

How we could make the retirement system more sustainable

Written by The Conversation

Our current retirement system is simply not sustainable, as our population ages and life expectancy increases. Australia incentivises people to structure their finances so they are asset rich and cash poor. They are then able to claim the pension and can leave an inheritance, which is in part paid for by taxpayers.

We need to do something to make the system more sustainable, and one idea is to restructure the system so that it works more like [HELP student loans](#) - you get the benefit up front but only pay it back when and if you are able. Pensions would be treated as a liability for retirees, to be repaid from the estate of the person when they pass away.

If the estate is insufficient, the debt does not need to be repaid and is written off. But if there is sufficient money to repay the debt then taxpayers are paid first, before anything can be inherited. This way the retirement system becomes more sustainable, and is targeted at those that need it.

This idea is not entirely original. The United Kingdom [has legislated](#) for local governments to provide support payments so that the elderly can receive care. This is then repaid when a person sells their home or passes away. The policy is largely revenue neutral as [only a small percentage of loans are written off](#)

While these agreements have commercial underpinnings, there is no reason something similar couldn't be integrated into our welfare system to provide a safety net.

Why we need to do something about the retirement system

Social security and welfare is the [single largest source of expenditure for the federal government](#). The largest component of this is assistance to the aged which is primarily income support for seniors. This was A\$29.8 billion [in 2005/6](#), or 14.6% of total expenditure, and has risen to A\$62.3 billion [in the latest budget](#), which is 15.9% of expenditure.

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Assistance to the aged has been increasing at the rate of 6.9% per year, compounded. It is unlikely that this trend will improve, as we have an ageing population.

There has been [a steady increase](#) in the proportion of the population aged 65 and over. It has increased from 12% in 1996 to 15.3% in 2016. At the same time [life expectancies have increased](#)

There have been [some measures to address this](#). The Keating government introduced compulsory employer contributions to superannuation from 1992, although it was only 3%. This was progressively increased to 9% by the Howard government from 2002.

But these policies are only recent and it will be many years before they provide material levels of income in retirement. For a person earning A\$60,000 the superannuation contributions and income calculated at an after tax return of 4% (adjusted for inflation) will provide a lump sum of just over A\$225,000 after 25 years and just over A\$500,000 after 40 years (in 2017 dollars).

In other words, this is simply too little, too late.

The structural problem within our current system

Meanwhile, our current retirement policies [incentivise people to maximise their dependence on welfare](#)

Recent [superannuation reforms](#) have imposed restrictions on contributions and increased the taxation of contributions on higher earners. These changes ignored the impact that receiving the pension has on the lifetime tax paid by low income earners. A single person receiving the full pension (no supplements) will receive A\$461,760 in (2017 dollars) over 20 years. This is a huge incentive to do whatever you can to receive the full pension.

In other words, spend now and get the pension.

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Furthermore, the structure of the assets test [incentivises people to hold on to their family home](#), even if it is inappropriate to their current needs. Any capital gains are also exempt from capital gains tax. This is problematic for a range of social and economic reasons, but most obviously it creates a class of retirees that are asset rich and cash poor.

The answer is not to simply increase pensions. It is to open up pensions to everybody, but treat them as a liability to be repaid. Welfare is not an entitlement, it should be based on need. Under the current system meeting that need is increasingly difficult.

Even if this is not the answer, something needs to be done. The question is whether any of our political parties have the stomach for these sorts of changes and whether young people will start to understand the massive intergenerational equity problems the current system creates.

Peter Wells does not work for, consult, own shares in or receive funding from any company or organisation that would benefit from this article, and has disclosed no relevant affiliations beyond the academic appointment above.

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