

Soft Compulsion

In general, Local Government employees in Western Australia are more likely to have accumulated a sufficient retirement nest egg when compared to their non-Local Government counterparts. Why is this so?

There are perhaps many factors but two significant ones are education about superannuation and the matching schemes offered by most Local Governments in WA.

The WA Local Government Superannuation Plan (WALGSP) has conducted hundreds of seminars and thousands of “one on one super health checks” over the last few years. The result of this is much greater take up of employer matching and a significant increase in awareness of the Federal Government co-contribution scheme.

Employer matching is where the employer contributes something extra to an employees’ superannuation, above and beyond the 9% SG, provided the employee also contributes something extra. Some Local Governments in WA offer up to 10% additional contribution if the employee also contributes 10%. A competitive employment market has also contributed to employers reviewing and improving their matching offerings.

According to an analysis of current member balances and contribution patterns and using a set of projection assumptions, 63% of members of WALGSP who work for Local Government are on track for retirement adequacy¹. Whilst this rate has been steadily increasing over the last two years the rate of increase has slowed. This means there is still a large number of West Australian employees, in Local Government, who, without changing their savings behaviour, are likely to end up with insufficient savings to fund a comfortable retirement. The situation in other states is likely to be similar or even worse given that employer matching is most prevalent in WA.

Local Government managers have the opportunity to change this and by doing so, demonstrate, that

once again Local Government is forward thinking when it comes to creating work environments of choice.

Soft Compulsion is perhaps the silver bullet for killing this retirement adequacy shortfall. So what is Soft Compulsion?

Essentially it involves individuals doing something extra unless they “opt out”. The idea is that employees automatically have a portion of their salary paid into their super account unless they choose not to. This concept can be applied for new employees or existing. With new employees, they are advised at the time of job offer that a percentage (say 1%) of their salary will be paid into their super, in addition to the 9% SG. The new employee has to make a selection NOT to have the 1% contribution paid into super.

For existing employees, the easiest way to implement this concept is at the time of a salary increase. For example, if we assume an incremental pay rise of 3% is on offer, the default position is for 1% to go into super and the remaining 2% is added to cash salary, unless the employee elects NOT to.

For employees of organisations that offer a matching scheme, the benefit can be even greater. For example if an employer offers one for one matching (up to a maximum of, say 5%) then an employee effectively receives an extra 1% by choosing to do nothing.

The table below illustrates the scenario for an employee currently earning \$45,000 per annum including 9% SG super. The proposal is for a 3% CPI salary adjustment. Under the soft compulsion concept, the employee will receive a 3% pay rise in the form of 2% added to cash salary, 1% extra into super as a post tax contribution (to take advantage of the Federal Government Co-contribution) and an extra 1% from the employer under their matching scheme.

¹ Retirement Adequacy in this case means having accumulated a lump sum that is equivalent to six times annual salary for the year immediately prior to age 60. Assumes 8% pa investment growth, 3% Salary Growth

<u>Financial Year Calculation</u>	<u>Current Situation</u>	<u>No Matching</u>	<u>Matching</u>	<u>Matching</u>
	<u>(Pre 3% Increase)</u>	<u>(Opt Out)</u>	<u>(Default Option)</u>	<u>Option 2</u>
			<u>Post Tax</u>	<u>Salary Sacrifice</u>
Package salary (includes SGC)	\$45,000	\$46,350	\$46,775	\$46,775
Less Super Guarantee Contribution (SGC)	\$3,716	\$3,827	\$3,827	\$3,827
Less Employer Super Match (the extra 1%)			\$425	\$425
Less Salary Sacrifice Contribution				\$425
Gross taxable salary	\$41,284	\$42,523	\$42,523	\$42,098
Other Assessable Income*	\$0	\$0	\$0	\$0
Less tax payable [incl Medicare]	\$6,854	\$7,245	\$7,245	\$7,111
Less personal contribution [after tax]	\$0	\$0	\$425	
Net take-home salary [A] : Annual	<u>\$34,430</u>	<u>\$35,278</u>	<u>\$34,853</u>	<u>\$34,987</u>
Net take-home salary [A] : Fortnight	<u>\$1,324</u>	<u>\$1,357</u>	<u>\$1,341</u>	<u>\$1,346</u>
Net contributions to super p.a.:				
Employer Super Guarantee [net of contribution tax]	\$3,158	\$3,253	\$3,253	\$3,253
Employer Additional [net of contribution tax]	\$0	\$0	\$361	\$361
Salary sacrifice [net of contribution tax]	\$0	\$0	\$0	\$361
After tax personal contribution	\$0	\$0	\$425	\$0
Government co-contribution	\$0	\$0	\$425	\$0
Total net contributions to super [B] : Annual	<u>\$3,158</u>	<u>\$3,253</u>	<u>\$4,464</u>	<u>\$3,976</u>
Total net contributions to super [B] : Fortnight	<u>\$121</u>	<u>\$125</u>	<u>\$172</u>	<u>\$153</u>
Total net benefit [A + B] : Annual	<u>\$37,588</u>	<u>\$38,531</u>	<u>\$39,317</u>	<u>\$38,963</u>
Total net benefit [A + B] : Fortnight	<u>\$1,446</u>	<u>\$1,482</u>	<u>\$1,512</u>	<u>\$1,499</u>

*It is assumed that there is no other assessable income or reportable fringe benefits

Projected Additional Benefit of Default Matching – Post Tax Option

\$78,200 over 30 years (in today's dollars)

Projected Additional Benefit of Default Matching – Salary Sacrifice Option

\$44,100 over 30 years (in today's dollars)

Assumptions

- Investment return of 7% p.a. net of fees and taxes.
- Cost of living increasing 3% p.a.
- Default Matching remains at 1%
- Salary at commencement is \$45,000p.a. and increases at 3% p.a.
- Member has no other assessable income or reportable fringe benefits and qualifies for Government Co-Contribution benefit.
- 2009/2010 Tax Rates

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