

# Australia

## Australia: Pension system in 2016

Australia's retirement income system has three components: a means-tested Age Pension funded through general taxation revenue; the superannuation guarantee, a compulsory employer contribution to private superannuation savings; and voluntary superannuation contributions and other private savings. Superannuation savings are encouraged through taxation concessions.

## Key indicators: Australia

		Australia	OECD
Average worker earnings (AW)	AUD	82 114	50 853
	USD	59 134	36 622
Public pension spending	% of GDP	4.3	8.2
Life expectancy	At birth	83.2	80.9
	At age 65	21.1	19.7
Population over age 65	% of working- age population	25.0	27.9

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## Qualifying conditions

The Age Pension is payable from age 65 for men and women. Pension age will increase by six months every two years from 2017 until it reaches 67 by 2023. The minimum age for withdrawing superannuation benefits is 55 years for people born before 1 July 1960, but increases gradually for people born after that date, so that the minimum age is 60 for people born after 30 June 1964.

## Benefit calculation

### Defined contribution

The superannuation guarantee was introduced in 1992. It consists of a mandatory employer contribution to an employee's superannuation fund (a private pension plan). Superannuation funds may be operated by employers, industry associations and financial service companies or even by individuals themselves. The mandatory contribution rate has been 9% of employee ordinary time earnings from 1 July 2002 until 30 June 2013. On 1 July 2013, the rate increased to 9.25%, before increasing again on 1 July 2014, to 9.5%. The Government has announced that the superannuation guarantee rate will remain at 9.5% until 30 June 2021. After this, the rate will increase by 0.5 percentage points each year until it reaches 12% on 1 July 2025.

Employers need not contribute for workers earning less than AUD 450 a month, but they can choose to contribute for these workers (this minimum has not been increased in the past). Employers need not also contribute for employees who are working part-time (30 hours or less per week) and under the age of 18. There is also a ceiling to the earnings covered by the superannuation guarantee. Employers need not contribute for employees' pay above this ceiling. For each quarter of the financial year 2015-16 this amount was AUD 50 810 (AUD 203 240 annually).

Low to middle-income earners who make personal after-tax (non-concessional) contributions to their superannuation fund may be eligible for the Government to make a matching 50 per cent co-contribution, up to a maximum of AUD 500 in 2015-16. Contributors with annual incomes less than AUD 35 454 in 2015-16 were eligible for the full co-contribution. For each dollar of income earned above AUD 35 454, the maximum co-contribution is reduced by 3.333 cents, up to a higher annual income threshold of AUD 50 454, above which no co-contribution was payable. If the co-contribution payable for an eligible contributor is less than AUD 20 the amount is increased to AUD 20.

The withdrawal stage of the superannuation guarantee complicates the calculations. Although there are some defined-benefit occupational plans, most employees are members of defined-contribution schemes. Members can withdraw the accumulated capital as a lump sum or as an income stream. In 2014-15, of those who made contributions, just over half had received all or part of their superannuation funds as a lump sum payment. For comparison with other countries, the capital from the superannuation guarantee is assumed to be converted to a price-indexed annuity.

### *Targeted safety net*

The Age Pension is designed to provide a safety net for those unable to save enough through their working life and to supplement the retirement savings of others. An income test and an assets test (means tests) are used to target Age Pension payments to those most in need.

Australia's Age Pension cannot be compared directly to benefits for the aged provided by other OECD countries, which are primarily aimed at income replacement. Australia's Age Pension is a flat rate payment and redistributive in nature. It aims to provide Australian seniors with an income adequate enough to ensure a basic living standard. In addition to cash payments provided by the Age Pension, Australian seniors can be eligible for a comprehensive system of concessions and assistance for health, rent, pharmaceuticals and other living expenses. The Australian government supports private retirement incomes through its superannuation arrangements, subsidised by taxation concessions.

In March 2016, the maximum single rate of pension with the Pension Supplement and Energy Supplement was AUD 873.9 a fortnight equal to an annual entitlement of AUD 22 677.27.

The value of the Age Pension is adjusted biannually. The Age Pension's value is increased in line with the Consumer Price Index (CPI) or the Pensioner and Beneficiary Living Cost Index (PBLCI), whichever is the greater. If necessary further increases ensure that the combined couple rate does not fall below 41.8% of national pre-tax Male Total Average Weekly Earnings. The single maximum basic rate of pension, excluding supplements, is 66.33% of the combined couple rate.

The Age Pension is reduced if annual income from other sources exceeds a threshold known as the 'income free area'. This is adjusted annually in July. In 2015-16, the fortnightly income free areas were AUD 162 for a single pensioner and AUD 144 for couples (or AUD 288 for a couple combined).

The Age Pension has a 'Work Bonus' income test concession designed to encourage people of pension age to continue to work. It allows pensioners to earn up to AUD 250 a fortnight without it being assessed as income under the income test. Pensioners who earn less than AUD 250 in a fortnight can accrue the unused amount of fortnightly concession up to AUD 6 500 to offset future employment income. The combination of the Work Bonus and the pension income free area, allows a single pensioner with no other income to earn up to around AUD 10 730 each year without it affecting their pension.

An assets test also applies. Almost 42% of all pensioners have their benefits reduced by the means test and are therefore on part-rate Age Pension. Within this group 57% have their pension reduced as a result of the income test and 43% as a result of the assets test. About 58% of pensioners are on the maximum rate Age Pension.

In 2015-16, the pension asset test thresholds for homeowners were AUD 205 500 for a single pensioner and AUD 291 500 for a couple combined. For non-homeowners the thresholds were AUD 354 500 for a single pensioner and AUD 440 500 for a couple combined. Assets above these amounts reduce the pension by AUD 1.50 per fortnight for every AUD 1 000 above the amount, for a single pensioner and for a couple combined. The family home is exempted from the asset test.

The Australian Government announced changes to the assets tests in the 2015-16 Budget to rebalance the assets test parameters so as to improve the targeting and long-term sustainability of the pension system.

Starting from 1 January 2017, the changes provided an increase in assets test thresholds. The new amount of assets (excluding the family home) pensioners can hold without any impact on their pension under the asset test is AUD 250 000 for a single home owner and AUD 375 000 for a home owner couple. For non-homeowners, the thresholds were increased to AUD 450 000 for a single non-home owner and AUD 575 000 for a non-home owner couple. The changes also increased the taper rate from AUD 1.50 to AUD 3.00 per fortnight, so that the pension is reduced by AUD 3 per fortnight for every AUD 1000 over the assets test thresholds. The assets test exemption for the family home was not affected by the changes.

Rent Assistance is available for eligible private renters and community housing tenants whose rent exceeds a specified amount. It is paid as part of the pension payment and may be reduced by income and asset tests applying to that payment. The value of the Rent Assistance is adjusted biannually in line with growth in the CPI and is paid fortnightly. In March 2016, the maximum single rate of Rent Assistance was AUD 130.40 a fortnight. This gives an accrued maximum annual entitlement of AUD 3 384.46.

Rent thresholds below which Rent Assistance is not payable are also adjusted biannually. In March 2016, the minimum rent for a single person for which Rent Assistance was payable was AUD 116 a fortnight. Rent Assistance is paid at a rate of 75 cents for each dollar of rent paid above the rent threshold until the maximum rate is reached.

Rent Assistance is not payable to people renting from a government housing authority, or to residents of Australian Government funded nursing homes or hostels.

## Variant careers

### *Early retirement*

Superannuation benefits can be withdrawn from age 55. The earliest age at which superannuation benefits can be withdrawn is increasing for all individuals born on or after 1 July 1960 (see the table below). Individuals who are still working can also access their benefits from preservation age, but only in the form of a non-commutable income stream. The Age Pension is not paid before the qualifying age.

Date of birth	Preservation age
Before 1 July 1960	55
1 July 1960 – 30 June 1961	56
1 July 1961 – 30 June 1962	57
1 July 1962 – 30 June 1963	58
1 July 1963 – 30 June 1964	59
After 30 June 1964	60

### *Late retirement*

It is possible to defer claiming superannuation until after 65 years of age. Employers are required to make superannuation contributions under the superannuation guarantee arrangements for their eligible employees regardless of age. In addition, the Age Pension has a ‘Work Bonus’ income test concession designed to encourage people of pension age to continue to work.

### *Childcare*

There is no specific protection for periods out of work in the superannuation guarantee system. Voluntary contributions are possible during periods without paid work.

## *Unemployment*

There are no credits in the superannuation guarantee system for periods of unemployment. Voluntary contributions are possible during periods without paid work.

## **Personal income tax and social security contributions**

### *Taxation of pensioners*

Older Australians and other Australians who receive a government pension may be entitled to personal tax concessions in addition to the standard reliefs.

The Senior Australians and Pensioners Tax Offset (SAPTO) is available to taxpayers in receipt of a taxable Government pension, as well as to Australians who are of Age Pension age and who meet all of the Age Pension eligibility criteria except the income and/or asset tests (see above). Since 2012-13, the SAPTO has been AUD 2 230 for singles with annual income up to a threshold of AUD 32 279 and is withdrawn at a rate of 12.5% for annual income in excess of the threshold. The offset is fully phased out for singles at an annual income of AUD 50 119 and above. The maximum offset for couples eligible for the SAPTO is AUD 1 602 for each member of the couple, who may have annual income of AUD 28 974 each before the SAPTO is withdrawn at a rate of 12.5% until the credit is fully phased out at an annual income of AUD 41 790 each.

Taxpayers eligible for the SAPTO benefit from a higher value of the low income Medicare levy threshold (in 2015-16 AUD 33 738 for singles and AUD 46 966 combined for couples). This means that pensioners receiving the full amount of the offset will pay no Medicare levy. The normal rate of the levy has been 2.0% of taxable income since 2014-15.

### *Taxation of private pensions*

Generally, superannuation is taxed at two stages: when concessional contributions are made and when investment returns are earned. Individuals who withdraw their superannuation before age 60 may also pay tax on the benefit payment.

Superannuation contributions are taxed as follows:

- When employers or members make *concessional* contributions (that is, contributions for which they claim a tax deduction), in general a 15% tax is levied on the contributions and is paid by the fund.
- Individuals with an adjusted taxable income up to AUD 37 000 receive a Low Income Super Contribution: a government payment (in effect a tax rebate) of up to AUD 500 per year, starting from 2012-13. For payments in relation to contributions made on or after 1 July 2017 the Government has legislated that this payment will be known as the Low Income Super Tax Offset.
- Individuals with a sum of income and concessional contributions above AUD 300 000 will pay an additional 15% tax on concessional contributions on the portion of the income that exceeds the AUD 300 000 threshold, starting from 2012-13. For contributions made on or after 1 July 2017 the Government has legislated that this threshold be reduced to AUD 250 000.
- When a member makes a *non-concessional* contribution (that is, a contribution from after-tax income) the member has already paid income tax on the contribution at their normal marginal tax rate. No further tax is applied to the contribution.

Investment earnings of the superannuation fund are also taxed at 15% during the accumulation phase (however, the effective tax rates are usually lower through imputation credits and the capital-gains-tax discount). Investment earnings on assets supporting a pension are tax free.

Since 1 July 2007, superannuation benefits paid from a taxed source (that is, where tax has been paid on contributions and earnings), either as an income stream or as a lump sum, are tax free for people aged 60 and over. Where benefits are paid from a taxed source to a person below the age of 60, those benefits are subject to taxation. Benefits paid from untaxed schemes (mainly affecting public servants) are also taxed, but at reduced rates when paid to those aged 60 or over.

The Government has legislated that from 1 July 2017 there will be an AUD 1.6 million cap on the total amount of superannuation savings that can be transferred to the (tax-free earnings) retirement phase. The cap will index in line with the consumer prices index in AUD 100 000 increments. This is not a cap on the amount of superannuation in the retirement phase – earnings in the retirement phase can grow above AUD 1.6 million, but no more than AUD 1.6 million can be transferred to the retirement phase. Superannuation savings in excess of the cap can either remain in the accumulation superannuation account, where the earnings are taxed at 15 per cent, or be removed from the superannuation environment. Members who breach the cap will be liable to pay tax on the notional earnings attributed to the excess capital.

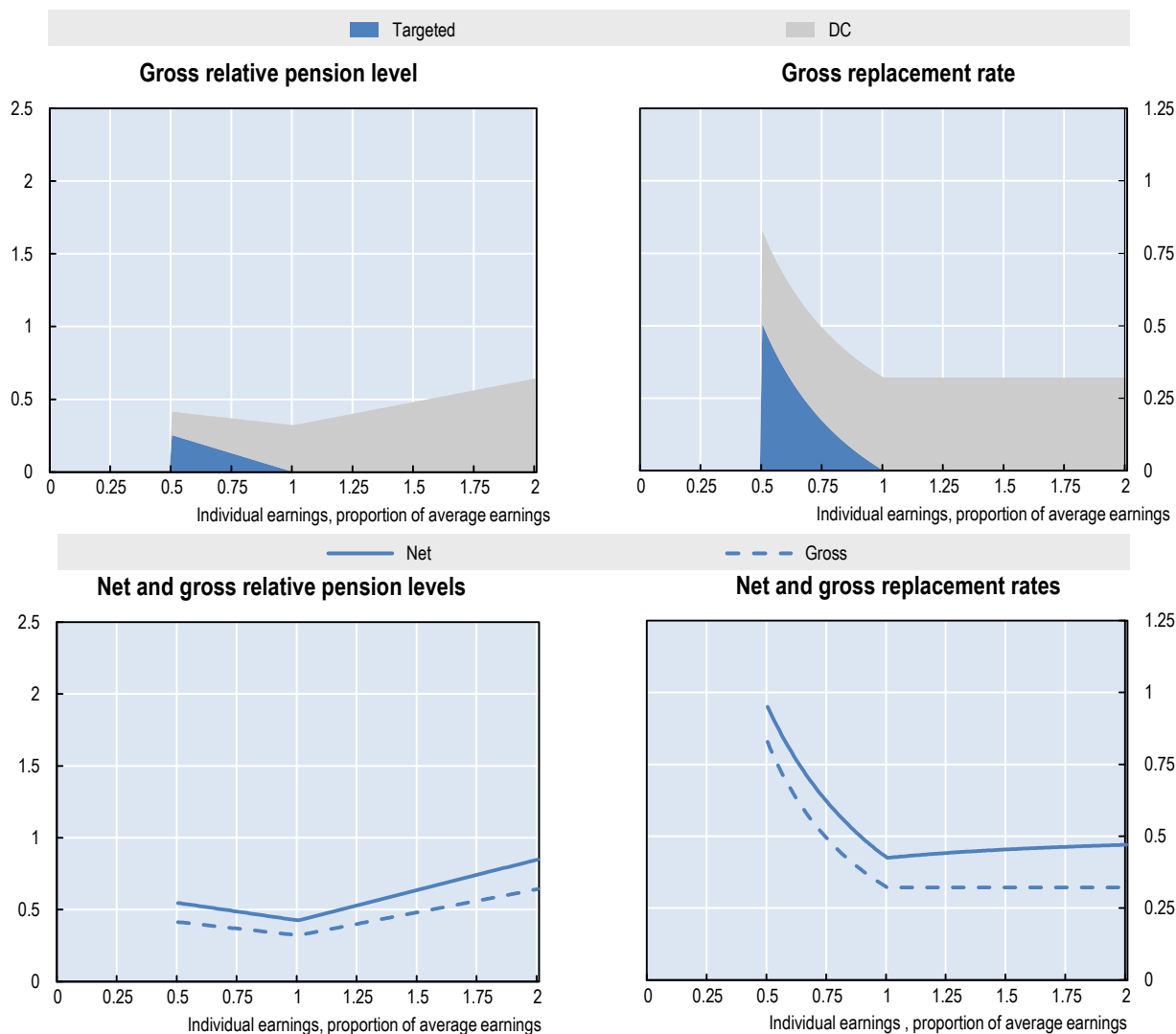
Furthermore, superannuation concessions are also limited by caps on contributions to superannuation.

- *Concessional* contributions that exceed an annual threshold are subject to an additional tax levied on the individual. The annual threshold is AUD 30 000 in 2016-17 and AUD 35 000 for people aged 50 years and over. The Government has legislated to lower the cap to AUD 25 000 on 1 July 2017 for everyone regardless of age. It will also allow catch up contributions of unused cap space from the prior 5 years for people with balances less than AUD 500 000, with effect for the 2018-19 and later financial years.
- *Excess concessional* contributions are taxed at the individual's marginal tax rate plus relevant levies, less an offset for tax payable by the fund, plus an interest charge. The individual may choose to pay this tax by withdrawing amounts from the fund.
- *Non-concessional* contributions are subject to a cap of 6 times the concessional contributions cap (i.e. AUD 180 000 in 2016-17), though members can bring forward up to two additional years' contributions, allowing them to contribute up to AUD 540 000 in any three-year period. The Government has legislated to lower the annual cap to AUD 100 000 for those with superannuation balances below AUD 1.6 million, with a 3 year bring forward period available for individuals under age 65. Transitional arrangements (reducing the person's cap amount) also applied if a person triggered the bring forward period in the 2015-16 or 2016-17 years and did not fully utilise the bring forward amount available before 1 July 2017.
- An additional lifetime non-concessional contribution cap applies to contributions derived from certain capital proceeds of eligible small businesses. This is in addition to the general non-concessional cap and in 2016-17 the lifetime threshold was AUD 1 415 000.
- Excess non-concessional contributions are subject to tax at the top marginal personal income tax rate plus relevant levies. However, as of 1 July 2013, individuals are able to avoid the tax by withdrawing the excess non-concessional contributions and associated earnings from the fund, with only the earnings being effectively taxed at the individual's marginal tax rate plus levies.

### ***Social security contributions paid by pensioners***

There are no social security contributions in Australia. The Age Pension and other benefits are financed from general revenues.

## Pension modelling results: Australia in 2063 retirement at age 67



Men Women (where different)	Individual earnings, multiple of average					
	0.5	0.75	1	1.5	2	3
Gross relative pension level (% average gross earnings)	41.4	36.8	32.2	48.2	64.3	79.5
Net relative pension level (% net average earnings)	54.6	48.6	42.6	63.7	84.9	105.1
Gross replacement rate (% individual gross earnings)	82.8	49.1	32.2	32.1	32.1	26.5
Net replacement rate (% individual net earnings)	95.0	61.8	42.6	45.4	47.0	41.6
Gross pension wealth (multiple of individual gross earnings)	18.2	13.7	11.2	9.0	8.1	7.3
Net pension wealth (multiple of individual net earnings)	20.9	17.3	14.9	12.7	11.8	11.4

Assumptions: Real rate of return 3%, real earnings growth 1.25%, inflation 2%, and real discount rate 2%. All systems are modelled and indexed according to what is legislated. Transitional rules apply where relevant. DC conversion rate equal 90%. Labour market entry occurs at age 20 in 2016. Tax system latest available: 2015.

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