FINANCIAL PLANNING
ASSOCIATION *of* AUSTRALIA

Tax Discussion Paper

FPA SUBMISSION | 5 June 2015

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

1 June 2015

RE: Tax Discussion Paper

Dear Sir/Madam,

The Financial Planning Association of Australia (FPA) welcomes the opportunity to respond to the Federal Government's tax discussion paper. Our hope is that this discussion paper is the beginning of systemic, generational change in the Australian tax system.

The discussion paper, as well as the Tax White Paper process generally, is an opportunity to renew the policy and regulatory framework that underpins our taxation system.

Our submission is informed by the FPA's fundamental policy principle of serving the public interest, and focuses on the elements of the Australian taxation system that intersect with the experiences and needs of professional financial planners and their clients.

There are many Australians who are financially excluded from financial services (including financial advice services), and we call on the Government to address this reality. We also call on the Government to use the Tax White Paper process to establish broad political consensus on the appropriate model for Government subsidies for retirement incomes.

Lastly, the tax policy development and tax administration processes in Australia need to be updated to reflect changes in technology and the complexity of the tax system.

Thank you again for the opportunity to participate in the Tax White Paper process. If you have further questions please do not hesitate to contact me on 02 9220 4500 or dante.degori@fpa.asn.au.

Yours sincerely,

Dante De Gori
General Manager Policy and Conduct
Financial Planning Association of Australia

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Treasury consultation

FPA submission to:

The Treasury

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1 – Executive Summary

Australians are best served by a tax system that is fair, accessible, and robust. These system values must also be embodied by the agencies that administer the tax system, as well as those who and establish new policies and review existing policy settings.

The complexity of the Australian taxation system produces challenges to the fairness, accessibility, and robustness of the tax system, and often is considered in isolation of the broader tax and transfer system. In our view, future tax policy development and assessment of fairness should be cognisant of the broader tax and transfer system.

As the peak professional body for financial planning in Australia, our view is that the complexity of the tax system is a driver of financial product complexity and complex financial strategy, and this can place the tax efficiency of financial products and strategies ahead of the investment case or the holistic suitability to the client. This is a challenge for the profession itself, but it is also a challenge for the tax system as financial innovation challenges the integrity of the tax system.

Tax system complexity also creates financial exclusion and inequality of opportunity for those without the financial literacy or access to professional advice required to interact with the system. The FPA is encouraged that the tax discussion paper includes questions that address the fairness and complexity of the tax system and the superannuation system.

Our view is that policy settings that reduce the complexity of the system (such as increasing technology-based interaction with the ATO on superannuation matters) or measures that reduce the impact of complexity (such as improving accessibility to professional financial advice) should be canvassed by the Tax White Paper as solutions to financial exclusion caused by complexity.

With respect to taxation and investment, we encourage the Treasury and the Government to adopt a wide-ranging examination of existing deductions and concessions to ensure that the initial policy basis for their introduction remains relevant, as well as ensuring that the existing structure or features of the measure does not introduce unfairness, unnecessary complexity, or challenges to system integrity. In our view, gearing strategies and capital gains tax both influence investment and savings decisions made by Australians, and influence them differently depending on whether or not they seek professional financial advice.

The relationship between taxation and superannuation also introduces complexity, as the operation of the tax system will affect the policy outcomes of the Australian retirement income strategy with respect to superannuation. The FPA's view is that broad political consensus on the policy intention of superannuation should drive tax reform for the superannuation system, as well as measures to reduce complexity and improve the accessibility of financial advice. Furthermore, the provision of aged care and disability care is fundamental to a holistic retirement income strategy and the tax system is a fundamental driver of incentives and disincentives to address aged care and disability care needs.

Lastly, robust tax policy development and tax review processes need to incorporate industry feedback that is driven from regulated entities, as well as their professional associations and other industry bodies. While the FPA is satisfied with the existing formal consultation arrangements for Government or agency-led change, we are concerned about issues that professional associations and other entities face a somewhat informal mechanism for raising technical issues. Where there is an established avenue to raise matters with Federal regulatory agencies, the result of this process may also be informal and/or uncertain from a legal point of view.

Our submission separates recommendations from responses to the discussion questions in order to provide context to our answers and provide additional matters for the Treasury and the Government to consider as part of the Tax White Paper process.

2 – Systemic issues and tax complexity

2.1 Complexity and financial product recommendations

Financial products are frequently developed to take advantage of instances where the tax system is used to promote particular economic outcomes (e.g. promoting investment in Australian companies, manufacturing, and agriculture). The tax efficiency of financial products is a key aspect of financial advice, and the complexity of the tax system can be an influencing factor in financial product recommendations, occasionally to the detriment of individuals and the integrity of Australian financial markets.

The relationship between tax efficiency and financial planning recommendations was elaborated in our responses to the Senate inquiry into forestry managed investment schemes in 2014 and the Parliamentary Joint Committee inquiry into agribusiness managed investment schemes in 2009. In our view, tax complexity is a driver of financial product complexity, as financial products can be designed to trigger various tax laws and rulings which result in deductions. In turn, the complexity of financial products is a risk factor that drives misselling, compliance-driven disclosure documents (opposed to client-focused disclosure), and conflicts of interest in remuneration structures.

In the case of non-forestry agribusiness MIS, the 2009 Parliamentary Joint Committee inquiry found that:

> "…the collapse of Timbercorp and Great Southern has undoubtedly focussed investors' attention on the importance of investing in commercially viable MIS. Such sentiment should temper the distortions evident when tax incentives cloud judgment about the viability of some projects"[1]

The Committee also emphasised the risks inherent in opaque MIS administration and high cost bases for schemes, stating that:

> "…there is currently potential for MIS to use unprofitable high cost structures to provide greater tax deductibility to investors, while directing a proportion of this tax-related investment to related entities charging above commercial rates for project services. Where investor focus is on minimising tax, rather than investing in the most profitable venture, this directs capital away from profitable uses and disadvantages traditional farming enterprises by increasing natural resource costs and encouraging oversupply."[2]

In the case of agribusiness MIS that caused significant investor detriment between 2007-2010 (such as Timbercorp, Great Southern, etc.) the complexity of the tax law *and* the tax administration and policy process caused opaque investment structures to be more attractive to retail investors than they

[1] Parliamentary Joint Committee on Corporations and Financial Services, Inquiry into aspects of agribusiness managed investment schemes (September 2009) p 46
[2] Above n 2 at pp 45-46

would otherwise be on their merits as an investment. In our view, the Treasury should consider how complexity in the tax system (whether derived from the laws, the administration, or the policy review process) affects outcomes for those who participate in the financial services sector.

2.2 Complexity and financial exclusion

The complexity of the Australian tax system is one of the key drivers for Australians to seek professional financial advice. The complexity of tax laws and tax administration in Australia makes it difficult for everyday Australians to plan for the future without the assistance of a financial planner.

The Tax Discussion paper makes the following observations regarding the impact of tax system complexity on Australians:

> "Complexity can divert resources away from more welfare-enhancing activities. It makes it more difficult for taxpayers to identify their tax obligations, and to incorporate tax consequences into their decision-making, without significant professional advice. While some professional advice is likely to be necessary to manage the innate complexity of the tax system (especially for business taxpayers), the extent of tax advice currently relied upon suggests the system is overly complex. Time and resources spent by taxpayers or their agents on their tax affairs is time not spent innovating, creating products, delivering services, generating wealth, or enjoying leisure."[3]

The FPA agrees with this assessment, but in our view the complexity of the tax system creates further problems for Australians that are connected to the uncertainty of circumstances when making a financial plan for the future.

- **Uncertainty of client situation** – Australians face risks that are common to the human experience, as well as particular risks connected to our environment, our climate, and our way of life. Our financial system has evolved to meet the needs of the many Australians who seek to address these risks, and Australian society has experienced significant financialisation as a result. The tax implications of this financialisation leave Australians with a significant advice need. As such, the complexity of the tax system causes Australians to become uncertain about how changes in their financial position will affect their tax affairs. This uncertainty creates a need for advice.

- **Regulatory and legislative change** – The complexity of the Australian tax system is compounded by the rate of change within the system. The number of avenues through which tax law and policy changes, as well as the number of entities who have the power to make tax changes with significant effects on the financial position of Australians, cause many to avoid keeping pace with the changes and seek financial advice instead.

[3] The Australian Government the Treasury, 'Tax Discussion Paper' (March 2015) p 169

- **Interaction of tax law and other systems** – The Discussion Paper notes that "the interaction between different parts of the tax law can create unintended incentives or disincentives that may be inconsistent with good policy outcomes. Confronted with this complexity and the opportunities it creates, taxpayers who can afford it are more likely to seek expert assistance to manage their tax affairs".[4] This is also true of the interaction between tax law and superannuation, tax law and investments, and tax law and retirement planning. The complexity of the tax system is compounded by its interaction with other complex systems and the administrative requirements of those systems, and forms a barrier to participation for the majority of those without access to professional advice.

As a result, the complexity of the tax system makes it more difficult for Australians to plan for their future without professional financial advice. In 2014, 16.9% of Australian adults are financially excluded to the extent that they only own one basic banking product.[5] Over 80% of Australians do not seek financial advice, and our research indicates that two million Australians have an unmet financial advice need. 30% of those do not intend to seek financial advice in future cite the cost as a key reason.[6] As a result of the costs involved in addressing tax complexity, the complexity of the tax system itself promotes financial exclusion.

It is not in the interests of a fair, egalitarian, and meritocratic society that Australians experience inequality of opportunity as a result of complexity in the tax system. We recommend that the Tax White Paper considers several policy options to alleviate the impact of system complexity on the ability of Australians to plan for their future:

- **Voucher/rebate system for advice:** A direct subsidy or rebate for seeking professional financial advice is the simplest avenue to assist Australians who are affected by tax system complexity. As the discussion paper states "taxpayers who can afford it are more likely to seek expert assistance to manage their tax affairs" in response to "complexity and the opportunities it presents."[7] A voucher/rebate system would be targeted at those who cannot afford even basic financial advice to help plan their financial affairs into the future.

  Controls on cost, quality of advice, and subject matter of advice can be implemented through a federal scheme to subsidise financial advice. The scheme can include a whitelist of licensees and authorised representatives who qualify for the subsidy on the basis of compliance with the scheme controls. This policy option would create a simple, well-understood mechanism to help Australians address tax complexity and other complex financial matters.

- **Improving non-advised avenues:** Improving the quality of tax information that is available to Australians could help to reduce the impact of tax system complexity. Services such as MoneySmart have been very useful to Australians who lack financial literacy, and the information

[4] Above n 3 at p 170
[5] Connolly C, 'Measuring Financial Exclusion in Australia', Centre for Social Impact (CSI) – University of New South Wales (2014).
[6] Investment Trends, 'FPA Member Satisfaction Report' (December 2014)
[7] Above n 3 at p 170

available on the ATO website serves a similar purpose. Financial counselling services are also a worthwhile avenue for Government funding.

Building on these resources, as well as introducing reforms to general advice regulation in the Corporations Act, can improve the transparency of the system. It could also reduce the time and resources used in managing tax affairs and dealing with disputes as non-advised Australians are able to access better information.

- **Reduce complexity:** A more direct approach would be to reduce complexity in the tax system as a whole. However, there is a degree to which simplifying tax measures will make them more costly or detract from their original policy purpose (e.g. see section 3.2 on CGT). The review and administration processes for changing to simpler systems are also costly, and constant change in the tax laws makes it more complex to plan for the future.

- **Tax policy development:** Another driver of complexity is the variety of entities, processes, and objectives involved in developing tax policy. While the FPA's position on this aspect is developed elsewhere in this submission (see section 5 generally), we recommend that the avenues for stakeholder feedback and policy development are simplified, that the policy development process incorporates the anticipated response from the financial services sector of new policy, and that impacts on superannuation and social security are discussed as part of changes to policy.

- **Tax deductibility of financial advice:** Implementing legislation and ATO policy to make initial advice fees tax deductible is a simple avenue for reducing the barrier to fair participation caused by systemic complexity in the tax system. Any deductions for upfront advice fees can be means-tested and/or capped to ensure that the deduction is targeted to those who do not have the means to seek advice. This measure would also address inconsistency and anomalies in the tax treatment of various forms of tax advice, as well as address inconsistencies in the tax treatment of how clients pay for financial advice services.

We also note that many of these recommendations would also improve the efficacy of existing policy initiatives, such as encouraging the use of superannuation for retirement income, as Australians who are able to access professional advice will be better equipped to understand how these policies can improve their financial situation. Lastly, better informed financial decisions that suit the needs, circumstances, and objectives of Australians will also result in better outcomes for the economy by reducing waste, administrative inefficiency as a result of poor advice, and improving the resilience of the financial system.

Recommendation 1:

The FPA recommends that the Treasury and the Government should consider improving the accessibility of financial advice and general information on tax in order to mitigate the impact of complexity on Australians.

2.3 Technology and tax administration

We are interested to see whether technology can help Australians access current information regarding their personal tax circumstances and superannuation position. In our view, many of the current difficulties with regards to engaging Australians with tax and tax administration, as well as the complexity of the law itself, stem from the inability of Australians to receive current and relevant tax and superannuation information about their personal circumstances.

For example, the Government recently passed the Tax and Superannuation Laws Amendment (2014 Measures No. 7) Act 2015, which implemented (among other measures) a system to for refunding excess non-concessional superannuation contributions. The policy reason for this change was that Australians who inadvertently exceed the cap ought not to suffer a steep penalty and/or have a dispute with their tax adviser or financial adviser. This is particularly the case where a person has inadvertently triggered the non-concessional contributions bring-forward provision in a previous year and then makes non-concessional contributions that are significantly over the cap in a different year.

The Act implements a refund mechanism and a penalty deeming rate to prevent abuse of the non-concessional contributions scheme while still preventing unfair outcomes for inadvertently excessive contributors. However, if the tax administration system allowed users to see their current contributions, be warned if they are close to or exceeding the caps, and are informed if they have triggered the three-year bring-forward provision for excess non-concessional contributions, then these measures would have been largely irrelevant. If users are able to access their information in a clear way well ahead of the end of the financial year, then the original penalty regime would have been a strict but fair way to preserve the original policy intent of the non-concessional contributions cap.

There are many other examples, such as requiring a CGT discount as opposed to calculating the exact amount of CGT accounting for inflation (see 3.2) that Additionally, there are other matters such as using this information to alert the user of concessions that they may qualify for, that are up-to-date . Much of the infrastructure for this may already exist as a result of the changes made to assist Australians to identify and consolidate their superannuation funds, as well as the Superstream reforms. This has been a positive development, and should be built upon as a foundation for Australians managing more of their own tax affairs.

2.4 Discussion questions (1, 4, 59)

1: Can we address the challenges that our tax system faces by refining our current tax system? Alternatively, is more fundamental change required, and what might this look like?

Our approach to tax issues needs to fundamentally change where the complexity of the tax system influences and is influenced by other complex systems, such as the financial services system and the Australian retirement income strategy.

One of the key challenges for the Government is to address the consequences of tax system complexity. The FPA has previously argued that financial system complexity creates inequality of opportunity between sophisticated and retail investors, and this argument extends to tax system complexity. We increasingly find that investors are priced out of the kind of professional financial advice required to ensure they have equal opportunity to engage with the tax system.

The tax system may be able to implement reforms that reduce complexity, or more fundamental changes to the system may be required, such as measuring and reporting on inequality caused by complexity, and Government policies designed to improve access to professional financial advice.

4. To what extent should reducing complexity be a priority for tax reform?

There is a degree of complexity that is necessary for a system that tries to target tax concessions and influence the behaviour of Australians in specific ways. Where that complexity is necessary, policy initiatives to reduce the impact of that complexity are also necessary. Also, as complexity increases, those with the means to seek professional advice will do so if the complexity of the measure produces opportunities to minimise tax liabilities or otherwise derive a benefit.

Those without the means to seek professional advice will also be affected by complexity, as they will either seek non-advised avenues to take advantage of tax system complexity, or try to ignore or avoid being affected by the measure.

In our view, tax complexity should be guided by the policy objective of the measure, as well as the sophistication of affected individuals/organisations. Where tax complexity introduces unfairness or challenges to the integrity of the system, tax policy review should consider alternative means to achieve the same objective, or consider whether a technology-based solution would simply the measure.

59. In what ways can reforms of tax administration best assist in reducing the impact of complexity on taxpayers? Are there examples from other countries of tax administration reform to reduce the impact of complexity that Australia should adopt?

We are interested to see whether technology can help Australians access current information regarding their personal tax circumstances and superannuation position. In our view, many of the current difficulties with regards to engaging Australians with tax and tax administration, as well as the complexity of the law itself, stem from the inability of Australians to receive current and relevant tax and superannuation information about their personal circumstances.

If users are able to access their information in a clear way well ahead of the end of the financial year, then many policy measures (such as excess non-concessional contributions penalties) can be implemented in a fairer way that aligns more closely with the policy intention of the measure. Furthermore, this information can be used to alert individuals to available tax and superannuation concessions, and simply the process to apply for these concessions.

3 – Taxation and investment

3.1 Leverage and investment

As with other aspects of the tax system, it is important to re-examine the policy purpose behind tax measures – including tax concessions – and ensure that the behaviour of Australians matches the policy intent of the measure. In our view, the discussion paper's focus on the difference in tax treatment between savings and investment is entirely appropriate. We welcome an open discussion of both the kinds of investment behaviour that tax concessions ought to subsidise over savings, and the degree to which the Australian taxpayer ought to subsidise it.

With respect to leverage, our view is that many clients can benefit from gearing strategies but too many Australians rely on leverage as a way to invest. This is particularly evident with respect to property investment, and our financial planners frequently encounter clients whose perspective on wealth creation and financial security is framed by negative gearing.

Non-advised investment decisions frequently involve gearing, as the tax treatment of losses and borrowed amounts are comparatively well understood by Australians and require little assistance to implement. However, in the best case, advised financial decisions with respect to negative gearing take into account the client's whole position and frame negative gearing within an holistic strategy.

Our concern with this attitude towards leverage and investment is that the tax efficiency of the investment is more important than the business case for the investment. This attitude is not limited to property investment, as gearing strategies are used to invest in simple and complex financial products have been the centrepiece of scandal in the financial services sector. While the Storm Financial scandal included conflicted remuneration elements and poor advice as causes of consumer detriment, it is nonetheless is a key example of the risks and consequences of financial advice driven by tax efficiency rather than an holistic consideration of the client's needs, circumstances, and objectives.

The Treasury and the Government should reconsider and articulate the current policy reasons for the expensive and diverse concessional tax treatment of leverage strategies, while preserving leverage as a means for appropriate clients who are willing to take on more risk to build their wealth.

3.2 Capital Gains Tax

The FPA is concerned about whether or not the CGT discount of 50% continues to serve the original policy purpose for which it was implemented. There are now various resources available to tax claimants through the internet, as well as vastly improved technology available for tax administration. These resources render the complexity of calculating CPI increases when CGT discount was introduced in 1999 to be very simple. We would question whether there is a continuing policy reason for the CGT discount, beyond any public benefit gained from ensuring that there is an incentive for investments not to be "churned" over periods shorter than a year.

If churning is an unfavourable policy outcome, then the size of the CGT discount is still up for consideration. Whether 50% after 12 months remains appropriate should be considered in light of alternative arrangements, such as a smaller discount from 12-36 months and a larger discount from 36 months onwards. At any rate, the structure of the CGT discount should be reviewed in light of the continuing policy purpose for the CGT discount.

Recommendation 2:

The FPA recommends that the Treasury and the Government uses the Tax White Paper to identify deductions and concessions that introduce unfair complexity, produce negative outcomes that undermine or outweigh the benefit and/or policy outcome of the measure, or are redundant as a result of technological change.

Where the policy basis of the deduction and/or concession remains relevant, the Treasury and the Government should then canvass options that aim to better direct the measure to the intended outcome, or examine other means to achieve that outcome.

3.3 Tax and life insurance

The discussion paper notes that:

> "As with stamp duties more broadly, insurance taxes are among the most inefficient taxes in Australia. Insurance taxes increase the cost of insurance to consumers and place a large burden on home insurance. They may lead to under-insurance or to people not insuring at all, particularly if householders are sensitive to price increases. In this regard, Tooth and Barker found that rates of non-insurance can be higher for particular demographic groups, including retirees with mortgages and single parents, leaving them more financially vulnerable in the event of loss."[8]

The FPA strongly agrees with this position, noting the significance of the underinsurance problem in Australia. We commend the Treasury for recognising the structural effects of higher insurance costs on retirees and single parents with mortgages. The FPA supports the Treasury and the Government in reducing the cost of insurance (particularly life risk insurance and life risk advice) by removing inefficient and unnecessary taxes on insurance policies.

3.4 Discussion questions (19, 21)

19. To what extent is the rationale for the CGT discount, and the size of the discount, still appropriate?

The FPA is not convinced that the policy rationale for the CGT discount is still appropriate, given that advances in technology have made determining the change in value of an asset after CPI significantly easier. We would support the Treasury and the Government either aligning the CGT discount to a

[8] Above n 3 at p 146

new policy objective such as the prevention of asset churning, and/or implementing a revised discount schedule the course of 12-36 months.

21. Do the CGT and negative gearing influence savings and investment decisions, and if so, how?

In our view, CGT and negative gearing do influence savings and investment decisions, particularly non-advised financial decisions. While CGT has an impact on the timing of investment decisions, negative gearing likely has the most significant impact on non-advised financial savings and investment decisions.

Negative gearing strategies themselves are not necessarily an inappropriate influence on financial decisions– especially where advised financial decisions with respect to negative gearing take into account the client’s whole position and frame negative gearing within an holistic strategy. However, financial planners frequently encounter clients whose perspective on wealth creation and financial security is framed by negative gearing.

Our concern with investment decisions driven by gearing is that the tax efficiency of the investment may be more important than the business case for the investment. This attitude is not limited to property investment, as gearing strategies are used to invest in simple and complex financial products have been the centrepiece of scandal in the financial services sector.

The FPA supports the policy review and comparison of tax treatment between savings and investments, particularly considering that many use negative gearing as an investment decision to compensate for the disadvantages of leaving one’s savings in cash.

4 – Taxation and superannuation

4.1 Alignment of tax, superannuation, and social security policy

It is important to recognise that the three pillars of Australia's retirement income strategy – voluntary savings, compulsory superannuation, and the Age Pension – are all fundamentally tied to each other and to the inherent values of the system itself. Changes to the tax system that affect the outcomes of the superannuation system will affect how individuals make decisions with respect to their voluntary savings as well as their access to the Age pension.

The interaction between compulsory savings and the Age Pension is quite complicated based on our current policy settings, primarily as a result of two factors; the current means testing settings for Age Pension eligibility, and the tax implications of holding assets inside superannuation in the pension phase.

In our submission to the Treasury on the Financial System Inquiry Final Report, we stated that:

> "A more ambitious project than that attempted by the Financial System Inquiry's Final Report would be to align the goals and operation of the Australian retirement income strategy, with a view to non-partisan political support for a minimum standard of living for Australian retirees. At a minimum, policy settings for the Age Pension and the superannuation system should be aligned to produce efficient, sustainable, and equitable retirement outcomes for Australians."

We also stated that:

> "…[W]e understand why many in the Australian public would be sceptical of a system which affords generous tax concessions to those who are sophisticated and/or wealthy enough to take advantage of them. We are also concerned with the public perception of the Australian superannuation system as a mechanism for facilitating intergenerational transfers of wealth outside of the Australian taxation system.
>
> To better align the Australian superannuation system with the proposed objectives of the system, political consensus on a minimum retirement standard for Australians must be achieved."

It is more important now than ever to establish a fair and non-partisan superannuation system in light of the findings of the 2015 Intergenerational Report. According to that report, by 2055 there will be only 2.7 working Australians to support every Australian over 65, compared with 4.5 today and 7.3 in 1974/75. The 2015 Intergenerational Report projects life expectancy at birth to be 95.1 years for men and 96.6 years for women by 2054/55, compared with 91.5 and 93.6 years today.

Australia needs broad political consensus on a superannuation system that meets the retirement needs of lower income and middle income earners in Australia. The superannuation system needs to use the limited resources available through tax concessions to assist those who need assistance with saving for their retirement. The Treasury and the Government should use the Tax White Paper process to implement measures that counter the perception that the superannuation system is only a means to derive concessional tax treatment for the wealthy.

Through various avenues such as the Financial System Inquiry and Treasury consultations, the FPA has put forward several policy initiatives that would address existing inequities in the Australian superannuation system and deviations from the initial policy intention of the system from the three pillars policy.

These include:

- **Account size limits on concessional pensions:** The Government could effectively address the cost of superannuation and ensure that superannuation fulfils its original policy objectives by introducing a cap on the volume of funds that can be incorporated into a retirement income stream product. If broad political consensus can be established on a volume of funds that can meet the retirement needs of Australians then there is no remaining policy reason to afford tax concessions to surplus funds.

  This approach is comparatively simple, both in terms of legal complexity and tax administration complexity, as it involves reporting across one or many product providers and could be attached to the funds release process for the superannuation fund. Funds that are surplus to the cap could either remain in accumulation stage, removed from the system, or fund aged care or disability insurance.

- **Limits on total tax concession per person:** This measure would involve tracking and capping the total tax concession available to each individual in the superannuation system. This option has its merits, as it would form a clearly-defined social contract with Australians who would rely on the superannuation system to build a retirement income. It also introduces a degree of clarity for Australians, who then know exactly just how much assistance the Government is prepared to offer if they choose to save through superannuation as opposed to reliance on the Age Pension or voluntary savings.

  However, this measure seems complex to administer and is fraught from a political perspective by the criticism that limiting the tax concessions, as opposed to tailoring the program itself, indicates that the Government is more interested in the cost of the measure than the benefit of secure retirement income for all Australians.

- **Introduction of lifetime contribution caps:** This measure mirrors the accounts size limits on concessional pensions in many respects, but is a control on the amount of funds that can enter the superannuation system per individual, as opposed to controlling funds that leave the system.

We anticipate that this would introduce slightly more complexity to the system through indexation and the problem of whether or not to retain non-concessional contributions if this measure is adopted.

- **Tax alignment in accumulation and pension phases:** The Treasury and the Government could also consider aligning tax on superannuation during accumulation and pension phases. This would reduce the incentive to use superannuation for tax efficiency purposes, and would also help to align superannuation to its original policy intention. Finally, implementing this measure would also reduce a significant degree of complexity in the system.

- **Tax and policy alignment:** Aspects of the retirement income strategy could be designed to fund each other and support their shared policy intention. For example, penalties and extra taxes (such as the extra contribution tax for high income earners) could be used to fund other aspects of the retirement income strategy such as the repealed Low Income Superannuation Contribution. This would improve the fairness of the tax system using existing tax avenues in order to limit complexity for the end user.

Recommendation 3:

The FPA recommends that the Treasury and the Government uses the Tax White Paper process to examine how the existing tax treatment of savings inside superannuation (during both accumulation and pension phases) affects financial decisions made by Australians. This examination must compare decisions made by Australians of varying financial literacy and access to professional advice.

Where the Tax White Paper process identifies deficiencies in the fairness and complexity of the superannuation system (analysed as a part of the whole Australian retirement incomes strategy), the Tax White Paper should canvass alternative tax policies to align superannuation with its original policy intent and produce better and fairer outcomes for Australians.

4.2 Aged care, disability care, and retirement incomes

Much of the discussion and policy development concerning tax and retirement incomes is focused on providing a retirement income for living. The stress that Australia's ageing population is placing and shall continue to place on the economy and the existing retirement income strategy will be compounded by the stress on Australia's aged care facilities and disability services.

In our view, the retirement income debate is incomplete if restricted to the three pillar policy. Aged care and disability need to be part of the retirement income policy discussion, as these factors will place significant stress on the existing policy even if reoriented towards the original policy intent.

Almost one in five Australians have a disability, and just over half of those with a disability are part of the labour force, as opposed to over 80% of those who are not disabled.[9] Of those, a higher proportion of disabled Australians are part-time employees rather than full-time, and tend to have a lower level of education than those without a disability.[10] All of these factors affect the amount of money that disabled Australians can divert into their retirement savings, whether impacting on their total earnings or their ability to set aside more than the superannuation guarantee.

Carers (particularly primary carers) also experience more difficulty than non-carers, as carers tend to have lower labour participation rates and earn less income than non-carers.[11] Factors that affect a carer's ability to generate income to contribute towards retirement or to receive professional advice, as well as a carer's immediate financial needs that become a higher priority than saving for retirement, will impact on their retirement income.

As public resources to grapple with these issues are limited, the financial services sector can play a pivotal role in policy solutions that incorporate aged care and disability care into the Australian retirement income strategy. Financial advice should be a part of this role, as Australians should be able to rely on professional financial advice to help fund their aged care and disability insurance needs.

We encourage the Treasury and the Government to consider establishing the key strategic priorities for incorporating these factors into the retirement income strategy discussion, and build upon the existing tax discussion concerning superannuation and the sustainability of the age pension to address aged care and disability insurance.

Recommendation 4:

The FPA recommends that the Treasury and the Government uses the Tax White Paper process to integrate aged care and disability care into the national retirement income strategy, and examine policy options that encourage Australians to consider their aged care and disability risks and needs.

4.3 Discussion questions (22)

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

In our view, the tax arrangements for superannuation during the accumulation phase are very complex, and create a barrier for Australians who engage with superannuation. The complexity of comparing superannuation funds, the difficulty in estimating returns, and the opacity of fees and features (such as group insurance products in super) means that most Australians will only get the most out of the accumulation phase of superannuation if they seek professional advice well before retirement.

[9] Australian Bureau of Statistics, 4430.0 - Disability, Ageing and Carers, Australia: Summary of Findings (2012)
[10] ABS, above n 8
[11] ABS, above n 8

The tax arrangements for the pension phase of superannuation are even more complex. Many Australians are ill-equipped to make considered decisions around whether to leave their superannuation balance inside the superannuation system or not, or whether various pension products that might allow them to retain the tax concessional status of their superannuation balance would be suitable for their circumstances.

Many will also not be aware of how to make non-concessional contributions to their super fund towards preservation age. This impacts on their superannuation savings, but critically it also impedes existing policy initiatives to enable contributions of funds derived from downgrading their home.

Furthermore, there is a perception that the behaviour of retiring Australians is that they are mistrustful and/or ignorant of the superannuation system, or are inclined to see their superannuation balance as a windfall to pay off their mortgage and spend recklessly with the backing of the Age Pension.

The pension phase has been the subject of some scrutiny in recent inquiries and consultations, particularly the Treasury's review of retirement incomes products and the Financial System Inquiry's focus on the pension phase. The focus of these inquiries has been on examining the behaviour of Australians as they approach retirement, as well as examining the appropriateness of regulations that inhibit innovations which could address longevity risk and simplify retirement planning.

In our view, the solution is not simply a product solution, or to establish a de-facto default retirement income product. The solution is to address the complexity (including tax system complexity) of retirement income by either reducing the complexity (e.g. addressing tax in accumulation and pension phases to align more closely with the policy intention of superannuation – see section 4.1) and/or introduce policies that reduce the barrier that complexity creates (e.g. policies to improve the accessibility of professional financial advice – see section 2.2).

5 – Tax policy development and administration

5.1 Discussion questions (64)

64. Are current tax review arrangements appropriate? How could they be improved?

The FPA is generally satisfied with the process for formal policy review programs, whether they are run by Treasury, the ATO, or other entities that are connected to the tax and financial services systems. This includes proposed changes to the law or to regulations, as well as consultations around changes to Federal Government or agency policies. In our view, feedback is timely and agencies have a good track record of reaching out to the FPA as a peak professional body to discuss the perspective of our members.

However, we believe that consultation and stakeholder engagement is a two-way process, and we would like to see formal standards and avenues for professional bodies to raise the concerns of our members about aspects of the law. This is particularly the case with technical aspects of the tax law and raising these matters with the ATO without a case study.

We appreciate that giving advice on the agency's point of view without an individual case, a determination, or another process that facilitates an administrative decision is difficult. Perhaps it is even more difficult if that decision does involve a determination or a process that facilitates an administrative decision. However, the existing avenues for raising technical issues with Federal regulatory agencies do need to provide a degree of certainty on the issue – or at least what steps from the legislature or the agency would be required to facilitate that certainty.

APPENDIX A – List of recommendations

Recommendation 1:

The FPA recommends that the Treasury and the Government should consider improving the accessibility of financial advice and general information on tax in order to mitigate the impact of complexity on Australians.

Recommendation 2:

The FPA recommends that the Treasury and the Government uses the Tax White Paper to identify deductions and concessions that introduce unfair complexity, produce negative outcomes that undermine or outweigh the benefit and/or policy outcome of the measure, or are redundant as a result of technological change.

Where the policy basis of the deduction and/or concession remains relevant, the Treasury and the Government should then canvass options that aim to better direct the measure to the intended outcome, or examine other means to achieve that outcome.

Recommendation 3:

The FPA recommends that the Treasury and the Government uses the Tax White Paper process to examine how the existing tax treatment of savings inside superannuation (during both accumulation and pension phases) affects financial decisions made by Australians. This examination must compare decisions made by Australians of varying financial literacy and access to professional advice.

Where the Tax White Paper process identifies deficiencies in the fairness and complexity of the superannuation system (analysed as a part of the whole Australian retirement incomes strategy), the Tax White Paper should canvass alternative tax policies to align superannuation with its original policy intent and produce better and fairer outcomes for Australians.

Recommendation 4:

The FPA recommends that the Treasury and the Government uses the Tax White Paper process to integrate aged care and disability care into the national retirement income strategy, and examine policy options that encourage Australians to consider their aged care and disability risks and needs.

APPENDIX B – Discussion question responses

1: Can we address the challenges that our tax system faces by refining our current tax system? Alternatively, is more fundamental change required, and what might this look like?

Our approach to tax issues needs to fundamentally change where the complexity of the tax system influences and is influenced by other complex systems, such as the financial services system and the Australian retirement income strategy.

One of the key challenges for the Government is to address the consequences of tax system complexity. The FPA has previously argued that financial system complexity creates inequality of opportunity between sophisticated and retail investors, and this argument extends to tax system complexity. We increasingly find that investors are priced out of the kind of professional financial advice required to ensure they have equal opportunity to engage with the tax system.

The tax system may be able to implement reforms that reduce complexity, or more fundamental changes to the system may be required, such as measuring and reporting on inequality caused by complexity, and Government policies designed to improve access to professional financial advice.

4. To what extent should reducing complexity be a priority for tax reform?

There is a degree of complexity that is necessary for a system that tries to target tax concessions and influence the behaviour of Australians in specific ways. Where that complexity is necessary, policy initiatives to reduce the impact of that complexity are also necessary. Also, as complexity increases, those with the means to seek professional advice will do so if the complexity of the measure produces opportunities to minimise tax liabilities or otherwise derive a benefit.

Those without the means to seek professional advice will also be affected by complexity, as they will either seek non-advised avenues to take advantage of tax system complexity, or try to ignore or avoid being affected by the measure.

In our view, tax complexity should be guided by the policy objective of the measure, as well as the sophistication of affected individuals/organisations. Where tax complexity introduces unfairness or challenges to the integrity of the system, tax policy review should consider alternative means to achieve the same objective, or consider whether a technology-based solution would simply the measure.

19. To what extent is the rationale for the CGT discount, and the size of the discount, still appropriate?

The FPA is not convinced that the policy rationale for the CGT discount is still appropriate, given that advances in technology have made determining the change in value of an asset after CPI significantly easier. We would support the Treasury and the Government either aligning the CGT discount to a new policy objective such as the prevention of asset churning, and/or implementing a revised discount schedule the course of 12-36 months.

21. Do the CGT and negative gearing influence savings and investment decisions, and if so, how?

In our view, CGT and negative gearing do influence savings and investment decisions, particularly non-advised financial decisions. While CGT has an impact on the timing of investment decisions, negative gearing likely has the most significant impact on non-advised financial savings and investment decisions.

Negative gearing strategies themselves are not necessarily an inappropriate influence on financial decisions– especially where advised financial decisions with respect to negative gearing take into account the client's whole position and frame negative gearing within an holistic strategy. However, financial planners frequently encounter clients whose perspective on wealth creation and financial security is framed by negative gearing.

Our concern with investment decisions driven by gearing is that the tax efficiency of the investment may be more important than the business case for the investment. This attitude is not limited to property investment, as gearing strategies are used to invest in simple and complex financial products have been the centrepiece of scandal in the financial services sector.

The FPA supports the policy review and comparison of tax treatment between savings and investments, particularly considering that many use negative gearing as an investment decision to compensate for the disadvantages of leaving one's savings in cash.

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

In our view, the tax arrangements for superannuation during the accumulation phase are very complex, and create a barrier for Australians who engage with superannuation. The complexity of comparing superannuation funds, the difficulty in estimating returns, and the opacity of fees and features (such as group insurance products in super) means that most Australians will only get the most out of the accumulation phase of superannuation if they seek professional advice well before retirement.

The tax arrangements for the pension phase of superannuation are even more complex. Many Australians are ill-equipped to make considered decisions around whether to leave their superannuation balance inside the superannuation system or not, or whether various pension products that might allow them to retain the tax concessional status of their superannuation balance would be suitable for their circumstances.

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59. In what ways can reforms of tax administration best assist in reducing the impact of complexity on taxpayers? Are there examples from other countries of tax administration reform to reduce the impact of complexity that Australia should adopt?

We are interested to see whether technology can help Australians access current information regarding their personal tax circumstances and superannuation position. In our view, many of the current difficulties with regards to engaging Australians with tax and tax administration, as well as the complexity of the law itself, stem from the inability of Australians to receive current and relevant tax and superannuation information about their personal circumstances.

If users are able to access their information in a clear way well ahead of the end of the financial year, then many policy measures (such as excess non-concessional contributions penalties) can be implemented in a fairer way that aligns more closely with the policy intention of the measure. Furthermore, this information can be used to alert individuals to available tax and superannuation concessions, and simply the process to apply for these concessions.

64. Are current tax review arrangements appropriate? How could they be improved?

The FPA is generally satisfied with the process for formal policy review programs, whether they are run by Treasury, the ATO, or other entities that are connected to the tax and financial services systems. This includes proposed changes to the law or to regulations, as well as consultations around changes to Federal Government or agency policies. In our view, feedback is timely and agencies have a good track record of reaching out to the FPA as a peak professional body to discuss the perspective of our members.

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