SUBMISSION

This Submission is in respect of the proposed changes to superannuation law under the Superannuation (Objective) Bill 2016 (**Objective Bill**); Treasury Laws Amendment (Fair and Sustainable Superannuation) Bill 2016 (**Taxation Bill**); Treasury Laws Amendment (Fair and Sustainable Superannuation) Regulation 2016 (**Work Test Regulation**) and the Treasury Laws Amendment (Fair and Sustainable Superannuation) Regulation 2016; Low Income Superannuation Tax Offset (**LISTO Regulation**).

This Submission supports the Objective Bill, the Taxation Bill, the Work Test Regulation and the LISTO Regulation. These changes are, however, subject to amendments announced by the Government on 15 September 2016 and will need to be updated to reflect these. Further, we observe that the measures are only the first tranche of changes to superannuation legislation contemplated by the 2016 Budget.

The remaining superannuation measures in the 2016 Budget are critically important, because these are the measures which raise revenue and which are subject to a range of views among stakeholders and the broader policy community. It would have been far preferable for the complete package of superannuation measures to be released together, in order to properly assess its strengths and weaknesses.

More broadly, the package of changes introduced by the 2016 Budget are modest relative to the scale (and regressive incidence) of the current tax concessions for superannuation. This should be borne in mind by all parliamentary members in their consideration of both tranches of legislation. It is important that the Government not lose sight of the core revenue and fairness benefits of the 2016 Budget superannuation measures.

1. Objective of the superannuation system

We support the insertion of an objective for the superannuation system. Section 5(1) of the Objective Bill provides:

> "The primary objective of the superannuation system is to provide income in retirement to substitute or supplement the age pension."

Together, the Objective Bill and Schedule 4 of the Taxation Bill require that for every Bill or regulation relating to superannuation, there must be a statement of its compatibility with the primary objective of the superannuation system.

> **Recommendation 1:** support the purpose of the superannuation system as drafted in the Objective Bill and support Schedule 4 of the Taxation Bill which, together with the Objective Bill, requires that for every Bill or regulation

relating to superannuation, there must be a statement of its compatibility with the primary objective of the superannuation system.

The Explanatory Memorandum to the Objective Bill and the Taxation Bill (**EM**) sets out five subsidiary objectives to support the primary objective of the superannuation system. The subsidiary objectives are to assist with assessing the compatibility of a Bill or regulation with the primary objective. The subsidiary objectives in the EM are:

- facilitate consumption smoothing over the course of an individual's life;
- manage risks in retirement;
- be invested in the best interests of superannuation fund members;
- alleviate fiscal pressures on Government from the retirement income system; and
- be simple, efficient and provide safeguards.

They are quite separate and distinct from the objective, although stated to support the primary objective.

This Submission does not seek to debate the primary objective of the superannuation system proposed by the Objective Bill. However we query why the subsidiary objectives are set out in EM rather than the Objective Bill itself. Locating the subsidiary objectives in the EM as a framework for assessing compliance with the primary makes them unlikely to be of significant use. A court would only refer to an explanatory memorandum in the event of ambiguity in the statute and it is not clear whether regulators would regularly refer to these subsidiary objectives.

We observe that the primary and subsidiary objectives are silent on the issue of gender equality. The bipartisan report of the Senate Economics Committee on the Economic Security for Women in Retirement[1] recommended that all government policy analysis in relation to retirement incomes include specific analysis comparing the impact of each proposal on men and women. We recommend that the Government should include specific reference to women's economic security in retirement on an equal basis with men as an objective of the superannuation system, to ensure gender equity is a continuing focus for policy makers.

Recommendation 2: Include a sixth subsidiary objective as follows:

- "be a system that impacts men and women equally."

[1] Senate Economics Committee, 'A Husband is Not a Retirement Plan': Achieving economic security for women in retirement (29 April 2016) Recommendation 15, http://www.aph.gov.au/Parliamentary_Business/Committees/Senate/Economics/Economic_security_for_women_in_retirement/Report .

2. Amendments relating to harmonising contribution restrictions

Currently, people aged between 65 and 74 can only contribute to superannuation if they are engaged in work for a minimum of 40 hours over 30 consecutive weeks, in the one financial year. In effect, this means that most people aged over 65 cannot contribute to superannuation.

Schedule 1 to the Regulation removes the “work test” for people aged between 65 and 74 to make deductible superannuation contributions. This Submission supports Schedule 1 to the Regulation. As the Explanatory Statement to the Regulation correctly notes, the effect of this change is that more people aged over 65 will be able to contribute to superannuation.

The work test as it currently operates can be capricious in its impact. For example, if a retired person returns to even modest levels of work, that person ceases to be eligible to make concessional superannuation contributions. The effect of this is to create a lump sum tax on working, which is undesirable because it discourages people in the 65 – 74 age bracket from engaging in paid work.

Removing the work test does benefit those on higher incomes more, because of their greater capacity to make voluntary contributions. A possible means of dealing with this is through the Transition to Retirement (TTR) provisions, which are not dealt with in this tranche of legislation.

In general the TTR provisions will help address the situation whereby some people, while having their accounts in tax-free pension mode, can still make concessional contributions to superannuation. However it is not clear that they will address this loophole entirely, and it may be exacerbated by liberalisation of the work test.

One possibility is an on/off switch for funds in pension (tax free) mode. If a person is contributing to a superannuation fund, then the fund is put into accumulation mode, and it can only switch to the tax-free pension mode if contributions cease. Another approach would be to confine concessionality to net contributions to superannuation. This allows abolition of the work test, but relatively few people will then wish to avail themselves of the opportunity to contribute. The revenue cost of such a measure would be minimal, with perhaps a net saving.

This Submission therefore supports removing the work test, but recommends confining concessionality in some such manner. These comments are also relevant to item 3 below.

> **Recommendation 3:** support Schedule 1 of the Work Test Regulation, which removes the “work test” for people aged between 65 and 74 who make superannuation contributions.

3. Deducting personal contributions

Schedule 1 of the Taxation Bill removes the requirement in the income tax law that an individual must earn less than 10 per cent of their income from their employment related activities for them to be able to deduct a personal contribution to superannuation and make it a concessional contribution. This Submission supports Schedule 1 of the Taxation Bill because it eliminates a differential in the system, where people who are self-employed are taxed at a different (higher) rate for voluntary superannuation contributions than employees. It also removes a discrimination against people whose employers do not allow them to salary sacrifice.

People on higher incomes are likely to benefit more from this measure. However, people on higher incomes save more in superannuation overall, and will therefore benefit from any kind of overall savings concession.

This Submission also notes that all superannuation contributions will remain subject to yearly caps on concessional contributions. These caps are to reduce from their current levels of $30,000 for those aged under 49 and $35,000 for those aged 49 and above. The concessional caps are not dealt with in this tranche of superannuation legislation and are important in ensuring vertical equity in the superannuation system.

> **Recommendation 4:** support Schedule 1 of the Taxation Bill, which removes the requirement in the income tax law that an individual must earn less than 10 per cent of their income from their employment related activities for them to be able to deduct a personal contribution to superannuation and make it a concessional contribution.

4. Tax offsets for spouse contributions

Schedule 2 to the Taxation Bill increases the amount of income an individual's spouse can earn before that person ceases to be entitled to a tax offset for making superannuation contributions on behalf of their spouse. This measure increases the income threshold for a person's spouse from $13,800 to $40,000, below which superannuation contributions made by an individual for their spouse entitle that person to a tax offset. The tax offset remains a maximum of $540 an income year.

The authors have some reservations about the rules on spouse contributions because they effectively permit a degree of income splitting. However we note the rules give the spouse, overwhelmingly the female spouse, a legal right to the superannuation contribution and retirement income. The offset will enable a low-earning spouse to build superannuation while working in a low wage job or part-time. On balance, this Submission therefore supports Schedule 2 to the Taxation Bill.

> **Recommendation 5:** support Schedule 2 of the Taxation Bill which increases the amount of income an individual's spouse can earn (from $13,800 to $40,000) before that person ceases to be entitled to a tax offset for making superannuation contributions on behalf of their spouse.

5. Low Income Superannuation Tax Offset

Schedule 3 to the Taxation Bill enables low income earners to receive a low income superannuation tax offset (**LISTO**). The LISTO is up to a maximum of $500 in one income year, for people earning taxable income of $37,000 or less. The practical effect of this measure is remove the tax penalty incurred by people on incomes of $37,000 and under who pay a higher rate of tax (15 per cent) on superannuation contributions than they do on other income income (zero tax up to the tax free threshold of $18,200, and 19 per cent on income of $18,201 to $37,000). At all such levels their *average* tax rate is less than 15 per cent; at $37,000 it is 10.45 per cent including the Medicare levy.

The LISTO brings the system closer to a sensible incidence of tax support. Stewart and Ingles have previously argued for a “Tax-Exempt-Exempt” (TEE) system for taxing superannuation whereby initial contributions are taxed at marginal rates, and fund earnings and payouts are exempt[2]. The LISTO is compatible with progress towards this objective, as are mooted changes tightening Division 293 tax.

Schedule 2 to the LISTO Regulation enables reporting to the Parliament and to investors about the LISTO. This Submission supports Schedule 3 to the Taxation Bill and Schedule 2 to the LISTO Regulation.

> **Recommendation 6:** support Schedule 3 of the Taxation Bill which enables low income (those earning $37,000 per year and under) earners to receive a low income superannuation tax offset (LISTO).
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> **Recommendation 7**: support Schedule 2 of the LISTO Regulation.

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[2] Ingles, D & Stewart, M, November 2015, ‘Superannuation tax concessions and the age pension: a principled approach to savings taxation’, Tax and Transfer Policy Institute Working Paper 7/15, https://taxpolicy.crawford.anu.edu.au/publication/ttpi-working-papers/7561/superannuation-tax-concessions-and-age-pension-principled .