SUPERANNUATION: ASSESSING COMPETITIVENESS AND EFFICIENCY

by RICHARD HACKETT-JONES – 1 September 2017

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My reform advocacy since 1996 has been based upon the premise that variable personal taxation rates not only cause numerous inefficiencies, but upon objective analysis fail to achieve optimum results both for the government and the individual taxpayer alike.

History shows us that when certain categories of investment are given concessional treatment, intrinsic merit is overtaken by exaggerated expectations, very often doing more harm than good to both the Commonwealth and the individual investor / taxpayer.

Such is the case in regards to the current superannuation (guarantee?) system. Obviously tax differentials are at the core of much of the dysfunction within the system.

I was employed as a Life Assurance agent between 1970 and 1978. At that time there were around 40 Life Assurance companies active in Australia, of which the top 3 or 4 wrote around 80% of the total business. The companies were mandated to invest 30% in Commonwealth Government securities and a further 20% in State Government guaranteed securities such as gas and electricity utilities. Typically a further 20% was invested in finance company debentures such as the Australian Guarantee Corporation or the Custom Credit Corporation (Westpac and NAB subsidiaries).The remaining 30% was invested in property and shares. The objective was capital stability. Commissions were generous and accordingly competition was fierce. Of course the outcome for the policy holder was reduced by the high marketing costs. Ordinary life assurance premiums were tax deductible, however the companies were subject to tax on fund earnings which had the long term effect of reducing the maturity value by nearly 30% in comparison to a similar plan held under a superannuation trust deed. Superannuation earnings were taxed at 5%. No tax was applied to contributions.

At this stage the following points need to be taken into account:

1. Superannuation was not compulsory; had it been so the the commission structure would have been less. Obviously a commissioned agent touting for business has a better chance of closing a deal if the prospective customer is mandated by legislation to engage in the process.

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2. The process of superannuating the workforce was under way well before the introduction of the superannuation guarantee. Of course the Military, the Commonwealth and State Public Services, Local Governing Authorities, Public Utilities, and pre-privatised entities such as Telecom (Telstra) and others made provision for their retiring workforces. Workers engaged in industries such as Banking, Insurance, Trustee, Pastoral, etc. were well catered for as tax deductibility for such schemes was introduced in 1915. Workers engaged in other industries, where the ordinary lower ranks were not provided for, it was common for the middle rank and executive employees to be superannuated.

3. Had the superannuation guarantee not been introduced, the retirement savings industry would still have thrived. Member's entitlements would have inevitably been under more scrutiny and management from the employers and their boards of directors. No reasonable board would have allowed such costly administration and management fees to prevail.

My website deals in much detail with what I refer to as "Retrograde Taxation". I use this term to describe taxes that not only cost the taxpayer and investor good money, but simultaneously reduce government revenue. Please refer to my response to "Better Tax / Re:Think" which Treasurer Hockey commissioned in early 2015. The submission process was stalled as the Treasury asked respondents to comment in more detail upon superannuation. I would be pleased if the commission would take some time and effort to comprehend the section headed "July 24 Postscript", Appendixes B & C, and the two responses to Treasury re Superannuation reform (2016) at the end of the document. However the entire document is provided as an attachment.

Please note my passing comments on death and disability insurance:

> "Death and disability insurance to a value that replaces Centre Link's obligation is important. However work needs to be done by both the government and the insurance industry to create a product, that in the event of a claim, takes first call over other forms of protection such as worker's compensation, vehicular third party, boating, sport and aviation. The consequently lower premiums would provide less drag on capital accumulation. Additionally this initiative would also further the prospects of the NDIS being sustainable in the long run."

The vital objective in so far as future revenue is concerned, is for the system to provide the maximum possible return at retirement for the low to median workforce in order that the cost to Government of providing the aged pension is reduced as much as possible.

The lower paid 50% of the workforce generate only around 25% of total earnings and therefore their share of the pool will never much exceed 25%. By shifting the tax burden away from all accounts up to the level where the safety net neutrality is reached, and thereafter taxing fund earnings at 30% would over time benefit all income sectors, as well as increasing total revenue. No contributions tax whatsoever should be applied. There is a lot to be said for not killing the goose that lays the golden egg. Lower fees and charges should be applied to

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accounts up to this point. Ideally fees and charges should be arranged so that final outcomes are not affected by more than 10%. Thereafter fees and charges should be allowed to reflect traditional standards common to the institutional investments sector.

Cash withdrawals that lower the account balance to the point of future social security dependency should not be entertained. The Winnebago can wait! Salary sacrifice, should be supported and encouraged only to the extent that, by actuarial projection, safety net neutrality is reached, and not beyond.

The Howard / Costello Lump Sum ‘initiatives’ of 2006 have ended up as an arbitrage mechanism. There was no liberalism present in allowing preferential tax treatment for people with a spare million dollars, in the name of superannuation. This million dollars far exceeded the aged pension thresholds both in terms of asset value and income potential. The one million very often became two in the case of couples. Nor was there any social engineering or socialism present. Even compassionate conservatism was absent. Perhaps there was some non-compassionate conservatism coupled with agrarian socialism in evidence! It is simply untrue to say to the taxpayer / investor with a spare $1.6m that he or she deserves no consideration from the taxation system as in the vast majority of cases somebody has worked very hard or been very smart to be in that position. However no properly designed system should encourage arbitrage, because every act of arbitrage costs everybody else money. The real consideration that is warranted is the abolition of the two highest personal income tax rates. This will benefit all expenditure and investment decision that such a person makes, reducing the perceived need to engage in loop-holes.

The sise and scale of the superannuation system alone is sufficient reason for a uniform taxation system. At between 0% and 50% we have five rates of tax. Comparative yield rates vary in each bracket. It is the lowest paid who receive the lowest comparative yield, yet they are the people who need it most. In fact, they are the people for whom the system was designed for in the first instance. The Commonwealth itself was meant to be a major beneficiary through slashing aged pension liability. The current state of play does only half the job, if that.

The initial costs associated with reform are no excuse for delay, as a reformed system will pay dividends for ever. In this current revenue negative setting, funding reform may have to come from outside the square. Try the Futures Fund; they have the capacity and collateral to bridge short term shortfalls.

Yours Faithfully,
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