

One of the Government's many challenges is to ensure that Australia's superannuation policy takes the pressure off the cost of funding the Aged Pension.

Under current arrangements, an individual transitioning their superannuation to a pension is able to take out all of the money saved as a tax free lump sum.

For most Australians, this will mean they will have more money to spend than they ever have had to spend in their life time. Will they invest the money wisely for their retirement or will they be tempted to spend their savings and rely on the Aged Pension?

This issue is of concern to the major super funds as they are concerned about the liquidity risk of superannuates withdrawing their money out on retirement.

This leads to an unwillingness by these superannuation funds to invest in long term illiquid assets such as infrastructure projects.

There is one simple solution that solves these challenges.

The solution is to require individuals who are transitioning into pension phase, and who wish to benefit from the current tax treatment of pension funds and pension withdrawals, to hold assets in their pension superfund equal to the present value of the Aged Pension based on existing mortality tables. Amounts in excess of the present value of the Aged Pension can be withdrawn as a lump sum.

As the retiree ages, the present value of the Aged Pension reduces and therefore the amount of assets required to be held in their fund also reduces.

This one change takes the budgetary pressure of funding the Aged Pension for an ageing population and removes the liquidity risk thereby enabling superannuation funds to invest in long term illiquid assets such as infrastructure.

There is an anomaly in the regulations to the Life Act which has remained unchanged since 1945.

The term "annuity" has been given special status by a regulation in the Life Act that states an annuity with a maturity greater than 10 years constitutes a life policy and as such can only be issued by a life company.

An annuity is just a simple fixed interest investment that pays back the principal over the life of the security.

The effect of this anomaly is to deny investors a market rate of interest when compared to fixed interest investments which repays principal on maturity.

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