A Plan to Simplify and Streamline Superannuation

Submission by the

National Institute of Accountants

Background and Overview

The National Institute of Accountants (NIA) has been calling on the Government to undertake a wholesale review of superannuation laws and policies for a number of years. The NIA has been of the opinion that superannuation reform has not had the systemic review it. It was therefore encouraging, and surprising, to hear the 2006 Budget announcements and the fundamental changes to superannuation policy they foreshadowed. These announcements have been mostly welcomed by the NIA and we look forward to working with the Government to ensure their effective and efficient implementation.

While the NIA broadly supports the changes, the NIA is concerned about the secretive way this policy reform was developed as this has prevented wider discussion on superannuation reform. There are a number of potential reforms and while the Government is free to choose the reforms it believes best address the needs of the country, without broader consultation some views and potential reforms may either not have been considered or only partially considered, or there is a perception that an option was not properly considered.

The NIA fully supports the need to make wholesale changes to Australia's superannuation system as the system is an unnecessarily complex. The blame for this lies largely with the continuous 'tinkering' with policy and legislation without looking at the overall impact of these changes.

One area the NIA does not believe has been fully explained to the public is why the decision was made to not to reduce or remove tax on superannuation contributions, and instead remove tax at the benefits stage. The NIA understands that the removal of tax at the benefits stage will reduce the complexity for retirees, however it must be said that this will not benefit all retirees as many of them currently take advantage of incentives in the system and access benefits free of tax.

Many commentators and industry advocates, including the NIA, have called for a reduction or abolition of the contributions tax. Contributions tax is a direct disincentive for people, especially younger people, from investing more in their superannuation. It is also an administration burden on funds.

While the NIA supports the measures to remove the benefits tax, the NIA is of the view that greater consultation would have achieved a broader review of the superannuation and allow greater ownership of the changes by those involved in the industry. With the Government and Treasury setting the agenda already, this has limited the ability to discuss alternatives.

All in all, the Government should be congratulated for a bold plan to actually simplify and streamline superannuation. However, the opportunity of using the significant current and projected budget surpluses to invest in retirement savings by reducing or abolishing contributions tax has unfortunately been missed.

The NIA would hope that other proposals to further reform superannuation and its complexity could be reviewed including the following:

- whether the 9 percent compulsory superannuation contribution is sufficient (and if not, should employees also make compulsory contributions);
- Should there be higher compulsory super contributions for those in certain age brackets? (either higher employer contribution or a minimum member contribution of over a certain age and income level); and
- Debate as to what should happen with the “Lost member” account.

Taxation of Benefit Payments

Any person who has undertaken study of the current taxation arrangements in relation benefit payments will appreciate the complexity that has been built into the current system. Such complexity has a number of costs. First of all is the costs to Government agencies in their regulation of superannuation and costs to industry and funds in their administration of the system. Such cost not only draw down on government revenues unnecessarily but also the cost of administering funds is passed onto fund members, thus reducing their end benefits.

Therefore, any reform to this complex current structure is welcomed. The devil, as they say, though is always in the detail. While a policy may be good, if it is not effectively implemented, not only can the policy intent be diminished but unintended consequences can creep in. The NIA therefore call upon the Government and its agencies to co-design the legislation and administrative arrangements with industry.

The main advantage of the Government's proposals is its simplicity. There is little more simple in taxation that simply removing it and removing the need to report on it. In this sense, we wish to congratulate the Government.

The NIA supports the proposals to treat payments, whether in a lump sum or pension the same. While there are obvious concerns that people may not invest wisely for their future and may "blow" their lump sum, the reality is few people take such a cavalier attitude to their life savings. With "baby boomers" having a higher expectation of what they want from retirement, they will be aware that the Government pension alone will not provide such a life style. They are also a generation that has experience and expects choice. They want to have control of their affairs and quite rightfully think it is none of the Government's business to tell them how they should live in their retirement.

The removal of the Reportable Benefit Limits (RBL) for those 60 and above is very welcome. Not only for the effect on recipient's of benefit payments but also for the funds. RBL calculations can be an 'administrative nightmare' for funds, and getting it wrong can cost them and their client. Removing the RBL's will allow resources in funds to switch to other areas and reduce the overall cost of administering funds. As more and more people move to the retirement stage, such administrative burdens have a real cost on fund administration.

The NIA understands the Government's intention to tax benefits when paid to those under 60. This will provide a direct incentive for people to defer retirement, where they can, to at least 60. Those who choose to retire at an earlier age should not gain the full benefit of the Government's proposals. However, and with the risk of increasing the complexity of the arrangements, for people who are suffering from a terminal illness and are under 60, the same generous rules in relation to taxing benefits should be applied.

The reduction of the complexity by amalgamating a number of components when making lump sum and pension calculations for those under 60 as exempt components and having a reduced tax component will ensure that while there will be some administrative costs with dealing with those under 60, such costs will not be as large as currently faced by funds. The proposals provide such people with some benefits but not the full range of benefits, and we support this.

While there is general support for the proposals to exempt lump sum death payments paid to dependants, there is concern about the arrangements for non-dependant beneficiaries of such payments and of the reversion of a pension into a lump sum. If the amount in the hands of the intended party, that being the deceased, was to be non-taxable, then there is no reason to tax that amount differently now that is being provided to others. Such benefits should be treated as it would have been in the hands of the deceased, not that of the recipient. This would be more equitable and less complex.

Payment Rules Simplified

The removal of the compulsory withdrawal requirements and the attendant “work test” is to be applauded. These requirements create an unnecessary regulatory burden and are against the Government’s professed aim of giving people more choice in how they administer their own retirement.

The current rules relating to pensions are complex. A simplified structure is overdue. It should not matter which type of pension product people choose as long as they meet Government expectations and standards.

The NIA supports the proposed simplified standard without the need for further alteration. They permit sufficient flexibility given the fact that needs for retirees are likely to change.

The NIA does not oppose the proposed changes to the “Transition to Retirement” provisions and the capping of the maximum draw down at 10% to avoid excessive withdrawals. The proposals are an improvement over the current requirements.

Simplified Contributions Rules

As with nearly any piece of legislation, there is usually some measures that may not be as favourable to a section of the community. The new rules in relation to contributions are generally more favourable but to some classes of individuals they are unnecessarily restrictive and may cause them problems with their retirement plans.

The current age based limits are complex and somewhat *ad hoc.* They penalise younger people making contributions while providing for generous contributions by older workers. The new rules in effect reverse this. While it is good to see that younger workers are not penalised, the reality is they are still more likely to be on lower salary and less inclined to make contributions.

The workers that will be most affected by the changes to the aged-based limits are older workers. Many of whom have not been making contributions to superannuation throughout their entire working life. These people are likely to have larger disposable income and as their retirement is approaching, are more likely to be thinking about making additional contributions. Some of these people will have well established plans for their retirement based on the current regime. For a few of these people the proposed changes may cause significant problems.

The NIA acknowledges that the Government has attempted to deal with this issue with the transitional rules, which allow taxpayers over 50 to contribute up to a maximum of the $100,000 up to the 2011/12 financial year. While this will suffice as a transitional measure, the NIA is of the view that the Government should introduce a more flexible system post 2011/12. This issue has been caused partly by the Government not engaging in widespread discussion before the proposals were announced, as it is an issue the industry could have been consulted on to come up with a solution. However, given the removal of the RBL's, the NIA acknowledges the Government's need to ensure that superannuation does not become or seen to become a means for the "well off" to avoid tax. Given the choice between the current RBL and the proposed no RBL but contribution limit, the NIA would support the proposals over the current system.

The capping of undeducted contributions effective from the announcement, while understandable may impact upon people not creating a mischief. Given that many people would make their undeducted contributions to their fund at the end of the financial year, we find that the capping on such contributions for the period from the 9th of May to the 30th of June 2006 possibly unfair. While we understand that the Government wish to protect the revenue by not allowing some people to take advantage of the new measures, it should be noted that by denying people access to make any undeducted contribution during the period to 30 June 2006, the Government is unfairly treating taxpayers who are not “cheating the system”.

Contribution Incentives for the Self-Employed

One of the most welcome changes to the contribution rules relates to those affecting the self-employed. For years the self-employed have been treated differently therefore treating their contributions the same is a reform that is well passed due, especially given the number of people who are now self-employed.

The extension of the Government’s co-contributions to the self-employed is also welcome.

Age pension arrangements

The NIA supports the proposed new “asset test taper rate” as providing greater relief to pensioners.

Given the other reform to pensions, the NIA does not oppose the removal of the 50% asset test exemption for complying funds.

Proposed arrangements for ETP’s and other employer payments.

The NIA supports the move to simplify ETP’s by reducing the number of component’s to two, in line with the proposed changes for those accessing superannuation before age 60. The NIA though would suggest that the threshold of $140,000 is insufficient and should therefore be aligned with the income threshold at which the highest marginal rate of income tax begins (being $150,000). The NIA understands the importance of ensuring that ETP’s are not used to hide other forms of payments, however the NIA believes that a higher threshold would reduce complexity by having less thresholds to be knowledgeable of.

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