13 Household wealth as a percentage of disposable income



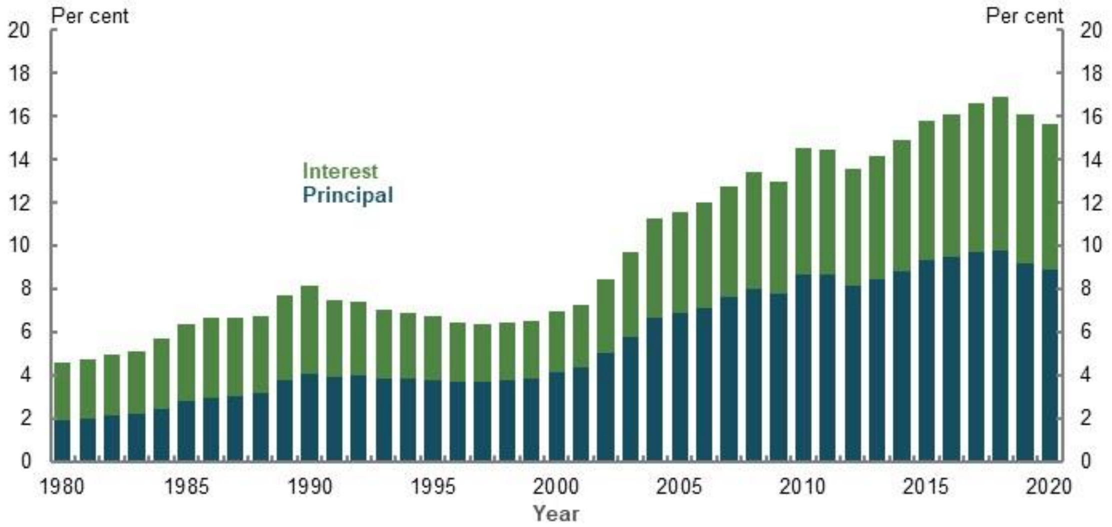
Note: Income is annualised gross disposable income before the deduction of interest payments. Net worth is all household assets series less household debt. Includes debt and assets held by unincorporated enterprises. Non-financial assets includes consumer durables. Residential land and dwelling assets includes all residential property, not just owner-occupied. Source: Analysis of (ABS, 2020a; ABS, 2020b).

Housing wealth

The value of housing has significantly increased since the 1990s, nearly doubling relative to household disposable income. Existing home owners have benefited from increases in their net worth.

However, the share of working-life income required to service a mortgage has more than tripled since 1980 (Chart 1D-14). Increases in home values mean prospective home owners need to spend more of their working-life incomes to finance their purchase. As a result, people have less income available to either spend during working life or invest in other savings vehicles.

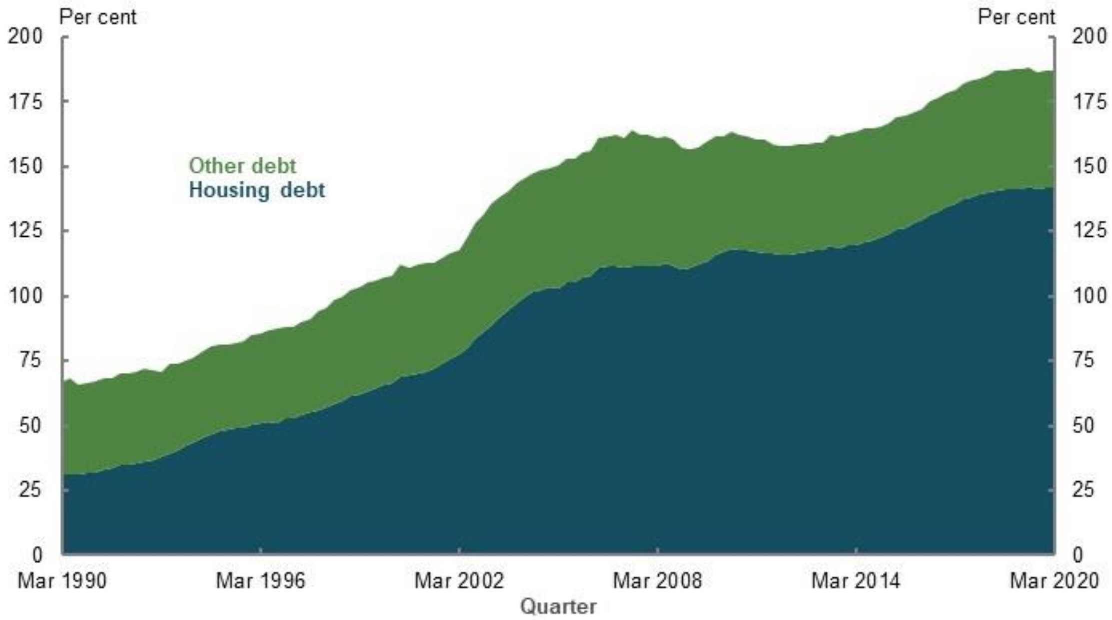
Chart 1D-14 Total home deposit and mortgage costs as a percentage of household working-life income



Note: This chart is a hypothetical comparison between different generations of households with the median income, who pay 20% deposit and service a 25-year mortgage for a median-value dwelling at the market variable rate. Working-life income is calculated post-tax, and assumes a 40-year period (ages 27-66). Analysis factors in deferral of first home purchase for recent generations. Analysis also assumes interest rates and wages move to a long-run average consistent with cameo modelling undertaken for the review. More information on these assumptions can be found in *Appendix 6A. Detailed modelling methods and assumptions.* Source: Analysis of (ABS, 2019c), (ABS, 2019k), (CEPAR, 2019), (ABS, 2020c), CoreLogic home price data and RBA Statistical Tables — Indicator Lending Rates F5.

Increased home values have coincided with rising housing debt. Household debt is now at historically high levels, mainly relating to increases in housing debt (Chart 1D-15) (RBA, 2020a). Studies note a correlation between increased national net household debt and pension assets as a per cent of GDP (Mercer, 2019b, p. 10). Increasing superannuation wealth, particularly as a result of the SG, may be increasing households' confidence about their finances and wealth, encouraging them to take on more debt as net wealth rises (Ruthbah & Pham, 2020a, p. 27).

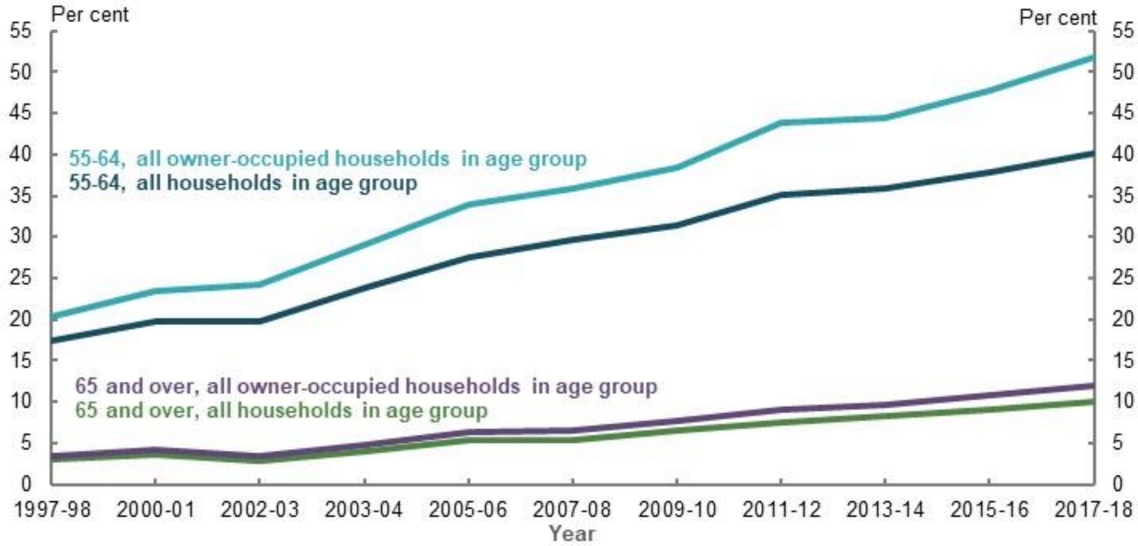
Chart 1D-15 Household debt as a percentage of disposable income



Note: Income is annualised gross disposable income before the deduction of interest payments. Other debt includes personal debt, student loans and other household liabilities. Includes debt owed by unincorporated enterprises. Housing debt includes all debt financing for residential property, not just owner-occupied. Source: Analysis of (ABS, 2020a; ABS, 2020b).

Increasing mortgage commitments have coincided with more owner-occupied households holding a mortgage at older ages. The median age for paying off a mortgage increased from 52 in 1981 to 62 in 2016 (CEPAR, 2019, p. 9). The rate of owner-occupied households aged 55 and over with mortgage debt has increased over the past 20 years (Chart 1D-16).

Chart 1D-16 Percentage of owner-occupied households with mortgage debt, by age group



Note: Age refers to age of household reference person. Series was conducted continuously by the ABS from 1994-95 to 1997-98, and then in 1999-2000, 2000-01 and 2002-03. From 2003-04 the series has been conducted every two years. Source: Analysis of Housing Occupancy and Costs 1997-98 to 2017-2018 (ABS, 2019n).

Indebtedness increases the likelihood of labour market participation (Belkar, et al., 2007), meaning households with mortgage debt at older ages are more likely to continue working.

Older owner-occupied households with mortgage debt are more vulnerable to negative economic and market shocks, especially if they retire. Declines in income or asset values could impede their ability to service mortgage repayments and push some households into financial hardship. The effects of wealth and debt on outcomes for retired households are explored further in *2C. Maintaining standards of living in retirement.*

Housing

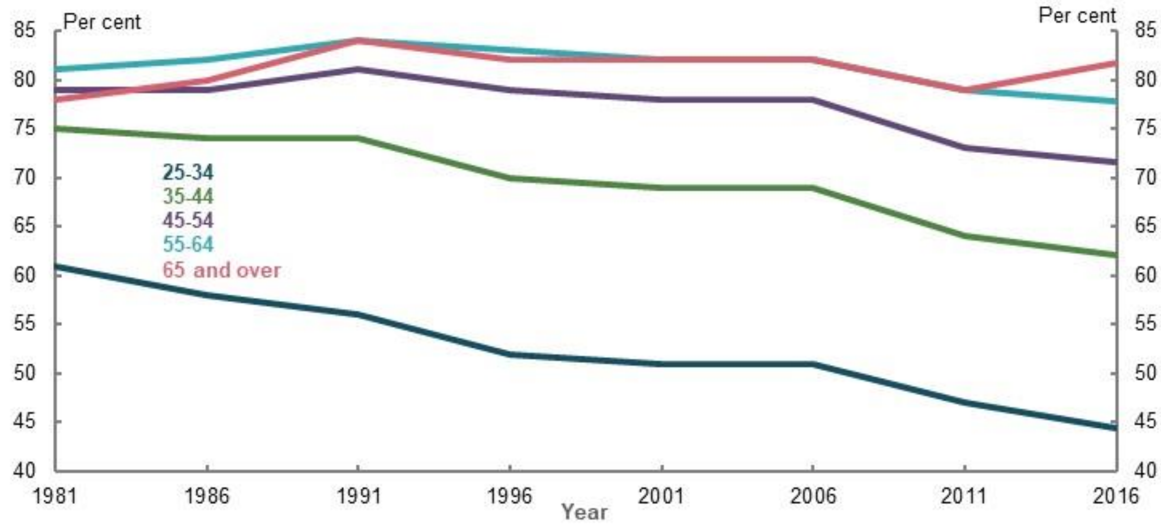
Housing status is a strong determinant of retirement outcomes. People who own their home outright have generally lower housing costs compared with renters, as well as a store of wealth that can be drawn on in retirement. People who rent may require incomes similar to working life to maintain living standards in retirement. This is further explored in *2C. Maintaining standards of living in retirement*.

Home ownership

Over the past 40 years, increases in home values and delayed workforce entry have contributed to falling home ownership rates. These factors have particularly affected lower-income and younger households.

Overall, home ownership rates have declined slightly from 70 per cent in 1981 to 67 per cent in 2016 (ABS, 2007, p. 13; ABS, 2016a).[68] Among people aged 55 and over, rates of home ownership have been consistently high. Home ownership has fallen among younger age groups (Chart 1D-17).

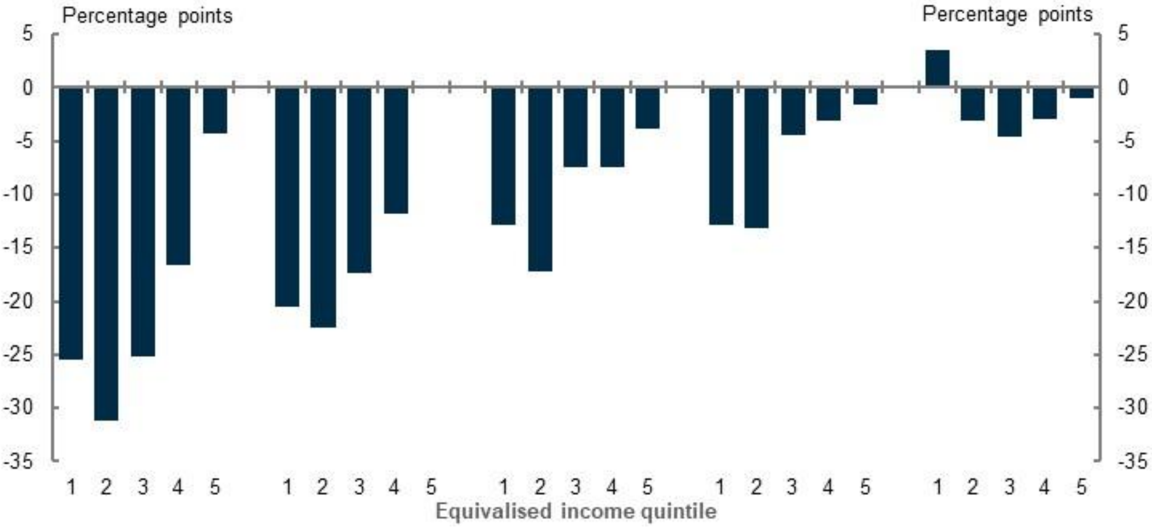
Chart 1D-17 Home ownership rates, by age group



Note: Per cent of occupied private dwellings. Age refers to age of household reference person. Excludes households with tenure type not stated. Source: (Daley, et al., 2018a).

Since 1981, ownership rates for lower- to middle-income households have fallen more for those aged under 65 than for those aged 65 and over (Chart 1D-18). In comparison, higher-income households have been relatively stable.

Chart 1D-18 Change in home ownership rates from 1981 to 2016, by age group and equivalised income quintile



Note: Age refers to age of household reference person. Equivalised means that income quintiles are adjusted for household size. Source: Analysis of (ABS, 1983) and (ABS, 2016a), based on previous analysis by (Daley, et al., 2018a).

The median age of people buying their first home increased from 24 in 1981, to 33 in 2016 (CEPAR, 2019, p. 9). Deferred workforce entry for younger generations delays their ability to start earning and

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68 As a percentage of all occupied private dwellings. Ownership rate includes all owner-occupied tenures. 2016 figure excludes dwellings with 'not stated' or 'not applicable' tenures.

save a deposit for a house. Increasing home values means younger generations not only start saving later in life, but also need to save more and contribute more of their incomes. Delays in household and family formation may also delay some people's home ownership intentions. While declines in home ownership among younger people may lead to lower rates of home ownership at retirement in future, the extent of this impact is not clear (Box 1D-4).

Home ownership is further explored in *3C. Home ownership status*.

Box 1D-4 Future of home ownership at retirement

Submissions highlighted the drop in home ownership rates among younger generations (Chart 1D-17), and raised concerns about potential future declines in home ownership among retirees. It is debatable, however, how much falls in home ownership rates at younger ages will flow through to future retirees.

- **'Catch up' at older ages.** Current falls in home ownership rates in younger age cohorts may be less pronounced if these cohorts 'catch up' and achieve home ownership similar to current retirees. However, evidence of such a catch up is mixed. One study suggested delayed home ownership was correlated with people marrying later in life (Baxter & McDonald, 2005). Conversely, a later study found that falls in home ownership rates among younger generations were driven by affordability and that significant catch up was unlikely (Stebbing & Spies-Butcher, 2015).
- **Effects of temporary migration.** Sustained net arrivals of migrants on temporary visas[69] over the past decade has increased the number of migrants in Australia (ABS, 2020m). Their inclusion in the ABS Census may lower home ownership rates, particularly among younger people, as temporary migrants are generally of working age and less likely to purchase homes. Excluding temporary migrants from the calculations increases the rate of home ownership for people aged 25-34 by 6 percentage points in 2016. Nevertheless, even after this adjustment, the rate *fell* 7 percentage points between 2006 and 2016.[70]
- **Renters who own other residential property.** A significant number of residential property owners choose to rent another property. In 2017-18, 12 per cent of households that rented their principal place of residence owned residential property elsewhere (ABS, 2019n). Over the past decade the proportion of renters who own other residential property has remained stable.[71]

Renters

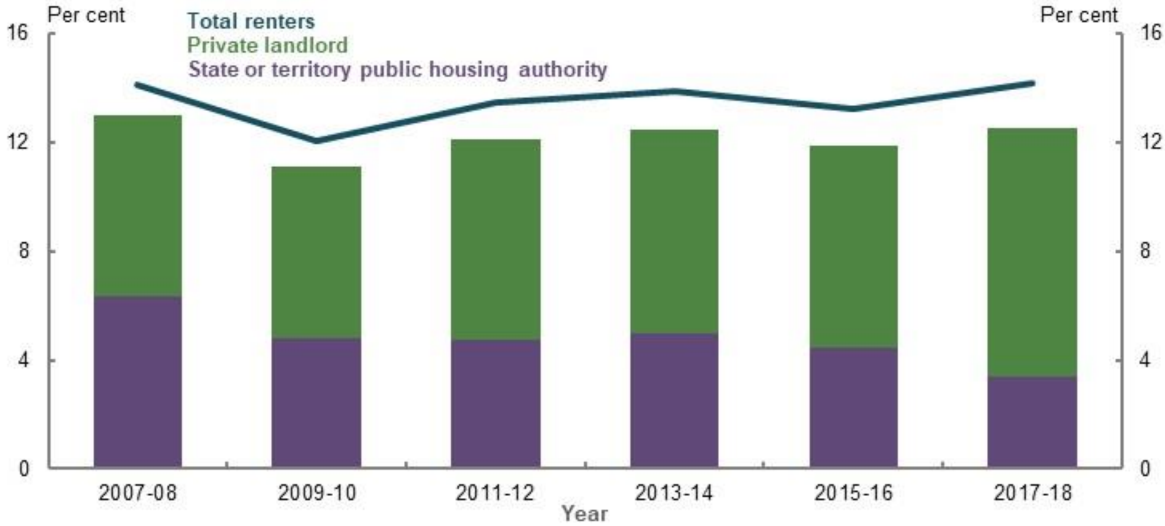
Current rates of home ownership for households aged 65 and over may not be maintained in future, particularly for lower- to middle-income households. If these households are unable to save enough to cover rents in retirement, their retirement incomes will likely be inadequate to maintain living standards.

The Government provides additional payments through Commonwealth Rent Assistance to age pensioners who rent, as they generally face higher housing costs than home owners. Commonwealth Rent Assistance is explored further in *2B. Policy scenario: Implications of increasing Commonwealth Rent Assistance*.

Renting through public housing has fallen. But renting in the private market has risen for households aged 65 and over, despite overall rates of renting remaining stable over the past 10 years (Chart 1D-19).

[69] Defined as visas permitting persons to come to Australia on a temporary basis for specific purposes. Main contributors are tourists, international students, those on temporary work visas, business visitors and working holiday makers (ABS, 2020m).
[70] Analysis of (ABS, 2006a); (ABS, 2016a).
[71] Analysis of Housing Occupancy and Costs 2007-08 to 2017-18 (ABS, 2019n).

Chart 1D-19 Proportion of households aged 65 and over that rent, by landlord type



Note: Age refers to age of household reference person. Private landlord includes real estate agent, person not in same household — parent/other relative, or other person. Total renters includes those with other landlord type, which includes owner/manager of caravan park, employer — Defence Housing Authority, government or other employer, housing co-operative/community/church group, and other. Source: Analysis of Housing Occupancy and Costs 2007-08 to 2017-18 (ABS, 2019n).

Over the past 10 years, the ratio of rents to household income have been consistently higher in the private market compared with public housing for households aged 65 and over that rent.[72] In future, greater renting through the private market could see more renters aged 65 and over facing higher housing costs as a proportion of their income.

[72] Housing Occupancy and Costs 2007-08 to 2017-18 (ABS, 2019n).