

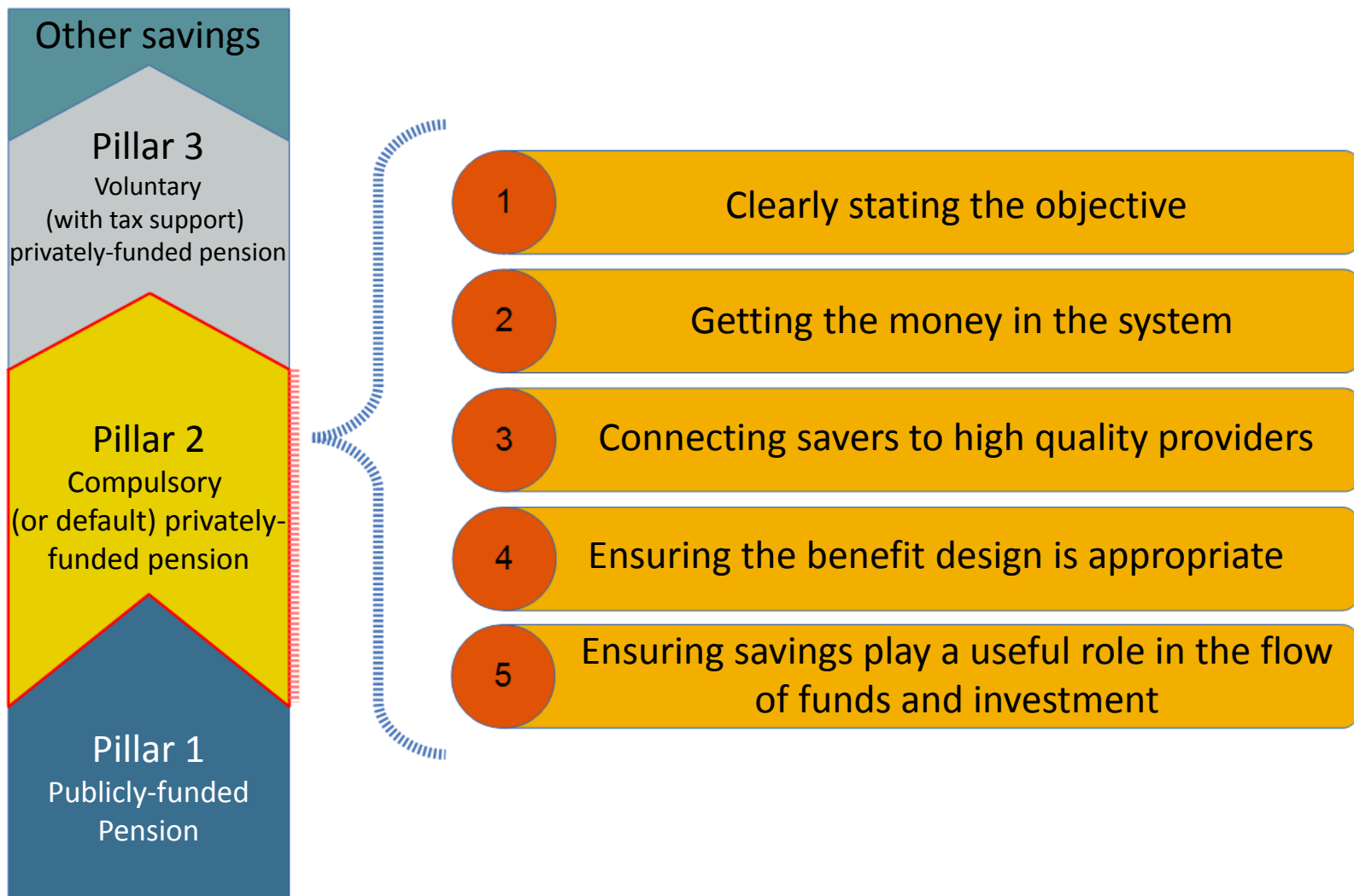
Pillar Two: Insights from Down Under

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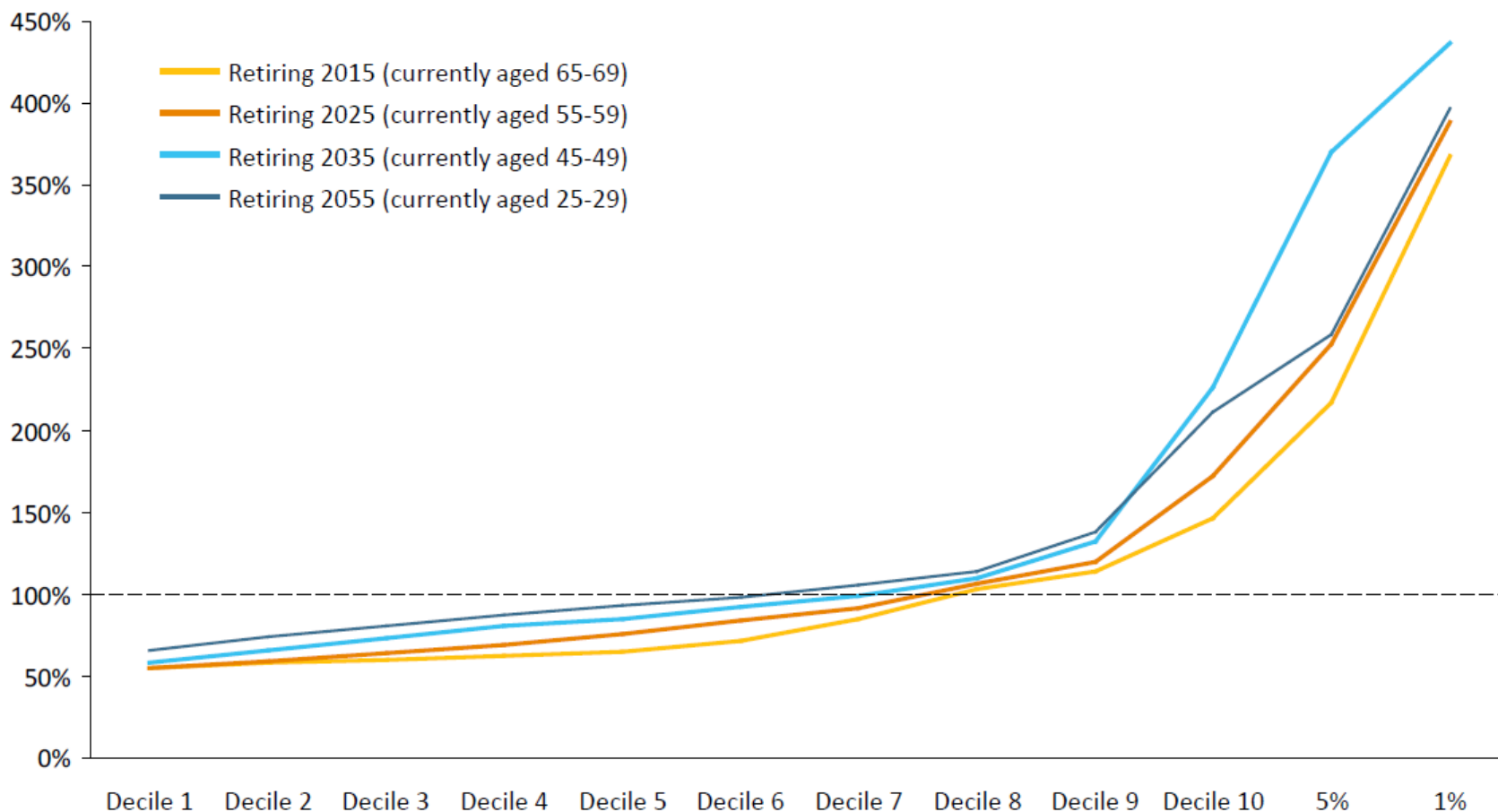


Five territories of pillar 2 design



Effectiveness of Australian system

Retirement income as a percentage of ASFA comfortable standard, single females



Source: ISA-Rice Warner Modelling (2015)

1. Clearly stating the objective

Why

1

Pillar 2 system exists to serve a public purpose. It will involve individuals and private firms with other purposes, who will need to be told “No.”

2

Pillar 2 involves the force of law, and fiscal support (tax expenditures and transfers. These need to be targeted, which requires an objective.

3

Pillar 2 interacts with Pillars 1 and 3. Where one pillar ends and another begins requires an objective.

What

1

Clear statement of what adequacy outcomes are sought (in terms of coverage and a budget standard).

2

Clear statement of the form of benefits desired.

3

Ideally, a clear statement of the well-being outcomes sought

1. Clearly stating the objective

Australia: current

- Superannuation *funds* have a sole purpose: to provide retirement benefits
- Superannuation *system* has no formally legislated objective
- Legislative history suggests:
 - *Coverage*: “All workers”
 - *Adequacy and well being outcome*: To provide “security and higher standards of living ... consistent with rising community expectations”
 - *Benefit*: “Income support”
- Problem: The lack of a clear adequacy objective has resulted in excessive and poorly targeted tax expenditures, incoherent Pillar 1 means testing, inappropriate conduct by firms and individuals, and efforts by politicians to direct savings into housing and other purposes.

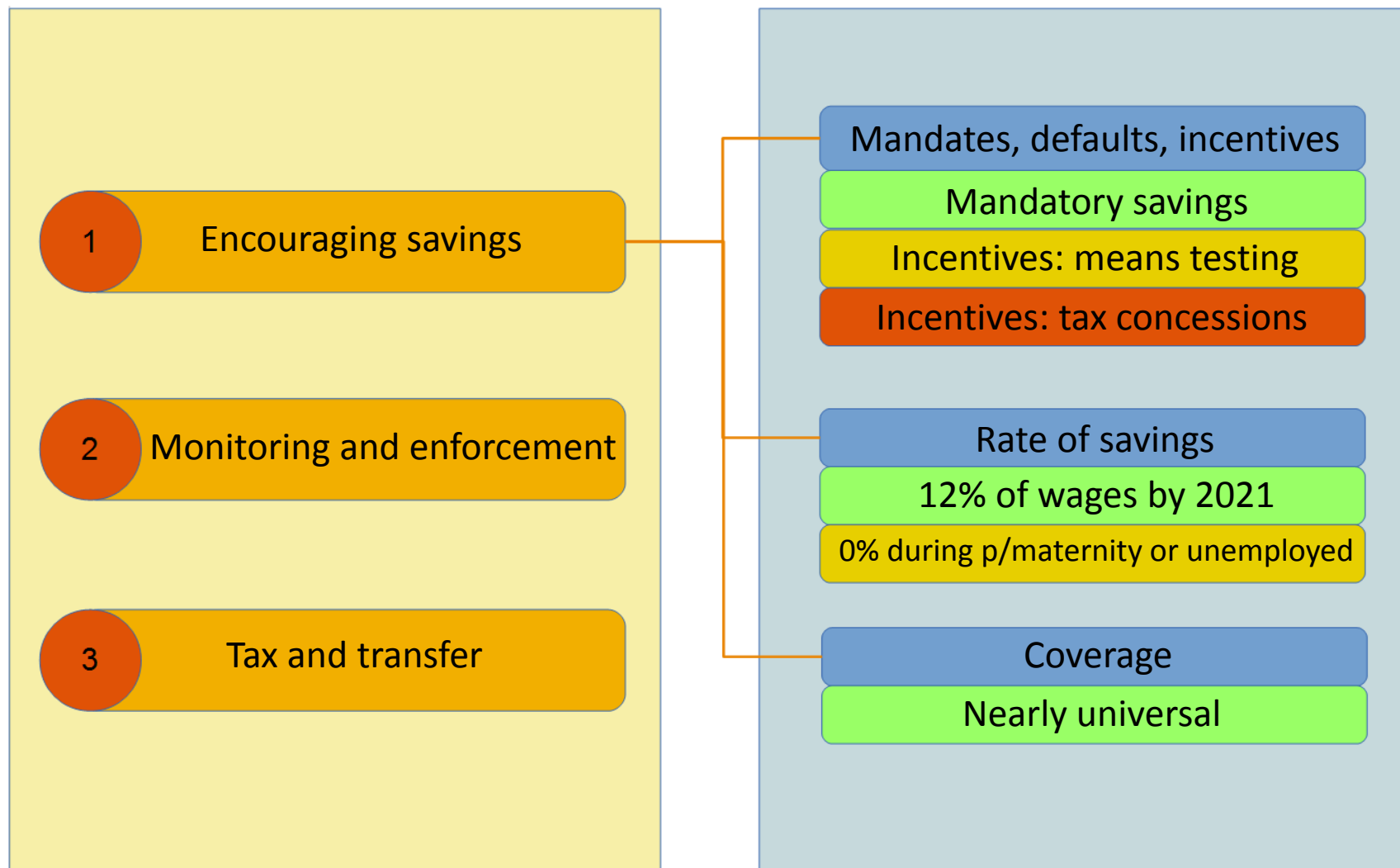
Australia: proposed (far from legislated)

- “To provide income in retirement to substitute or supplement the Age Pension.”
- Problem: No objective for adequacy, therefore this will provide no guidance regarding the level of mandatory savings, targeting of public support, and other interactions between Pillars.

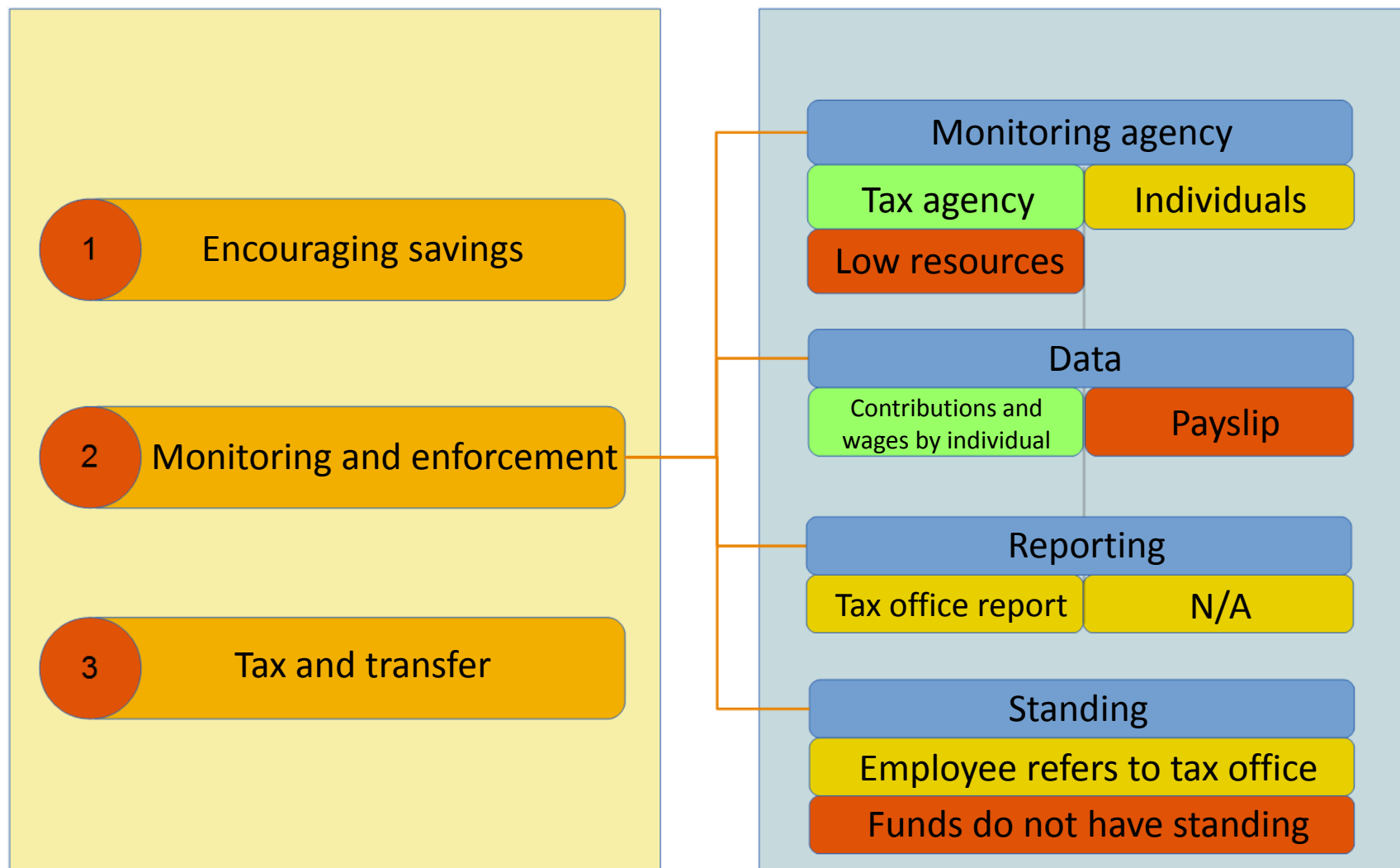
Australia: recommended

“To deliver financial security and dignity in retirement to all Australians by providing regular income that is, when combined with any public pension and other sources of income, sufficient to secure a comfortable standard of living by reasonable community standards.”

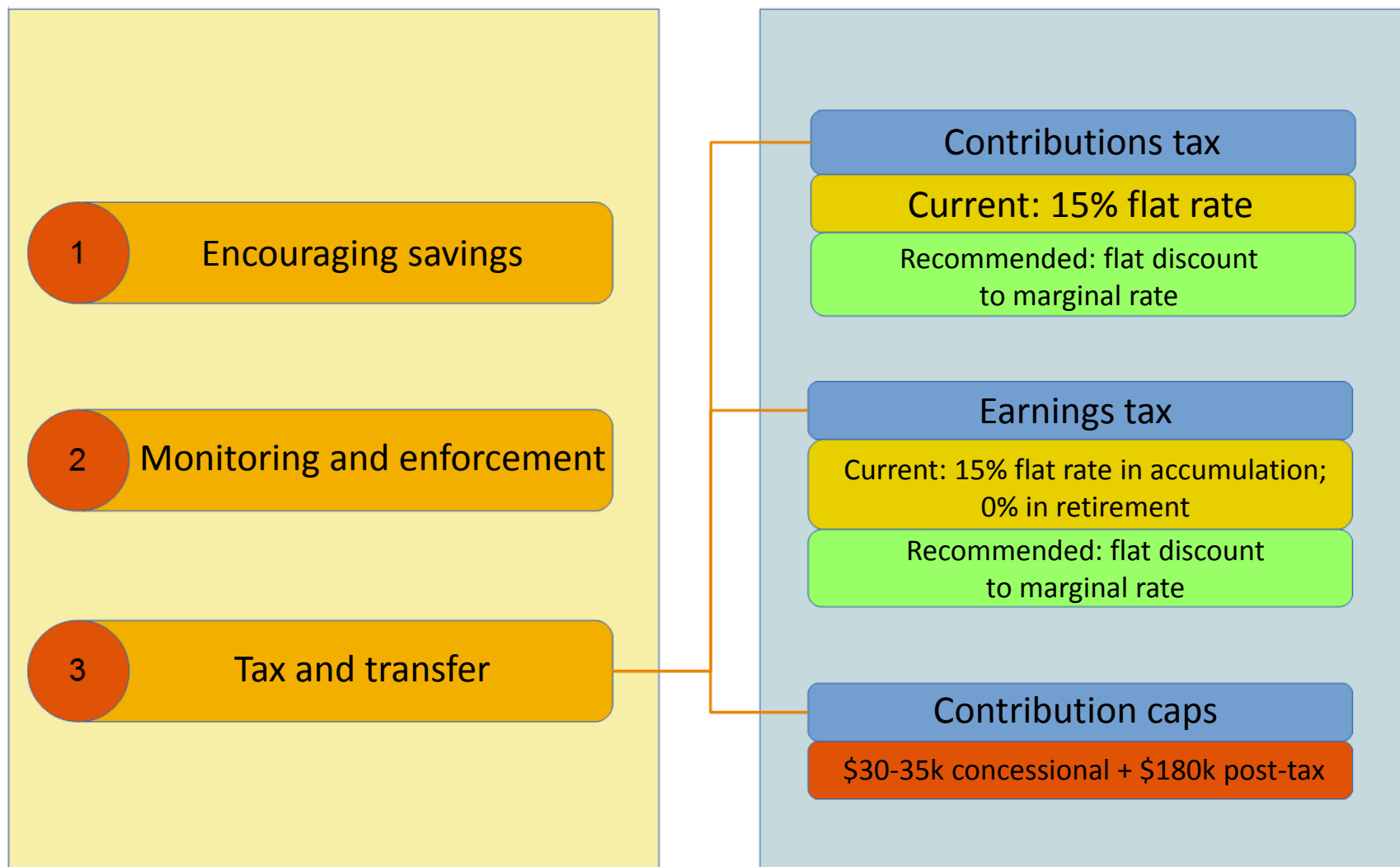
2. Getting the money in the system



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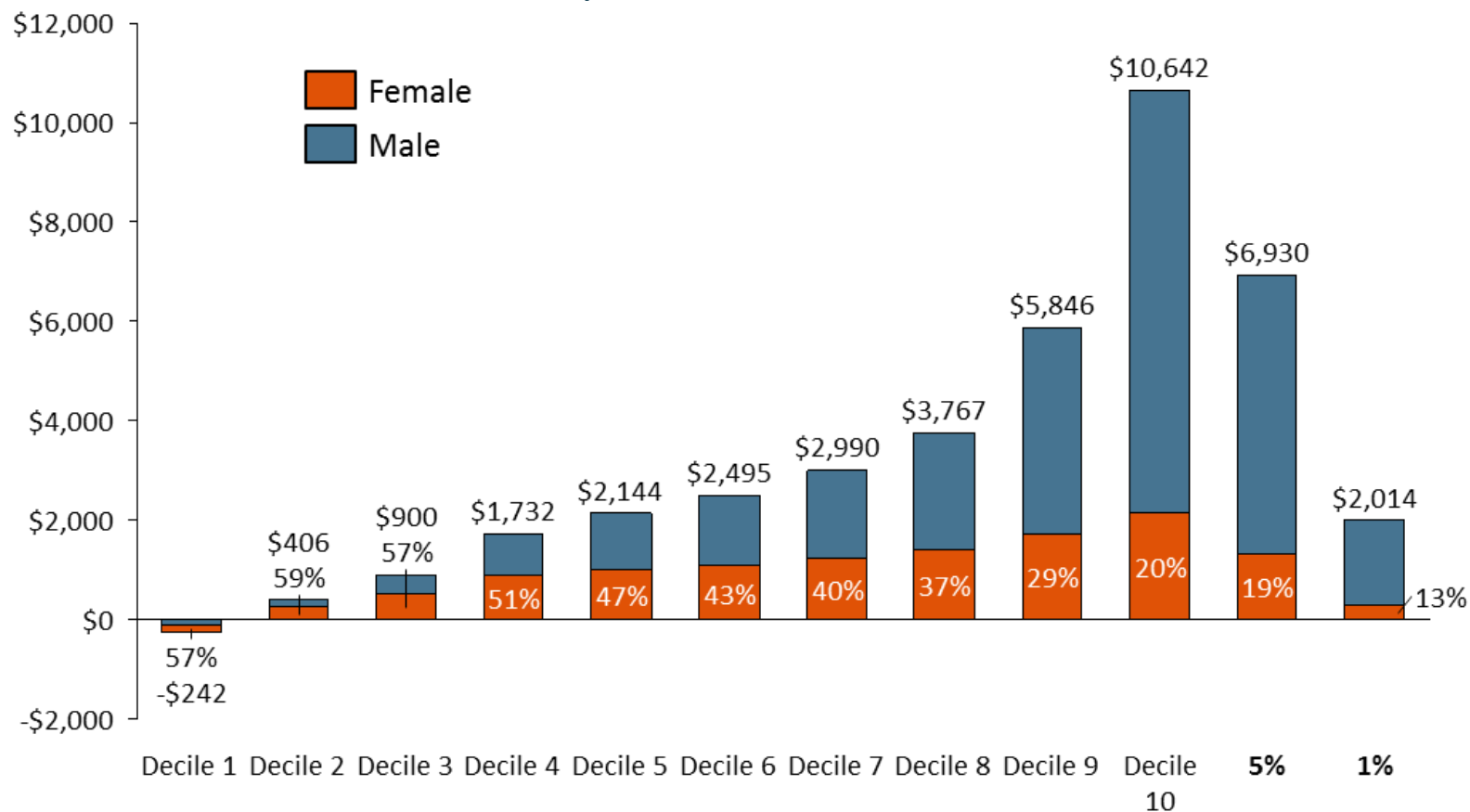


2. Getting the money in the system



Distribution of tax support

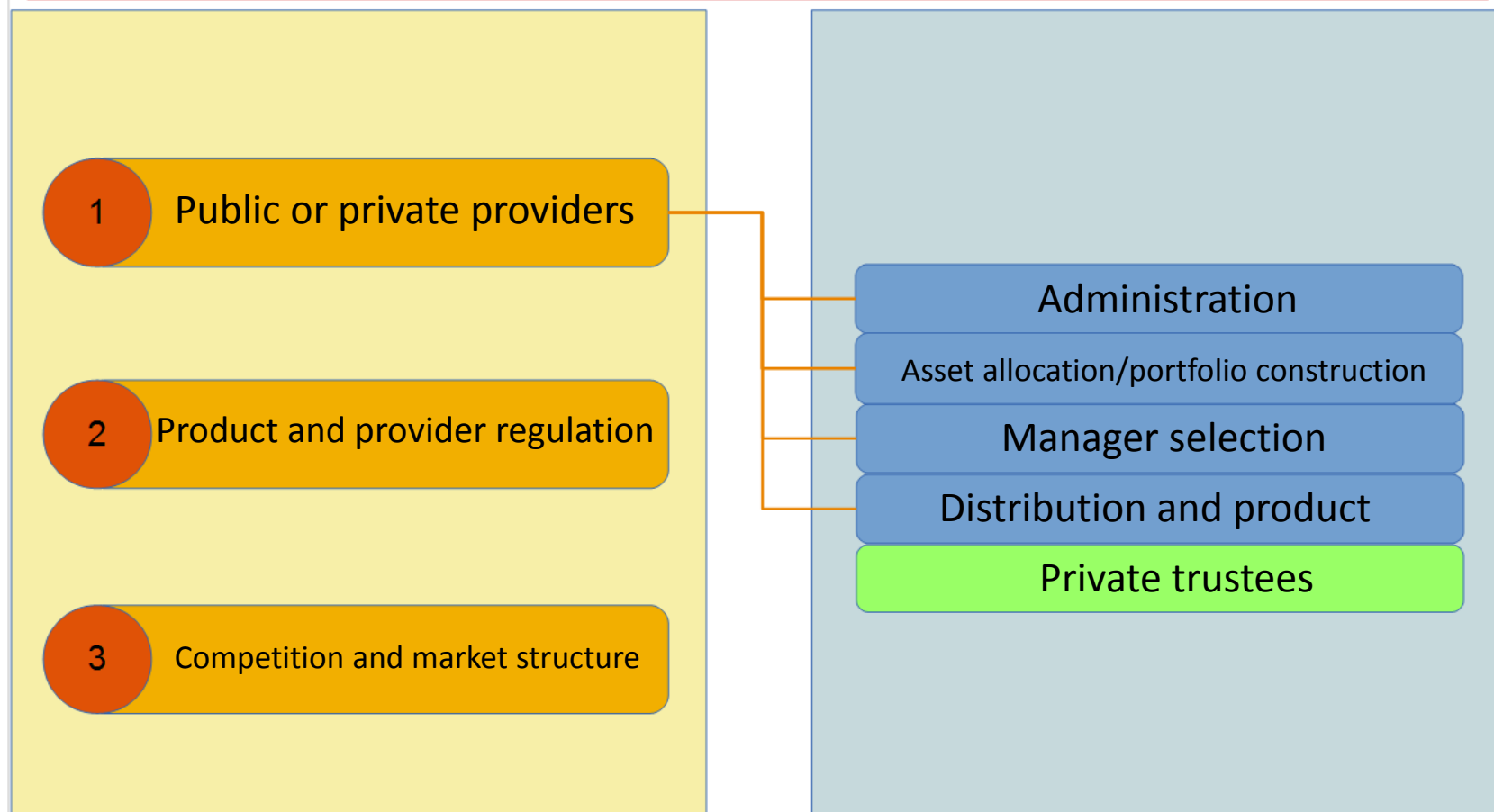
Tax concessions by income decile, \$ million, 2014-15



Source: Treasury TES 2014, with ISA estimates of quantile and gender splits from the ABS Survey of Income 2011-12, the ATO percentile distribution of taxpayers and the Treasury distribution of contributions for the April 2102 Roundtable adjusted by ISA for Division 293 Tax

3. Connecting savers to providers

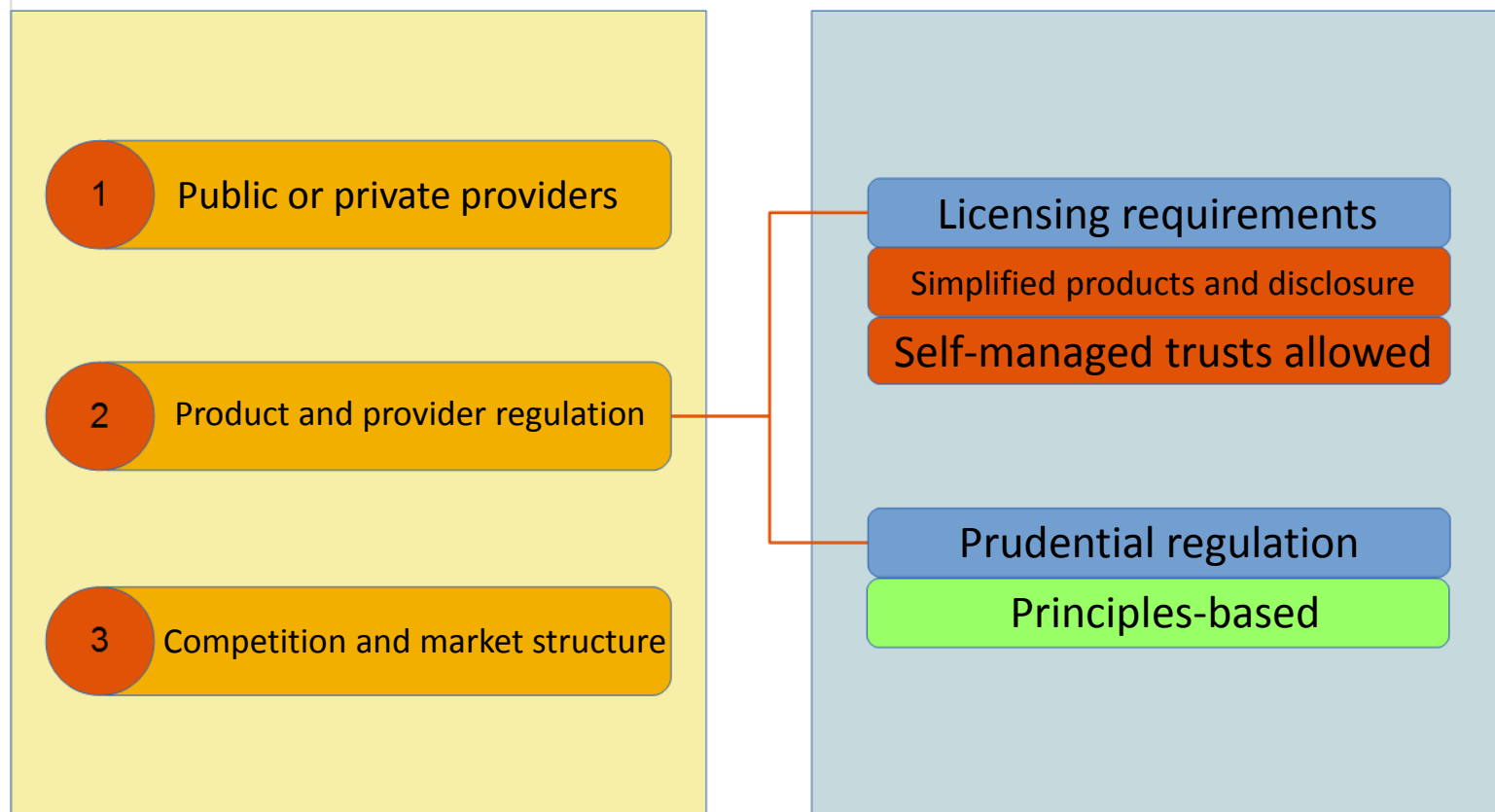
Encouraging people to save does not mean that their savings will be placed with a high quality provider.



3. Connecting savers to providers

The limited capacity of individuals to choose what is best for them means that competition and markets rarely work effectively within pension systems – leaving too much power in the hands of pension providers. The problem is only exaggerated where pension providers are commercial financial institutions. Conflicts of interest can therefore exist between the fiduciary duty to act in the interests of the pension fund members and beneficiaries and making profits for shareholders.

Ashcroft & Stewart, International Organisation of Pension Supervisors (2010).

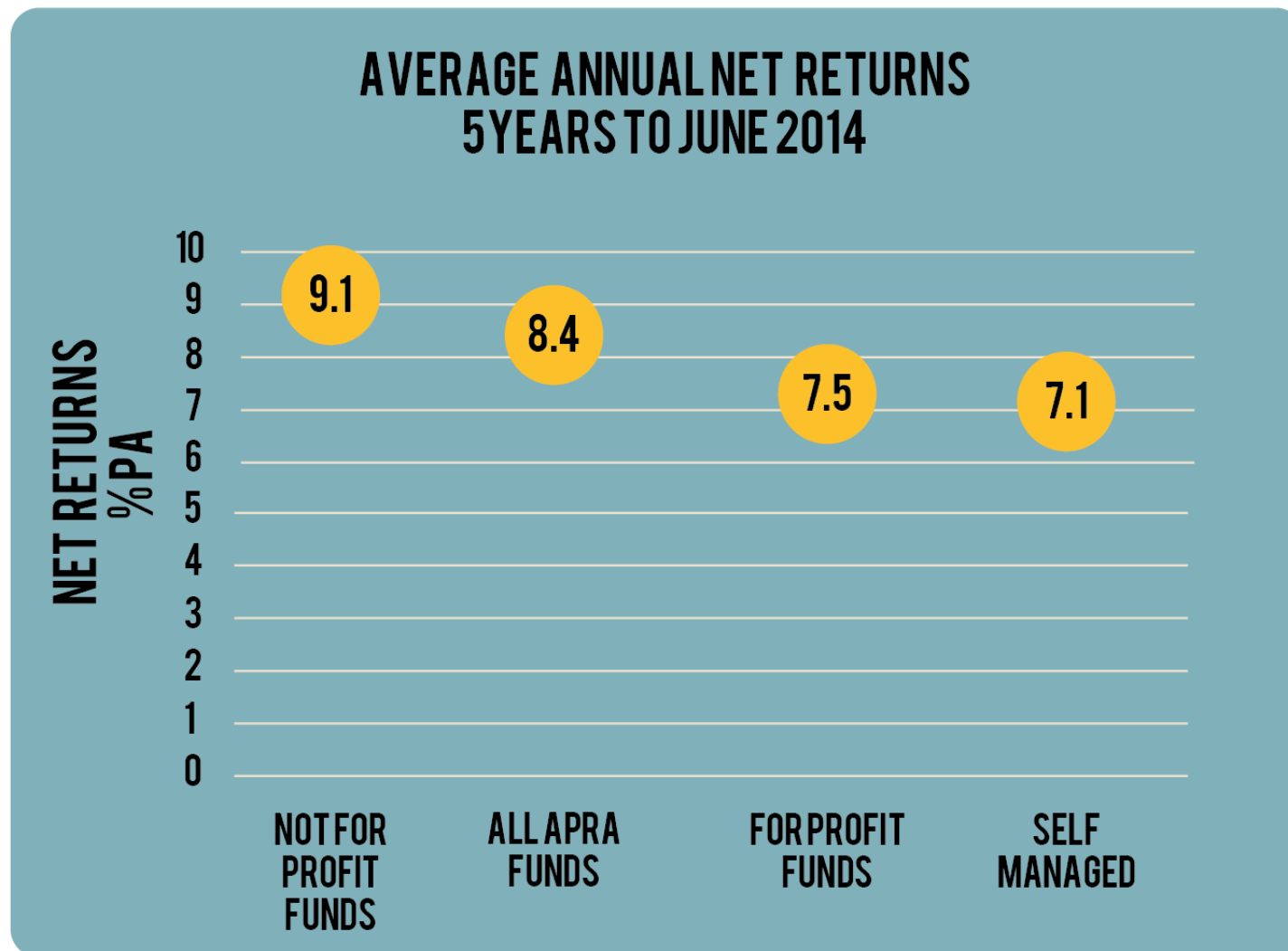


**Industry
Super
Australia**

Ashcroft & Stewart, International Organisation of Pension Supervisors (2010).



Performance by segment



4. Benefit design

A mature pillar 2 must provide retirement income that :

1. Lasts for life
2. Is sufficiently stable through volatility that beneficiaries can rely on it
3. Maintains purchasing power
4. Is sufficiently high (i.e., efficient) to achieve adequacy objectives

Consumer demand

Age pension means test

Separate accumulation and pension phases

Defaults

Accumulation only

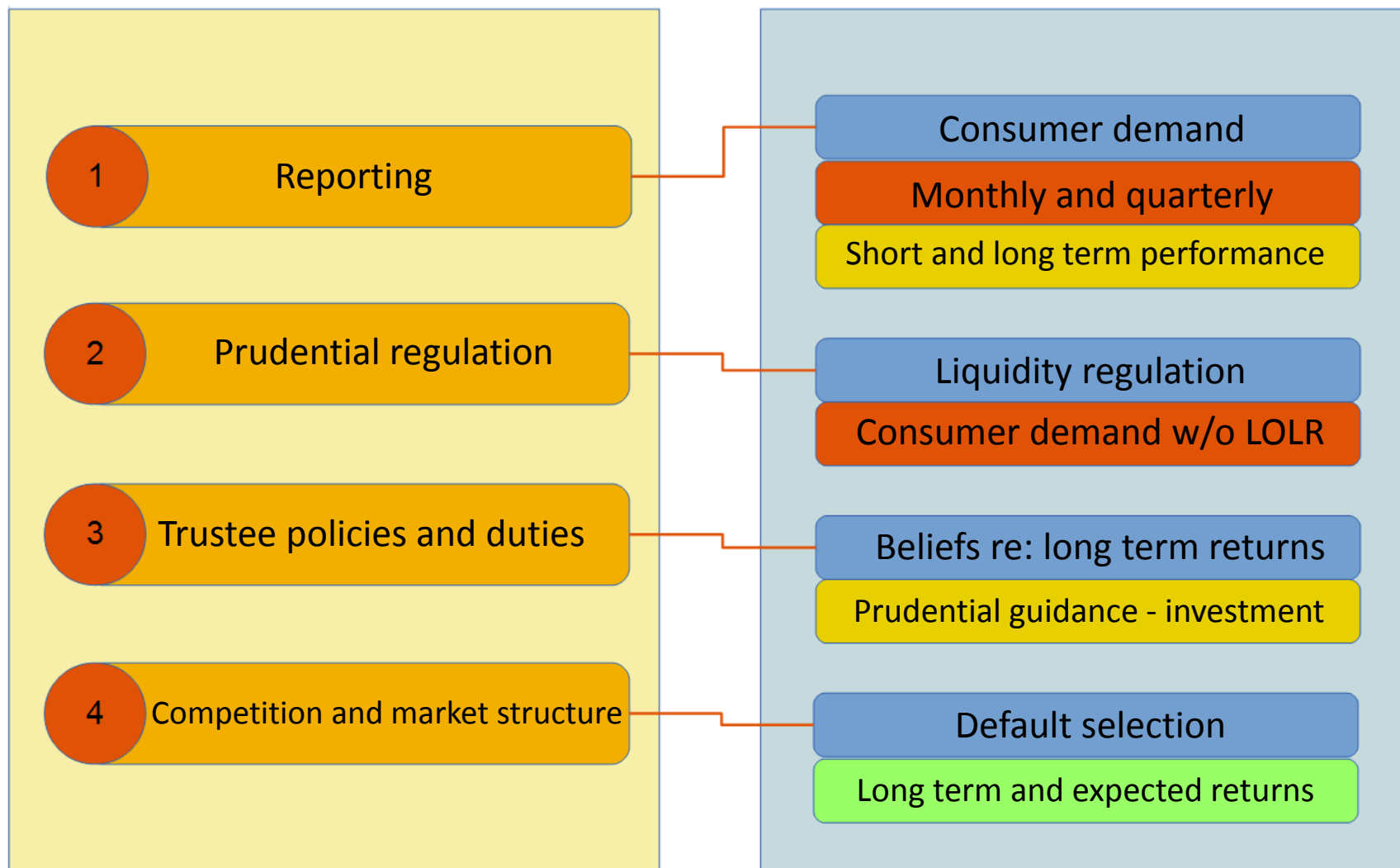
Proposed: trustee pre-selected option

Recommended: whole-of-life default

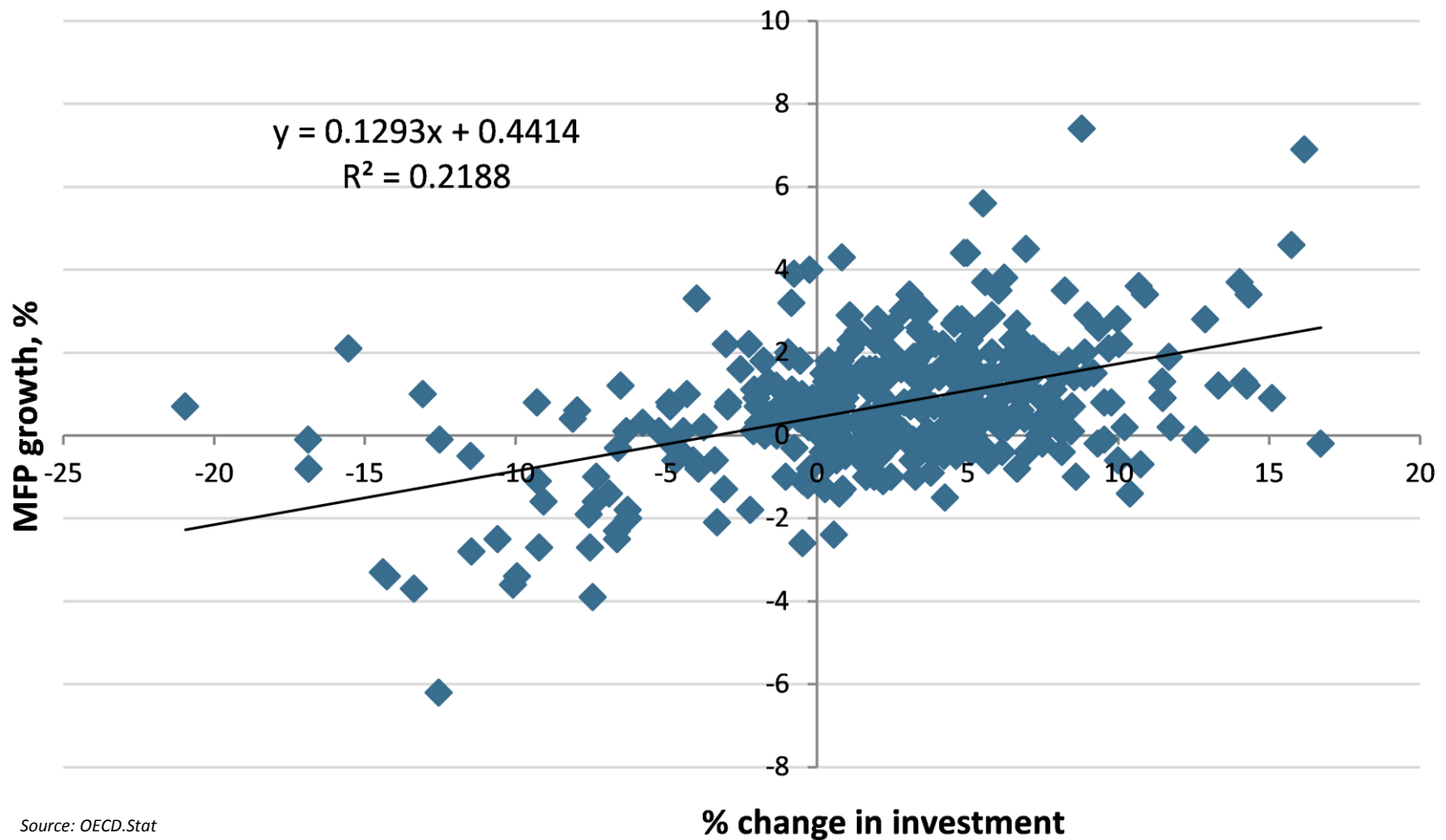
Risk sharing

Risk pooling

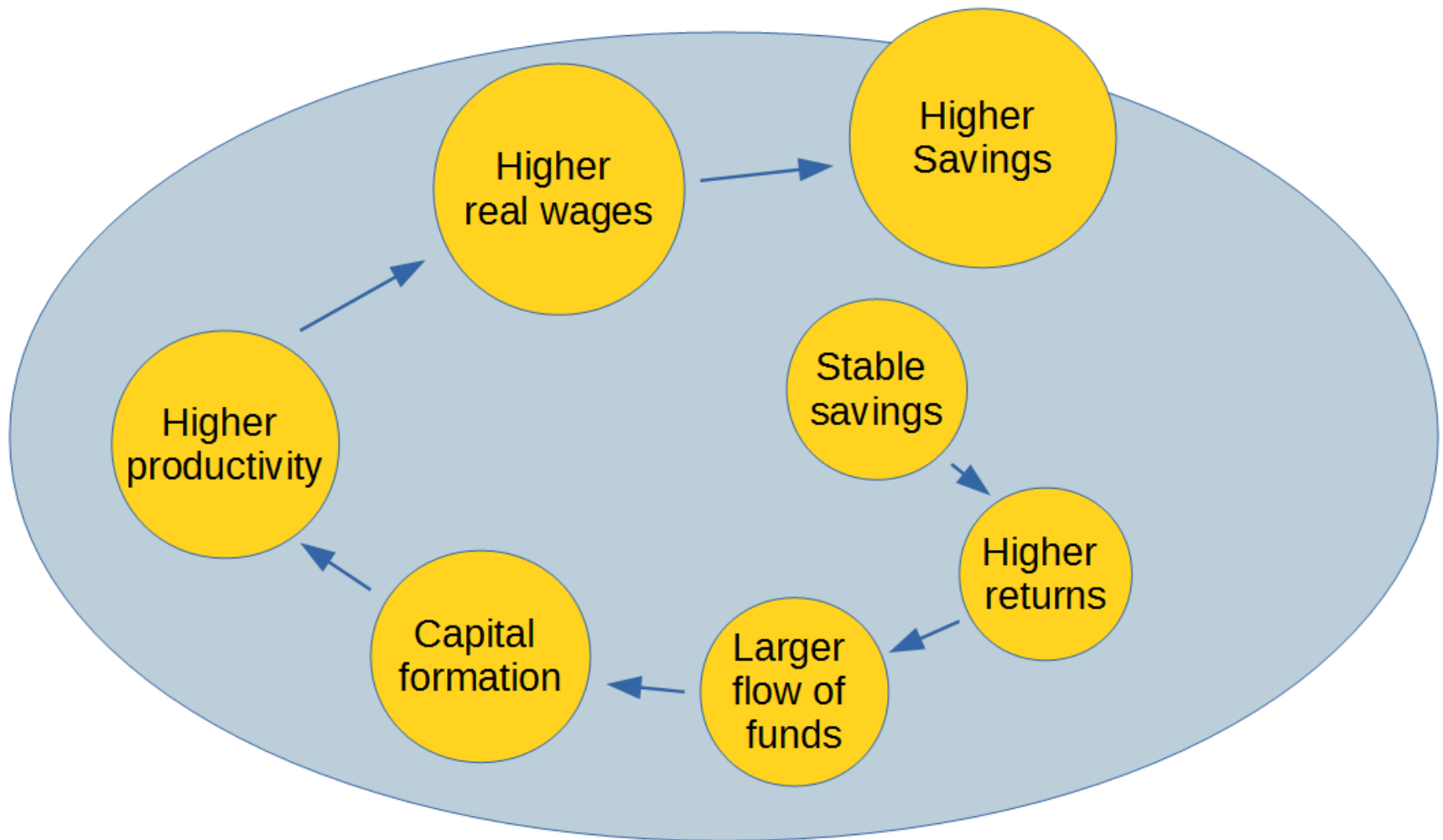
5. Flow of funds and investment



Investment lifts productivity



Pillar 2 economy facing potential



Key lessons from Australia

