Tax White Paper Task Force
The Treasury
Langton Crescent
PARKES ACT 2600

Re: Tax Discussion Paper submission – superannuation

Thank you for the opportunity to make a submission as part of the Tax White Paper process.

This submission focuses on question 22 in the Tax Discussion Paper:

> How appropriate are the tax arrangements for superannuation in terms of their fairness and complexity? How could they be improved?

Though superannuation has been subject to constant change, and of period of stability and certainty would be welcome, this should not prevent necessary or beneficial reforms.

1.0 Superannuation tax concessions: contributions and accumulation phase

There are many aspects of superannuation which are unnecessarily complicated. One such area is the restrictions on contributions, including the 10% rule, work test and the age-based restrictions. As the Australian workforce ages people need flexibility to move between work and retirement whilst saving. The rules restricting some people from contributing to superannuation, on the basis of age or type of employment, should be abolished.

The superannuation system lacks sufficient benefit for the superannuation guarantee contributions of low income earners, or incentive for them to make additional contributions. Low income earners should not pay more tax on their compulsory superannuation contributions than their effective tax rate on salary and wages. People who will likely draw upon the age pension should be encouraged to build some superannuation savings to supplement the pension in retirement.

On a related note the Low Income Superannuation Contribution (LISC), currently scheduled to cease, is a good policy which does not require additional action by taxpayers, unlike the co-contribution. The LISC should be retained and indexed to increases in the superannuation guarantee rate, so that it continues to serve the purpose of offsetting the contributions tax on compulsory superannuation contributions of low income earners. The co-contribution should be re-evaluated for cost-effectiveness.

The concessional contributions cap is too high for most people to benefit from in most years, while also being too low to allow some people, such as small business owners, to catch up on super contributions when approaching retirement. As saving for retirement should occur over decades an annual contribution cap makes little sense. A lifetime concessional contributions cap would be more effective.

Concerning wider reform of the superannuation contribution rules the simplest way would likely be to extend the LISC, both in terms of the amount of contributions tax offset and the income level at which people can access the concession, while lowering the income threshold for Division 293 tax.

Another option would be to abolish both the LISC and Division 293 tax and instead institute a marginal tax rate system for concessional contributions. Under this change an amount of superannuation contributions each year, such as $5,000, would be subject to no contributions tax, with progressively higher tax rates applying to higher contribution brackets. However to avoid complex administration this would require taxation of super contributions to occur at the individual level, as recommended by the Henry Tax Review.

2.0 Superannuation tax concessions: retirement and pension phase

As noted in the Tax Discussion Paper the different tax rates applying to super funds in accumulation phase and pension phase creates tax planning opportunities. The Henry Tax Review recommended aligning the tax rates between accumulation and pension phase at 7.5%. The Financial System Inquiry, though unable to make tax related recommendations, did suggest aligning the tax rates as this would "reduce costs for funds, help to foster innovation in whole-of-life superannuation products, facilitate a seamless transition to retirement and reduce opportunities for tax arbitrage."

I concur with this assessment, and add that such a change would return the decision to commence a pension to the need for income in retirement.

Alternatively, reforms could be made to the rules for Transition to Retirement Income Streams. When announced the concept was that people would take increasingly higher pension payments while slowly decreasing hours worked. Instead there is a tax incentive, the concession on income in pension phase, to take a pension while still working full time. There is limited reason to provide a tax incentive for drawing a superannuation pension earlier than needed. One option would be to not allow super funds to claim Exempt Current Pension Income (ECPI) for Transition to Retirement pensions.

3.0 Reforming superannuation: change and complexity

In closing I would like to make a few general comments about changes to the superannuation rules.

In recent years some superannuation policies, if implemented, would have resulted in significant increases to the administrative burden on superannuation funds. This was often because measures better suited to being implemented at the individual level were instead designed to apply at the super fund level. It should be noted that super funds do not have detailed knowledge of the activities of the member individually or in relation to other super funds. Additionally there is a significant time lag between when transactions occur and when information is collated and lodged in a tax return. When designing a superannuation policy consideration should be given to whether it is better suited to being implemented at the individual or fund level.

There are now over one million SMSF members and therefore a similar number of SMSF trustees, or directors of corporate trustees. As such, thought should be given in the designing of a superannuation reform or policy to the administrative burden it places specifically on SMSF trustees.

Finally, there are issues between the operation of the superannuation and age pension systems which are not going to be considered as part of the Tax White Paper process. The government should give strong consideration to conducting a Review of Retirement Income. One issue which should be included in the terms of reference of such a review is calculating at what level the superannuation guarantee rate should be set to meet the objectives of the superannuation system, and when this rate should be reached.

About the Author: Luke Smith

I am a CPA and Tax Agent, with a background in public practice accounting for SMSFs and an interest in superannuation and retirement issues. I write for SolePurposeTest.com, an SMSF and superannuation news site for SMSF trustees and professionals.

Contact: submissions@lukeksmith.com