PO Box 3150
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15 January 2020

Retirement Income Review Secretariat
The Treasury
Langton Crescent
PARKES ACT 2600

Dear Sir/Madam

SUBMISSION TO RETIREMENT INCOME REVIEW

Please find attached the main component of this submission to the Retirement Income Review ('the Review'). That component seeks to add to the Review's fact base regarding Australia's current tax treatment of superannuation.

The facts presented in the attached highlight:

- how the current concessional income tax treatment of superannuation disadvantages low income people in favour of high income people in each of the three phases of members' investment in superannuation funds;

- how that disadvantage could be removed by redesigning current tax treatment in line with the acknowledged ideal income tax treatment of collective investment vehicles (putting all members on an equal tax footing with no concessional treatment): first, have contributions come out of after-tax income; and, second, integrate members' annual taxable income in their (untaxed) superannuation funds with the members' personal income tax assessments; and

- how associated concessional tax treatment can then be designed so that all members are treated equitably, regardless of income level (with the lowest income members getting annual cash refunds).

The current tax treatment of superannuation starkly discriminates against low income members in favour of high income members. The tax treatment is not targeted at those who need support most.

Beyond the clear absolute or relative disadvantage faced by low income members in each phase of superannuation, a number of features underline that discrimination. These include $100,000 of non-concessional investment allowed per year and the ability to retain superannuation investment in accumulation mode indefinitely.

Moreover, the extent to which the current income tax concessions favour higher income members weakens the sustainability of those concessions. Figure 4 of the Review's Consultation Paper shows aggregate tax assistance given across income groups (in present value terms).[1] Even absent the numbers of members in each group that figure illustrates how the benefits of the tax concessions very much favour higher over low income members (the lowest income members actually being tax disadvantaged).

[1] Australian Government, *Retirement Income Review: Consultation Paper*, November 2019, p 18.

There is therefore no trade-off involved here between equity and sustainability, two of the Review's suggested principles for assessing Australia's current retirement income system. The comprehensive changes to current tax treatment presented in the attached component this submission, or perhaps a range of alternative ad hoc changes (though, no doubt, with associated shortcomings), would both remove current inequities of concessional income tax treatment and improve its sustainability.

Absent such changes, at a minimum the purpose of the current superannuation guarantee (SG) and associated income tax concessions should be clarified. In their current shape, they could perhaps be best explained in terms of tax concessions for higher income people enabling them to achieve higher wealth and higher income in retirement.

If only such minimal action were to be taken, given the level of discrimination against low income members in favour of high income members, serious questions are raised regarding the worthiness of increasing the SG and, indeed, of the current superannuation arrangements as a whole.

Any assessment of overall worthiness of current arrangements would also ideally take into account their effect on economic efficiency – a principle that the Review has not included in its Consultation Paper. Economic efficiency is all about the best allocation of Australia's land, labour and capital resources.

A definitive assessment of the effect of current superannuation arrangements on economic efficiency would be challenging. The availability of the age pension itself affects people's decisions concerning how much to save (rather than consume) and when. Enforced superannuation contributions further impacts up-front consumption/saving decisions by workers. And then there are the effects on resource allocation (and consequences on productivity and long-term growth) of government involvement by way of tax concessions (and tax disadvantages) and regulations on workers' long-held investments in superannuation funds.

Yours faithfully

Wayne Mayo
Tax Economist

RETIREMENT INCOME REVIEW: TAX TREATMENT OF SUPERANNUATION

The Review is to establish a fact base of Australia's current retirement income system.

That fact base must include the impact on members of superannuation funds (which hold both compulsory and voluntary savings/investments) of the current tax treatment of superannuation.

That is particularly so given the fact that current income tax treatment of superannuation disadvantages low income members in each of the current three phases of saving/investment in superannuation funds: contribution phase; accumulation phase; and pension phase. Such disadvantage is particularly notable given that compulsory superannuation arrangements were designed with a focus on enabling lower income people to be better off in retirement than relying solely on the age pension.

Appreciation of the clear absolute and/or relative disadvantage faced by low income superannuation investors logically leads to speculation as to what changes could be made to the income tax treatment of superannuation to remove, or at least lessen, that disadvantage. Such change would bolster and strengthen the outcomes that our retirement income system is delivering.

CURRENT INCOME TAX TREATMENT DISADVANTAGES LOW INCOME PEOPLE…

Disadvantage is determined in this submission by comparing the tax rate applying in each of the three phases of a saver/investor's superannuation investment with the marginal personal tax rate faced by the same saver/investor on comparable phases of alternative direct non-superannuation investments.

Contribution phase

Fact 1: Low income people are relatively disadvantaged when contributing to superannuation

A general flat rate of 15 per cent tax is paid by superannuation funds on compulsory superannuation contributions made by their members out of pre-tax earnings. The low income superannuation tax offset (LISTO) going to eligible members' superannuation funds generally results in those with taxable incomes less than $37,000 per annum not paying more tax on their contributions out of that income than they do on the rest of their income.[2]

In contrast, those with taxable incomes above $37,000 per annum (currently with marginal personal income tax rates above 19 per cent) attract a positive tax advantage. That incentive increases with increased marginal tax rate of the savers/investors on their earnings being invested, until the extra 15 per cent tax on contributions kicks in for those with annual taxable incomes at or higher than $250,000.

Thus, investors with annual earnings below $250,000 who do not attract LISTO only face 15 per cent tax on their superannuation contributions. But their same wages income would have attracted tax rates higher than 15 per cent were it channelled to alternative non-superannuation investments.

[2] See Australian Government, ibid, p 5. In fact, it would seem that LISTO may result in those with earnings towards the upper end of the current $18,200 to $37,000 tax bracket paying less tax than they would on capital investment in non-superannuation opportunities (nil versus 19 per cent, respectively).

Similarly, even though those with earnings above $250,000 face 30 per cent on their superannuation contributions, they would have attracted 47 per cent (including 2 per cent levy) on the funds alternatively going to non-superannuation investments.

It is instructive to note that the LISTO has been introduced to remove the absolute disadvantage faced by low income superannuation investors but the absolute advantage faced by higher income investors has not been removed. Low income contributors face a clear disadvantage relative to higher income contributors (those on very low incomes get no tax concession at all).

Accumulation phase

<u>Fact 2</u>: *Low income people are disadvantaged in the accumulation phase of their superannuation investment*

During the accumulation phase, the taxable income of people's investments in superannuation funds attracts a flat 15 per cent tax.

Consequently, in each year that taxable income is earned in their superannuation funds, people with taxable income below the tax-free threshold face an absolute disadvantage from the tax treatment of their superannuation investment. Investment by them in alternative non-superannuation opportunities would attract nil income tax.

Those with taxable income outside superannuation high enough to get them into the current 19 per cent tax bracket can be regarded as attracting modest absolute benefit from tax concessions on their taxable income in superannuation. Annual taxable income from alternative non-superannuation investment opportunities would likely be taxed at 19 per cent rather than 15 per cent.

However, higher income people achieve more generous income tax treatment on their superannuation investments the more their marginal personal tax rates are above 19 per cent. Their annual taxable income from alternative non-superannuation investments is not taxed at a fixed 15 per cent but is taxed, appropriately, at their personal income tax rates, currently ranging from 32.5 per cent to 45 per cent (ignoring the 2 per cent levy).

Low income people therefore face both an absolute and relative tax disadvantage in the accumulation phase of superannuation.

Pension phase

<u>Fact 3</u>: *Low income people are relatively disadvantaged in the pension phase of their superannuation investment*

When people trigger the pension phase of their superannuation investment, the same zero income tax rate applies to the taxable income of their investments in their superannuation funds. And when funds are withdrawn from their funds no further income tax applies, consistent with non-superannuation investments.[3]

Again, the generosity of a zero tax rate on annual taxable income tax treatment increases as the

[3] Appropriately, income tax applies to annual taxable income from investments, including any arising from the sale of assets, not to amounts received on termination of investments.

marginal tax rate of the person concerned increases: from no special treatment for those below the tax-free threshold to maximum generosity to those whose annual taxable income from alternative non-superannuation investments attracts the highest personal tax rate.

BUT REDESIGN OF INCOME TAX TREATMENT OF SUPERANNUATION COULD REMOVE CURRENT INEQUITIES…

Income tax redesign required, not expenditure tax design

<u>Fact 4</u>*: Any redesign of the tax treatment of superannuation needs to be set in an income tax framework not an expenditure tax framework.*

Income taxation of superannuation is the relevant framework for redesign of superannuation taxation because investing in superannuation (whether voluntary or compulsory) is just one of many investment possibilities, each of which sees its annual taxable income subject to income taxation. People's wages are subject to income tax. Taxable income from their various possible investments out of their wages is also subject to income taxation.

In contrast, while expenditure taxation comes in various formats – like pre-paid (pay-roll tax) and post-paid (GST) – it is essentially a tax on wages. Personal tax assessments within an expenditure tax framework would see amounts invested up-front out of wages deductible (ie tax free) and ultimate investment proceeds taxed (as with a cash flow tax). Absent above-normal profits, therefore, no tax is imposed on investment income.[4] The personal tax on ultimate investment proceeds is then just a delayed tax on the original wages income.

Nevertheless, some argue that expenditure tax design would be suitable for superannuation in the following form: no tax on contributions to superannuation funds (contributions tax deductible); no tax on annual income of superannuation funds; but full marginal tax rates on cash distributions in the pension phase.

Arguments in support of such design often include the observation that at least high income people would be taxed at their full marginal rates when their untaxed superannuation contributions and earnings on those are ultimately distributed.

But, as noted, under competitive conditions, under such design (a post-paid expenditure tax design) the only tax paid is essentially delayed income tax on the wages underlying the original contributions. In other words, the same ultimate post-tax superannuation payout would result from either: contributions from untaxed wages subsequently growing at each year's going return to be ultimately subject to a given personal tax rate on distribution; or, up-front contributions from wages reduced by the same personal tax rate and again growing at each year's going return with no further taxation.

In sum, under an expenditure tax framework, wages underlying contributions could be taxed up-front (pre-paid expenditure tax) or tax could be left to apply only to ultimate distributions (post-paid expenditure tax) – but either way, under competitive conditions, there is essentially no tax on the

[4] For further explanation as to why cash flow taxes impose no tax on normal investment income see, for example, P Swan, "Income taxes, profit taxes and neutrality of optimizing decisions", (1976) 52 *Economic Record*, 175 and W Mayo, "Rent Royalties", (1979) 55 *Economic Record*, 206.

investments made, only on wages underlying the investments.

And who would benefit most from only wages being taxed, not the superannuation investment income? Again, the higher the marginal tax rate of the superannuation investor the greater the benefit to the investor (relative to the income tax payable on alternative non-superannuation investments). Those with incomes below the tax-free threshold, for example, would achieve no benefit because their investment income is already tax free.

Shape of ideal income tax redesign of superannuation arrangements

<u>Fact 5</u>: *The current relative disadvantage of low income people in the contribution phase of superannuation would be addressed by having all contributions (compulsory or voluntary) by everyone come out of after-tax income*

Marginal personal tax rates would apply to everyone's annual contributions.

- Those below the tax-free threshold would pay no tax on their contributions.
- Those paying tax at 47 per cent on some of their annual taxable income would pay tax at 47 per cent on some or all of their contributions.

Superannuation contributions by people in each income range (including those who become non-residents for income tax purposes) would have the same income tax treatment as do the up-front amounts invested by those people in alternative non-superannuation investment opportunities. Current absolute or relative tax disadvantage of low income superannuation contributors would be removed.

This treatment would have the additional benefit of removing current administrative requirements associated with superannuation contributions. Ad hoc fixes like the LISTO and the 30 per cent contributions tax rate applying to those with annual earnings of $250,000 and above would no longer be required.

Having contributions come out of after-tax income would not be achieved by some sort of complex matching arrangements where superannuation funds had to know the marginal tax rate of members. Contributions to superannuation funds would simply be subject to personal income tax.

Low income members with earnings below the tax-free threshold would not notice any change to the tax treatment of their pre-tax contributions to superannuation (with those pre-tax contributions currently remaining unchanged in their funds courtesy of the LISTO).

In contrast, higher income members would perceive a negative tax impact on their contributions. Take a $1000 concessional pre-tax SG contribution by a member in this category earning below $250,000 per annum. The contribution is paid by the member’s employer to the member’s superannuation fund out of the member’s gross remuneration. Under current arrangements, 15 per cent tax is paid on that contribution by the member’s superannuation fund.

Under the change proposed here, the $1000 of pre-tax contributions would still go to the member’s fund but the full $1000 would remain untaxed in the fund to earn future income. In addition, the $1000 of earnings would be included as assessable income in the member’s personal income tax assessment. At the margin, instead of 15 per cent being paid on that income (by the superannuation fund) the member’s marginal tax rate would apply via the member’s regular income tax assessment.

No doubt much complaint would come from higher income members, perhaps the more so because the focus would likely be on their marginal tax rate applying without factoring in the previous 15 per cent tax paid on members' behalf by their superannuation funds.

Nevertheless, the net extra tax faced by higher income earners merely reflects the level of advantage attracted by these people relative to those below the tax-free threshold.

<u>Fact 6</u>: The current disadvantages of low income superannuation investors in the accumulation and pension phases would be addressed by integrating members' annual taxable income in their superannuation funds with their personal income tax assessments

Integrating members' taxable income in their superannuation funds with their personal tax assessments would see:

- abolition of different the tax treatment between accumulation and pension phases of superannuation;

- no tax payable by superannuation funds on their members' annual taxable income in the funds (as with other trusts); and

- annual taxable income of individual superannuation fund members as measured by their superannuation funds (along with associated tax credits and rebates) allocated to the income tax assessments of those superannuation investors (both compulsory and voluntary).
  - Those below the tax-free threshold (after these allocations) would pay no tax on their allocations – and any associated refundable credits (like imputation credits attached to franked dividends received by the superannuation funds) would result in cash refunds to them.
  - Those above the tax-free threshold (before these allocations) would be currently liable for tax at 19 per cent or more on some or all of their allocations – though associated refundable tax credits would reduce tax payable (and could result in cash refunds if they reduced tax payable to nil).
  - Those who become non-residents for tax purposes (and whose funds accept non-resident members) would be allocated their annual taxable income and, like now, receive superannuation payments. Consideration could be given to applying tax within the fund at, say, 15 per cent to taxable income attributed to non-residents during the accumulation phase (like now) and the pension phase (unlike now).

As well as removing current disadvantage faced by low income members, such redesign could remove much complexity from current arrangements.

Such integration design is the acknowledged ideal income tax treatment of companies and other collective investment vehicles.[5] For companies, this ideal is often seen as impractical.[6] The reasons usually given for this impracticality are: multiple classes of shares; issues with foreign shareholders; part-year sales; and, more generally, problems with the allocation of annual taxable income to individual shareholders.

However, aside from the relatively minor issue of locals becoming non-residents for tax purposes,

[5] See, for example, W. Mayo, "Time to upgrade Australia's company tax system from imputation to integration", (2018) 33 *Australian Tax Forum*, 754.
[6] For references to some views of impracticality see Mayo, ibid, 756.

these reasons given for integration being impractical for companies do not apply to Australia's superannuation funds. Local individuals hold unique ownership interests in the income within their superannuation funds, interests which cannot be sold to others.

Moreover, a superannuation fund's annual taxable income is already allocated directly amongst its individual members (while this may be somewhat opaque with pooled funds, it is explicit with self-managed funds). But, currently, it is the taxing of this annual taxable income within the funds themselves at a flat 15 per cent and zero per cent in the accumulation and pension phases, respectively, that gives rise to all the tax disadvantage suffered by low income members in these phases.

Under integration redesign, members (like trust unit-holders/beneficiaries now) would receive a distribution statement from their superannuation funds shortly after the end of the financial year showing: the amount of annual taxable income allocated to them and any associated tax credits or rebates. Similarly to discretionary trusts now, untaxed income ultimately distributed as cash would not attract any tax consequences.[7] Unlike regular discretionary trusts, however, individual components of the allocated taxable income would not retain their character. Taxable income calculated by the superannuation funds would simply be allocated directly to members' personal tax assessments.

Understandably, it might to some seem particularly inappropriate for personal tax to be imposed on members' taxable income in their superannuation funds when that income is retained and not distributed as cash to those being taxed. But that is exactly the outcome when shareholders sign up to dividend reinvestment plans of their companies. These shareholders are then still taxed on the dividends even though their companies retain them for reinvestment (issuing matching new shares to the shareholders[8]).

In fact, sound structural design of income taxation has annual taxable income taxed everywhere at investors' personal tax rates *regardless of business structure*.[9] That is what happens now to the annual taxable income from a sole trader's business activities and to the annual taxable income of companies under our full imputation system when that income is distributed immediately (as franked dividends plus imputation credits).[10] In addition, annual taxable income of trusts is required to be distributed to individual unit-holders/beneficiaries for assessment.

Moreover, since recent removal of tax on distributions from superannuation funds, the structure of superannuation taxation is more consistent with sound design for the taxing of investment income. A move from current tax treatment of superannuation to an integration approach would essentially only involve changing tax rates: from a general fixed 15 per cent to marginal tax rates applying to contributions; and from a fixed 15 or zero per cent on annual taxable income of superannuation funds again to marginal personal tax rates.

[7] CGT cost base adjustments that apply to units in unit trust for distributions of untaxed income are not relevant and inclusion in assessable income of untaxed income distributed by companies (unfranked dividends) would not apply.

[8] With superannuation funds, the implicit distribution and reinvestment is fully reflected in members' accounts in the funds – so no extra action would be required.

[9] Going one major reform step further and aligning taxable income with commercial profit (which includes annual change in value of investment assets and liabilities) would result in income tax having minimal effect on the pattern of investment and its financing with positive effects on post-tax productivity and long-term growth. See, for example, Mayo, ibid, 754-755.

[10] Under Australia's current full imputation system of company tax, however, companies are able to retain taxed income indefinitely. They are not required to distribute taxed income in the year it arises. Nevertheless, that shortcoming could be addressed by upgrading imputation to integration as espoused by Mayo, ibid – an upgrade essentially involving compulsory dividend reinvestment when taxable income is retained by companies.

Of more obvious practical relevance, therefore, is the fact that the integration approach for the taxation of superannuation would impose personal tax each year on retained taxable income associated with superannuation investments that people were compelled to make or previously decided to make voluntarily under current arrangements. And that taxable income, taxed every year at personal rates, cannot be accessed generally until preservation age.

However, low income members might immediately see the benefit to themselves from integration design compared to their current situation. Appreciation of this fact logically raises the question whether concessional tax treatment need accompany an integration-style redesign of taxation of compulsory superannuation.

- Under such redesign, current disadvantage faced by low income people is removed – the very people, less likely to save for their retirement, for whom a better level of retirement income was a particular aim of the current compulsory system.

- For high income people, compulsory superannuation is more likely to simply substitute for saving for retirement that would have occurred anyway – with extra tax concessions just providing incentive to shift more investment funds into a tax-preferred environment.

Such considerations raise the fundamental question what is the purpose of compulsory superannuation. Despite the altruistic nature of that question, given the history of superannuation tax concessions favouring higher income people, higher income people would understandably complain if no concessions accompanied integration-style tax treatment of superannuation. They would argue that they are being forced to contribute and/or wait to access payouts from their superannuation investments when the tax treatment of these investments is essentially the same as for alternative direct non-superannuation investments.

Such complaints would be expected to be reflected in a zero estimate in Treasury's Tax Expenditure Statement for the cost to revenue of superannuation under the above integration approach to superannuation taxation with no associated tax concessions.

Moreover, absent some concessional treatment, under integration-style redesign, some low income superannuation fund members (like those in the current 19 per cent income tax bracket) would face explicit annual tax payments on their taxable income allocated to them by their funds.

Consequently, so long as compulsory superannuation is retained, integration redesign would inevitably require some equitable concessional tax treatment of superannuation contributions and/or the annual allocations of superannuation funds' taxable income to their individual members.

… AND ASSOCIATED CONCESSIONAL TREATMENT COULD BE PROVIDED ON AN EQUITABLE BASIS

The above treatment of contributions which sees marginal tax rates automatically applying to post-tax contributions would remove the current disadvantage faced by low income people in the contribution phase of superannuation. It also involves no complexity for administrators of superannuation funds and would result in reduced cost to tax revenue.

Simplicity would be furthered by applying equitable concessional treatment only to annual taxable income allocated to members' personal tax assessments by their superannuation funds and not also to members' superannuation contributions.

It is that approach to concessional income tax treatment that is taken in this submission.

Refundable cash rebates the best form of equitable concessional treatment

Equitable concessional treatment to annual taxable income allocated across superannuation fund members would necessarily provide benefits across the spread of marginal tax rates faced by members. Refundable tax rebates would be a suitable form of concession for this purpose. That is because such rebates would provide cash payments for those whose tax payable before the rebate (taking into account their allocated taxable income from their superannuation funds and associated tax credits) is less that the rebate amount.

The annual cost to revenue of the concessional treatment would simply be the aggregate of rebates provided. Such explicit, observable cost – compared to the ideal benchmark of people being taxed on their annual taxable income in their superannuation funds at their marginal personal tax rates – should be no different in concept to the current implicit cost measurement of superannuation concessions (in accumulation and pension phases) in Treasury's Tax Expenditure Statement.

Under integration-style redesign, significant revenue savings would be expected, particularly from the replacement of a zero tax rate in the superannuation pension phase with marginal personal tax rates plus refundable cash rebate.

As noted, this would be a source of serious complaint, no doubt, from high income members – but the complaints would be over a situation (tax rate at their marginal tax rate less rebate benefit) that low income members would likely relish, members who currently face a tax rate at or higher than their marginal tax rate on their superannuation taxable income.

Fixed percentage rebate per dollar of allocated income is most practical form of concession

There are many ways that refundable cash rebates could be constructed to provide concessional treatment to annual taxable income allocated across superannuation fund members.

A rebate could be tapered, with the level of rebate reducing over time, size of superannuation balance or level of tax bracket. The aim of such tapering would be to minimise non-concessional contributions by high income people and to encourage such people to withdraw their superannuation balances. Such tapering could potentially enable abolition of many of the current complex rules relating to annual contribution limits and limits on superannuation aggregates.

Alternatively, a rebate could simply be set at a uniform percentage of allocated taxable income.

It might be argued that it is inappropriate to provide both low income and higher income people with the same percentage concession per dollar of allocated income. After all, compulsory superannuation was introduced with a particular focus on improving the retirement income of lower income people.

Nevertheless, of these various possible forms of rebate design, the most practical is a set percentage rebate common to all superannuation fund members.

<u>Fact 7</u>*: A refundable tax rebate set at a percentage of annual allocated taxable income from superannuation would provide equitable concessional treatment across all fund members*

The level of the rebate would be set taking into account such considerations as personal income tax rate scale, degree of concessionality required and cost to revenue.

A refundable tax rebate of 19 per cent of annual taxable income allocated to members by their superannuation funds would have the following effects on members in different brackets of Australia's current personal income tax rate scale.

Fund income with no associated tax credits. For purposes of illustration, the taxable income allocated is first assumed to be only $100 for all members arising from income that has no associated tax credits/rebates/offsets (the effects of franking credits associated with franked dividends is shown later).

In contrast to current arrangements, integration-style redesign plus a 19 per cent superannuation tax rebate would be sensitive to members' differing levels of income.

- Those with taxable income (including allocated superannuation income) <u>below the tax-free threshold</u> would receive their 19 per cent concessional rebate as cash in hand.

    - Someone in this category being allocated $100 of taxable income would receive a $19 cash refund from the concessional superannuation rebate. The $100 would stay in the fund.

    - Such members would receive cash in hand that recognises their actual personal income tax status. They could decide to spend it on consumption or reinvest the cash into superannuation or elsewhere.

- Those with a marginal <u>personal tax rate of 19 per cent</u> would have their tax payable cut by up to the full amount of their 19 per cent rebate and would receive some of their rebate as cash in hand if the rebate was greater than their pre-rebate tax payable.

    - Someone in this category being allocated $100 of taxable income would either: pay no extra tax on that allocation because the 19 per cent concessional rebate matched the 19 per cent tax otherwise payable on the income (if the person's taxable income before the allocation was above the lower bound of the 19 per cent income tax bracket); or, receive some of the $19 concessional rebate as cash in hand (if the person's taxable income before the allocation was below the lower bound of the 19 per cent income tax bracket).

    - The full $100 of income would stay in such members' funds.

- Those with a marginal <u>tax rate above 19 per cent</u> would most likely have their tax payable reduced by the full amount of the rebate.

    - People in this category – say, on a 47 per cent marginal tax rate – being allocated $100 of taxable income would also attract a $19 cash rebate from the concessional superannuation rebate, resulting in an extra $28 of personal tax payable (rather than an extra $47 that would be payable on non-superannuation taxable income).

    - Again, the full $100 of income would remain in the fund.

These simple illustrations highlight the inequities of current arrangements which discriminate against low income superannuation fund members in favour of higher income members.

The illustrations show that, with integration-style redesign plus superannuation tax rebate, all members would retain the $100 in their funds and receive cash in hand tapering out and being replaced by increasing tax payments as incomes rise. In contrast, currently, regardless of members' income levels:

- in accumulation mode, all members would have their $100 of income in their funds reduced by $15; and,

- in pension mode, $100 of income would remain untaxed in the fund.

Fund income with associated franking credits. Where the $100 of taxable income allocated to members comes solely from franked dividends received by their funds ($70 of franked dividends plus $30 franking credits) the impact of the associated $30 of imputation credits (reflecting company tax already paid) shifts from members' accounts in their superannuation funds to the members' personal tax assessments.[11]

That shift would be reflected in $30 of extra cash in hand for the lowest income members and reduced personal tax payable by highest income members. All members could decide to reinvest this $30 back into their superannuation funds to bring the $70 of franked dividend income remaining in the fund back up to a pre-company tax level of $100.

- Those with taxable income (including allocated superannuation income) below the tax-free threshold being allocated $100 of taxable income arising solely from franked dividends ($70 dividend plus $30 credit):

    - would receive in hand the $30 cash refund for the imputation credits, a refund required to ensure their zero tax rate is achieved, plus an extra $19 cash refund from the concessional superannuation rebate ($49 cash in total); and

    - could decide to reinvest the $49 of cash into superannuation or elsewhere.

- Those with a marginal personal tax rate of 19 per cent (say, whose taxable income before the allocation of $70 plus $30 imputation credit was above the lower bound of the 19 per cent income tax bracket):

    - would receive a net $11 imputation credit to ensure their 19 per cent tax rate is achieved on the $100 of taxable income plus an extra $19 tax credit from the concessional superannuation rebate, a total of $30 of credits which would be refundable as cash in hand to the extent that the credits were greater than their pre-credit tax payable; and

    - could decide to reinvest their total $30 of reduced personal tax (and any cash refunds)

[11] Some commentators erroneously continue to say that shareholders "who pay no tax" should not attract refunds of excess franking credits attached to their franked company dividends. Of course, franked dividends have already been taxed at 30 per cent ($100 dollars of taxable company income attracts $30 company tax before being distributed as $70 of franked dividends). Where a zero tax rate applies to the franked dividends plus credits (someone below the tax-free threshold or, the usual target of the above commentators, superannuation fund accounts in pension mode), our 'pure' imputation system rightly refunds the $30 so that a zero tax rate is actually achieved. The commentators, instead of asking why a zero tax rate applies in the pension phase of superannuation, focus on the imputation credits which ensure the legislated zero tax rate is achieved in relation to franked dividends (as it is for other forms of taxable income in the pension phase, like; unfranked dividends, interest income and rental payments on property).

back into their superannuation funds (bringing the $70 remaining in their funds to $100).

- Those with a marginal tax rate above 19 per cent would again most likely have their tax payable reduced by the full amount of the rebate.

    - People in this category on a 47 per cent marginal tax rate would pay the usual extra $17 of personal tax to achieve a 47 per cent tax rate on the $100 of allocated income but would also attract a $19 cash rebate from the concessional superannuation rebate, resulting in a net reduction in personal tax payable of $2.

    - Again, $70 of income remains in the fund (and the $30 less personal tax payable compared to the above illustration where the $100 of allocated income had no associated credits could be reinvested to bring the $70 up to $100).

In sum, current inequities in accumulation and pension phases of superannuation could be addressed by integration-style redesign of superannuation taxation where members' annual taxable income in their funds (along with any associated tax credits) is allocated to members' personal tax assessments. And a refundable tax rebate set at a fixed percentage of allocated taxable income could provide accompanying concessional income tax treatment that provides equitable treatment for members across the various income tax brackets.

CONCLUSION

Current taxation arrangements for superannuation blatantly discriminate against low income in favour of high income members.

That blatant discrimination could be addressed by: requiring contributions to be made from after-tax income; allocating members' annual taxable income in their (tax-free) superannuation funds to their personal tax assessments; and providing refundable cash rebates equal to, say, 19 per cent of allocated taxable income at least for low income members.

The absence of redesign of tax arrangements to remove current discrimination against low income superannuation fund members would seem to put serious questions around an increased superannuation guarantee and, indeed, the compulsory superannuation system itself.

15 January 2020