Submission to the Tax Forum: Personal Tax (Superannuation)

Dr Carol J Steiner

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Tax on Super Contributions: Tax concessions for super contributions were introduced to encourage more saving for retirement. Instead, tax concessions for super contributions have created a tax minimisation scheme for high-income earners who would accumulate substantial retirement savings without the tax inducements, while doing little to encourage low- and middle-income earners to voluntarily contribute to super.

ABS Social Trends (2009) reported that only 20% of workers voluntarily contribute to super after tax and only an additional 7% do so through salary sacrifice, most of them being higher income earners. Further, super tax concessions cost the budget tens of billions of dollars every year, with no guarantee that these concessions will reduce the demand for pensions.

These are very good reasons

- *to abolish tax concessions on voluntary super contributions; and*
- *to make employer Superannuation Guarantee (SG) contributions tax-free.*

The former will end salary sacrifice as a tax minimisation scheme for high-income earners, freeing some of the taxes no longer foregone to be used for the latter, which will increase the retirement balances of the vast majority of workers whose only super savings come from employer contributions. Because the tax-free status applies only to SG contributions, it will be equitable and capped, so as not to advantage higher income earners or open-endedly damage tax revenues.

These two changes will also make it simpler and more efficient for super funds and the ATO to manage and monitor tax obligations. We would no longer need the concessional and non-concessional distinction between contributions. Nor would we need to have any limits on how much can be voluntarily contributed to super or when, as all contributions apart from SG ones would be after-tax contributions.

Tax on Super Earnings: In the interests of efficiency and to make investments in superannuation more attractive than market investments, *the current 15% rate of tax on earnings within superannuation should be maintained, but it should be a flat tax, not subject to deductions, offsets or credits.* 15% is already a very favourable tax rate and should not be reducible. This will simplify tax management and reporting for super funds and make it easier for the ATO and investors to monitor tax obligations.

Tax on Benefits: Tax concessions on superannuation contributions and earnings to encourage saving for retirement are wasted if superannuation is not used to reduce pension demand and increase the financial security of retirees. Tax-free withdrawals from superannuation funds thwart these aims when they are not regulated.

Currently, people can start emptying out their super savings while paying low or no tax long before they reach pension age, once they reach “preservation age.” They can take lump sums to buy caravans and boats, to travel, to give gifts to their children, and to indulge themselves in any way they like, confident that a pension will be waiting for them when they need it.

This makes mugs of the tax system, the government and taxpayers who have been foregoing billions in taxes so people can look after themselves in retirement. This has to stop if we expect to reduce demand for pensions.

Therefore, I recommend *lump sum withdrawals from super between preservation age and pension age be tax-free only*

- So long as total lump sum withdrawals constitute up to no more than 10% of one's total super savings or $20,000, whichever is less; or
- When lump sum withdrawals are made only for these special purposes
  - Paying out mortgages in full,
  - Funding major medical and dental procedures or treatments, and/or
  - Making provision for care of disabled dependents.

All other lump sum withdrawals should be treated as income for tax purposes and taxed at the taxpayer's marginal rate so there is no advantage or inducement to reduce one's super savings before pension age.

Further, *all lump sum withdrawals from super between preservation age and pension age, except for the special purpose withdrawals, should be counted in the pension assets test*. This is to prevent people, especially well-funded retirees, from emptying out their super accounts just enough to qualify for the pension.

In addition, *all lump sum withdrawals from super between pension age and pension application should be counted in the pension assets test,* again to prevent retirees running down their super savings by delaying applying for the pension.

Finally, *the value of all Transition to Retirement Pensions (TARPs) drawn between preservation age and pension age should be included in the pension assets test*.

Although not strictly a tax issue, *I'd also recommend that anyone with a super balance of more than $500,000 (single or couple) between preservation age and pension age be required to purchase or preserve the value of an annuity paying the equivalent of a full pension for their average life expectancy*. This is to ensure that they do not run down their super balance indulgently to qualify for a pension. *People with super balances between $500,000 and the assets test limit for a part pension should still be eligible for a health care card even if their annuity makes them ineligible for even a part pension.* The $500,000 figure represents a best guess at the amount needed to fund an annuity equivalent to a couple's aged pension for normal life expectancies. It should be properly set by actuaries annually, but only for people who reach preservation age in that year. It should not be adjusted annually for people already beyond their preservation age.

These tax changes should genuinely reduce demand/eligibility for pensions among middle- to high-income earners with substantial super balances, while making it possible for more low- to middle-income people to go into retirement debt and worry free, with new dentures, hips or knees replaced, with secure accommodation and care arranged for their disabled dependents, and with a bit of savings preserved for emergencies or indulgences in their retirement. These tax changes will also ensure that taxpayers get some economic and social benefit from all the taxes foregone in superannuation tax concessions. And we shouldn't overlook the substantial efficiency dividends offered by a much simpler system of superannuation taxation.