Submission to Tax Expenditure Statement Consultation

Thank you for the opportunity to comment on the Tax Expenditure Statement (TES) Consultation Paper.

My comments are directed towards the tax expenditures pertaining to superannuation in the TES paper. Additionally, my comments provide input into the proposed Treasury periodic analysis of the long-run interactions between superannuation and the Age Pension and estimates of the future costs and benefits of superannuation and its tax concessions.

Calculating tax expenditures for many items (e.g. GST on water and sewerage) is relatively straight forward. However, this is not the case for superannuation. This is because one tax expenditure (e.g. superannuation contributions) can impact on another tax expenditure (e.g. superannuation earnings), and tax expenditures in previous years can impact on tax expenditures in later years (e.g. superannuation earnings). The TES paper could discuss these issues in more detail in its analysis of superannuation tax expenditures, because a knowledge and understanding of these issues is important to informed public commentary and policy discussion of superannuation, which in turn influences the effectiveness of the superannuation and retirement systems.

Without a (SGC) superannuation system, there would be no 9.5% compulsory SCG employer contributions, and considering the overall household savings rate, most of the contributions would otherwise be consumed. Consequently, most of the $2.3trillion pool of superannuation savings (and associated earnings) would also not exist. The same would apply to voluntary contributions and associated earnings, although a higher portion of these contributions would not otherwise be consumed. Therefore, it makes more sense to use the expenditure tax benchmark rather than the income tax benchmark when calculating the tax expenditure for superannuation contributions and earnings.

The TES paper does not spell out that taxation revenue from superannuation exceeds the taxation revenue that would otherwise be collected from of the portion of salary and wages that is currently contributed to superannuation (with the taxation revenue otherwise collected being calculated using marginal tax rates, and allowing for that some portion of the contribution amount would not be consumed). Published ATO statistics show that annual taxation revenue from superannuation exceeds $30billion annually, whereas the taxation revenue otherwise be collected from the portion of salary and wages that is currently contributed to superannuation would be less than $25billion annually. The TES paper superannuation tax expenditure figures give the impression that superannuation is a drag on Government taxation revenue, when the situation is somewhat the reverse. Many commentators pick up on the TES paper figures and misuse them, which can then influence Government policy, much to the detriment of the superannuation and retirement systems.

The TES paper does not elaborate on the impacts of taxation of superannuation at the contributions, earnings, and pension stages. The most efficient method to tax superannuation is the pension stage, with taxing the contributions stage being the least efficient. This is because delaying taxation allows the account balance to compound over an individual's working life. The effect is quite profound with a system that taxes contributions providing a pension equal to about 40% of pre-retirement income, a system that taxes earnings providing a pension equal to about 50% of pre-retirement income, and a system that taxes pensions providing a pension equal to about 60% of pre-retirement income. Furthermore, delaying taxation of superannuation also increases the overall amount of taxation revenue. Note that delaying the taxation of superannuation also offers an alternative to increasing the percentage of salary and wages contributed as SGC contributions, (thereby decreasing pre-retirement living standards by reducing pre-retirement disposable income). This means that it is a no-brainer that superannuation taxation should be delayed to the extent that it is possible. Of course, the difficulty with delaying taxation until the retirement income is the cash-flow shortage to Government taxation revenues.

The TES paper does not elaborate on the distribution of taxation of superannuation across individuals, and its impact on other expenditures such as providing the safety net aged pension. It is problematic to determine what represents a fair superannuation taxation system (for everyone). However, a system that taxes superannuation at a pension stage (only) at the prevailing individual taxation rates could be considered as fair. If superannuation is taxed at an earlier stage, then it is obvious that it would be fair to tax individuals who will accumulate lower superannuation balances at a lower rate (and which reflects the comparative tax rates that would apply if superannuation was taxed at pension stage). Furthermore, it makes little sense to tax individuals who will not accumulate a sufficient superannuation balance to fully provide for their retirement income and will need to draw on the aged pension. This is because taxing their superannuation at contribution or earnings stages reduces the impact of compounding, only to replaced (but at a significantly higher cost) by higher aged pension payments.

This submission would make the following recommendations:

(1) Recognise that superannuation taxation revenue provides more taxation revenue for the Government that it would obtain if superannuation (with SGC contributions) had never existed.
(2) Recognise that the current taxation of superannuation is inefficient in terms of when superannuation is taxed.
(3) Recognise that the distribution of tax across individuals (with a mostly flat 15% tax rate) is inefficient and unfair.
(4) Reinvest the superannuation taxation revenue (above the taxation revenue that would otherwise be obtained without superannuation) by reforming the taxation of superannuation - so that becomes more efficient, fairer, reduces the need to increase SGC payments, and reduces aged pension safety net payments.
(5) Transition to a progressive scale for taxation of superannuation contributions and earnings, say from 0% to a maximum of 25%, based on income percentiles and/or superannuation contribution amounts and/or superannuation balances. For individuals with very low incomes and unlikely to become self-sufficient in retirement, it makes sense to set a zero-tax rate for contributions and earnings. In my opinion, this is the main reason superannuation will not reduce aged pension payments as everyone would hope, and amounts to a wasted opportunity.
(6) Transition from earlier stage superannuation taxes to later stage taxes. The original Keating superannuation system partially did this by taxing superannuation pensions and providing a non-refundable tax credit of contributions and earnings taxes. Unfortunately, it still removed money from the superannuation system at the early contribution and earnings stages (thereby reducing the final accumulation balance) and did not provide a refundable tax credit (thereby increasing the dependence of low income people on the aged pension). One approach would be to progressively decrease the contribution tax rate as superannuation earnings taxes increase in conjunction with the maturing of the superannuation system.
(7) Transition to a pension phase only taxation system. I do not know how the Government would affect a transition to a pension phase only taxation system, without effectively reversing the Howard superannuation reform that superannuation should be tax-free. No doubt that change was popular but it was not efficient. In my opinion, it would have better to reduce the contribution and earnings tax rates, and leave the pension phase taxation in place (but with the tax credits being deemed refundable).