# Treasury Consultation: MRRT Repeal Exposure Draft Legislation

SUBMISSION

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Industry Super Australia

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## About Industry Super Australia

Industry Super Australia (ISA) is an umbrella organisation for the industry super movement. ISA manages collective projects on behalf of a number of industry super funds with the objective of maximising the retirement savings of five million industry super members. Please direct questions and comments to:

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# SUMMARY

The exposure draft *Minerals Resource Rent Tax Repeal and Other Measures Bill 2013* outlines the legislative provisions to abolish the Minerals Resource Rent Tax (MRRT) and abolish or modify a number of expenditure and revenue measures.

Industry Super Australia's (ISA) comments on the exposure draft legislation are generally limited to the proposed two year pause in the scheduled increase in the Superannuation Guarantee (SG) and the abolition of the Low income Super Contribution (LISC). These measures will have a significant and detrimental impact on the 5 million members of Industry SuperFunds, and requires ISA to strenuously argue against these proposed measures. ISA submits these proposals will:

- negatively impact on the adequacy and equity of our retirement income system;
- lead to an increase in future age pension expenditures;
- reduce the savings pool available for investment in the economy – especially infrastructure; and
- create an alarming precedent for retrospective increases in taxation on individuals.

With the aging of our population such that the dependency ratio will halve in less than a generation from now[1] we must do everything we can to bolster private savings to take pressure off the age pension.

ISA estimates that the repeal of the LISC and pause in the SG will reduce aggregate superannuation savings by $53 billion by 2021-22, reducing available capital for infrastructure investment by around $5bn based on current industry wide asset allocations.

The repeal of the LISC will constitute an increase in superannuation taxes for nearly one in three working Australians, diminishing their retirement savings by up to $27,000 in current dollars (15% loss) and leading to further pressure on future Governments to increase the adequacy of the age pension. The repeal of the LISC will be particularly damaging to the retirement savings of women who constitute an estimated two-thirds of those eligible. Staggeringly, the abolition of the LISC will negatively impact on the retirement savings of almost one in two women. ISA submits that the Government and superannuation industry must explore every possible alternative option to ensure the maintenance of the LISC.

Consistent with the broad recommendations of the Henry Tax Review the previous Government implemented changes to improve the equity of concessional contribution caps, concessional contributions for high income earners, and co-contribution scheme which saved an estimated $2.5 billion per annum[2]. From a budget sustainability perspective these savings more than fully offset the $0.9 billion annual cost of the LISC.

ISA recognises the Government's policy to repeal the MRRT requires steps to mitigate its impact on the budget position. However, the detrimental impact on over three million Australians from the rescinding of the LISC demands a review of this measure.

There is a moral imperative upon the Government, Parliament, and superannuation industry to find a solution and deliver the community a bi-partisan and unified approach to this issue.

It is central to the integrity of compulsory super that all Australians receive a tax concession on mandatory contributions – without the LISC one in three won't. To punitively tax more than three and a half million lower income earners cannot be a sustainable feature of our superannuation system.

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[1] Source: IGR 2010 (by 2050 for every person over 65 there will be 2.7 working age people compared to 5 today)

[2] Source: Budget Papers 2009-10 to 2011-12

ISA is proposing one solution in this submission, and should this not be agreeable to the government, will continue to exhaustively propose solutions until one is found.

Before finalising the legislation for introduction **ISA recommends the Government**:

1. Publishes estimates of the long term impact of the measures on superannuation savings;
2. Considers the impact on long term budget expenditures to the aged;
3. Considers the impact on superannuation fund investment in the economy – especially infrastructure;
4. Works with the Superannuation industry to find alternative savings to retain the LISC - including the proposals put forward in this submission; and
5. If it determines to proceed with the measures regardless, remove the retrospective application to the LISC which will result in an increase in taxation on contributions already made in the 2012-13 year.

# 1. The impacts on equity and adequacy

Schedules 6 (pause in the SG) and 7 (repeal of the LISC) of the bill will have a detrimental impact on the equity and adequacy of our retirement income system.

Almost every working Australian in receipt of Superannuation Guarantee contributions will be detrimentally affected by these measures.

3.6 million low-income earners (two thirds of whom are women), with Adjusted Taxable Incomes (ATI's) below $37,000 per annum, stand to be most disenfranchised.

The abolition of the LISC in particular is contrary to the recommendation of the Henry Tax Review to adopt a more equitable distribution of superannuation tax concessions.

## 1.1 SG Pause

The bill amends the scheduled increase in the SG from 9 to 12 per cent by delaying its progression by two years from 2013-14 to 2015-16. However the two year delay results in reduced SG contributions for a period of seven years, with contribution rates not reaching an equal footing with the previously announced schedule until 2021-22.

This has a significant impact on retirement savings for individuals who are reliant on the SG with the largest impacts felt by younger members on moderate incomes. The reduced contributions will cripple long term retirement outcomes for these individuals: they will experience consistently lower balances, undermining the compounding effect of investment earnings through until retirement.

An estimate of these impacts in current dollars on retirement accumulations by age and income from the pause in the SG using standard assumptions[3] is shown in the table below:

[3] CPI 2.5 percent, wages growth 3.0 percent, net earnings 6.2 percent

**Table 1** – Impact on retirement accumulation from pause in SG (expressed in 2013 dollars)

| | Income p.a | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| **Age Now** | **$20,000** | **$25,000** | **$30,000** | **$35,000** | **$40,000** | **$50,000** | **$60,000** | **$70,000** | **$80,000** | **$90,000** | **$100,000** |
| **18** | -$4,421 | -$5,527 | -$6,632 | -$7,738 | -$8,843 | | | | | | |
| **25** | -$3,438 | -$4,298 | -$5,157 | -$6,017 | -$6,876 | -$8,595 | -$10,315 | -$12,034 | -$13,753 | -$15,472 | -$17,191 |
| **30** | -$2,873 | -$3,591 | -$4,309 | -$5,027 | -$5,746 | -$7,182 | -$8,618 | -$10,055 | -$11,491 | -$12,928 | -$14,364 |
| **35** | -$2,400 | -$3,000 | -$3,601 | -$4,201 | -$4,801 | -$6,001 | -$7,201 | -$8,401 | -$9,602 | -$10,802 | -$12,002 |
| **40** | -$2,006 | -$2,507 | -$3,008 | -$3,510 | -$4,011 | -$5,014 | -$6,017 | -$7,020 | -$8,023 | -$9,025 | -$10,028 |
| **45** | -$1,676 | -$2,095 | -$2,514 | -$2,933 | -$3,352 | -$4,190 | -$5,027 | -$5,865 | -$6,703 | -$7,541 | -$8,379 |
| **50** | -$1,400 | -$1,750 | -$2,100 | -$2,450 | -$2,800 | -$3,501 | -$4,201 | -$4,901 | -$5,601 | -$6,301 | -$7,001 |
| **55** | -$1,170 | -$1,462 | -$1,755 | -$2,047 | -$2,340 | -$2,925 | -$3,510 | -$4,095 | -$4,680 | -$5,265 | -$5,850 |

## 1.2 Low Income Super Contribution (LISC)

The low income super contribution was introduced in response to the Henry Tax Review and was designed to address the inequitable contribution tax treatment of low income earners' SG contributions. The Henry review found the flat 15 per cent contribution tax was regressive in its impact, with low income earners paying more tax on their super contributions than their take home earnings.

The LISC operates as a tax offset, effectively refunding the contribution tax paid by low income earners on their SG contributions, thus allowing low income earners to accrue a tax concession on their contributions like all other income earners.

The operation of the LISC restores a fundamental tenet of our compulsory superannuation system whereby the Government offers compensation to individuals, by way of tax concession, for their deferral of consumption caused by the SG.

The LISC is also one of the few dedicated measures designed to improve the retirement income adequacy of women. Women are most heavily concentrated in the lower income rungs where the LISC operates, with an estimated two thirds of the 3.6 million total eligible population being women. This factor alone should heavily weigh against the abolition of the LISC.

The LISC is also particularly impactful on total retirement incomes for low income earners, with many recipients obtaining the full benefit of the LISC as they have insufficient income and assets to be in the taper range for the part pension.

An estimate of the impacts in current dollars on retirement accumulations by age and income from the abolition of the LISC using standard assumptions[4] is shown in the table below:

[4] CPI 2.5 percent, wages growth 3.0 percent, net earnings 6.2 percent

**Table 2** – Impact on retirement accumulation from abolition of LISC (expressed in 2013 dollars)

| | Income p.a | | | | |
|---|---|---|---|---|---|
| Age Now | $15,000 | $20,000 | $25,000 | $30,000 | $35,000 |
| 18 | -$26,644 | -$26,674 | -$23,067 | -$11,193 | -$5,006 |
| 25 | -$20,711 | -$20,734 | -$17,930 | -$8,700 | -$3,891 |
| 30 | -$17,300 | -$17,320 | -$14,977 | -$7,268 | -$3,250 |
| 35 | -$14,221 | -$14,467 | -$12,511 | -$6,071 | -$2,715 |
| 40 | -$10,723 | -$12,085 | -$10,451 | -$5,071 | -$2,268 |
| 45 | -$7,656 | -$9,800 | -$8,730 | -$4,236 | -$1,895 |
| 50 | -$5,077 | -$6,706 | -$7,292 | -$3,538 | -$1,583 |
| 55 | -$2,955 | -$3,940 | -$4,712 | -$2,956 | -$1,322 |

The removal of the LISC has the potential to diminish total retirement savings in super by up to 15 per cent for young low wage workers.

The loss of this benefit will almost certainly place further pressure on future governments to increase the adequacy of the age pension.

## 1.3 Combined impact

Taken together the combined effect of the pause in the SG and the repeal of the LISC have a significant negative impact on the retirement savings of Australians. Moreover, these negative effects are disproportionately borne by the most vulnerable: those who are eligible for the LISC and those for whom the SG is critical to savings.

The most significant effects will be felt by lower income earners (especially women) with the abolition of the LISC resulting in even greater harm than the pause in the SG.

With women currently retiring with over 40 per cent less in superannuation savings than males, the impact of the policy runs counter to the stated policy objectives of the Government and will undermine the benefit of the proposed Paid Parental Leave Scheme.  In addition, taking the PPL and the LISC together, these policy changes will significantly and negatively affect the equity of the distribution of net Government transfers in respect of Australian women.

**Table3** – Combined Impact on retirement accumulation from pause in SG and abolition of LISC (expressed in 2013 dollars)

| | Income p.a | | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **Age Now** | **$15,000** | **$20,000** | **$25,000** | **$30,000** | **$35,000** | **$40,000** | **$50,000** | **$60,000** | **$70,000** | **$80,000** | **$90,000** | **$100,000** |
| **18** | -$29,910 | -$31,040 | -$28,542 | -$22,855 | -$12,731 | -$8,843 | | | | | | |
| **25** | -$23,258 | -$24,137 | -$22,194 | -$17,772 | -$9,900 | -$6,876 | -$8,595 | -$10,315 | -$12,034 | -$13,753 | -$15,472 | -$17,191 |
| **30** | -$19,434 | -$20,168 | -$18,545 | -$14,850 | -$8,272 | -$5,746 | -$7,182 | -$8,618 | -$10,055 | -$11,491 | -$12,928 | -$14,364 |
| **35** | -$16,008 | -$16,851 | -$15,495 | -$12,408 | -$6,911 | -$4,801 | -$6,001 | -$7,201 | -$8,401 | -$9,602 | -$10,802 | -$12,002 |
| **40** | -$12,219 | -$14,080 | -$12,947 | -$10,367 | -$5,775 | -$4,011 | -$5,014 | -$6,017 | -$7,020 | -$8,023 | -$9,025 | -$10,028 |
| **45** | -$8,908 | -$11,470 | -$10,818 | -$8,662 | -$4,825 | -$3,352 | -$4,190 | -$5,027 | -$5,865 | -$6,703 | -$7,541 | -$8,379 |
| **50** | -$6,125 | -$8,104 | -$9,039 | -$7,238 | -$4,032 | -$2,800 | -$3,501 | -$4,201 | -$4,901 | -$5,601 | -$6,301 | -$7,001 |
| **55** | -$3,832 | -$5,109 | -$6,173 | -$6,048 | -$3,369 | -$2,340 | -$2,925 | -$3,510 | -$4,095 | -$4,680 | -$5,265 | -$5,850 |

Note: the combined impact of the measures is less than the sum of each measure modelled in isolation due to interactions between the LISC and SG.

## 2. The Impacts on Aggregate savings

The aggregate impacts on the superannuation saving pool from the pause in the SG and repeal of the LISC will be significant.

ISA estimates the pause in the SG will reduce aggregate superannuation savings by an estimated $40 billion by 2021-22. This is broadly consistent with other estimates including *Deloitte Actuaries and Consultants* who have estimated an impact of $77 billion by 2033[5].

ISA has also estimated the impact on retirement savings from the repeal of the low income super contribution, with a further $13 billion in savings being lost by 2021-22.

Whilst this is a small percentage of our total superannuation savings pool, the size of the total pool relative to GDP means the impact is far from insignificant.

There are measurable and lasting opportunity costs to the economy from the diminution of the savings pool.

For example with a loss of an estimated $53 billion of total savings over the next seven years, ISA estimates almost $5 billion less will be invested in domestic infrastructure over the period across the super sector, using conservative assumptions about asset allocations and returns, during a period in which it is of critical importance for the Australian economy to be boosted by expenditure on public infrastructures assets.

[5] Deloitte Actuaries & Consultants (2013) *Dynamics of the Australian Superannuation System The next 20 years: 2013 – 2033* Page 7

## 3. The Impacts on Long Term Budget outlays

ISA suggests the Government fully consider the long term budget impact from the pause in the SG and abolition of the LISC and publish a detailed analysis before proceeding.

The long term costs will principally be felt through increased aged pension outlays resulting from lower personal superannuation savings.

Significant further pressure will also be brought to bear on the adequacy of the age pension as a direct consequence of removing the LISC which would otherwise deliver significant supplementary income to full rate or near full rate age pensioners.

The LISC does not entrench a structural cost in the budget. This is due to the offsetting superannuation savings which accompanied its introduction and the fact that the structural policy settings for the LISC where eligibility is anchored at the $37,000 personal income tax threshold will fall in real terms relative to wages.

ISA estimates that the previous Government implemented $2.5 billion per annum[6] in structural savings to superannuation through:

- The halving of concessional contribution caps;
- Pauses in the indexation of concessional contribution caps;
- Reducing the concessional contribution caps for over 50's
- Capping the value of the concessional contribution concession for high income earners;
- Reductions in the matching rate for the low income co-contribution; and
- Broadening the income definition for the low-income co-contribution.

Taken together these savings more than adequately pay for the introduction of the LISC, while resulting in a more effective and equitable distribution of concessions.

## 4. Alternative funding for the LISC

If the Government is determined to secure its stated budget objectives, ISA urges it, in consultation with the Parliament and superannuation industry, to explore every possible alternative to avoid the repeal of the LISC.

Possible alternatives include the repeal of the superannuation co-contribution scheme which is less well targeted than the LISC. This alone would save an estimated $375 million per annum. The Government could also re-consider the generosity of its proposed PPL scheme by setting the income cap for calculation of benefits at a lower level.  ISA estimates this could save a further $500 million per annum depending on design. These two changes combined would allow the Government to retain the LISC while adhering to its budget objectives.

## 5. Retrospective impacts

Should the Government decide to proceed with the complete removal of the LISC, it must address the retrospective impacts which will result from the existing drafting.

[6] Source: Budget Papers 2009-10 to 2011-12

As currently drafted the repeal of the LISC will remove the entitlement for eligible contributions already made in the 2012-13 year. Under the proposed provisions the Commissioner for Taxation will be required to deny taxpayers the benefit of the LISC on eligible contributions already made.

The exposure draft legislation therefore not only produces an unfair and unsustainable outcome for low income taxpayers but puts the Commissioner in an untenable position.

The bill's proposed retrospective treatment of the repeal of the low income superannuation contribution is unprecedented and inconsistent with the bill's treatment of other provisions. The retrospective application of this particular provision is also inconsistent with other recent repeals of tax offsets.

With the possible exception on anti-avoidance measures, retrospective changes to the tax arrangements should be avoided. Retrospective changes interfere with bargains struck between governments and tax payers.

Whilst it is understood that Parliament does have the power to make retrospective law[7] Parliament has expressed the view that retrospective changes should be avoided and retrospective amendments to tax law limited where possible to anti-avoidance measures.

It is suggested that retrospective law changes that are based on budgetary or policy considerations are contrary to the rule of law in that the law must be clear and applied equally. The retrospective application of laws, including concessions, result in market uncertainty and reduce confidence.

There is a colourable argument that retrospective application in this case removes a valuable right held by a low income earner.

It could also be argued that the measure is an arbitrary exaction of a right as the removal of the right does not apply equally to all taxpayers.

## 5.1 Inconsistent treatment within the bill

The savings provisions in all the other measures within the bill that remove or infringe upon an existing right are implemented on a prospective basis. Schedule 8 which repeals various income support bonuses takes effect on Royal Assent whilst Schedule 9 which repeals the schoolkids bonus has a savings provision that also takes effect on Royal Assent but also allows the payment of the bonus after Royal Assent for an eligible person on a bonus test day prior to Royal Assent.

The inconsistent treatment of the savings provisions throughout the bill with the retrospective repeal of the low income superannuation contribution could be considered to be arbitrary when compared to the treatment of other measures with in bill.

## 5.2 Inconsistent treatment with other tax changes

The treatment of the LISC is inconsistent with the Commonwealth's previous prospective removal or changes to other tax arrangements.

*The Tax and Superannuation Laws Amendment (2013 Measure No 2) Act 2013* amended the Income Tax Assessment Act to reduce eligibility for tax concessions related to film tax offset. The changes introduced

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[7] *Polyukovich v The Commonwealth* [1991] HCA 32

measures to restrict eligibility to the film tax offset and was not retrospective as it only applied to filming commencing after Royal Assent.

The Net Medical Expenses tax offset was phased out in the 2013-2014 Budget with prospective operation from 1 July 2013 and included transitional arrangements for taxpayers who incur costs for disability aids, attendant and care or aged care expenses until 1 July 2019.[8]

The Entrepreneur's Tax Offset was removed in the 2011 budget with a prospective operation from 2012-2013. To compensate for its removal the government increased the size of the small business asset write off arrangements from $1,000 to $5,000.[9]

The 2012-2013 budget decision to limit the concessional tax arrangements associated with large Eligible Termination payments or 'Golden Handshake' payments was not retrospective and applied from 1 July 2012.

The changes made to the concessional tax treatment of fringe benefits tax (FBT) for living-away-from-home allowances and benefits in the 2012-2013 Budget generally took effect from 1 October 2012 and included some transitional provisions beyond this date.

The 2012-2013 Commonwealth Budget prospectively abolished the mature aged worker tax offset for workers born on or after 1 July 1957.

We strongly submit that the retrospective nature of the repeal of the LISC should be reconsidered by the Government.

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[8] Australian Government, *Budget Measures: budget papers no 2. 2013-2014*

[9] Australian Government, *Budget Measures: budget papers no 2. 2011-2012*