ELIZABETH HAMMOND

Provision for Retirement: A State or Private Responsibility?

Even to your old age and grey hairs I am he, I am he who will sustain you.
I have made you and I will carry you; I will sustain you and I will rescue you.
Isaiah 46:4.

I. INTRODUCTION

The first few months of 1988 have seen a revival of public debate about the tax treatment of occupational superannuation funds. Unfortunately, much of the debate appears to have come from political motives and is centred on preventing potential adverse tax changes that may be recommended following the completion of the corporate tax review by the Federal Government. This is, however, really only one aspect of a much wider debate that should be occurring in Australia — that is, how *we,* as the current working population, expect to provide for our future retirement.

There is an inherent problem in all discussions about retirement income in that, unless one is approaching retirement age, the whole question seems too far into the future to worry about and best left to another day. This attitude, for both an individual and for Australia as a whole, is not acceptable as action must be taken now in order to adequately provide for everyone in the future. A recent Economic Planning Advisory Council paper No. 29, *'Economic Effects of an Aging Population'*, highlights the problem facing Australia over the next forty years or so — our population is getting steadily older. This is a situation which Australia has in common with a number of other Western industrialised countries. The implications for Government expenditure, particularly in the area of social security, are quite severe and should be responsibly faced now while there is still time to consider and implement the best alternative course of action.

The provision of an adequate retirement income for all is essentially a question of what type of society we wish to live in in the future. It is a question to which Christians can have an input and this paper is an attempt to apply

ELIZABETH HAMMOND is an Economic Research Assistant in the Commonwealth Bank of Australia.

some biblical principles to the issues surrounding the provision of retirement income. Firstly, some essential demographic information is provided then Section 2 examines the alternative means available for providing retirement income, outlining the current mixture of policies applied in Australia. Section 3 provides a few basic biblical principles and guidelines (by no means intended to be exhaustive) while Section 4 applies these to issues surrounding the future provision of retirement income. This section is intended to commence discussion, not conclude it. There is therefore *no* conclusion to the paper.

Australia's Ageing Population

Australia's population, over the course of this century, has progressively been getting older. Table 1 shows the proportion of the population within certain age bands from 1901 to projected figures for 2025. In 1901, 35% of the population were aged below 15 and only 4% were older than 65. By 1986, only 23% were under 15 while 10.5% were over 65. By 2025 it is projected that 19% will be in the youngest group and 16% will be over 65 years. Increased life expectancy is one reason for the development but the sharp fall in the birthrate in more recent years is the dominant cause of the ageing structure as a whole. It must be remembered that these are projections based on certain assumptions about fertility, mortality and immigration rates, albeit extensions of present trends. If major changes occur, the actual figures may differ from those presented.

Table 1

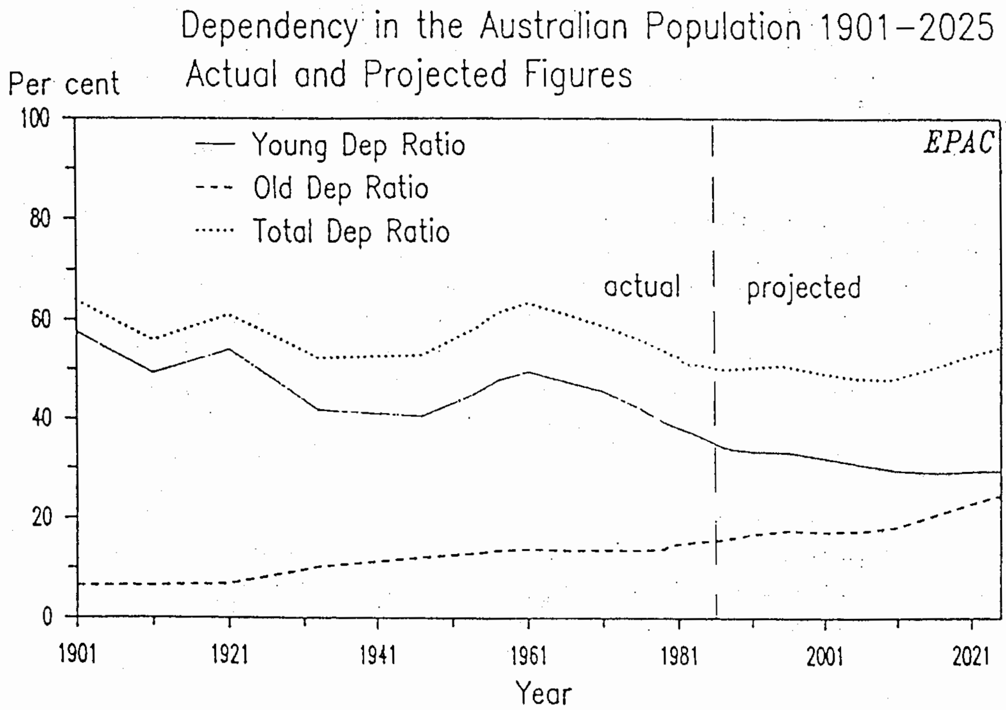
The Population of Australia: 1901 - 2025

Year	Population (m)	Growth rate (per cent)	Proportion aged (%) 0-14	15-44	45-64	65+	75+
1901	3.79	-	35.2	48.7	12.0	4.0	1.0
1933	6.63	1.8	27.5	47.4	18.6	6.5	1.7
1961	10.51	1.7	30.2	41.4	19.9	8.5	2.8
1986	15.97	1.7	23.2	47.3	19.0	10.5	3.9
2005	20.21	1.2	20.9	43.2	24.0	11.9	5.4
2025	23.86	0.8	19.1	39.9	24.9	16.1	6.6

Source: ABS, Census data and Cat. nos. 3101.0 and 3222.0, projections extended beyond 2021 by request

An important concept in demographic studies is the dependency ratio — the ratio of the size of the population outside the normal workforce age (deemed to be 15 to 64) to those inside it. Chart 1 shows both the young and old dependency ratio projected to 2025. The overall ratio is projected to increase after 2010. The old age dependency ratio increases from 15% in 1986 to 25% by 2025. The rise is concentrated in the period after 2010.

Chart 1



The EPAC paper referred to earlier provides estimates of the increased level of government social expenditure (defined as social security and welfare, health, education and employment) that will result based on the population projections presented. If productivity growth were zero, the ratio of social expenditures to GDP would grow from 20% of GDP in 1985 to 22.6% of GDP in 2025. This would imply an increase in the tax burden on the working population to fund the rise. This question and the question of sharing any productivity increase that does occur are examined further in Section 4.

II. ALTERNATIVE MEANS FOR PROVIDING A RETIREMENT INCOME

There are essentially four different ways in which retired persons may provide themselves with an income:

* by self provision
* by relying on their extended family
* by being a member of an employer (or union) sponsored scheme, or
* by relying on the State to provide an income out of general tax revenue.

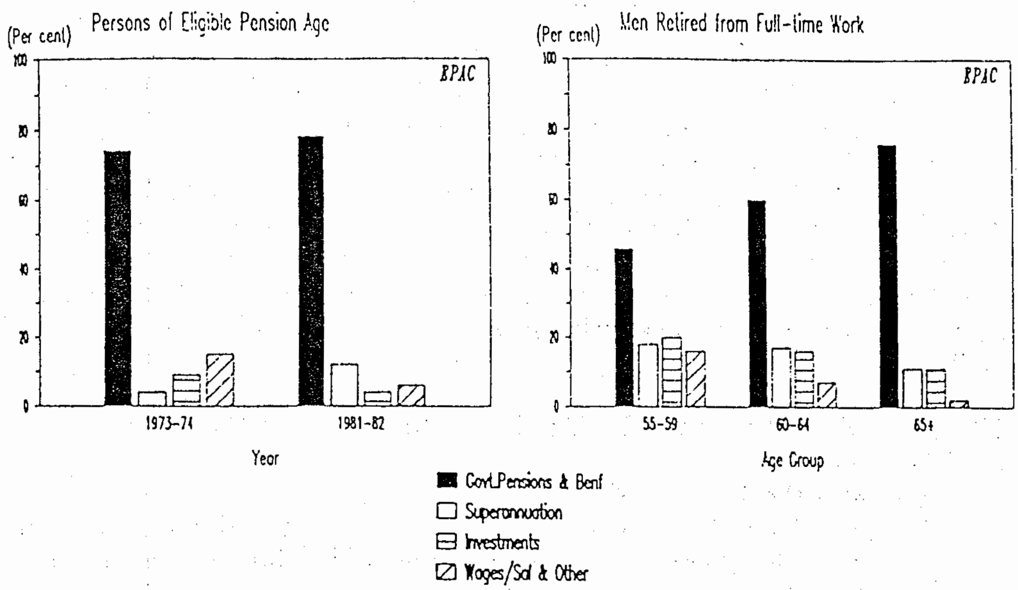
A combination of these approaches is most commonly used and it is the interaction of public and private provision which causes the most difficult problems to arise in this topic. In the past, self provision or relying on one's own family were the only viable means available. With life expectancy shorter, people often kept working until their health declined. Nowadays, there are a variety of investments that can be used to provide for retirement. People may own a business which when sold provides retirement capital or have saved during their working life for this purpose. Superannuation is a specific form of long-term contractual saving and is subject to a favourable tax regime. Why this should be and who benefits from the subsidies is further examined in Section 4.

Employer-based occupational superannuation funds are a fairly recent phenomenon but their coverage in the workforce is growing. One of the problems has been that, being employer specific, benefits are dissipated or lost when an employee changes jobs. This is being dealt with by a number of initiatives including the approved deposit fund scheme. Another problem with this method of retirement provision is the categories of workers for whom it is unsuitable, such as part-time employees and women who take time out of the paid workforce to care for children or elderly relatives.

The final form of provision, by the State, is often called Pay-As-You-Go — the current group of aged pensioners receives pensions funded by the working population's taxes and they expect in return to be provided for by their children's generation's taxes. It is an implicit inter-generational contract which may run into difficulties if we start promising ourselves benefits that will cost a lot more in percentage terms for our children to meet than we are currently willing to pay for our parents.

Chart 2

Principal Source of Income



The current mixture of retirement income provision for Australians of pension age (65 for men, 60 for women) is illustrated in Chart 2. Government pensions are by far the greatest source of income and older retirees rely more on the pension than younger retirees. This mixture may change in the future as more retirees leave the workforce with higher superannuation benefits. Table 2 shows the proportion of persons of eligible age who receive the aged pension. The percentage has declined in the first half of this decade because of the imposition of tighter income and assets tests. Australia relies on a means-tested system rather than a universal system as in some other countries.

Table 2

Proportion of Persons of Eligible Age Receiving Age and Service Pensions: 1947-1986.

	Age Pension	Service Pension	Total
1947	31.5	-	-
1954	42.1	-	-
1957	45.7	-	-
1961	51.0	-	-
1971	61.2	-	-
1976	75.4	-	-
1981	75.9	12.9	88.8
1982	74.7	11.1	85.8
1983	74.2	9.4	83.6
1984	70.7	8.1	78.8
1985	67.5	9.9	77.4
1986	69.7	10.0	79.7

Sources: Annual Reports, Department of Social Security, (various issues) Canberra.
Data provided by the Department of Veterans Affairs

A single pensioner with income less than $40 per week receives $116.10 per week pension. The pension reduces by 50 cents for each $1.00 of extra income received. A married couple with income less than $70 per week receive $193.50 per week which also reduces by 50 cents for each extra $1.00 of income. The assets tests apply according to whether the pensioners own their own home. If a single pensioner owning a home has assets up to $83,250 they may retain the full pension. Over this level, the pension gradually reduces. A married couple has a limit of $118,500 before reductions occur. Higher limits apply to non-home owners. Before we turn to examine a number of the issues surrounding the future provision of retirement income in Australia, Section 3 analyses some biblical principles which may provide guidance for our deliberations.

III. DISCERNING SOME BASIC BIBLICAL PRINCIPLES AND GUIDELINES

a. Rest from the Labour of Life

The 'rest of God' is a strong concept in both the Old and New Testament. There is, of course, the commandment in Deuteronomy 5:12 to observe the Sabbath but this seems to be a foreshadowing of a longer term rest. Hebrews 4:1-11 discusses this wider concept linking the OT promises of a land for God's people (Psalm 95:8-11) with the NT promises of 'rest for God's people'. The idea seems to be connected with God's ultimate blessing and Christ's return. A Christian's final rest, therefore, is to be with God and, in this sense, 'retirement' is really alien to biblical thinking. Our ministry is to continue throughout our lives though it obviously may change as we grow older. Our society affords the luxury of an extended period after paid employment has ceased and people will need resources for this time.

b. Honouring parents
This is a strong biblical idea supported by the commandment in Deuteronomy 5:16, the curse in Deuteronomy 27:16 if not done, and Jesus' own example — Luke 2:51-52. Jesus also comments on the importance of supporting parents — Mark 7:9-13. Family structures and obligations have a prominent place in scripture. Our society, based as it is on the small nuclear family which is also fairly mobile, has relied on the State to a great extent to fill the void left by the absence of the extended family.

c. Justice/Injustice
This is a strong and complex theme in the Bible and is only dealt with superficially here. The basis is the character of God Himself (Exodus 34:5-7) and involves justice being commanded of us. Psalm 82:3-4; Isaiah 56:1-2; Micah 6:8; and Deuteronomy 15:7 are a few examples. Injustice is definitely condemned e.g., Deuteronomy 24:17-18; Proverbs 14:31; Proverbs 21:13 and Galations 2:10.

d. Care and respect for old age
Old age is seen as a mark of God's blessing such as Zechariah 8:1-5 and Proverbs 16:31. Respect should be shown to the aged — Leviticus 19:32. Finally, God's continuing care of us, even into our twilight years, is emphasised in Isaiah 46:4, quoted at the beginning of this paper.

IV. APPLICATION OF BIBLICAL PRINCIPLES TO ISSUES SURROUNDING THE PROVISION OF RETIREMENT INCOME

It seems fairly clear that the State not only does but should have a substantial role to perform in the provision of income for retirement. The biblical themes of justice and care for the poor demand at the very minimum some social 'safety net' to ensure no-one is left without the resources to feed, clothe and adequately house themselves. It is an open question whether because the State adopts this role one's own personal responsibility is therefore automatically fulfilled.

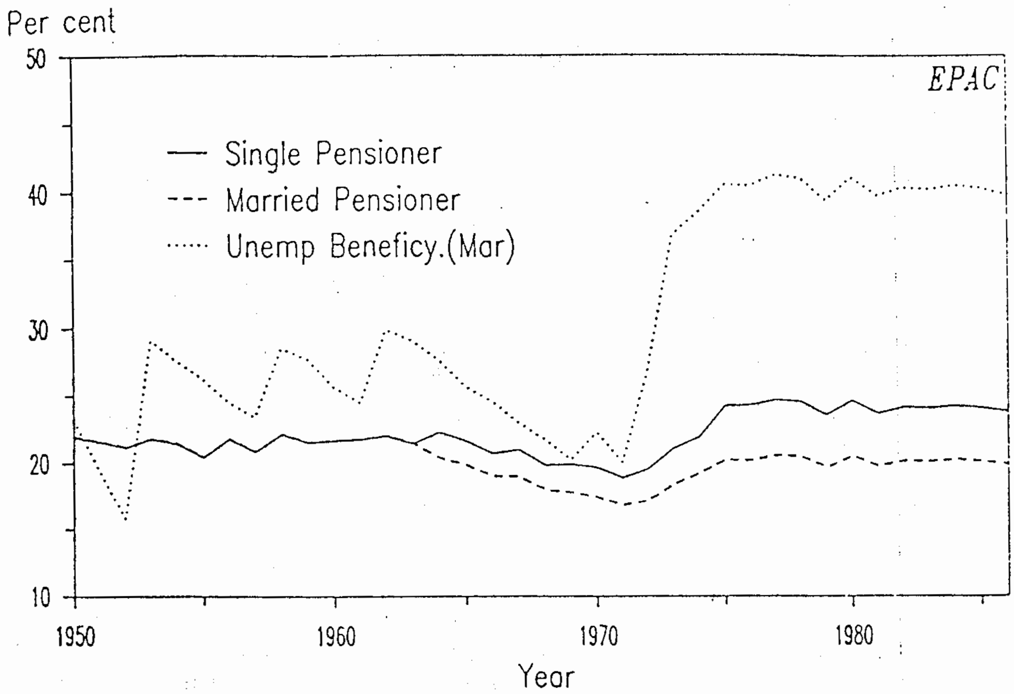
The extent of the State's involvement needs careful consideration, bearing in mind the limited resources available and the amount needed for an individual to participate fully in our society. At first sight it might appear fairest to give everyone an equal amount from the State but individuals emerge from their working life with vastly different resources. Some may have nothing at all, others may be able to maintain a high standard of living without earned income because of past investments. Inequality in working life tends to be perpetuated into retirement and, following God's revealed special preference for the poor, a targetting of the State's scarce resources to those who have least seems to accord with the biblical principles. It is on this basis that means testing and asset testing of eligibility for the aged pension may be advocated. The minimum level of the full pension awarded should thus be higher than it otherwise would have been in the absence of such means testing.

At present, the age pension is automatically indexed to price movements via the Consumers' Price Index. There is a problem as to whether this is an appropriate measure of increases in the cost of living for pensioners, given they are a special sub-set of the population. A more serious problem, though, is the question of fairly sharing any productivity increases that may occur. If pensions are maintained at their current real value and projected into the future the pensioners' share of national income will decline presuming that Australia continues to experience moderate economic growth.

There is a longer term policy goal to link the aged pension to the level of average weekly earnings. This is to ensure that the retired section of the population gains some of the benefits of an increasing productivity level. Chart 3 demonstrates that, over the longer term, there is a tendency for the pension to rise with earnings, for example, the maximum rate of age pension for a single person was 21.9% of average weekly earnings in 1950 and 23.8% in 1986. From a biblical standpoint of care and respect for the aged it does not seem correct to sanction a situation where the standard of living of our retired part of the population is falling further behind that of the whole society. The cost of maintaining the aged pensioners' relative living standards will have to be met and increased taxes are often not welcomed.

Chart 3

Ratio of Maximum Benefits to AWE (1950 to 1987)



The workforce's general coverage by superannuation is slowly expanding as unions, particularly, are beginning to include it as an issue in wage negotiations. Superannuation has traditionally had a favourable tax regime applied to it, ostensibly to encourage people to save for their own retirement and, one would presume, to thereby save the public purse some money. The facts of the situation are, however, less straightforward and the structure of superannuation as it currently stands needs changing if it is truly to fulfil the task demanded of it. Australia has had a history of preferring lump sum payments to annuities or periodic pensions because of concessional tax treatment, unlike other countries. The result was a large capital sum at retirement which people could use for many and varied purposes relying then on the aged pension, when they became eligible, for day to day living expenses. The rules of the game have changed since 1983 and lump sums are progressively becoming closer to pension payments in terms of their tax treatment. This process, as all changes to superannuation must be, is a very long term one.

It appears that superannuation is used to fund early retirement for a number of people (see Chart 2) after which reliance is on the age pension. Aggregate saving behaviour is also affected, it appears, by superannuation savings but there is conflicting evidence as to the final result. What is clear is that the cost of the superannuation tax concessions is fairly high, estimated at $2610 million in 1984-85 and $3140 million in 1985-86. These figures represent a situation of growing superannuation funds — deductible contributions are increasing now while taxable payments will eventually rise in the future. Mature funds may thus have a lower net cost to government revenue in the future. We do need to examine, though, whether this money is being well spent in terms of it achieving its stated objective.

Table 3

Estimated Value of Superannuation Tax Concessions to Prospective Lump Sum Recipients

Starting Salary	Years to Retirement	After-tax Lump sum: With Concessions $	After-tax Lump sum: Without Concessions $	Value of Concessions at retirement: $	Value of Concessions at retirement: % of lump sum
22,300(a)	20	69,000	41,000	28,000	41
22,300	30	131,000	77,000	54,000	41
22,300	40	229,000	128,000	101,000	44
44,600(b)	20	127,000	68,000	59,000	46
44,600	30	247,000	124,000	123,000	50
44,600	40	439,000	203,000	236,000	54

(a) Average Weekly ordinary time earnings at August 1987
(b) Twice AWE

Source: Office of EPAC estimates

Assumptions:
(a) Real earnings increase at 2% per year
(b) Real rate of interest = 4%
(c) Contributions = 10% of earnings
(d) Contributions are paid by the employer
(e) Marginal tax rates as at 1 July 1987, with tax thresholds indexed fully to the rate of growth of average earnings (including lump sum tax thresholds).
(f) Zero inflation

Table 3 provides an estimate of the value of superannuation tax concessions to specific potential retirees. The figures are illustrative only but serve to show that the concessions benefit higher income earners more as they provide relief at the higher marginal rates of tax. It is possible that these people would be able to provide for their retirement without the extra tax concessions not available to those on average weekly earnings. Tax expenditure, like social security expenditure, perhaps needs to be targetted more closely.

A final point for consideration is the desirability of moving closer to a situation of fiscal neutrality. Differing tax treatments for various assets inevitably leads to distortions in economic behaviour. The tax treatment of superannution funds is only a part of the wider question of taxation of savings generally. Though beyond the brief of this workshop on the provision of retirement income it is an aspect which is often ignored in public debates on the topic.

This paper was prepared prior to the changes to superannuation arrangements announced in the May 1988 Economic Statement.