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TITLE: **The great superannuation tax concession rort**

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Suppose the Government announced a $25 billion spending package with the aim of helping people to accumulate superannuation. The package comprises two components: the first relates to how much you earn and therefore contribute to super and the second relates to how much you have stashed away in your super fund. The package gives you nothing if you earn below $35,000 per annum; $2205 if you earn $100,000; and $28,350 if you earn $1 million. It gives you even more if you make more than the minimum superannuation contribution.

How fair would you say that package is?

Then the package apportions money relative to the size of the earnings on your accumulated superannuation. It gives you nothing if you have no lump sum. If you have accumulated $100,000 you get $3600; half a million and $1 million of savings will net you $18,000 and $36,000 respectively.

Now how fair is the package?

The government is so pleased with the brilliance of its package that it decides to implement it every year for the rest of time. Unfortunately, however, the package is causing too much fiscal stimulus so its cost has to be offset somehow. And there are some choices the government can make here: everyone can pay extra tax of $2500 per annum or wait longer for their emergency treatment and elective surgery or miss out on having adequate dental care. You get the picture?

Obviously it wouldn't be a very popular spending package except in some select quarters. It would never be introduced into the House and it would never pass the Senate. Yet this scenario precisely reflects what is happening with our existing tax treatment of superannuation savings.

Superannuation is the most concessionally-taxed investment in Australia with contributions, fund earnings and payouts all receiving concessional treatment. According to Treasury, the effective marginal tax rate on superannuation savings is highly negative.

The system is skewed to assist the rich in a number of ways.

1. It converts a progressive income tax system into a flat 15 per cent tax for super thus benefiting those on higher tax rates. Astonishingly, the top five percent of individuals account for 37 per cent of concessional contributions.

2. It provides little or no benefit to low-income earners, including women working part-time. An executive earning $300,000 per annum with a million dollar retirement account, however, can receive $37,000 of concessions, 2.5 times the value of the age pension, for every year of their working life.

3. It delivers substantially greater benefits for men than women because women earn less and tend to have broken work histories.

4. Allowable contributions are such that high-income earners could easily retire with $5 million in super assets, which would then allow them to draw down around $500,000 a year in retirement, tax-free.

The system has become so skewed that the annual cost of providing superannuation tax concessions to high-income earners is much greater than the cost of simply paying those same individuals the age pension. Providing tax concessions for superannuation as a mechanism to help insulate the budget from the cost of providing for an ageing population is not sensible.

Australian superannuation fund assets, currently over $1 trillion, are expected to reach almost $9 trillion by 2041. Because the size of the tax concessions are related to the size of the accumulated lump sum, reflecting the low (15 per cent) tax rate on fund earnings, the forecast growth in superannuation assets imposes a question mark over whether the current system will be sustainable with an ageing population.

Because of super tax concessions, the retirement income system will increasingly emphasise *income maintenance* after retirement rather than *income support* for retirees on low incomes. This shift in goals has occurred without proper public debate. There needs to be a more appropriate balance between the two goals.

Transition to retirement (TTR) pensions have opened up a huge rort where well-off older workers with the opportunity to receive a TTR pension while simultaneously ‘salary sacrificing’ into super are able to reduce their effective tax rate on earnings to a 15 per cent flat rate.

Our paper *The great superannuation tax concession rort* explores a number of possibilities for reform.

Option 1 removes the most egregious of current concessions and would involve, for example, taxing the earnings of superannuation funds during the payout stage and the abolition of salary sacrifice arrangements. This option would raise $4 to $5 billion per annum and, in terms of salary sacrifice, would affect only a minority (five per cent) of contributors, largely high-income earners.

Option 2a changes the tax on contributions and fund earnings (currently 15 per cent) and the tax on fund capital gains (currently 10 per cent) to 30 per cent, comparable with the standard marginal tax rate; it would raise approximately $18 billion per annum.

Option 2b taxes superannuation contributions at an individual’s full marginal tax rate. This option would deliver greater benefits to low-income earners and significantly fewer benefits to high-income earners. Combined with the higher tax rate on fund earnings, it would raise about $21 billion per annum.

These increased revenues could be used to finance significant tax reform. Yet another use would be to raise the age pension itself. The greater the weight of the pension in the retirement income system relative to superannuation tax concessions, the more redistributive the system and the greater its impact on poverty amongst the aged.

Option 3 combines Option 2b with a new rebate for *all* superannuation contributions. This could be either a 50 per cent rebate subject to a low ceiling (**Option 3a**) or a simple proportional 18 per cent rebate with a much higher ceiling **(Option 3b)**. The existing co-contribution would be abolished. Both these options would cost around $18 billion per annum and would produce net savings of about $4 billion per annum.

In conclusion, the current superannuation tax system is not rational. We recognise that many people have lost money from superannuation in the current global crisis, but tax reform must deal with the structure of the tax system well beyond the period of the crisis. Our preference is to do away with concessions and spend the money saved on more worthy initiatives. But our fallback is to redirect existing concessions so that they are fairer. Both alternatives under our Option 3 deliver some tax assistance to the well-off but either would be a considerable improvement on the current system.

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