Research that matters.

TITLE: **Super subsidies: a budget spending secret**

AUTHOR: **David Richardson**

PUBLICATION: **The Canberra Times**

PUBLICATION DATE: **07/08/12**

LINK: ***http://www.canberratimes.com.au/national/public-service/super-subsidies-a-budget-spending-secret-20120806-23p1p.html***

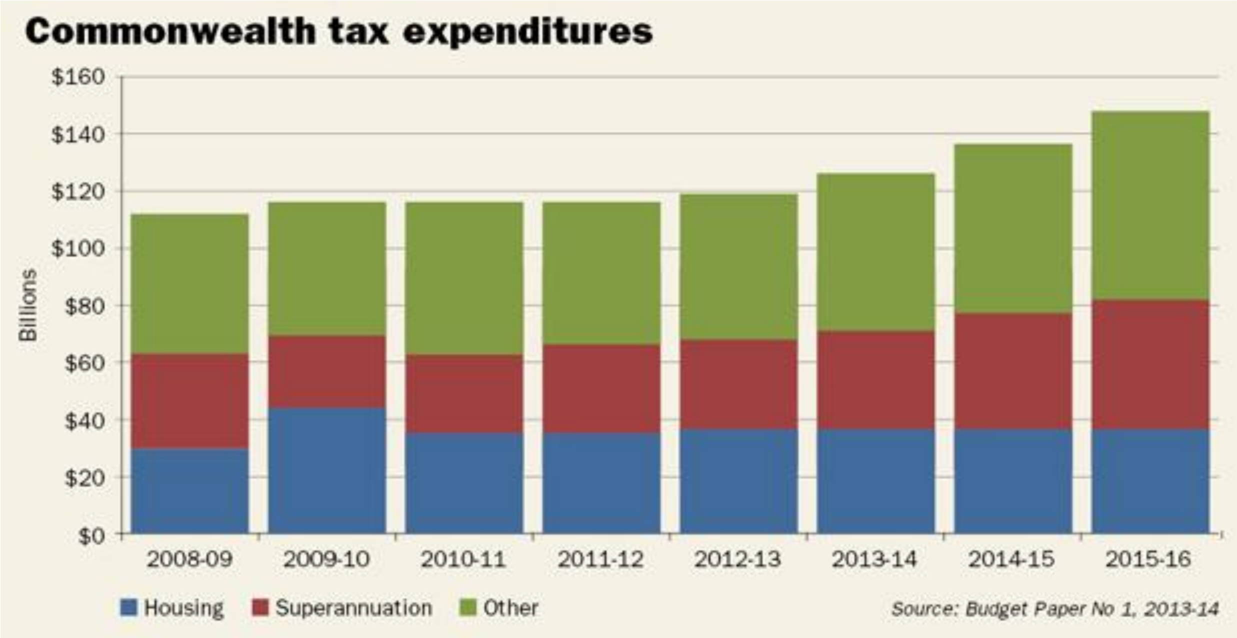
The budget papers mask some public spending by classifying it as 'tax expenditures'

The amount the federal government spends on superannuation subsidies is forecast to hit $45 billion in 2015-16. Yes: $45 billion! That's well over 10 per cent of the government's total projected outlays and bigger than the amount spent on the age pension. These huge concessions go disproportionately to high-income earners.

Treasury data shows that the top 5 per cent of individuals account for more than 37 per cent of concessional super contributions. The concessions work by taxing super contributions and earnings at 15 per cent rather than the taxpayers' marginal tax rate. This is a big concession to someone on a 45 per cent marginal tax rate but in fact a penalty for someone with a zero marginal tax rate.

While there were some initiatives in the 2012-13 budget to address the bias in super concessions, there is much more that could be done and a broader discussion to be had. Given that the budget papers are now more than 10 centimetres thick, you would think there would be a lot of information about super subsidies, right?

Wrong. Super tax concessions get two mentions in appendix F to the chapter headed ''Statement 5: revenue'', in *Budget Paper No 1*. If you can find it, the meaning is obscure and assumes the reader knows what a ''tax expenditure'' is.



"Tax expenditures" are so called because they perform the same function as an expenditure might, but instead of being an outlay they are given as a tax deduction or rebate. The latter have the effect of reducing tax receipts rather than increasing outlays. There is the same impact on the budget balance and, no matter what they are called, they involve a government diverting resources towards a particular outcome. However, as "tax expenditures", the items concerned are almost invisible and impossible to find in the budget papers unless you know what you are looking for. The Organisation for Economic Cooperation and Development, in its *Best practice guidelines - Off budget and tax expenditures*, even goes so far as to call tax expenditures " 'back-door' expenditures".

By contrast, an ordinary outlay, like the family tax benefit, receives a lot more scrutiny and debate. Even within government, spending items are under a good deal of scrutiny in the budget round and in the parliamentary debates that follow. And when the budget and the financial year are over, the government eventually publishes the exact amounts it did spend under the various headings.

Those processes rarely happen with tax expenditures. In fact, governments like tax expenditures because they give the misleading impression of a government much slimmer than it actually is. Instead of showing extra government spending of $45 billion in super tax concessions, by classifying them as a tax expenditure both spending and taxing look smaller by $45 billion. We kid ourselves that government activity is smaller than it is.

For many items, the decision to classify them as a tax expenditure or an outlay has been quite arbitrary. A measure designed to help people or encourage certain behaviour is diverting government resources for that purpose whether it is called an outlay or a "tax expenditure" (a rose by any other name!). Yet having both outlays and tax expenditures causes confusion among people trying to understand the budget.

Years ago, the Parliament and the auditor-general began a campaign to reclassify some tax expenditures as outlays and, as a consequence, the family tax benefit and other former tax concessions are now regarded as just other government spending items that are up for debate at any time. But the agenda behind reclassifying tax expenditures as outlays has since run out of steam. In the interest of transparency and accountability, it is important that the superannuation tax concessions be exposed to the light by reclassifying them as outlays in the budget papers. There is no need to change legislation or anything else to do so.

Putting super concessions on the outlays side would also help insulate the tax system from plunder by high-income earners under future governments. We saw that largesse going to the rich increased massively under the Howard government, but a future government, though it may be tempted, would find it very hard to give gifts in the form of super concessions to top-income earners if that meant a large increase in outlays.

In the event that the government decides not to convert tax expenditures into explicit outlays, the government should consider the OECD guidelines, especially those that the Australian government has not yet adopted: guidelines 12, 13 and 14.

The intention of guideline 12 is that, when the government specifies self-imposed spending limits, it should include tax expenditures. Adopting this approach would mean that the present spending limit of 23.7 per cent of gross domestic product, recorded in the last Howard/Costello budget, would be increased to a spending and tax expenditure limit of 34.4 per cent of GDP, reflecting tax expenditures at 10.7 per cent of GDP in 2007-08. This should not necessarily be taken as endorsing expenditure caps, but the point is that if such a cap is to be used then it should include tax expenditures.

Guideline 13 goes to the points made above, which is that it is important that tax expenditures receive the same scrutiny as ordinary budget outlays.

Guideline 14 relates to the management of individual portfolios. Under the Australian system, the treasurer is responsible for the tax system and hence also the super tax concessions. However, in principle, the minister responsible for retirement incomes should be in a position to take policy to cabinet that embraces the totality of government arrangements that affect retirement incomes. That allows the separate initiatives within retirement incomes to be fine-tuned to meet the ministry's policy objectives.

Moving tax expenditures to the other side of the budget would more than meet the intentions of the OECD guidelines.

Finding super tax concessions in the budget papers is like the quest for the Higgs boson; both require a lot of energy. Wading through the budget papers is a lot of work, and even then one must invest more time in understanding the concepts and work out how they compare with other budget items. The government should instead show tax expenditures as explicit outlays and present them on the outlays side of the budget. If it resists that, then at the very least the government should adopt OECD guidelines that would improve the reporting and scrutiny of tax expenditures, and also bring them within any self-imposed spending caps that the government may adopt. Then we may come a little closer to having a proper debate about whether superannuation concessions are the best way to spend $45 billion when there are so many other priorities - from the Gonski recommendations to the national disability insurance scheme - competing for funding.

David Richardson is a senior research fellow with The Australia Institute and a former economist with the Parliamentary Library.