COMMONWEALTH OF AUSTRALIA

Official Committee Hansard

HOUSE OF REPRESENTATIVES

STANDING COMMITTEE ON ECONOMICS, FINANCE AND PUBLIC ADMINISTRATION

Reference: Improving the superannuation savings of people under 40

FRIDAY, 10 FEBRUARY 2006

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HOUSE OF REPRESENTATIVES

STANDING COMMITTEE ON ECONOMICS, FINANCE AND PUBLIC ADMINISTRATION

Friday, 10 February 2006

Members: Mr Baird *(Chair)*, Dr Emerson *(Deputy Chair)*, Mr Ciobo, Mr Fitzgibbon, Ms Grierson, Mr McArthur, Mr Robb, Mr Somlyay, Mr Tanner and Mr Turnbull

Members in attendance: Mr Baird, Mr Ciobo, Dr Emerson, Ms Grierson, Mr McArthur and Mr Tanner

Terms of reference for the inquiry:

To inquire into and report on:

Improving the superannuation savings of people under 40 with particular reference to:

- Barriers and/or disincentives to contribute to superannuation
- Current incentives in place to encourage voluntary superannuation contributions
- Improving their awareness of the importance of saving early for their retirement

WITNESSES

Committee met at 9.10 am

CHAIR (Mr Baird)—I declare open this public hearing of the House of Representatives Standing Committee on Economics, Finance and Public Administration of the inquiry into the superannuation savings of people under the age of 40. The inquiry was referred by the Minister for Revenue and Assistant Treasurer, the Hon. Mal Brough, on 12 May 2005. To date, the inquiry has received 64 submissions from various parts of Australia. Submissions have been received from individuals, interest groups, governments, policy developers, industry and unions. Copies of these submissions are available on the committee's website. The committee's inquiry focuses on the early years of saving for retirement incomes, incentives in place to save, the disincentives or barriers to saving, and the need to increase the awareness of the importance to save for retirement. Given recent studies into the impacts of an ageing population in Australia, it is timely to consider the financial wellbeing of the under-40 age group when they reach retirement age. Today, we will be hearing from representatives of the Australian Treasury, the Department of Families, Community Services and Indigenous Affairs, the Department of Industry, Tourism and Resources, Certified Practising Accountants Australia, the Australian Industry Group, Mr Noel Whittaker of Whittaker Macnaught and an individual, Mr Anthony Zeitoun.

[9.12 a.m.]

BARSON, Mr Roger, Acting Group Manager, Social Policy, Department of Families, Community Services and Indigenous Affairs

EMERSON, Ms Lee, Branch Manager, Office for Women, Department of Families, Community Services and Indigenous Affairs

FLANAGAN, Ms Kerry, Group Manager, Women and Youth, Department of Families, Community Services and Indigenous Affairs

HARTLAND, Dr Nick, Branch Manager, Seniors and Means Test, Department of Families, Community Services and Indigenous Affairs

WARBURTON, Mr Mark, Branch Manager, Financial Well-Being Taskforce, Department of Families, Community Services and Indigenous Affairs

CHAIR—Welcome. I remind witnesses that, although the committee does not require you to give evidence under oath, this hearing is a legal proceeding of parliament and warrants the same respect as proceedings of the House itself. The giving of false or misleading evidence is a serious matter and may be regarded as a contempt of parliament. The evidence given today will be recorded by Hansard and will attract parliamentary privilege. I refer members of the media who may be present at this hearing of the need to fairly and accurately report the proceedings of the committee. We have a written submission to this inquiry from the Department of Families, Community Services and Indigenous Affairs. Do you wish to make any further comments or would you like to make some opening statements to it?

Mr Barson—Thank you for inviting us. We were the Department of Family and Community Services at the time we made our submission, but now we are the Department of Families, Community Services and Indigenous Affairs. Thank you for inviting us to appear. We have provided a submission to the inquiry which seeks to address the three terms of reference. For your information, our broad interests in this inquiry come from our roles in administering the age pension element of the retirement income system, given that any initiatives that improve superannuation savings will result in less reliance on the age pension in the future and will enhance the sustainability of the retirement income system in this country.

We advise the government on Aboriginal and Torres Strait Islander Affairs. Superannuation has not been an important policy priority for this group, given the other enormous disadvantages that many face. However, it is true that providing advice and information to young Indigenous people as they enter the workforce or even during their training for the workforce may be beneficial and will become increasingly important for this group. We have a role in improving the financial well-being and future security of many different groups such as young families, people who are carers, people with disabilities, Indigenous Australians and women. We have a broader role in supporting the government’s workforce participation agenda.

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The government has given significant priority in recent years to reforms to improve workforce participation, particularly amongst groups with low labour force attachment. The welfare to work package in the 2005-06 budget builds on reforms to provide a balance of incentives, services and obligations to support people to move from welfare to work, which is a great interest of our department. Any initiatives that are designed to improve the workforce participation rates of any vulnerable groups will contribute to improved superannuation balances. We are particularly interested there in sole parents, people with disabilities, and mature workers.

Beside our broad pension responsibilities we have other programs that assist people to improve their superannuation savings, including, as I said, programs that support workforce participation, such as child-care, employment support for people who are carers and people who have disabilities, initiatives designed to encourage people to plan early for their retirement, such as the financial literacy programs that we run, and initiatives that provide an incentive to save for retirement, such as the concessional treatment of income streams in the means test for the age pension. As part of our approach to these things, we work collaboratively with a range of other government and non-government stakeholders. For example, we obviously work closely with the Department of Employment and Workplace Relations on those workforce participation issues and with the Treasury on retirement income and financial literacy issues. So we have that broad range of interests.

We would be happy to respond to any of the committee's concerns or questions on our submission, but before we do so, I would like to hand over to Ms Flanagan from the Office for Women, which plays a very important role in this area.

CHAIR—Is that the Office for the Status of Women, which now reports to the minister for education, or is that within—

Ms Flanagan—Just to make things even more complicated, we are still located in the Department of FaCSIA, but we report to Minister Bishop. We are now just called the Office for Women. We are FaCSIA—we think it rolls off the tongue much better than FaCS. I would also like to thank the committee for inviting the Office for Women here today to represent the specific issues women face in accumulating superannuation savings. The Office for Women included comments that related specifically to women saving for retirement in the Family and Community Services submission that you have before you. Women's experiences of saving for retirement and accumulation superannuation are impacted on by life events that are different from those experienced by men. We can expect to see an increase in the average size of women's superannuation savings as more participate for longer periods in the workforce. But while women, in particular, continue to combine work with family and other caring responsibilities, they will enter retirement with fewer savings on average than men. The government has introduced a range of measures to assist women to have higher superannuation balances, such as the superannuation co-contribution scheme and the spouse contribution tax offset.

We also have evidence that women may make choices to combine work and family pressures that impact on their savings on retirement, such as taking casual jobs, and being more likely to channel any excess funds they may have into mortgages or child rearing costs. Sole parents, the majority of them women, face particular challenges in saving for retirement. While the government has put in place measures to assist division of superannuation on marital breakdown, evidence suggests that this group may be particularly vulnerable as they enter retirement.

For these reasons the Office for Women thinks it is important to recognise that approaches to increasing the superannuation savings of women in Australia will need to be specially tailored for and properly targeted at women in order to offer the sort of advice and information they require to encourage them to prioritise superannuation savings. Research has shown that women experience lower levels of financial literacy than men. Women of all ages, and especially women under 40, need to be able to access relevant advice about the importance of retirement savings generally. Limited knowledge about superannuation terms and concepts, including basic compulsory superannuation entitlements, and a lack of available information sources targeted towards women's circumstances make it difficult for women to understand how they can increase their superannuation savings.

The women's ministers around Australia are working to champion women's understanding of superannuation and the importance of saving for retirement. The work will go towards addressing women's overall financial literacy and their understanding and appreciation of the importance of superannuation savings. I would like to thank the committee members. We wish you well with your deliberations on this important matter.

CHAIR—I commend you for your paper, which is very well written and very informative. You have provided us with information that we have not had before. I was interested in table 1—the estimated average wealth by asset type and age, 2000—which you presented and which we have not seen before and which shows that this age cohort, particularly in their thirties, are not as badly off as I had assumed in terms of superannuation coverage and preparedness. It would seem that the age cohort that we should be particularly concerned about is the under-30s. Could you take us through that chart and perhaps elaborate on the key issues?

Dr Hartland—There are two things I would say about table 1. The first is if you look at the distribution of assets that people have you can see the value that is placed by the Australian community on owning your own home. The family home receives generous treatment under the means test—and quite properly. We believe there very good reasons for people to have their own home. It contributes to security. We know from other research around financial stress that people who do not own their own home face greater levels of financial difficulty. So that is one of the things that stands out for me. I guess the other thing is the superannuation balances on the face of it look low. We do not think that is the full picture. If you look at figure 1 you can see that projections are that, as the cohort of people who have access to the super guarantee—and who have lived more of their lives when there has been an emphasis on saving for retirement—ages, their superannuation balances will increase markedly, so that when they hit retirement they will have larger superannuation balances. That cohort effect is reflected in the projections in the *Intergenerational report* about what contributes to the age pension outlays remaining under control.

CHAIR—To what extent are the under-40s age group constrained in contributing more to superannuation?

Dr Hartland—Labour force participation is probably the most important contributor to being able to accumulate a superannuation balance over life, as I am sure our colleagues in Treasury have emphasised and as Ms Flanagan's contribution also illustrates. So for the under-40s it is to the extent that they can remain in the labour force, remain in a job. In some ways we would expect better outcomes for them as they move through their age group. But the crucial thing is keeping them in the labour force and keeping them in employment, so they can contribute.

CHAIR—That is a given, I would imagine. One of the recommendations we had was for people under 35 to be able take out part of their superannuation—up to 50 per cent—for any purpose. Others have recommended that they should be able to access part of it to assist them to pay the mortgage on their own home. I do not know what your views are on that.

Dr Hartland—To some degree this is mainly a Treasury matter. In considering it, you would need to balance the benefits of owning your own home, which we believe are there, and the benefits of having money in a bank account earning compound interest. Managing that balance would be mainly something for our colleagues in Treasury. I think the comment that FaCSIA would make is that it would be a balance. The committee is considering this because of the benefits around home ownership and how you would find a balance between those sorts of competing aims. That is what we would draw your attention to. I know that sounds like we are ducking the question—

CHAIR—You are.

Dr Hartland—The reason for that is we are.

CHAIR—Ms Flanagan, you have described the issues of women coming and in and out of the workforce. How do you see that we address those issues in terms of super? You have described the problem without coming up with a solution to it. In terms of this particular inquiry not bringing out knock-out types of recommendations so far we see the problems. We hear—as the expression is—politics, but how do we balance it out when women by nature of events in their lives are going to be taking time out for various things? They are going to be in part-time employment and taking maternity leave—sometimes extended maternity leave. This reduces the incentive to save. There is the pressure on single mums, and we continue to marginalise them on an ongoing basis. That is a real concern. Your charts show that because of the co-contribution we are making some inroads there, which is encouraging, but how do we address the circumstances of the group of women you are describing? There are no easy answers, so I am not suggesting that you are going to come out with some silver bullets for us.

Ms Flanagan—There are a range of issues. At the moment we do have a superannuation scheme that is mainly geared to in effect the amount of work that you do. The government has moved, though, to try to recognise when to provide other incentives through the superannuation co-contribution, which does have a direct impact on women who are hopefully in stable relationships where their partners have the capacity to make those sorts of contributions. The thing that I suppose we need to consider is the impact over a lifetime. I have heard suggestions many times before about people being able to access their superannuation in those early stages, but inevitably if you are not able to recontribute to it, as you go through life, you end up poorer in retirement. So when you think about the life course, it is incredibly difficult to come up with suggestions that have the most benefit, taking into account the life course.

We believe that there are things that can be done around financial literacy, assisting women with financial literacy, that will have the most impact on those that are able to find work. For example, if women move jobs a lot and work in casual employment and part-time work then it is difficult for them, because they have superannuation balances all over the place. So giving them some assistance to understand how they can combine those and reduce and administrative fees and things like that are important elements.

CHAIR—What is the average length of time that women are taking off in terms of maternity periods? Is it one year or five years?

Ms Flanagan—We can get the committee some statistics, but my understanding is that many women who are currently in employment return to employment probably within the first two years of the child being born, but some others then make decisions to stay out until primary school age.

CHAIR—It might be interesting to have an average figure, because if you are looking at an average time of five years out, with several children and so on, it is quite a fair period in which they are not contributing, especially if they end up separated. The husband's super scheme is being fuelled and nothing is happening for the wife. I think it is a challenge for us.

Dr EMERSON—Peter McDonald at the ANU researched it and about three years is the critical point. Most women who are going back, or who are wanting to go back into the workforce, will make that decision within the first three years.

CHAIR—But if they have more than one child, does that mean six years or do you mean three years per child?

Ms Flanagan—It depends how quickly they have them.

Dr EMERSON—That is right. This is absolutely just an assertion now, but it is more likely that in most cases they would have one, go back to work, and then have another one rather than say, 'Right, I will stay out of the workforce while I have all my children.'

CHAIR—That is right, until the youngest one starts school. We do have a bit of a fix on that. Can I ask your office—I might ask the minister informally as well—to look at some real recommendations. We have baby bonuses et cetera. Is it a role of the government during that time to be providing some superannuation support?

Dr EMERSON—The baby bonus could—

CHAIR—It would appeal to my socialist friends.

Dr EMERSON—Social democrats.

CHAIR—I do not know. Perhaps you can throw it around within the Office for Women and guide this normally male dominated committee—except for Ms Grierson.

Ms GRIERSON—Lucky I came, wasn't it?

Dr EMERSON—While we are shooting the breeze here, one possibility might be to identify a part of the baby bonus as a superannuation contribution.

CHAIR—I am sure you have your views, but the key challenging time in terms of money is when children are young and often there is all the pressure of losing part of an income stream as well. It is a real factor for a lot of women. At the end of the day, they end up with very little super. We clearly need to address that. I do not know that we have come to grips with it yet in the inquiry. That is not a reflection on the inquiry; it is just that our witnesses have been male dominated and they are concerned about other factors as well. I would like that addressed.

Ms Flanagan—If they are within intact relationships, they in effect enter retirement with a partner's superannuation available to them as well. I think the real dilemma is where family breakdown occurs before that time. Again, there are arrangements in place to split superannuation at that time. I think it is when you get into double and triple jeopardy. At that time a woman might not be working, she might no longer have access to accumulated superannuation from a partner, and she might then have to try to combine a caring role with taking a casual or a part-time job rather than a full-time job. We also know that women, on average, get paid less than men, so there is a huge range of issues that impact.

CHAIR—Yes, that is true.

Mr Barson—I would just reiterate the point that was made about maternity payments. Maternity payment is a very important contribution by the government toward the costs of having a child and, as you made the point, Mr Chairman, it is geared very much around the costs of early childhood and supporting younger families at that time. Similarly with family tax benefit, a payment that is made to support families, in particular with young children, is very much geared around the needs of that family and those children at that point in time. We would suggest to the committee that that is the prime focus of those payments, and taking anything away from those payments at an early point in time would have disadvantages. But I understand the point that was being made.

CHAIR—We are not trying to say it was wrong or anything; we are just trying to think laterally of how we might address that issue.

Mr McARTHUR—I will raise two issues. First, you talk about home ownership being a very important part of the total assets. Do you have a view on these reverse mortgages that people are using to get a cash flow? Secondly, what is your view on the co-contribution; how much is required to get a pension that supports a person in their retirement?

Dr Hartland—I will start with the reverse mortgages. With our colleagues in Treasury, we have provided the committee with some details on how reverse mortgages are treated under the income and assets test. Have you received that?

CHAIR—Which one?

Dr Hartland—We understood that Treasury took a question on notice around the treatment of reverse mortgages under the income and assets test for age pension, and we understood that that had been provided.

CHAIR—Yes.

Dr Hartland—If it has not been given to the committee members, I can briefly outline—

CHAIR—Question No. 15.

Dr Hartland—Would you like me to explain the treatment?

CHAIR—Yes.

Dr Hartland—The existing treatment reflects, in my estimation, a moderately generous treatment of this form of income, and I will come back to why in a moment. As you may know, when we are assessing age pension, we look to two things: the income the person has and their level of assets. Reverse mortgages have a particular treatment under both of those tests. Under the income test, if you take out an amount of a reverse mortgage, it is not counted as income at the time it is received, and that is standard with any loan. If you take out a $100,000 loan, we do not say, ‘You have just received $100,000 of income.’ What we do say is that if you invest that loan or put it in a bank account, then the amount will be deemed, which is a mechanism we have for assessing the income from financial assets.

To that degree, reverse mortgages get the same treatment as loans. They are not assessed as income at the time they are received, but they are looked at in the income test through this deeming mechanism. Under the assets test, the first $40,000 of an unspent home equity conversion loan is not counted for 90 days. If after 90 days the person who receives it has not spent the loan, then the full amount is included in the person’s assets. That treatment under the assets test is slightly more generous than what would occur with other loans. So if you took out another type of loan the equity that you had received in the loan would be counted under the asset test immediately. That dispensation reflects a policy view that these forms of finance are a potentially important component of overall support for people who might have a lot of assets tied up in their house.

As I said, our tests encourage investment in a house as there are benefits for home ownership, but for people with a lot of money tied up in a house but not many other assets, they might not have the capacity to, say, fix a roof that had gone bung or improve the house, and that there was a need to provide some flexibility around that. The treatment under the assets test gives them some capacity to draw down some capital effectively from the home to improve the home or make a repair that is needed without being penalised under the assets test.

So that broadly is the treatment. It reflects the view that reverse mortgages have a place in the overall system of support as a source of finance to fix loans. In a sense, that is the current policy treatment. We are seeing the industry change. We are aware that there are a lot of claims by industry that reverse mortgages will become a much greater part of finance in the future. We have not seen evidence at this point of that becoming widely used by our customers but, on the other hand, we have not actually searched the database with that in mind to see what we could glean. At this point, we are not seeing through ministerial correspondence and other items like that a great number of customers corresponding with us about this issue. But it is one of the parameters of the tests that we are monitoring, and we are aware that we may be seeing some changes in the industry as we watch. If things did change, then there would be a role for us in briefing the government on whether those parameters remained appropriate. Is that clear?

CHAIR—Well, not terribly. Anyway, we will let that one go through to the keeper, I think.

Dr Hartland—There was a second question from Mr McArthur, which was about the co-contribution—

Mr McARTHUR—What is the figure that your department thinks it should be? I know it is an impossible question. I am reminded of the Singapore example where they went up to a 19 to 21 per cent contribution to make the scheme work. I know that they do have some health benefits out of that. It just strikes me that the nine per cent is never going to being sufficient without a co-contribution. I am just interested in your view.

Dr Hartland—I do not think that we would have a view specifically on the co-contribution, but clearly from the analysis that we have summarised for you in our submission and from what other people have said, nine per cent is not going to meet people’s retirement expectations. So people need to find a way of putting more in; whether that be through a mechanism like the co-contribution or through voluntary salary sacrificing into superannuation. For our part, I guess, we provide incentives. Our payments have a couple of incentives in them for contributing to superannuation and, I suppose, in terms of the overall system, that is where we would point to FaCSIA’s contribution.

Broadly, there are two main areas where our system of payments has incentives. The first is that when you are in the phase of drawing down your superannuation balances through, say, an income stream of a certain nature—broadly, those that do not allow access to the capital for the life of the stream—they are treated very generously under the assets test. There has been a 100 per cent discount under the assets test and more recently that has been amended to 50 per cent. That is a strong incentive for people to make contributions to super throughout their working life and to use income streams to support their retirement. The second main mechanism is where the system as a whole provides an incentive for superannuation contributions by way of the treatment of salary sacrifice which is not counted as income for people below age pension age.

Mr CIOBO—I want to touch on a range of things but, in the interests of punctuality, I will not. On page 10 of your submission you make reference to the general issues with respect to superannuation balances being a function, the final one of which says:

... attitudes towards making voluntary superannuation contributions.

I am interested to know two things with respect to that: first, have we seen a change of attitude, a trend line, demonstrating a change in attitude? Perhaps that is tied to financial literacy, perhaps it is tied to labour force participation. I would be interested in your comments on that. Secondly, given significant amounts of real wages growth in the past 10 years, and coupled with tax cuts and a change of attitude, have we seen more money flowing into superannuation through voluntary contributions, or we are just seeing increased balances as a consequence of higher real wages growth?

Dr Hartland—In terms of attitudes, I think we are seeing a greater awareness among people of the need for higher balances. I think we are seeing people becoming less accepting that the age pension is appropriate for them in their retirement and therefore realising that they will need to save harder throughout their working lives.

Mr CIOBO—When you say ‘I think’, is that based on anything, or is that gut instinct? Has FaCSIA done surveys on this? What is the basis for your thinking on that?

Dr Hartland—I suspect it is based—this is a fairly unstructured kind of view that I am putting to you.

CHAIR—We want to know whether it is research based.

Dr Hartland—No, it is not. We have not done trend research. We have some snapshots of attitudes, and those are showing that people are aware that their retirement expectations are an issue. I would be chancing my arm. If you are asking for research based, no, I do not have something to go underneath that.

CHAIR—I do not know whether you have funding available within the department to do some research amongst the under-40s which might give us some clues. We have seen research in terms of how young people spend their money. The various major insurance groups did this, but it would be good to have some hard data.

Mr CIOBO—I guess what I am trying to ascertain is: do we actually know attitudes are changing, or are we just all assuming attitudes are changing because we are seeing an increase in balances which may very well just be driven by increases in the super contribution levy and so forth?

Ms Flanagan—Lots of wage increases. From the perspective of the Office for Women, first, if you want to see a trend line in voluntary contributions, Treasury would be able to give those to you rather than us. We certainly have done some research on the financial literacy of women, and we know that women’s financial literacy is lower and therefore I would assume—

Mr CIOBO—Lower than men’s, or lower over time?

Ms Flanagan—Lower than men’s, and that they need to receive financial information in different ways. We also know that they are more risk averse in terms of their investment strategies. Knowing all of that, I would also chance my arm and say that I expect that you would find, if we were able to do a disaggregated trend line, that you would find that women possibly are not putting into voluntary contributions and that that might be one of the areas you want to target in any education campaign designed for under-40s. Not only putting in further voluntary contributions for women, but also for women under 40—just in fact in giving the message about the importance of superannuation per se. I know that many big firms do pay superannuation guarantee on casual jobs, but many of them do not, and to explain the impact of that over the life course, for example.

Mr CIOBO—In your submission you say 63 per cent of those that are utilising the super co-contribution are women. Is that a consequence of income, or is that a consequence of recognising the advantages of utilising the co-contribution and therefore it is stronger among women?

Ms Flanagan—I think it is probably spouses contributing on behalf of their wives.

Mr CIOBO—I did not really get an answer about whether or not we are seeing an increase in voluntary contributions through real wages growth and tax cuts. Do you have information on that?

Mr Barson—That is mainly a Treasury thing.

Dr Hartland—I was going to say that we are seeing an increase in the proportion of Australians over the age of 65 who are fully self-funded in retirement already. The *Intergenerational report* includes some long-term projections of the customer cohorts having increased assets who are, therefore, less reliant on the age pension.

Already in the administrative data, of people coming onto the pension as new grants compared to the stock, we are seeing a greater number of people who are asset tested and reduced cohorts fully reliant on the age pension. We are starting to see in the system already some benefits from people having increased superannuation balances. That does not go to your question, I have to say, about whether it is voluntary or compulsory, but we are seeing the system start to move more towards a greater number of people on the assets test because of their high balances.

Mr CIOBO—But that is really a reflection of increased labour force participation by women, isn’t it?

Mr Barson—I think digging into the reasons behind it is something that you might wish to discuss with Treasury.

Dr EMERSON—I have a couple of quick questions which follow on from the chair’s question about what age a baby would be when women typically make a decision about going back to work. That is a fairly hard job in its own right, but just to make it a little harder: if you are able to uncover such information, it would also be useful to know if there are any trends there. We know that the attitudes of women as to the age at which they are having babies are changing quite dramatically now, and we would not want to get into a policy situation where we say, ‘This seems right now,’ and in five years time it is wrong. That is just a suggestion. Was the baby bonus increased recently?

Mr Barson—It goes to $4,000 on 1 July.

Dr EMERSON—Obviously I accept the point that the reason we have a baby bonus, and the reason we have family payments, is that is when costs are higher. It is also self-evident that that is also when superannuation contributions are low. Because we are having an inquiry for people under the age of 40 as to their adequacy, we keep learning or relearning the point that that is the reason there is not a lot of super going in, or perhaps not enough, because other financial needs are pressing. If we are to get into a situation of increasing the size of the baby bonus, why do we not think of allocating at least part of that increase to superannuation? It addresses both issues: adequacy of income while you are having children, and the inadequacy of retirement incomes and that very period being the one where no provision is made for superannuation. That is more by way of an idea than expecting you to respond, because you probably do not have the authority to do so. Similarly, is it not the case that the family tax benefit is linked to male total average weekly earnings, MTAWE, rather than the CPI, or is it just CPI? All pensions are linked to MTAWE—

Dr Hartland—The age pension and disability support pension and other pensions are linked to MTAWE.

Dr EMERSON—I think it might be CPI actually.

Mr Barson—I would not want to be quoted, but I believe it is CPI.

Dr EMERSON—Again it is the same thinking; if policy decisions are being contemplated to increase family tax benefit beyond CPI, there might be some merit in thinking about some part of that being hypothecated to superannuation. Any comments would be welcome, but I understand the constraints under which you are operating.

CHAIR—We are also speaking rhetorically in terms of what we could think about in this inquiry.

Mr Barson—I will comment on the first point that you made, which is certainly the undertaking that we have made to provide whatever information we have on return to work, and point out again that that is complex because it is not a case, as you would understand, of having one child and then returning to work. It is complicated by the fact that most families have more than one child. So, in many cases, we are looking at the period after the birth of the last child when a woman will return to work rather than a period per child. We will pull that out, but we may find that there are several different cohorts in it rather than a single average point which is more meaningful to you. I hear what you say about the family tax benefit and maternity payment. They are, of course, matters of government policy, and that is something the committee may wish to consider.

Ms GRIERSON—I have to put on the record that I disagree with my colleagues on the baby bonus. It is a poor substitute for paid maternity leave for women, which would therefore give them an income stream. It is for the care of a child, and I always thought it should be paid as an income substitute if it is going to be issued that way. Certainly, there should be the ability for women to make lump sum payments into super if they have that resource availability. I do differ quite strongly on the baby bonus.

I would also say that your age dependency ratio projections are startling. When you see them in print, they are always 2½ working people per person over 65 by 2050. You may not be able to help me on this, but if that is a projection, what is the projection in terms of the superannuation accumulation? Is there a comforting parallel growth in people's putting away super for retirement?

Dr Hartland—These projections are mainly sourced from Treasury. They are very important for us too, but if you look at figure 1 on page 6 in our report I think you can take some comfort in that it is showing that, as today's cohorts who are working move through their lives and come to retirement age, they will have much greater superannuation balances. The *Intergenerational report*, which measured the projected expenditure on age pension into the future, found that, while there was an increase in age pension to be expected from the ageing population, the increased asset base that is occurring at the same time of these groups means that that increase is a relatively small amount of GDP. While it is obviously something that the department and government will wish to keep monitoring, it is not something that would cause you concern by itself.

Ms GRIERSON—There seems to be a bit of an offset, doesn't there? It is quite good.

Dr Hartland—Yes.

Mr Barson—Treasury would no doubt be able to dig further into that for you.

Ms GRIERSON—Yes. With that co-contribution, are there ways you think it could be more strategically targeted to balance out women's inconsistent income stream or to particularly reward the younger people or under-40s to actually get into super to make those contributions? Are there ways you would suggest that it could be more strategically targeted to look at those life impacts and saving impacts, I suppose?

Ms Flanagan—I suppose this goes back to the point that we continue to make, that we know that women's financial literacy is not perhaps as good as it could be. If you wanted to target some messages like that, specifically to women, that would be a suggestion we would support. We think that that would be a good idea.

CHAIR—Thanks very much. We appreciate your attendance today.

[10.05am]

DAVISON, Mr Michael John, Superannuation Policy Adviser, Certified Practising Accountants Australia

KELLEHER, Ms Noelle, Member, Financial Advisory Services Centre of Excellence, Certified Practising Accountants Australia

CHAIR—First, our apologies that we are running a bit late for a variety of reasons. I now welcome representatives of Certified Practising Accountants Australia to today’s hearing. Although the committee does not require you to give evidence on oath, I should advise you that these hearings have the same legal standing as proceedings before the parliament. We have received a written submission from you today. We would invite you to make an opening statement and then we will proceed to questions.

Mr Davison—First we would like to thank the committee for the opportunity to appear here this morning. As you say, you have our submission in front of you. I do not intend to rehash the whole submission. Instead, I will briefly highlight a couple of points and then answer any questions the committee may have. Having followed proceedings in this inquiry over the last few months, one of the common themes that has emerged to me is that many younger Australians are often not in a position to contribute extra to their super above the minimum compulsory level due to the many conflicting demands on their income, such as housing, family, education expenses, et cetera. We share this view, but unfortunately we do not believe there is an easy answer.

CHAIR—It is true, I agree with you.

Mr Davison—However, we do believe that there is action we can take now to maximise the superannuation savings that people do have, as well as providing incentives to encourage those who can make additional contributions to do so. The most immediate and effective way to maximise super savings would be to abolish the contributions tax.

CHAIR—What a surprise that you have come up with that! What organisation was it you are representing?

Mr Davison—As a result of this tax, the effective level of the compulsory SG contribution going to superannuation accounts is not nine per cent but only 7.65 per cent. Our research, which is conducted by the National Centre for Social and Economic Modelling out at the University of Canberra, found that, for many Australians, this level of contribution is not enough for them to maintain a reasonable standard of living in retirement. Our research also found that removing this tax has a rough equivalent effect of raising the compulsory contribution to 12 per cent.

CHAIR—Do you have any evidence to show that young people are then more likely to respond to your incentive?

Mr Davison—I do not see that in itself as an incentive. It is more maximising what we already have going in. For many people—

CHAIR—That is obviously an expensive option that would be available in terms of recommendations. To abolish it, I think our colleagues said, would cost $3.3 billion.

Mr Davison—It is about $3 billion, yes.

CHAIR—But you do not have any evidence to back up that we are likely to see more contribution from the age cohort in which we are interested?

Mr Davison—No.

Ms Kelleher—One of the important things is to look at how to set up whatever changes so it works. In the past we have been looking for people to respond and actually opt into systems. Maybe one of the reverse psychologies is that you make it voluntary, but it is people actually opting out. So, yes, it might be something that is considered expensive, but if it can be set up so that you actually have to opt out. You have it working the way you want it to work to start off with and, instead of its being people's inertia to put more money in, it might be their inertia to take more money out, or not to put it in. Use a model that will actually work in our favour as opposed to against us. I think that is one of the things that needs to be on the table in terms of looking at the options.

Mr Davison—Talking about incentives to make voluntary contributions and just to touch on a question that was raised with the last witnesses, there have been a lot of new incentives over the last few years which should help to encourage people to contribute to super, such as the co-contribution, the removal of the surcharge last year et cetera. APRA has quarterly statistics on the super industry and those statistics show that voluntary contributions have been falling quite steadily since the late nineties, probably 1998 and 1999, for two reasons: one is probably that it was also on the tail end of the closure of many defined benefit schemes. In the past there were some quite generous defined benefit schemes with a commitment on the part of the employee to make compulsory contributions to the scheme to push up their benefit. With the demise of those schemes and moving to an accumulation type fund, that compulsion for additional contributions has largely gone. Plus, we saw the surcharge come in in 1996, which we also felt was a big disincentive. It is probably too early to see whether current new initiatives will change that. Certainly, statistics over the last few years suggest that the voluntary contributions have dropped considerably whilst compulsory contributions have increased, primarily because the rate of compulsion has increased over the years to nine per cent.

CHAIR—Two years ago?

Mr Davison—Only two years ago, three years ago that we hit that nine per cent rate. Having talked about incentives, there are still two barriers to making additional contributions to people who are in a position to do so. First, the current age based contribution limits often prevent individuals, especially those under 35 and the self-employed, from making larger contributions to their super when they were most able. As an example, a young professional in their twenties who may have few financial commitments is in a much better position to make additional contributions than an equivalent in their late thirties who may have a mortgage and a young family to support, yet they are prevented from making those additional contributions because of the relatively low limits.

Secondly, not just the self-employed but also those who are unemployed—for example, parents who are staying home to look after their kids—do not receive the same level of encouragement to make additional contributions as do the employed. First, they are not entitled to the full tax deduction for their contributions over $5,000. We have seen that this effectively discourages these people from making contributions above the $5,000. Also, they are ineligible for the co-contribution which provides a much greater benefit for low income earning employed than does the deduction that the low income non-employed person would receive. As you discussed with the previous witnesses, the co-contribution is very much limited to the employed, and if you are talking about how to improve super savings for women, people at home, students et cetera, the fact that they are ineligible for the co-contribution is a bit of a shame. It would certainly be a good step in the right direction to help improve their savings.

Finally, I have a question for the committee, and it is one that I am surprised has not really been touched on yet. We are talking about improving super savings, but we have not actually talked about to what level we are trying to save. There is obviously a recognition that the level is low, but where should we be going, how much should people be saving? If we are talking about increasing savings, we really need to be talking about to what level, and as such we strongly advocate the introduction of a retirement savings target. As I said, I have only touched on those points.

Ms GRIERSON—We have had recommendations that there be some projections on people’s superannuation in annual reports, so that they get some idea of healthy targets.

CHAIR—It is likely to be one of our recommendations, that people have regular projections of where they are likely to be, what their income will be in retirement at their current savings level of contributions to super. I do not know whether it was yours, but one recommendation was that young people consider that $50,000, I think, was the amount that they wanted to have in retirement; another survey said $39,000. You take it across the board how much you think you will need in retirement.

Ms Kelleher—The issue that people have, particularly when they are younger or even all the way through, until they are staring retirement in the face, is that nobody really has an appreciation of what they need to have saved to be able to get the income they want. I suppose it would be nice to say, ‘Yes, people, go and get your projections on a regular basis,’ but the reality is that if you make it too hard, and there is not a rule of thumb that they can use to estimate what they are aiming for or whatever, they will just ignore it, particularly when they are younger, because it is too hard. Once you add work, family and travel commitments and all the things that get in the way of ordinary day life, things that are not of immediate focus just get put on the backburner. Any target or whatever needs to be something that you can relatively easily understand; it is a bit of a guide and you do not need to go off to a financial planner and spend two, three or five grand to get just a simple answer as to what you are looking for. It is really only when people are actually looking at retirement that they say, ‘I need this amount of income.’ Most people would say, when they get to retirement, that they do not want a cut in their lifestyle. The reality is that they need exactly what they are earning all the way through their life by the time they get there.

CHAIR—What are you saying? If the projections are set out as their likely earnings, it also should provide a breakdown of what the average cost of retirement would be.

Mr Davison—That is part of the problem, I think; projections are all well and good and it shows you what your super will give you when you retire, but there is no indication of what you actually need, and I think there is a big gap. Work has been done. The Senate inquiry into adequacy arrived at a number around 65 per cent of pre-retirement income, yet that number has never been rigorously tested. It just seems to have been accepted. The Association of Superannuation Funds of Australia has done some very good work and come up with a figure of about $43,000 or $46,000 as a couple to maintain a comfortable lifestyle in retirement. That figure is not necessarily achievable for someone who is earning in the $20,000 range or even $100,000, so there is still quite a gap there.

Mr CIOBO—Income goes up when you retire; is that right?

Ms Kelleher—Hopefully!

Mr Davison—Yes, so there is still quite a gap for people to actually know what they should be saving. Some of the anecdotal evidence we have had from our members is that people see the compulsory SG level set at nine per cent and assume that that must be enough, because that is the amount the government has set for them—especially young people. They are not necessarily thinking about retirement savings with all the other distractions that they have, so they are not really listening or taking notice of anything more than that nine per cent.

Dr EMERSON—That is exactly the dilemma. The financial pressure is the greatest at exactly the same time as the need for superannuation contributions for your retirement is greatest, or the benefit from it is greatest, because you get the benefit of accumulation. Everyone in this room understands that problem; it is just finding a solution to it. I do not think the solution can ever be just heavily grounded in better education or exhortations or whatever, because people say, ‘Yes, I understand that, but I am really flat out just trying to make ends meet here,’ and so on. I was interested in the concept of opting out, and using the inertia, particularly of young people who do not get around to filling out pieces of paper and are not bothered with all the complexity of these things. Could you elaborate on a scheme that might involve extra superannuation which is voluntary in nature, effected through an opt-out provision—that is, your decision not to participate is made by sending off a form saying, ‘I am opting out of this scheme’?

Ms Kelleher—I suppose, as a starting point, what you do not have you do not miss. If it is set up as an opt-out system when you first start work, you effectively would have a percentage of your salary being salary sacrificed into superannuation. The opt-out bit could be done easily in terms of giving your employer the form to say, ‘Do not put money into super for me, only have the compulsory super’. It is generally accepted that, with savings plans, if you have a percentage of your salary going away each month, when you get pay increases your savings go up at the same time. There is no reason why it could not be set up so that super at least picks up some of that, so you would then have the money going in. In theory, individuals could opt out at any time. There is no reason why it would need to be an annual opt-out. It could fit in nicely with salary packaging arrangements and salary review arrangements that employers have in place at the moment. From the employer’s perspective, in theory, it would be no different from what they are doing at the moment where they are saying to employees, ‘Would you like to put more into super?' So it actually becomes, 'Would you like to either not put as much in, or would you like to put in more on top of what is part of that opt-out arrangement?'

Dr EMERSON—Is it not slightly tax preferred— that is, if it is beneath the limit beyond which employers cannot claim a tax deduction? Is that right?

Ms Kelleher—Yes. There are maximum deductible limits that employers have to look at with SG and salary sacrifice at the moment. One of the issues with those is that they actually do not reflect real life anymore. I do not think the age based deduction limits actually work; they contribute to this issue as to whether people under 40 are putting enough money into super. Someone under 35 really only has the $13,000 that they can claim. The chances are that in their twenties, they probably do have some capacity to put in extra money but could be finding that that low ceiling is what is stopping them if they wanted to put money into super. You would have to consider how to make an opt-out situation equitable across the board.

There is no reason why you could not have a flat maximum deductible limit for everybody, regardless of age. If you were looking at the issues of how to do catch-up arrangements for people going in and out of employment, you could consider having a total lifetime maximum deductible limit that I think the tax office would be able to manage, although they will freak out when they read this comment. They have information that they could use, given the co-contribution information that is going into them at the moment in terms of employer contributions et cetera. So there would be a system that could be worked out on that front. You would have to modify that end as well.

In terms of whether super is really concessionally taxed, over the years as tax cuts have come through from the individual's perspective and with the corporate tax rate et cetera, it is only marginally advantageous to put money into superannuation these days, because not only do you have the 15 per cent tax on the way in, but also you have the tax on the way out, and when a lot of people look at whether or not it is advantageous, they forget to look at the end benefit tax.

Dr EMERSON—What is the tax on the way out if you are within reasonable benefit limits?

Ms Kelleher—It depends on how you take it out. If you take it out as a lump sum, you have the first step tax-free of the 126; if the balance is within your RBLs, you are looking at 16½ on that, with Medicare. If you are taking it as a pension, you have no tax-free step per se. If it is within your RBLs, you will be paying tax at your marginal rate, less a 15 per cent rebate. I suppose you have 15 per cent on the earnings while it is in the fund. When you do the figures, unless your money is in there for a long, long time, it can be marginal as to whether you are better off putting money into super. I suppose the issue for people who are in their twenties looking at putting money into super is that it is marginally tax efficient, depending on where they are sitting on the scales, but then it is locked in until they get to 60.

Mr McARTHUR—Some commentators would say that there are a lot of tax benefits in super. That is a pretty strong statement that it is marginal.

Ms Kelleher—It is a strong statement, but I would say, based on people with whom I have spoken, the constant feedback I get is, 'Why would I put money into super?'

Mr McARTHUR—Is that factually true?

Ms Kelleher—Is it factually true?

Dr EMERSON—I can help out there. The tax expenditure statement shows that half of the cost of all tax expenditures is superannuation; it is many tens of billions. So there has to be a concessionary element in superannuation, otherwise it would not account for all of half of the value of 270 tax expenditures; there has to be.

Ms Kelleher—Yes, but the thing is, there is not enough in there for people to say, ‘That is my preferred savings vehicle.’ What we are trying to say is, for retirement purposes or for savings purposes, ‘We want super to be the preferred vehicle, because it is in there, it is for their retirement.’ Looking at some of the submissions, comments about reverse mortgages or being able to take out money to buy the home et cetera, super can be seen as being the cash cow because it is where people have a substantial portion of whatever savings they have. We also have to be really careful that we are not robbing Peter to pay Paul. What if people cannot save for a housing deposit. To some extent, should they really be using their super to pay for that housing deposit that they cannot save for anyway? I get really concerned when I hear the advertising on the radio about, ‘Come to us for a mortgage; we’ll lend you 100 per cent of your housing costs.’ It is like, ‘Hang on a minute; if I can’t save the deposit, will I really be able to pay off the mortgage anyway?’

The research that CPA have done et cetera shows that younger generations have a culture of debt. They come out of university with a debt already. They are encouraged to use their credit cards. ‘I want it now; I will put it on the card.’ It is not, ‘I will save for it.’ We are looking at people who have that concept of debt and it is okay to have debt, and it is probably okay to have a substantial amount of debt. However, we are trying to say to them, ‘Here is something that has some tax concessions in it that you cannot touch for 40 years; put your money into it.’ The equation just does not work in terms of getting over the perceptions that they have. Even in terms of the current structure, there are many perceptions: to start off with, the nine per cent super contribution must be enough because it is a government figure. There is the perception of the maximum deductible contribution figures: ‘If I put in something, it must be enough,’ not even on a regular basis. You have the perception with the reasonable benefit limits: ‘Because they are reasonable, that must be all I need to have.’ Then you have the added perception of ‘excess benefits are bad’. Once you start compounding all of those sorts of things, it does not paint a really good picture in terms of someone wanting to look at super as being money that they will save for retirement.

Dr EMERSON—I guess we understand that, but if you got rid of reasonable benefit limits, if you got rid of all taxes on the way out, then people would say, ‘You beauty, I am 50, I will now have enough to just run my house and draw $20,000 or $30,000 a year and put the rest into super, and when I hit retirement age, preservation age, I will then take it all as a lump sum, pay off the house and everything else, and then go on the age pension.’

Ms Kelleher—I do not think anyone who will have been here thinks that there should be no tax on super. That is certainly not the impression that we want to leave with. The system has to be set up to work, to make sure that people have adequate retirement incomes. Adequacy should not take into account the age pension, because that really is meant to be a safety net. Yes, there are a lot of people who do need it, but it should not be there so please say, 'Well, we always have that safety net.' So that comes into the adequacy equation.

No-one is saying, 'Don't tax super and don't put restrictions in terms of not being able to take all your benefits as a lump sum.' If it were structured the right way you might get to the situation where people say, 'Yes, I am happy to take a pension,' and not want any lump sum. It is all about setting it up to work as opposed to setting it up to fail. It is a challenge that everybody has: the government, the industry and individuals in terms of taking responsibility for their own destination.

CHAIR—Part of the problem in terms of taxation is that it is a skewed continuum. The people we are most trying to get in are the ones for whom 15 per cent tax is the least attractive, as opposed to the other end in terms of the age factor, for whom it is an incentive. If you did a profile of those under 30, there are only a relatively small number who are earning above that 30 per cent tax rate.

Ms Kelleher—From the tax contributions tax cut side of things, one option might be to cut the contributions tax on SG contributions; that might be a way of directing the tax savings towards the compulsory bit. Then you can set up something as an opt-out—

Dr EMERSON—Ultimately people are going to do it anyway and they will not change their behaviour in response to it.

Mr Davison—It is unfair that we have a compulsory system, you do not have a choice and then you are being taxed on it.

Dr EMERSON—I understand that. If you are trying to change people's behaviour and you take a tax off an action that is compulsory, they will still do it.

Mr Davison—A lot of people who have SG contributions made to super for them may not be in a position to make voluntary contributions because of those other demands on their income, but maximising the SG contribution that goes in by, for example, removing contributions tax, makes a big difference. It is the equivalent of an extra three per cent contribution.

Ms GRIERSON—If the contributions tax were to be reduced, what about targeting people who are young, on low incomes, who are part-time or some other ways to try to benefit people who are struggling to make superannuation contributions?

Mr Davison—One of the things we are trying to get away from is the complexity of the super system, it is a nightmare.

Ms GRIERSON—That would make it very complex.

Mr Davison—The evidence we have seen from our members and from surveys is that the complexity turns people off, there is a quite a big disconnect with people and their superannuation.

Ms GRIERSON—But incentives are always incentives.

Ms Kelleher—You can look at incentives like that but my concern would be who is going to be administering it? If we are putting it into the super funds to administer, how old is everybody and what is pink, purple, blue, whatever. Any incentive that the individual might get in terms of some added tax cuts in the super is probably going to be eaten away by the administration costs associated with administering the system to actually get there.

Ms GRIERSON—The other thing you have raised is contribution splitting, and you suggested that rather than allowing contribution splitting throughout the super, it would be far easier to do it at the end point when people are taking their super out.

Mr Davison—One of our longstanding concerns with contribution splitting—we support the concept very strongly, but younger couples are not necessarily going to know what their super savings are in 30 or 35 years time, yet each year they have an opportunity to split their contributions with the aim to have two RBLs and two tax free thresholds. But, they do not necessarily know if they are going to need two RBLs. There is the also expense of advice to do the split, the need to run two super accounts maybe unnecessarily, plus the administrative burden that goes with that. They may actually get to retirement and realise it was all a waste of time and expense. If the end benefit were able to be split, the family unit would know its retirement needs at that point and whether they need to access two RBLs. They may be in a situation where they actually want to take pensions, so the tax free threshold lump sum amount would be irrelevant and they do not need to do it. It would be a lot easier.

The government has long said the three reasons for doing this has been the RBLs, the tax-free threshold and the third reason has been allowing non-working spouses to have control over their superannuation. As a family unit, decisions about family finances tend to be made together so whether the super is in one account or two is probably irrelevant. In the unfortunate situation where they split at some stage, there is provision now to split superannuation on divorce so that is pretty well covered. We believe the benefits of splitting outweigh the benefits of the system we have now.

Ms GRIERSON—You talk about retirement incomes and the tax incentives that super offer but a lot of people choose the tax incentives of negative gearing to acquire some potential income, retirement savings. Is there any way you could use superannuation contributions to negatively gear against your existing home mortgage? There are competing needs. Home ownership is a priority for most young people. Is there a creative way of doing that? Is it justified?

Ms Kelleher—Negative gearing only works if you are doing it with an investment property, so as a starting point you cannot negatively gear your home and get a tax incentive for doing it. There are the competing conflicts of—negative gearing is a generally accepted wealth creation mechanism, be it over property, shares or whatever. Unfortunately you cannot borrow superannuation and therefore immediately there is the conflict of a normal wealth creation mechanism that anybody else would use not able to be used at all in superannuation.

Ms GRIERSON—You are getting a tax incentive basically from the government and you are certainly getting some reductions on interest rates. The beneficiary is not necessarily going to be the individual, it is going to be the government in the long term that saves on having to prop people up who do not have home ownership and who are going to go on pensions or who cannot support themselves. It is not a benefit that is going to work for the individual so much, but it is certainly going to encourage home ownership and superannuation mutually rather than separately.

Ms Kelleher—I cannot see how borrowing for your home, your personal home that you are living in, gives you any incentive. It gives you no tax benefits except I suppose capital gains on your house when you die.

Ms GRIERSON—I will leave it at that because I do not think we are talking about the same thing, but that is alright, thank you.

Mr TANNER—The answer to this may lie in that you lose the capital gains tax benefits but is there anything to stop somebody entering into a contract with their best mate to each buy a home and live in the home that the other has bought and rent to each other and both negatively gear?

Ms Kelleher—Within the small funds, the sole purpose test, the investment strategy and the in-house asset rules are anti-avoidance provisions, such as part 4A of the tax act. There is probably enough in there to get the funds into trouble. Part of it relies on—

Mr TANNER—I am thinking about individuals doing it.

Ms Kelleher—Individuals could do that. I do not know many people who are prepared to buy an investment property and rent it to a mate. If it is being rented at commercial rates and all those sorts of things then yes, you would get your negative gearing. But, I think there is a lot of trepidation for people saying, 'You own my house and I will do improvements to my house', then you could suddenly turnaround and sell tomorrow because you have gone bankrupt. I cannot see that people would do it. They might do it for close family members but certainly not friends.

Mr TANNER—I think the real barrier is that you lose the capital gains tax exemptions. That is probably the answer to the question.

Mr CIOBO—Ms Grierson teased out one of the issues I wanted to ask about—superannuation splitting. Can you tease out lifetime contributions for the committee? Secondly, you made some comments, Mr Davison, in your opening remarks that voluntary contributions have decreased significantly and I was interested in research and/or ballast behind that claim.

Mr Davison—APRA's super statistics that are put out on a quarterly basis splits up total contributions into voluntary and compulsory. Over time, they have actually trended down quite significantly. We have not done any more research than what are the publicly available APRA statistics.

Mr CIOBO—The issue then is that despite growing real wages and despite tax cuts, we are not seeing any more of that money flowing into super, in fact we are seeing the opposite.

Mr Davison—Yes. There are probably a couple of reasons for that. Firstly, it has come off the back of the surcharge in 1996, in that we would have seen a lot of salary sacrifice contributions reduce over time. Secondly, we have come off the back of the demise of a number of defined benefit funds where people were forced to make those contributions. It is early days to tell whether initiatives like the co-contribution and surcharge reduction last year are going to change that trend. Our hope is that it does and early indications from Treasury's numbers on co-contribution is that there has been great interest and great support for the scheme. That would suggest that it will turn voluntary contributions around on the whole, but unfortunately we will be waiting another one or two years before we actually start seeing that trend.

Ms Kelleher—One of the comments before was that the number of self-funded retirees has increased. Can that be seen as being a sign that the compulsory super and tax incentives are actually working? I would suggest it is still a long time before we know whether any of the compulsory super and tax incentives are working simply because a lot of people who are self-funded at the moment are probably self-funded off the back of defined benefits that they would have been entitled to from their employers. A lot of the defined benefit funds were very generous; some of them had compulsory employee contributions, some of them also had voluntary employee contributions for which the amount of employer defined benefits would be increased accordingly. A lot of people did take advantage of that. Since the introduction of compulsory super and even going back to the enterprise agreements in 1986 when productivity super was brought in, more and more of the defined benefit arrangements have been closed down.

We have come to the point where probably most people under 40 do not have defined benefits and are relying purely on SG and voluntary contributions. The people that are retiring at the moment are still largely people who, where they are self-funded, have had the advantages of either they have received a defined benefit on their retirement or at some point of time their employer has closed their defined benefit fund or the defined benefit sections and as such they have received the defined benefit plus an augmentation, potentially, in terms of encouragements to get out of the defined benefit into the accumulation. I think it is a long time before we actually see whether anything that is in place at the moment has done anything to address the adequacy issues.

Mr CIOBO—Could you make some comments about the lifetime contribution limit and your proposal with that?

Mr Davison—Coincidentally, internally, our centre of excellence is doing some work on maximum limits at the moment and over the next couple of months. There are a couple of options; you could have a much larger limit which accumulates over time, for example, replacing the lowest limit for the under-35s, which is about $14,500 a year, with the $40,000 or the $100,000 limit. The downside of that is that you end up with a large lifetime limit. Another option is having a higher lower limit or getting rid of the under-35 limit altogether and having a $40,000 limit a year. If you do not actually approach that limit in any one year, you could have the balance of the limit roll over into the next year so you are accumulating your unused limit through your lifetime. It is early days in our work, we are hoping to have something done by March or April.

Mr CIOBO—If you had a lifetime contribution limit, how would that work from a practical point of view? You would need to allow for indexation or something like that so how would you marry up your indexation against your—

Mr Davison—If we had a rolling annual limit, you could still index that.

Mr CIOBO—So, you would have a formula to calculate a lifetime limit and then put it back into annual instalments, is that how it would work?

Mr Davison—Yes. If it is $40,000 a year, index that amount and it then accumulates over time.

Mr CIOBO—Would we really moved from what we are doing now if we were to do that?

Mr Davison—We are smoothing it out in that it will follow changes in work patterns.

Mr CIOBO—Because I could attribute a future value to the annual limits that apply now.

Mr Davison—For someone who is under 35, if you are a higher income earner, say a young professional, a limit of $14,000—

Mr CIOBO—What we are actually talking about is increasing annual limits rather than—

Ms Kelleher—The annual limits at the moment have been structured so that your $100,000 plus is on the basis of not having made much super in prior years and this is how you catch up. Whereas, an annual limit that is the same across the board—which I suppose is the current system—enables you to catch up; do not worry about making it now, you will catch up down the track.

Mr CIOBO—I am not sure that is right.

Ms Kelleher—A single limit means that there is a strong message of, 'think about it over your lifetime'.

Mr CIOBO—I am not sure that assertion is right. I think in fact policy is to say, 'There are many of you who have not made contributions in the past and so we want to enable you to catch up now', rather than saying, 'Don't worry about it now, we will let you catch up.'

Ms Kelleher—The perception is, 'It's there, so I don't have to worry about it because I can catch up.' A lot of this is dealing with perceptions and perceptions are a powerful thing.

Mr Davison—One of the problems is, yes you have a larger limit to be able to catch up later in life but you are not necessarily going to be in a position to make those contributions, whereas you might have been in a position earlier in life or in the middle of your career to have made those contributions but at the moment the limits stop you doing so.

CHAIR—That is a valid point.

Dr EMERSON—In terms of declining voluntary contributions and the various explanations you put forward, would not one of them be increasing compulsory contributions and a notion that people have, rightly or wrongly, an optimal level of contributions. And, as the compulsory rate goes up the voluntary rate goes down and they still achieve what they consider to be their optimal level.

Ms Kelleher—I would suggest that if you did not have compulsory they would not be going into super anyway. A lot of employers did the compulsory super so that as your pay increased it went into super so you never had that money, and if you did have that money it was probably not going into super anyway because you were going to spend it. I do not think we can say that compulsory super is actually replacing or taking away from the voluntary. I think the assumption has to be there would have been no additional voluntary.

CHAIR—If you were on this committee, what would be your dot point key recommendations as to the incentives and disincentives of super for under-40s?

Mr Davison—Four dot points would be identifying a savings target so you actually know what you are working towards, restructuring contribution limits, one thing that we did not touch on is addressing the inequities towards the self-employed and the incentives they get, and finally removing contributions tax.

Ms Kelleher—I would add an opt-out system as opposed to opt-in.

CHAIR—Is there merit in perhaps removing it for the lower end of the contributions tax? Because of the wage factor, the levels of taxation that you pay and the incentives, is it a factor perhaps for under-25s or under-30s?

Mr Davison—There is definitely more benefit in removing contributions tax at the lower end. Unfortunately, it adds a level of complexity which we would much rather see the super system move away from.

CHAIR—It is not that complex is it?

Ms Kelleher—It is because contributions tax is not a separate tax, it is part of the income tax regime. You would have to work out how to redefine what is the assessable income of the fund to exclude contributions relating to whatever age group or whatever it is that you are trying to exclude it from. Otherwise, you would have to structure a rebate system that the tax office would then have to work to feedback into the super funds. You would end up with a reverse surcharge situation, which would be just as horrible as the old surcharge mechanism. Removing contributions tax in segments, apart from saying ‘all SG contributions are out’, becomes very difficult in terms of how to do it. Either the income tax legislation has to be restructured, because it is just an income tax that happens to be on contributions, or else a rebate system has to be worked out that hopefully the super funds themselves are not going to be the ones responsible for making sure it is right or wrong or tracing member accounts here, there and everywhere to get the money in the right spot.

Dr EMERSON—Could you do it on income rather than age?

Ms Kelleher—Super funds do not have that information, again it would be reverse surcharge.

Mr Davison—We have already seen the administrative complexity and difficulty and even nightmare that surcharge has been for super funds over the last almost 10 years. We would not want to see it again.

Dr EMERSON—But, it could be done without those complexities on the SG, on the compulsory component?

Ms Kelleher—It would be easier because, from a compliance perspective, the funds have to know what SG contributions they are receiving, or there is the assumption that any contributions that they are receiving are SG contributions. They can build in thresholds or tests to exclude excess salary sacrifice that would be over and above SG contributions. There would be a way of building it in.

Dr EMERSON—They need to know it anyway.

Ms Kelleher—Yes, and there is the assumption that any contributions that they are getting are SG unless they have other reasons. It would piggyback on what they are doing already.

Dr EMERSON—Based on that assumption, would people then be able to get relief from the contributions tax for non-compulsory super because the super fund is assuming everything is compulsory?

Ms Kelleher—No. From a fund's perspective you would make sure you got something from the member/employer to actually tell you what the contributions are, which they are collecting at the present point anyway.

CHAIR—We had a very interesting contribution by Ms Galbraith from the Australian Services Industry in relation to a cash-back scheme for under-40s whereby there was a cash back in terms of a tax rebate at the end of the financial year in terms of the voluntary contribution. Does that attract the same complications?

Ms Kelleher—You probably have the same complications. At the same time I would like to see any tax cuts relating to super actually going into super. Again, it is a bit like robbing Peter to pay Paul; you put money into super but then get some back in your pocket?

CHAIR—It was not getting money back from what they contributed, it was a cash back they were recommending.

Dr EMERSON—Tax rebate for your contributions.

Ms Kelleher—Which is effectively like getting a tax deduction. It would not have as many complications because you would be able to drive it through the tax returns. With the co-contribution information that the tax office currently has they could probably do the matching as they would have done with the surcharge. That would put the administration out of the funds and into the tax office. Are the costs involved with that such that it might have been a cheaper way just to put the tax cuts into the superannuation so you know they are sitting in the superannuation?

Dr EMERSON—You have given very good reasons why selective cutting to the contributions tax is administratively very difficult, and if the government of the day said they cannot afford to abolish the whole thing, then this might be a way to achieve a result because it is minimising administration costs.

Ms GRIERSON—It is a tax incentive for young people trying to accumulate other savings for other purposes, to pay off their HECS or to get a deposit for a home.

Ms Kelleher—When you look at the super fund tax rate, everybody is talking about cutting it and they are talking about abolishing it, particularly the contributions side, down to zero. One option might be that 15 is too high. Maybe it should be 12 or 10, something like that. Is that the easier option? Does that keep the relativities right?

CHAIR—I understand your brief in terms of your shareholders in your organisation but focussing on where the inequity is the greatest is how best to address that inequity. The chances of this committee putting through a recommendation for abolishing the contributions tax worth $3.3 billion is probably remote at being accepted. We are trying to concentrate on the inequities of that cohort and how best to handle that. The answer is not clear on what is the best way to do it.

Ms Kelleher—There is no easy answer to this. The issue too is this group is looking at the under-40s, but can I suggest that the over-40s have probably got more of an issue, particularly the people in the 40s to 50s bracket, who have not had the benefit of SG contributions for ages, they have not had the benefit of defined benefits and therefore they are in the middle of nowhere. It has to be for the benefit of everybody.

Mr TANNER—What would you think of a tax-free threshold contributions tax—the first $5,000 was tax-free?

Mr Davison—That could go back to having it on the SG, just having the SG contributions tax-free. It is a similar concept.

Ms Kelleher—You could do it; you are just picking a different figure.

Mr TANNER—It is basically the equity issue that is the problem.

Ms Kelleher—It would not necessarily be a hard thing for the funds to run because they just look at the first $5,000 of their members. If you are looking at $5,000 per person, how do you deal with someone who is in two funds? Do they get the $5,000 twice? It might be that there is a balancing item in the tax office.

Dr EMERSON—It would certainly give you an incentive to invest in lots of different funds.

Ms Kelleher—That might be something that the tax office could balance up with the co-contribution information it is getting. For example, if one is in 10 funds, fund number one will get the $5,000 and other super funds will get a bill for the tax that should have been paid on the $5,000. There would be ways of dealing with that issue.

Ms GRIERSON—Is there any way to remove the multiple death and disability components that young people are paying who have lots of different superannuation accounts? Is there a simple way to do that?

Ms Kelleher—There is no simple way because a lot of funds have compulsory base insurance. With choice of super—

Ms GRIERSON—But, you are only going to be able to use it once.

Mr Davison—Theoretically if you have five funds and paying five sets of premiums you get five benefits.

Ms GRIERSON—So, they will pay five benefits?

Mr Davison—Assuming each fund is operating individually.

Ms GRIERSON—It will not be much comfort when you are dead.

Mr Davison—The difficulty is that the five benefits will be reduced by five sets of premiums when you may not need that same level of death benefit. Hopefully the awareness around super coming from the choice campaign will start to improve that. Choice and portability, hopefully will address that. The ATO is running campaigns.

Ms GRIERSON—It would be good if that was one of the outcomes.

Mr Davison—It is a difficult situation.

CHAIR—That has been most interesting. Both of you are very well informed on the area. I do not know whether you have made our job easier. Everything is hard; there is always some reason why it is not possible. We may come back to you.

Proceedings suspended from 11.02 am to 11.13 am

CHESWORTH, Mr Peter, Head of Division (AIG), Office of Small Business, Department of Industry, Tourism and Resources

GREENWELL, Mr Anthony David, General Manager Policy, Office of Small Business, Department of Industry, Tourism and Resources

LEE, Ms Margaret Adelaide, Manager, Tax and Workplace Relations, Office of Small Business, Department of Industry, Tourism and Resources

CHAIR—I welcome representative of the Office of Small Business from the Department of Industry, Tourism and Resources to today’s hearing. Although the committee does not require you to give evidence on oath, as you know, it has the same standing as proceedings before the parliament. I invite you to make an opening statement and then we will proceed to questions.

Mr Chesworth—I would like to make an opening statement to outline the role of the Office of Small Business and what we see is the key issue facing small business in this area. As we outlined in our submission, the charter of the Office of Small Business is to provide policy, advice and support to the government on small business issues. One of its key roles is to consult with small businesses and their representative bodies on issues of concern. Our submission made to the committee reflects the views of small business stakeholders on superannuation savings issues that have been brought to our attention in a variety of ways over time. It was intended to bring together those views with background to provide the context for their concerns for consideration by this committee. The current inquiry has particular reference to the barriers, disincentives to contribute to superannuation, current incentives in place to encourage voluntary superannuation contributions and improving the awareness of the importance of saving early for retirement. The key issue for small business is outlined in our submission and relates to the incentive for unincorporated self-employed small business operators to save for their retirement through superannuation, given that they fall outside the compulsory superannuation guarantee requirements.

CHAIR—You mentioned the self-employed small business operators falling outside the compulsory superannuation requirements. Do you think it is necessary to compel them to contribute towards it? In my electorate there are many young, self-employed guys who fall outside the limits and you just wonder sometimes what will happen if they are not making that contribution. In my electorate a lot of people who are very active with a lot of physical activity have back injuries, et cetera, and then they start to struggle a bit. What are your views on that?

Mr Greenwell—Incentives are a key part of it. Your question is whether we think there would be advantages in it being compulsory for self-employed people. I would have to say that essentially that would be a policy decision of the government to make in that area. Obviously the compulsory superannuation system has worked fairly well in the case of employees. That is all I can say in that area.

CHAIR—Do you have figures on the extent of voluntary contributions by self-employed small business people?

Mr Greenwell—No, we do not. We could try to obtain those for the committee.

CHAIR—That would be useful. It seems that we have a whole group of people who are falling outside of the intention. We all know why, but if they are not taking advantage of the voluntary contribution then somewhere along the line they are going to fall back on government assistance. On page 2 of your submission you note that 37 per cent of owner-managers of unincorporated enterprises had no superannuation and owner-managers of incorporated enterprises did have superannuation and that owner-managers of unincorporated enterprises who did have superannuation had much lower median superannuation account balances. Is your department concerned about these figures?

Mr Greenwell—We do not provide policy advice to the government on superannuation issues. We do look at it from the perspective of the small business sector, and naturally we would like to see small businesses adequately catered for in terms of superannuation. As we mentioned in our submission and as the figure you have just quoted indicates, there are significant numbers who are not getting into the superannuation system. The information available to us is that the majority of small businesses put their money into their business; they like to grow their business, especially in the early days when it is being established. What has prompted our submission in the first place is that we have had a lot of feedback from small business operators and their representative bodies over several years, that they feel that their incentives are not as strong as employees to put money into superannuation. That is the basis of our submission, which is this 75 per cent deductibility. Their inability to access the co-contribution scheme is also a factor.

Dr EMERSON—Based on those figures, if there are 607,000 owner managers of unincorporated enterprises aged between 20 and 44, and 37 per cent of owner managers of unincorporated businesses have no superannuation, then that means something like 240,000 young people aged 20 to 44, owner managers of unincorporated small businesses have no super. Mr Ciobo will confirm that that is a very rapidly growing cohort in the Australian population. If it is a problem now, it is going to be a very big problem in 20 or 30 years time unless some change is made. Is the voluntary contribution such that the tax treatment is so unfair?

I was one of these for a while until I became older than 44. I ran a business and we made some extra cash and were looking at paying a fair bit of tax, which is fine, but I was advised to take $20,000 and put it into a super fund. That seemed to be a very attractive option for me and I did it. If you put $20,000 into a super fund then $15,000 of it is tax-free?

Mr Greenwell—No. If you are under 35 now, there are aged based limits on how much you can contribute each year.

Dr EMERSON—If you are an unincorporated small business?

Mr Greenwell—Yes. The first $5,000 of your contributions will be fully deductible to you as a tax deduction and that money goes into the super fund. If you put in any extra than that, up to the aged based limit which is about $14,000 at the moment, the balance of that is only 75 per cent deductible to you. A person who is a business owner who runs their business as a company and pays themself as if they are an employee under the superannuation guarantee system gets full parity for deductibility on each dollar going into the super fund—I did a rough calculation this morning—they would have to put in about $16,000 to get the equivalent of the age based limit.

Dr EMERSON—It seems to me that is an argument for incorporation, in favour of incorporation. If you are going to suffer those sorts of penalties then for $800 you can get incorporated and that problem is solved. If you are over—

Mr Greenwell—The age based limit is up to 35.

Dr EMERSON—What if you are over 35?

Mr Greenwell—In 2004-05, the age based limit for those 35 to 49 years was $38,700.

Dr EMERSON—That means that every year, if you were considering putting in $20,000, which is a lot of money to put into a super fund, then in those circumstances, 35-plus people, you are getting the first $5,000 of the $20,000 tax deductible and then the remaining $15,000 is taxed at—

Mr Greenwell—The tax deduction is 75 per cent of that remaining amount.

Dr EMERSON—It seems to me a pretty strong incentive, and an incredibly strong incentive compared with the alternative of taking that $20,000 as cash salary or profit on your unincorporated business.

Mr Greenwell—You are saying it is still a strong incentive to put it into superannuation?

Dr EMERSON—It seems to me anyway, I did it.

Mr Greenwell—It is.

CHAIR—It is not the same as treating yourself as an employee.

Mr Greenwell—That is right; that is the basis of the argument in our submission. If a small business owner is incorporated, they can get full deductibility for that $20,000; if they are unincorporated they cannot.

Dr EMERSON—Under the Work Choices legislation, you are going to be required to incorporate anyway if you have an employee.

Mr Greenwell—No, I do not think so.

Dr EMERSON—Then you will be covered under the federal system. If you want to be covered under the federal system, my understanding is that you need to be incorporated at this point.

Mr Greenwell—There will not be a system though—

Mr CIOBO—This is what we are hoping!

Dr EMERSON—What system are you going to be covered under if it is not the federal system, if the government wins the High Court challenge and the government's intention is fulfilled, which is that there is no state system?

Mr CIOBO—We have to refer that, otherwise we do not have unincorporated.

CHAIR—Why did they set that up in the first place, that differential with self-employed people?

Mr Greenwell—We do not know the rationale behind it. It occurred in 1980, so Treasury would be the best people to provide advice on the rationale behind that.

Mr CIOBO—In terms of your assessment about those that are not covered by superannuation, do you have any research available that perhaps highlights where they are sitting with respect to business assets or personal assets? What I mean by that is, yes, they may not be covered by superannuation but they may have superannuation assets of sorts in other forms. Do you have any research on that?

Mr Greenwell—We have not carried out any research on that. The strong anecdotal evidence that comes through to us in the Office of Small Business on the attitudes of small business owners is that they see their business as their retirement income, their retirement nest egg when they decide to leave the workforce.

Mr CIOBO—Is that a realistic expectation? Do you have any research on that?

Mr Chesworth—It depends a lot from business to business.

Mr CIOBO—I am saying overall.

Mr Chesworth—Small businesses comprise 95 per cent of all businesses in Australia or even slightly more than that, so it is fair to say that there are some small business that would be better placed to sell their businesses than others.

Mr CIOBO—You hear that eight out of 10 small businesses fail in five years. It would seem to me that the expectation that this small business is going to be my superannuation lump sum is ill-conceived. Is that what you are witnessing?

Mr Chesworth—It would be fair to say that there is a level of misconception out there. The levels of business failure in Australia are actually far lower than that bush telegraph anecdote that so many fail in such a short period of time. Most succeed and there are other ways in which businesses can end as well. Certainly the government has put in place initiatives to address this very recently as part of the Building Entrepreneurship in Small Business program. There is a succession planning element, and the government will be calling for submissions to provide funding to organisations to help small businesses sort out these succession planning issues. It is fair to say that a lot of small businesses probably enter into a business, particularly if you are aged under 35 or so, and the last thing you are thinking of is what you are going to be doing with it when you are 55 or 60.

Mr CIOBO—On the Gold Coast, and I am sure this applies to other parts, we see evidence and I hear of evidence, of people who have obtained a superannuation lump sum, relocate looking for a sea change or whatever and invest a large proportion of that lump sum into a business in which they generally have no prior experience, only to whittle it away over time. Do you any evidence on that? Would you care to make any comments on that?

Mr Chesworth—Being a public servant, I have some former work colleagues who have done precisely that. There is always going to be a market for the sale of businesses. It is certainly wise for prospective business purchasers to do their research very carefully. Certainly the franchising sector holds itself out as being a model for people who have limited business experience to be able to enter into a business.

There are franchising systems that range from a turnkey franchise to ones where they would provide ongoing support for six months. Certainly it does appear to be an issue, but is it an issue or is it just part of the way markets operate, in that, as part of a capitalist system, there are those businesses that will do very well those that will fail.

Mr CIOBO—Do you have evidence or research that demonstrates that those aged 55 and over or aged 60 and over that start up a business have a greater or lesser chance of success versus somebody who starts up a business at 30?

Mr Chesworth—The Office of Small Business has not undertaken any research but we could have a look to see whether there is any research out there. Certainly, we work closely with industry associations.

Mr CIOBO—I would be interested. If we see large numbers of the baby boomer generation taking lump sums and investing the money—maybe the failure and success rate reflects the average, in which case there is no need for government concern. Alternatively, if we were to see a blow-out in unsuccessful businesses for those aged 65 and over, or whatever the figure is, then perhaps it would be an area of policy concern. In that regard, I would be interested.

CHAIR—I am not sure whether you have any recommendations to make to us in this inquiry, given your experience with small business. I suppose you have highlighted some inequities.

Mr Greenwell—It was our intention to highlight the sorts of information that has been brought to our attention in the work we do in the Office of Small Business. As Peter mentioned in his opening remarks, we consult with small businesses and we have other consultation forums with industry associations and that sort of thing. This particular issue is something that has cropped up for many years now. It is seen to be an inequity that, if it were addressed or removed, may encourage more self-employed, small businesses to commit to superannuation savings.

Mr CIOBO—At point 15 in your submission, you state:

Bringing the deductibility level of self-employed business operators in line with those of companies would also provide a stronger incentive for self-employed people to contribute to superannuation.

I know there was some discussion on that of which I missed a small portion, but have you done any calculations on cost to revenue of doing that?

Mr Greenwell—No, we have not. There was an increase of this threshold from $3,000 to $5,000 on 1 July 2002, I think.

Mr CIOBO—Who would do that—yourself or Treasury?

Mr Greenwell—Treasury.

Mr CIOBO—I will direct that to Treasury.

CHAIR—Do you have an average profit figure for small businesses for those aged under 40?

Mr Chesworth—We will see whether we can dredge up a list of them. I suspect, to my best recollection, the ABS statistics are fairly limited in this area because of the relationship of profitability with other issues, such as taxation. It is often difficult to get hold of that information. If we could take it on notice, and if we can find something we will provide it to the committee.

CHAIR—Thanks very much for coming today. We appreciate the input and look forward to the further comments you might have following our inquiry today.

Mr Chesworth—Thank you.

[11.39 am]

BURN, Dr Peter, Associate Director Public Policy, Australian Industry Group

CHAIR—Welcome. Although the committee does not require you to give evidence on oath, I should advise you that these hearings are legal proceedings of the parliament and therefore have the same standing as proceedings before both respective houses. We have received a written submission from you. Do you wish to make any additional submissions or make an opening statement?

Dr Burn—Thank you. I will make a brief opening statement. While we are not experts in superannuation, we nevertheless have a firm tradition of support for superannuation, and we are closely involved in some of the leading industry funds—the Superannuation Trust of Australia and the Australian Retirement Fund. To hit the high spots of our submission: first of all, we regard this as a very important area, and we regard this review as a farsighted initiative. As far as barriers are concerned, the biggest barrier against people making contributions to superannuation, clearly, is their employment. Particularly for people under 40, there is a high incidence of families with children, including single parents with children, and students, and for this the benefits of diversity of part- and full-time work arrangements are clearly very important.

In our submission we refer to the level of the superannuation guarantee charge, the compulsory levy on employers. We support that levy but do not think that it should be raised. At the micro level of the individual firm, raising the compulsory component would reduce the ability to negotiate other flexible conditions of employment for a variety of employees, particularly those who are seeking part-time work. It would also raise the cost of employment in general, in much the same way as the payroll tax would do. Raising the superannuation guarantee charge would therefore reduce the job creating potential of the economy, and of business, and therefore increase the barrier to further superannuation contributions for people under 40, and for anyone else for that matter.

We submit that tax on contributions should be reduced or removed. This is a longstanding policy of the Australian Industry Group. It should be seen against the background that Australia's taxation system, as with other comprehensive income tax systems, discriminates against saving and double taxes it, and that the arrangements relating to superannuation go part of the way towards correcting the bias against saving. It does not go all the way. It could go further by reducing and removing the contributions tax; that would increase both the level of saving and the level of retirement incomes, both worthy objectives. It would also increase the tax on higher retirement savings in the future.

On current initiatives to encourage superannuation, we fully support the very generous co-contribution scheme. We also support the idea of splitting, which is now available. I mention that because of the clear benefits for people under 40.

As to awareness, we think there is a lot of scope to improve awareness, particularly in the promotion of the co-contribution scheme, and in splitting. There is a current opportunity to get out there and explain why super is beneficial and how it can be made more beneficial. We support also anything that can draw attention to people of the benefits of saving, especially the power of compound interest. We think that there is a role for government in providing information about the benefits and the responsibilities that people have to self-provision of retirement income, and we would include superannuation in that.

In summary, Australia Industry Group’s main points are that this inquiry is a very worthy initiative. Primarily, anything that can be done to increase employment, or anything that is not done that would worsen employment, would be very beneficial. We support the reduction in the superannuation contributions tax and we support measures to improve awareness, especially around the very generous arrangements for co-contributions and splitting.

CHAIR—Thanks very much. You have talked about one of the ways in which the contributions of young people can be increased with the suggested removal of the contributions tax, which is worth some $3.3 billion. Obviously, that is a significant part of it. Do you have other ways in which you would see that we can significantly increase for that under 40 group?

Dr Burn—Only the obvious ones of providing people with information about the benefits of superannuation, and we draw attention to the very strong, but perhaps under appreciated, power of compound interest. We also think that there is a lot of scope to improve the take-up of the co-contribution scheme by improving people’s awareness of that scheme, perhaps through employee and employer bodies, and of course general financial planning, which I think is put forward in a number of submissions before the inquiry.

Dr EMERSON—When you say that increasing the superannuation guarantee increases cost to business, is it not true that we have not seen the last wage increase in Australia’s history, and if, in lieu of a wage increase, money were put into superannuation, that does not increase business costs?

Dr Burn—If one is a substitute for the other, that would not increase business costs.

Dr EMERSON—Why do you feel that they would not or could not substitute?

Dr Burn—We would be interested in any proposal that did that, but are not aware of a current proposal to do that. In commenting on any increase in the costs of superannuation, we were just commenting on that in isolation rather than as a trade-off for some other thing. However, it would be interesting to see how the mechanism of improving or increasing the superannuation guarantee charge across the board could be seen as a substitute for wage increases when wages are determined under a variety of arrangements. For example, an increase in the minimum wage or a discount in the increase in the minimum wage and basic award wages, substituted for the superannuation charge, would not affect people necessarily on above award wages. The trade-off would be incomplete in that sense, and could well be associated with a net increase in costs for employers.

Dr EMERSON—Yes. Let us just explore that for a second. I cannot remember the figures but the proportion of employees who are award dependent is 20 per cent Australia wide—I think it is something like that. Therefore is there any reason why an increase in the minimum wage would automatically flow through to all awards?

Dr Burn—It is only convention.

Dr EMERSON—There are still 80 per cent of people outside of that category, most of whom are then subject to some form of enterprise bargaining, common law contract, or an AWA—I think is about three per cent. With all of those, would not there be potential, given that they are in some way or another contracts or negotiations between employers and employees, to arrive at an understanding in those negotiations, that at least X per cent of any wage rise could go into superannuation?

Dr Burn—That is totally correct and that is available on an enterprise bargain, but not within the context of a compulsory levy. There is scope to increase voluntary levies or employer contributions, and that exists under all those contracts and arrangements. An increase in the compulsory component would be across the board and apply to all employees, all those who are subject to the levy obviously, but that would reduce the discretion, I would have thought, for a variety of negotiations, some of which people may well prefer instead of an increase. For example, it might reduce the ability of the employer to contemplate scope for more part-time employment, thus reducing the scope for people who are looking for part-time employment to find suitable hours of work and therefore benefit from the standard contribution.

Dr EMERSON—In relation to that point about part-time work, we had discussions last Friday about the limit of $450 a month below which the employer does not need to provide superannuation guarantee contributions. There seems to be a concern, that I would probably share, that there is some manipulation of that, particularly in the services sector, say in restaurants, so that they employ a lot of people on $425 a month and save nine per cent. That seems to be one practice that is going on. Do you have any comment? The other one is it is $450 a month per job, and if you are in three jobs you might be earning $1,300 a month and getting no super. Do you have any comments on that because it goes to the heart of this under-40s group and why young people are perhaps not taking out the super that we had hoped for.

CHAIR—Also that group are just being marginalised for the future.

Dr Burn—Yes, there is no doubt that behaviours change around those thresholds. That applies to all thresholds, whether it is the age pension, income earning thresholds, the payroll tax thresholds or whatever. There is no doubt that they affect behaviour at the margin. I think that is really all I can say on that.

Mr CIOBO—On that point regarding superannuation contributions, I will put an assertion to you for your reaction. Your comment that it would increase the costs of employment and detract from the ability of employers to create jobs and pay higher wages is a comment that is static in nature. What I mean by that is that if you look at it with a longer term point of view, and say, ‘Well the more people who contribute to personal super the less reliance there will be on the public purse, therefore, the lower the level of taxation’, in the most basic of terms. The reality is that it is going to be better for business to contribute more to superannuation because that will place less of a burden on government to raise revenue.

Dr Burn—It is an interesting argument, but we would say that in the same dynamic context the creation of more jobs would have a better benefit for people, exactly following that reasoning you have put forward. To the extent that there is a trade-off, we would support the creation of jobs and putting income in people's hands from which they can save, including via super.

CHAIR—In your point that a similar increase in employer contribution from nine per cent to a higher amount, you compared that to the payroll tax but payroll tax is quite different because there is no benefit at all in the individual employee's hand. This one has a direct and compounding benefit and a benefit overall to the economy.

Mr CIOBO—I guess the most stark differences are if you are hiring someone. I know employers will say, 'This is a $50,000 per annum job including super,' but I am not aware of any of them saying, 'This is a $50,000 per annum job including payroll tax.'

Dr Burn—The incidence of payroll tax is probably worth discussing in some detail perhaps at another time.

CHAIR—It is a regressive tax; we can all agree on that.

Dr EMERSON—John Freebairn did some work to say it was equivalent to company income tax.

Dr Burn—There is a lot of work and a lot of tax experts that show that they are all the same as one another, is there not.

Dr EMERSON—They all hurt.

Dr Burn—On the benefit to the economy, first of all, a cost to the employer is a cost to the employer; that it benefits employees is very good, just as taxes benefiting the general community is very good. It does not change the nature of the fact that it is a cost on employers, and a cost that comes off their bottom line and affects their competitiveness. I think that needs to be borne in mind as well.

Mr CIOBO—Those assertions are absolutely correct, but by your own admission, part of our role as legislators is to achieve a balance, and clearly we could say, 'There should be no taxation at all' and there would be no imposts at all, but there would obviously be ramifications that flow from that. I guess a thrust for the committee is to try to determine how we go about addressing what, clearly for those under 40, is not a priority for most with respect to their superannuation. We are seeing in figures that the compulsory nine per cent is certainly having a beneficial impact. The question for this committee becomes one of, among other considerations, should we increase that compulsory nine per cent and what are the costs and benefits of doing that? We are aware of the benefits of doing it, and what we are soliciting from you is, beyond saying that it is an additional cost to business, what are the costs of doing that?

Dr Burn—Right. Let us not forget the additional cost to business, but going on to other costs, we think that the chief other cost relates to the extra prescription over total remuneration. If you increase the compulsory component of remuneration, you decrease the ability to offer a variety of alternative mixes in people's remuneration package. The benefits of greater flexibility in those packages, including all aspects of work arrangements, are that you can cater for a variety of desires on the part of the workforce. Even apart from the additional money cost on business, there is the decrease in discretion and the ability to cater for workforce needs.

Mr CIOBO—When the nine per cent—

Mr McARTHUR—According to the Treasury submission, the nine per cent created $21 billion worth of superannuation in 2002-03. So, there are $21 billion worth of savings in the Australian community that your group can then borrow against. If you did not have the superannuation levy, you would not have that amount of savings. Your group would have a bit of a dilemma: on the one hand you say it is an extra cost; on the other hand it means that there is a source of capital available to industry and commerce. What do you say to that?

Dr Burn—I say that that would be most relevant if there were no other sources of capital other than the domestic quantity of saving, but clearly there are. Businesses borrow internationally from the international pool of saving, and the impact of superannuation guarantee on the total available funds from which business can borrow is neither here nor there, frankly.

Mr McARTHUR—Yes, but some commentators would suggest that the savings in the Australian economy are lower than some of the other western developed economies, and so this is quite a substantial contribution to the total savings pool surely, because it is real money and it is a real saving that has been undertaken by the community.

Dr Burn—There are some questions about whether it increases the total savings pool, but we do not agree with those arguments in their entirety, because there is no doubt some substitution between superannuation and non-superannuation savings. I think there is a Reserve Bank study that shows a degree of substitution. My point however, is that we think your argument that business relies on this to fund business expansion, and would be materially affected in its absence, overlooks the fact that business borrows from a global pool of funds, and the amount of funds that are added to that because of the superannuation guarantee are not really a convincing argument for us. There is no shortage of funds. The world has got a savings glut in fact.

Mr McARTHUR—Except that the savings that are generated from this nine per cent are very substantial, as reflected in the share market, the investment funds and their contribution to purchase of share portfolios et cetera. It is quite significant, without doubt. I think that from your group’s point of view, is it a factor?

Dr Burn—We think that it increases savings. We do not think it increases or improves to any significant extent, the availability of funds to business.

Mr McARTHUR—I rest the case.

Mr CIOBO—Can I ask another question. If there was an increase, let us just say from nine per cent to 11 per cent, I take it from your submission that effectively you are saying, ‘Well this represents a two per cent increase in the cost of business,’ but would not most businesses effectively keep the cost of that employee consistent and simply divert that two per cent from take home pay, so to speak, into super?

Dr Burn—Well if business had the discretion to do that, but business does not have the discretion to do that at all because we have minimum wages and award wages. I know that there are processes in place that will decrease the compulsory component of wages and other conditions that are embedded in awards, but that is a long-term process, I submit.

Mr CIOBO—They are global thresholds.

Dr Burn—That is true.

Mr CIOBO—Including super.

Dr Burn—Minimum wages? I think not. I think the superannuation guarantee charge is not included in the minimum wage.

Dr EMERSON—If it is being paid to some—

Dr Burn—The minimum wage is handed down periodically. It does not include the superannuation cost that employers will pay on top of that.

Dr EMERSON—On top of it. I see what you mean, yes. In relation to what Mr Ciobo was saying about the age pension, the earlier submission from the Department of Family and Community Services is all about the ageing population and so on. The age pension is currently equivalent to 2.9 per cent of GDP, just over $21 billion. That is a lot, but by the early 2040s it will be 4.6 per cent of GDP. Businesses and individuals will be paying those extra taxes, and in the case of businesses and individuals who are employers, I think Mr Ciobo was thinking of it as an investment in the future. If we do not do something about that 4.6 per cent of GDP, then the after tax return to business or to employers in terms of their personal income tax, will be higher because they are going to have to pay for the age pension. I do not think it should be considered just as a cost, but as a way of getting down costs in the future, or increasing after tax returns for business in the future.

Dr Burn—We agree with the importance of the growing pension bill. We submit that an increase in employment and therefore wages, would also reduce the age pension bill in the future. So, the relativities between the points that I am making, that is the substitution between higher wages or more jobs and a higher levy, tend to be cancelled out, because both the higher jobs and higher remuneration and the levy would have the impact on future pension payments. We think though that the reduction in the superannuation contributions tax would have a clear benefit both in terms of reducing future pension payments and in raising future tax revenues too, without adding to the cost to the business and therefore decreasing the opportunity for further employment growth.

Dr EMERSON—We understand that. For your analysis to work, implicit in that is that you have more people in work and more incomes, and therefore they will save through non-superannuation devices, or through voluntary contributions to superannuation sufficiently to achieve the same reduction in dependency on the age pension as compulsory super would. Now that is an empirical question, but it seems to me that there will be some leakage and it will not achieve the same result.

Dr Burn—As you say, that is an empirical question. We would need the elasticities and the projections.

Dr EMERSON—Exactly, and the elasticity will not be one.

Mr CIOBO—I understand the thrust of what you are saying, Dr Burn. I guess also though of consideration is the fact that structurally we are nearly at full employment now. I know this is now getting into margins, but at the end of the day these will be considerations for the committee as well.

Dr Burn—It is a very relevant and very important question about full employment. Our concerns are really more at the bottom end of the income distribution. Some of the Treasury projections about adequacy of retirement income as contained in their submission are quite eye-opening; admittedly they include the age pension component. We do not have a single labour market obviously. We have 5.3 per cent, or whatever the latest number was, unemployment, but a much higher rate of unemployment for unskilled people. We think that employers are much more sensitive to costs in looking at unskilled employment, than they are in employment in general. We think that we have to be very wary about raising the cost of employment across the board, when we have very strong suspicions that the incidence in terms of jobs, is very much felt amongst unskilled people, for which the market is far from fully absorbed.

Dr EMERSON—The Fair Pay Commission perhaps could have a role here in its terms of reference, that is, that a proportion of any increase in the minimum wage could go to superannuation. That does not then increase your cost.

Mr CIOBO—Thinking laterally.

Dr Burn—Well that is where the whole arrangement came from to some extent, the trade-off of wages and super, and so it is an extension of a tried process.

CHAIR—Thank you for coming. We appreciate your input.

Dr Burn—Thank you very much.

Proceedings suspended from 12.07 pm to 12.48 pm

ZEITOUN, Mr Anthony, Private capacity

CHAIR—I now welcome Mr Anthony Zeitoun to today’s hearing. Although the committee does not require you to give evidence under oath, the proceedings before this committee have the same standing as those before the parliament. We have received your written submission and I now invite you to make a statement. Perhaps you can expand on some of the ideas that you have put forward.

Mr Zeitoun—First, thank you for allowing me to appear before this committee. As a bit of background, I am currently a product manager in the financial services industry and work in the area of superannuation retirement income. I have put forward this proposal as an individual who has been a product manager for a number of years. In my experience, I have dealt with advisers, financial planners, clients, peers in the industry and peers outside the industry. The main feedback I am getting around superannuation and putting money aside is not along the lines of incentives; it is more along the lines of the first plan a client should go through. What they should do is get rid of the non-deductible debts, including their biggest debt, which their home loan. My proposal tries to get super working in such a way that everyday people can understand and also have some current day benefit without losing the preservation of super et cetera; that is what I want to go through. I will go through a few points to give you an understanding of how the proposal would work.

The main hurdle at the moment for such a product is the sole purpose test, which does not allow for this kind of product to be out in the market. Even though there are some do-it-yourself superannuation funds that have some aspect of property in them, it does not work exactly like this. The target market for such a product would be the under-40s or possibly the over-40s, but particularly those under 40. I am finding that more and more people, as they get older, are getting bigger debts. Prior to 2000, I remember that people in their 40s or 50s would not be able to get a 30-year loan from a bank. Now mortgage providers are permitting people to have longer loans. Therefore, when they retire they are using their super to pay off their debts. That is another reason why I have put forward this proposal.

The way this will work is that you have a superannuation fund as it is today with a number of options—the Australian equity fund, the balanced portfolios et cetera—and one of those is a mortgage offset option. That option would allow you to invest your super into an underlying wholesale mortgage trust type product, which are already available today. Currently you can invest into a mortgage trust with your superannuation money and you could, by chance, take a mortgage from the same provider. However, your super does not benefit from that arrangement; you would be just earning your returns from the mortgage provider and paying interest on your mortgage. This proposal will allow people to put their money into super and see the benefit today by reducing the interest on their mortgage today; therefore they can concentrate on their super strategy later in life, which is the salary sacrificing or voluntary contributions.

I want to mention a few issues that will come out of such a proposal. One is the potential to boost house prices by having such an offer in the market. The way to remedy such a boom would be to cap the mortgage at a maximum of $400,000, for example. You would also have a maximum amount that you are allowed to offset on that mortgage. Your superannuation would be able to offset up to a maximum of, say, 80 per cent of your mortgage; you would not be able to use all of your super to offset the whole mortgage amount.

Another issue would be: how do you allow for growth in super if all your super is doing is offsetting interest? In the larger paper I propose that only a certain percentage of SG contributions can go into such an option. You would put, say, 80 per cent of your superannuation contributions into such an option; the remainder of the contributions must go to another portfolio, be it Australian equities et cetera. Then, if you make voluntary contributions, you may be able to put 100 per cent into such an option. Therefore, you are attracting people to put more into super and offset their mortgage at the same time. I would put rules in there. For example, if you wanted to remain in this option, you must put voluntary contributions into this superannuation product to maintain a balance in that mortgage offset account. That is the basic part of how this product would work. For it to work would require the sole purpose test within the SIS regulations to be updated, but there would be no requirement for any further incentives et cetera.

Mr CIOBO—I am sorry; could you just go over that point? What did you say you would need to enable this to work?

Mr Zeitoun—It would require the sole purpose test within the SIS legislation to be updated to allow for a broader definition of the sole purpose test. Currently you cannot use your super for any other benefit.

CHAIR—Thanks for that. We have had several proposals in which people have been looking at the ways in which you could perhaps use your superannuation for assisting with mortgage, which is often the biggest challenge for young people. One of the reasons they do not get into super is because they give that a priority. This is a more scientific way of going about it. I suppose the challenge is the way it would dilute the benefits going into super per se. In terms of how it works, does the guarantee levy actually go to your super or will it enable you to take out a bigger mortgage? It is like a lien over your asset; how does it work?

Mr Zeitoun—You would be putting your contributions into the superannuation product, and it would be totally separate from your actual mortgage. Your superannuation would remain preserved, and it is in its own super fund. The relationship is in the underlying structure of where it gets invested. At the moment when you choose an Australian share fund et cetera that Australian share fund sits below that platform. It does not know what type of money it is; it does not know if it is super, cash or whatever. All it does is offer a return back to the super fund. In this way, your ETP or superannuation moneys would remain protected in the same way as normal super, except that the underlying fund it is being invested into is the same provider as for your mortgage. Therefore, you are using your super to offset the amount of your mortgage with that provider.

CHAIR—Offset the amount—

Mr Zeitoun—The interest within the mortgage.

CHAIR—The interest, is it? It pays for the interest on your mortgage?

Mr Zeitoun—It is the same way as the current redraw facilities operate with a bank product, whereby the extra money you have put into your loan reduces the amount payable in terms of interest with your regular payments. The difference between this and the redraw capability of current banking products is that with super you cannot take out your money, which is the temptation with the current redraw facilities available with banking products. In this way, people know that if they put it into super, it will offset their interest, they will pay off the capital more quickly, and therefore they can concentrate on their super strategy. Other rules I would have in there would be that it is only for owner-occupiers, so your own home only, and you can only do it once.

CHAIR—What would be the loss to your super savings through that scheme?

Mr Zeitoun—The potential loss would be the return on your super balance.

Mr CIOBO—How would that work with respect to the tax calculated on earnings? How would you see that operating?

Mr Zeitoun—It would most likely be factored in somehow in the underlying trust. It would be taken into consideration, and it would be factored in also to the rate of the mortgage. I would see it as all being within the one provider. It would be a tricky one, because there are no real earnings on it as such, so there is the potential, depending on how it is set up, that there would be no tax on earnings on that side. It depends how the regulations would be changed to allow for some sort of payment of tax on earnings. If it is offsetting, there would not be any earnings.

Mr CIOBO—You would have two separate accounts in reality—you have your super and your mortgage?

Mr Zeitoun—Correct.

Mr CIOBO—The earnings on your super are then paid across to the mortgage?

Mr Zeitoun—No, not the earnings on your super. There are no earnings on your super. Your super is basically funding your mortgage with a relationship down the bottom with a wholesale fund. Let me give an example. With a $250,000 loan, you have $100,000 in your option. The $100,000 will reduce your mortgage down to $150,000, so you will be paying interest on only $150,000 instead of $250,000.

CHAIR—What happens in terms of default?

Mr Zeitoun—On the house?

CHAIR—Yes.

Mr CIOBO—Sorry, before you go on, can I just finish this point? Do the earnings on the $100,000 that you have sitting in the super account continue to accrue in the super account?

Mr Zeitoun—The amount in the super account does not have any earnings because all you are doing is using that $100,000 to offset interest, which would otherwise be payable to you by a return if it is a standard mortgage fund.

Mr CIOBO—So the fund manager, or whatever the entity is, is then taking that $100,000 and utilising it for what purpose, would you see? Would you see constraints on what that money is utilised for?

Mr Zeitoun—It is utilised for mortgages.

Mr CIOBO—Just to pay down their own debt?

Mr Zeitoun—Correct. In the case of a default, your house and your super are totally separate.

Mr CIOBO—What about in a situation where you have a mortgage fund? It has been suggested to me that some of these mortgage funds might be a bit wobbly, especially in a cooling off period in the property market, and this then ties into the question asked by the chairman: how would you see that work? Would you view it as being safe enough?

Mr Zeitoun—Yes, sure. The way I would see it working is that the mortgage and the super are totally separate. The super is preserved and it cannot be touched; it is just used for the purposes of offsetting interest. The mortgage basically is a standalone product that is linked to the superannuation product. Say, for instance, you could not afford the mortgage any more, that would go as per the normal process—

CHAIR—Basically it is the interest component on the super that goes to repay the mortgage?

Mr CIOBO—No, it is not. That is what he was saying.

Mr Zeitoun—No. It is the money within your super. It is exactly the same as a redraw facility with a bank. Your super money therefore is just taken away from your outstanding balance.

Mr CIOBO—But that $100,000 in super, to use your example, is that being reloaned to customer No. 2 who comes in to take out a mortgage?

Mr Zeitoun—It would be reloaned, so through that inter-funding—

Mr CIOBO—It is not actually quarantined at all?

Mr Zeitoun—No. Well—

Mr CIOBO—But you just said before it was quarantined. My point is—

Mr Zeitoun—No. Within the way it would be structured, there would be a way to align it to your own specific mortgage. You would have to break it down within that fund. That underlying fund would be able to break it down into individual clients.

Mr CIOBO—Sure, but in case of a mortgage trust falling over, that would be because the total value of mortgages exceeds the value of the assets that underlie the fund—correct?

Mr Zeitoun—Yes, correct.

Mr CIOBO—That is why it falls over.

Mr Zeitoun—Yes.

Mr CIOBO—So, even if you tie it back to the individual mortgage, if a fund fell over, you would still lose a proportion of your super?

Mr Zeitoun—Yes.

Mr CIOBO—Exactly. This is my point: is it really safe enough?

Mr Zeitoun—Currently—

Mr CIOBO—Or do you view the level of risk as being equivalent to investments in the share market or whatever?

Mr Zeitoun—It is probably less. The main mortgage fund providers at the moment do not have all of their funds in mortgages. Actually, most mortgage funds at the moment have probably less than 80 per cent of the funds invested in mortgages. A mortgage fund on the risk return chart would be much less than a share market type fund, so it would be a lower risk.

CHAIR—In terms of taking out a mortgage for $400,000, we have $100,000 in super funds and $300,000 through a bank loan. What eventually happens to the super funds, because there is this $100,000 debt? Does that super fund money end up going directly into the bank or whatever?

Mr Zeitoun—No. The relationship would be with the same provider.

Ms GRIERSON—But the mortgagee still pays $400,000?

Mr Zeitoun—Correct.

Ms GRIERSON—Against a loan of $400,000?

Mr Zeitoun—That is right.

Ms GRIERSON—But their interest rate is lowered to the interest rate on—

Mr Zeitoun—No, the part within the super is put into the mortgage but is protected under the superannuation regulations. The actual superannuation is not seen within the mortgage fund; it is the interrelation between the underlying fund which funds the mortgages that provides this reduction of interest payable.

Ms GRIERSON—I am a little bit confused by it. You are saying that the profits of this deal are really only the savings on interest?

Mr Zeitoun—Correct.

Ms GRIERSON—How do they flow back to the individual?

Mr Zeitoun—The individual is saving their interest today and seeing the effect of that saving today instead of waiting until retirement. Therefore, by reducing the interest payments with their regular repayments for their mortgage, they would be able to pay off that mortgage more quickly and therefore concentrate on their super.

Ms GRIERSON—But the reality is to put $100,000 back into super, which is what they have to do if they want to stay in that home and not sell it, is a huge hurdle, is it not?

Mr Zeitoun—That is right.

Ms GRIERSON—The only benefit is if you are projecting that people’s income streams are much more lucrative after, and then they have to do a catch-up?

Mr Zeitoun—Well, this is only on the $100,000 example; there would be other lower examples, but it would work in much the same way as the current redraw type banking products.

Ms GRIERSON—Do you think that people under 40 would find that attractive?

Mr Zeitoun—Yes.

Ms GRIERSON—Do you think there are other things they would find more attractive to get them into super?

Mr Zeitoun—Not really. Speaking to peers and advisers, they were quite excited if something like this could be put together, because it would allow their clients to see the benefits today and benefits in the future.

Ms GRIERSON—Would they not just take out a mortgage on the whole of the amount when they are available now, so they do not need a deposit? You can see that this might be attractive if you just cannot get a deposit together?

Mr Zeitoun—I was not looking at it from a deposit point of view. I was looking at reducing the interest so that more of your repayments reduced the capital, so therefore your loan, instead of being over 30 years, would be over 10 years. Then later on you can concentrate on your super savings.

Ms GRIERSON—Thank you.

Mr CIOBO—On page 2 of your submission you suggest that the mortgage offset should be capped at 80 per cent of the mortgage value so that the mortgage is never paid out using eligible termination payments. Could you expand on that a little more?

Mr Zeitoun—Basically, I did not want to see the client in a position whereby the $100,000 equals a $100,000 mortgage, because then it just does not make sense. You cannot physically use your superannuation to pay off your mortgage. I wanted a bit of space between what is owed and what is being offset so that that scenario could not occur. Even though they are two different amounts of money, it could easily occur in theory with the amounts being the same. What are you actually paying off? You would have an excess amount in your mortgage which would defeat the purpose of what I am trying to do.

Mr CIOBO—Notionally, though, your return on your super is equivalent to your mortgage interest rate, isn't it?

Mr Zeitoun—Notionally, yes.

Mr CIOBO—You talk about providing a degree of attractiveness, and I ask this out of ignorance—I am genuinely interested—for those that are older and who have accumulated a fairly substantial lump sum in their super, does this not provide good incentive to just keep upgrading the home?

Mr Zeitoun—Part of how I would set this product up would be that you can only use it as an owner-occupier and only once. Are you talking about upgrading to a new home?

Mr CIOBO—Or extending it.

Mr Zeitoun—The mortgage is capped at the $400,000 mark. If their line was already at that amount, they would not be able to go in excess of that. If the rules of the product have not specified it, there is potential for people to do that if it is their first property that they are going to use this for. With part of this product, you would only be able to do it once and that would be it. But you are right, there is the potential for that to occur with the ageing clients.

Mr CIOBO—It would occur to me, going back two years when we saw a period of downturn in equities, and when returns of negative 10, 15 per cent were in order, that this is providing notionally a positive 6.5 per cent return, if you took that as the average. It would be pretty attractive for a lot of people to park funds in there. Do you see any implications from that?

Mr Zeitoun—Not really. It is already an option that you could invest in today in terms of a mortgage trust, and it is considered a more conservative investment today, already, so I do not see anything negative about it. It would of course depend on how the mortgage trust is structured. If your worry is—I know that some mortgage trusts recently—

Mr CIOBO—It is not a worry. I am genuinely asking, I am just trying to tease out what the positives and negatives might be.

Mr Zeitoun—The only negative I see for someone in the younger age group is that instead of having that money available for them as a redraw, it is no longer available as a redraw. Apart from that, you are basically getting people to save for their retirement at an earlier stage, because the people in their 20s and 30s are the ones getting the big loans which are not allowing them to save for their super. In this way, it is a sort of transparent relationship. They can actually see what their actual super is doing.

Mr CIOBO—As contributions came into their super account, they would be credited against—

Mr Zeitoun—Correct.

CHAIR—I think that provides an interesting model. All these people from Treasury are sitting behind you and I am sure they have their calculators out. We will ask them what they consider to be the problems with that type of scheme, or plusses. Thank you for your attendance today.

[1.13 pm]

COLES, Mr Anthony, Manager, Retirement Income and General Rules Unit, Department of the Treasury

GALLAGHER, Mr Phil, Manager, Tax Analysis Division, Department of the Treasury

LEJINS, Ms Erica, Department of the Treasury

LONSDALE, Mr John, General Manager, Superannuation, Retirement and Savings Division, Department of the Treasury

LOVE, Mr David, Manager, Corporations and Financial Services, Department of the Treasury

RILEY, Mr John, Senior Adviser, Financial Literacy Foundation, Department of the Treasury

CHAIR—I now welcome the representatives of the Treasury to today's hearing. As you have already given evidence, you know about the status of the proceedings et cetera. We have a written submission but would appreciate your input. This is the second time we have seen you. We look forward to hearing what you have to say. We have talked to a number of people. I would like to say that we have clear views in terms of the way forward. The reality is that is not the case, and there are a whole lot of questions to ask you as our views evolve. This is going to be one of the last of the formal sessions that we have, and of course yours is fairly critical. I appreciate what you will be able to tell us before we proceed to questions.

Mr Lonsdale—We do not have a particular opening statement, other than to thank you for this second opportunity to come and talk to you. You have our submission.

CHAIR—Yes, we do.

Mr Lonsdale—And our supplementary work that was submitted after the last public hearing process. We are in your hands.

CHAIR—Colleagues, there are a number of things that we wanted to talk to you about. Rather than us all have a go here and there, some of the issues that I think we want to talk about are: the cash back program; being able to use super funds as an offset against a mortgage—and you have heard one formalised proposal today—and the question of people who are below the threshold in terms of contributions. The committee heard that a whole lot of people that are being marginalised on an ongoing basis, often younger people, single mothers et cetera. Companies often seem to be structured so that they avoid paying the super levy. We wonder what we can do about that. We also heard concerns about women who generally move out of the workforce when they have children and they clearly lose a significant advantage then. There is also concern that small business owners are not required to make deductions, and what does that mean in the longer term? In addition, there are differentials in terms of small business people.

They have a tax-free threshold of $5,000 in terms of the super contribution and it is 75 per cent for the rest; whereas if they are employees and are paying themselves a wage they can have it all deductible, and is that fair? There is also the question of consolidation of accounts—young people putting funds into a range of accounts. Even a very senior person in the ministry that you have quite a bit to do with was talking about their offspring having multiple jobs, going to different accounts and then losing it by the admin fees that are applied—having the ability to consolidate that into one account. The ease of access in terms of the website that you have set up enabling people to do that is another issue. These are a few that we might get into collectively. We probably have our own list. Colleagues, do you want to add to that list? Maybe we could jump into it collectively rather than go round one at a time.

Dr EMERSON—Yes, I would like to add the $450—

CHAIR—I mentioned that. I suppose thresholds is another one in terms of the different age cohorts that we currently have and whether that should be abolished overall.

Dr EMERSON—Paid maternity leave.

CHAIR—That is the question I have raised of women in the workforce having to leave and what incentives we can provide. We have the baby bonus for upfront expenditure but what about the continuation of being involved in super? Are we marginalising women and treating them differently because of this? Is there anything further?

Dr EMERSON—We had a discussion, I think before you came, about the extent of the concessionary nature of superannuation taxation, and we have had some witnesses saying there is very little in it these days. I do not agree with that, but it would be good to get to the bottom of that.

CHAIR—There is also the age differential factor, particularly for the under-30s. Is the incentive for the tax concession and putting money into super discriminatory in terms of that age cohort, when you consider the amount that is being earned? For the majority, the tax incentive would be not there or even a negative tax input. Shall we try to do that in bites and see how we go? Perhaps we can start with the proposal to use super for mortgages, as one person suggested—he recommended that 50 per cent of all super for those under 35 could be used for any purpose—and the offset proposal that you have heard about.

Mr Lonsdale—That is quite a comprehensive list of issues.

CHAIR—Those are just a few of our concerns.

Mr Lonsdale—Any one of those we could spend a long time on. We are happy to talk about all of them. As I said, we are in your hands. Before we get to the specific ones, if I could just make a general comment on the proposals or the package of proposals that we tried to bring out in the submission, and that is, it is very important to be clear about the problem. One of the themes that we bring out in the submission is that coverage rates for people, or for employees in general but particularly under-40s, are very high—in the nineties. We have total contribution levels increasing.

CHAIR—Is this the co-contribution scheme?

Mr Lonsdale—No, total superannuation contributions increasing in the data that we have presented in our submission.

CHAIR—Is that related to just salary levels going up overall? The actual quantum does not tell us much. What we have been told is that the actual level of voluntary contributions has gone down.

Mr Lonsdale—That is correct. In the submission we disaggregate that into SG components, voluntary components and additional components. It is true that there has been some reduction in additional contributions for the under-40s. In the submission we outline a range of possible reasons for that, and it could link to poor investment returns in the period that we present. It could relate to the closure of some corporate funds and how that relates to defined benefit funds. It could relate to the increase in the SG rate at the same time. It could be a whole range of things. Depending on where you come to and the reason, that can drive where you actually go to.

We present what we think are quite high replacement rates for people who are under 40 who contribute to super for a long time, say 30 to 40 years, with an unbroken work pattern. We set that out in the appendix to the submission. Coupled with that we provide projects that come from Mr Gallagher on the co-contribution take-up that we think will happen. That, I think, provides quite a noticeable turnaround in additional contributions or the voluntary part. When you put all that landscape together it is important to try and come to some conclusions, and that can be very difficult.

CHAIR—I think there is an interesting point that has just been pointed out by the secretary of the committee. Chart 8 shows that the SG system in conjunction with the age pension is projected to provide a spending replacement rate of 82 per cent for an individual aged 25 now who is on medium earnings in the next 40 years of future contributions. The question is: what if there was no age pension component? What happens then?

Mr Lonsdale—The age pension component is a critical part of that calculation and has been a longstanding part of our retirement incomes policy. It is in fact the first pillar. Can we shed any more light, Phil?

Mr Gallagher—Yes, in the *Intergenerational report 2002-03*, we shows that the age pension expenditure was projected to go from three per cent then, 2002, up to 4.6 per cent of GDP. More recently in 2005, the Productivity Commission has re-conducted that exercise and got essentially the same result. They got 4.6 per cent of a larger GDP, but they did get 4.6 per cent. This gives us one of the most affordable age pension systems, and that includes the full MTAWE indexation of the pension, and it includes the indexation of the pension income test and asset test thresholds to the CPI as is legislated. So we have a very affordable system. We have a three-pillar system. The first pillar is an important foundation of the system. We do not have any political party in particular talking about removal of the age pension, and I think we have demonstrated it to be affordable. Normally we would not project without the age pension, because it is the foundation of our retirement income system. It is particularly important for women, and it will be particularly important over the shorter term when people who have not had 30 years accumulation, as the under-40s will, come to retirement.

CHAIR—Let us proceed.

Mr Lonsdale—That was basically the general comment, other than to say that, when we talk about under-40s, we are talking quite generally. I think in the submission we highlight some special cases where people may have broken work patterns and that may impact on their superannuation—for example, lower participation rates—or people who are not subject to the SG, and how that relates to superannuation going forward and retirement incomes. The comments that we are making are quite general in relation to under-40s.

Dr EMERSON—What you seem to be saying is that, apart from a few problems such as broken employment, perhaps we will get to the thresholds where people do have to contribute SG. The under-40s problem is not acute because they are in there, they are at nine per cent and they have a hell of a long time over which to accumulate that nest egg. Is that right?

Mr Lonsdale—That is correct, the replacement rates are very healthy.

CHAIR—Can we just perhaps go through some of your views—I think I can anticipate what you are going to say—about using part of your investment in the super scheme towards mortgages et cetera.

Mr Lonsdale—I think the key policy issue would be what affect that has on the overall objective of retirement incomes policy and how such a change would add to someone's retirement incomes. If you are taking money out of the system then we think that that would impact on the end result that you would get, and that is broadly the policy issue.

CHAIR—Yes. On one hand it may make it more attractive. I do not know whether you have done any modelling because it is going to be a subjective judgment; I am not quite sure.

Mr Gallagher—We have. Back in 1997 we did some modelling in the Retirement and Income Modelling Unit, which was published and is available on our website. I am certainly happy to table this paper. Essentially, we showed that with the policy being advocated by the Real Estate Institute at that time, 1997, we could decrease national financial saving to the extent of 0.18 per cent of GDP by 2019-20, because you are taking money out of financial accounts and essentially locking it up into the value of the housing stock. You have the problem that it does not provide a retirement income. There are also significant issues with the targeting of this policy. The people who are at the margin may not be the ones to access it, because the people who have healthy contributions and therefore have the money to make use of it for their housing are probably not marginal in terms of their access to housing. There are always problems, certainly in a universal system like superannuation, in any targeted implementation of a policy. We have had a number of release tribunals that have looked at this, and there have been great difficulties in deciding, on a welfare basis, who should get their release of superannuation money for particular purposes.

Mr Coles—I guess the other issue involved in all this is that it adds another level of complexity, not only in respect of the superannuation fund. I think it has been suggested that only one set of money could be taken out in respect of the superannuation to set up the mortgage offset account or to allow for the withdrawal to pay for the loan for the house, but who is going to do that? How does the super fund know that person A has not got another superannuation fund with another account holder? Are the superannuation funds supposed to identify? Is there supposed to be a central database and so forth? The targeting of the concession—how do we identify that? We are building a much more complex, much more difficult system for, as Phil was saying, who is going to benefit? Is it going to benefit people on lower incomes who want to buy their first home, or is it actually going to benefit those who want to get a larger house?

CHAIR—Yes, I think that the general view of the committee is turning in your direction at this stage so we will not spend more time on it. What about the marginalised group, those who fall within the $450 a month threshold, and where employers seem to be structuring employment so that they fall below that; also women and the self-employed? I do not know where you would like to start on that. What are the issues in terms of, say, abolishing the threshold on the $450 a month process?

Dr EMERSON—Or dropping it. I think you could either abolish it or lower it significantly—and we have discussed this in your absence. It is $450 per job and it is not uncommon for young people to have, say, three part-time jobs, so it could be $1,300 worth of income each month attracting no SG. As the chairman said, I have heard anecdotal evidence and material in writing that, in the restaurant industry in particular, it makes good economic sense for the restaurateur to put on a lot of staff, keep them all under the limit, and then save nine per cent of the wage costs. That is why we are interested in whether that $450 could either be abolished or lowered.

CHAIR—If you look at the evidence, I remember that the people who provide the super predominantly to the restaurant and catering industry were in agreement that there was some rorting going on in terms of that with companies, restaurants and others. The major providers did not seem to have a problem with abolishing the threshold, especially as it relates to people who are often marginalised, single mums who have other responsibilities et cetera. Your response?

Mr Lonsdale—Just in terms of background first. I think it is important to note that the SG exclusion threshold has remained the same, I think since 1992, at $450 per month. It has not moved. In that time we have had real wages growth as well, so that has, I guess, pushed many people who were previously below the threshold into the SG system, which has meant significant growth. It is an issue that has been looked at several times before. The key policy issue on whether to move it one way or another, or abolish it, is the effect it has on employers and that can be difficult to assess.

Ms GRIERSON—Do you think there may be a push towards a black economy in those low-paid areas again, where people get paid cash in hand rather than a proper payment to avoid that?

Mr Lonsdale—I am not going that far. The simple point I am making is that if we were to reduce the SG exclusion threshold, that would be an additional cost to employers and that would need to be met in some way. Depending on how you saw that filter through, that would either have an effect on the labour side or on capital, and the incidence is unclear. That is the typical key policy issue that is presented on that.

Ms GRIERSON—Why would you not just adjust it in line with the increase in wages? Why has it not been increased to keep pace with wage increases?

Dr EMERSON—We did not want it to increase. We want it to fall; we do not want it to increase.

Ms GRIERSON—Sorry, that is what I mean—fall in accordance with that.

Dr EMERSON—We want to stay constant in nominal terms, at worst.

Ms GRIERSON—Yes, that is right.

Mr Lonsdale—What we are saying is that the threshold has not moved.

Ms GRIERSON—Yes, you said that, since 1992.

Mr Lonsdale—Yes.

Ms GRIERSON—It seems that you are singling out, or the policy is singling out, people on low incomes. Given that the job increase has been in part-time and casual work particularly it is more likely that it is impacting on more people.

Mr Lonsdale—Which policy is that—the policy to keep it where it is?

Ms GRIERSON—To keep it where it is.

Mr Lonsdale—The point I am making is that the fact that the threshold has remained where it is has pushed more people into the SG system as wages have grown.

Ms GRIERSON—I am not sure that we can make that direct link.

Mr Coles—One of the issues that need to be taken into account is that at the introduction of the SG legislation there was consideration as to what threshold it should be set at, and the original argument was that it be around about $250. The reason that that did not proceed was on the basis that that nine per cent of $250, back in 1992, would probably be eaten away by fees and charges.

Dr EMERSON—They would not get anything.

Mr Coles—They would not actually get anything. I think what John is getting at is that more people are now capable of earning $450 in that month and will be getting their superannuation. Therefore, it is a balancing of the policy rationale as to how much should be given to these people to create their superannuation savings, and how much of that is going to be an effective mechanism to actually give them something for their retirement income that will not be eaten away by fees, charges and other expenses.

Ms GRIERSON—What if a person has four different super funds. I know that amalgamation is a little bit easier and choice is a little bit easier. Is there any way to amalgamate salaries and capture it without putting that burden on the employer? Is there any way for government to capture that lost income, in terms of a super contribution and SG?

Mr Coles—The rationale is that the best way to get people involved in their retirement income is to get them thinking about their superannuation and what it means to them—to actually start educating and providing further assistance to them so that they understand the value of their superannuation.

Mr McARTHUR—You are 33; how do you think about when you are going to be 65?

Mr Coles—I might hand down to John Riley who is with the foundation.

Mr Riley—In the Financial Literacy Foundation we are basically trying to increase the financial knowledge of all Australians so that they better understand their options and choices in using and managing their money. We are implementing a national strategy that will include an information and an awareness raising campaign to draw attention to the issue. There will be website and a handbook associated with the campaign so that people can go and find out some information and understand that, irrespective of the amount of money they earn or where their starting point is, if they manage their money a bit better, it will have real benefits for them. In terms of people under 40 and so on, we are not focussing specifically on superannuation. It is a broader range of activities that we are involved in.

CHAIR—Are you talking about the information aspect of it, because I really want to focus on the—

Dr EMERSON—on the marginalised—

Ms GRIERSON—I would like to press the point. I will give you an example of my young daughter who has four employers, only one of those is capturing any super; she has an SG on it. The others are obviously people in catering and hospitality who have huge numbers of young people on their books and they never reach that threshold and therefore never have to pay. That does not seem right to me, and nor will it promote her interest in retirement saving or in being in a superannuation fund.

CHAIR—That is part of it.

Ms GRIERSON—It makes them cynical, it makes them dismissive of those sort of measures. I will press the point. I understand the risk. I know of instances where people are paid cash in hand in that field as well, continuously and constantly with young people. I will say to them directly: ‘Why are you doing that? If you get injured, all those things happen you, the risks, you are getting no cover at all.’ They say: ‘Well, we want the job. Someone else will have it if we don’t do it.’

CHAIR—Especially if it is taken in conjunction with the recommendation of a consolidation. Super companies are saying how difficult it is. It must be possible and we have asked them to come back to us.

Ms GRIERSON—I am wondering if it is possible for, say, government, the Treasury, to tender a service like that, that assists young people to amalgamate their super or their incomes in a way that would benefit them. Would a superannuation fund be interested in taking on that challenge, or is it just not worth their while? But it would be worth their while if there was some government incentive or subsidy to assist that?

Mr McARTHUR—Mr Riley, if you had a 30-year-old son, how would you persuade him to take on super? What would your line be, with all the wealth of knowledge you guys have got?

Ms GRIERSON—With wealth you just make co-contributions for them.

Mr Riley—I think we would look more broadly at the benefits and the options and choices.

Mr McARTHUR—The objective and the whole point of our inquiry is to get them into super. I want to know how you are going to convince your 30-year-old son to take it up, and take a bit more than the nine per cent.

Mr Riley—There is a whole range of things there and incentives in place that my colleagues here are better placed to talk about, co-contributions being one of them.

Mr McARTHUR—It gets down to actually persuading the individual, because basically the other evidence we have had is that there are a whole lot of disincentives for them to take it up. They have other commitments: they have the housing loan, they have education. Why should a 30-year-old even be interested? If he is paying his nine per cent, how can you persuade him to put a little bit more in? Why should he do that?

Mr Lonsdale—It is an interesting point. I think it goes to the retirement income system that we have. One of the foundations of it is that people are generally myopic—they value present consumption much more than future consumption, and because of that they do not contribute to superannuation or broader retirement incomes in the absence of the SG.

Mr McARTHUR—I want you to tell me why you guys would get your own son or daughter to take it on. Just a theoretical—you.

Mr Coles—In essence—

Ms GRIERSON—Contributing voluntarily to their super. It is interesting, isn’t it?

Mr Lonsdale—You need to think about their remuneration as a whole. Part of what we are saying in our submission is that a person starting now in employment—so it is a different issue from what we were discussing a bit earlier—will have nine per cent of their income contributed, if they are an employee, into their superannuation. It can be perfectly rational for that person to invest in other things. They could be buying their own home. Owning a house is an important cultural part of our society, and that costs money. They could be doing further education. They could be paying off a HECS debt, which is also important. They could have other forms of savings. Because of the preservation rules and so forth, the money will be tied up until they are aged 65. They may wish to invest in the share market or in other housing. I think while superannuation is a very good and a very important vehicle for retirement income, when you look at the life cycle—the government has implemented a mechanism to enable individuals to save for their retirement through superannuation, through the introduction of the SG, through the co-contributions, which is a great vehicle for $1,500 return—it does not mean that other vehicles are not better or more targeted or more suited to that person’s individual needs at that time. It is a balance, and I guess from the government’s point of view, it is part of their choice.

One of the things I was coming back to is that if you get people involved and they have some sort of control over their superannuation, that gives them some sort of choice as well. It is a different issue as to whether they can—if they are below the threshold and not able to contribute to superannuation—but if they are educated from childhood to see the value of savings, to actually understand important things about budgeting, then that will get them into a position to think about things.

CHAIR—There is a different level of taxation according to the choices that are made. If they invest in their own home, there is the tax on the way in, but there is then no capital gains tax at all. If they invest in a second property, there are negative gearing provisions. If they invest in shares, they can take the interest component off their taxation as well. You have competing areas to try and provide the incentive. That is the issue.

Can I take you back to the marginalised group, in particular women who leave the workforce. I do not know whether you have given any consideration to what we can do in terms of that grouping within the community, especially if 40 per cent of marriages end in divorce. There are a lot of women who will not have the benefit of contributing during the years of childrearing, and yet at the end of their working life they will have inadequate superannuation cover. It is an issue that has concerned us when looking at that marginalised group.

Dr EMERSON—The baby bonus on the government side and on Labor's side—I think it is called a baby bonus—are both in lieu of paid maternity leave from a business. Can you clarify that if a business offered paid maternity leave under the superannuation guarantee it would be subject to the nine per cent guarantee, under an award, an agreement or whatever? Is there merit in considering, as a good employer if you like, the Commonwealth of Australia—offering paid maternity leave and having a belief in superannuation itself—that nine per cent of the baby bonus should go into superannuation? That is just meant as a subset of the question that the chairman put to you.

Mr Lonsdale—I think we would have to come back to you on that particular question. On the broader question of women and superannuation, women with broken work patterns, what we would point to would be the general context and the general policies that are in place now. We have had some quite new ones in relation to superannuation splitting. We have the co-contribution. We have transitions retirement, which seeks to maintain the link with the workforce for people who have reached retirement age. There is a whole range of direct policies that we set out in the submission. The other contextual point is to note that participation rates for women have been on the increase recently. Again we have set this out in the submission. That is a general—

CHAIR—That would reflect the general increased participation in the workforce, but what about the case, for example, of a woman who is married to a plumber and they have three kids. She has been out of the workforce for years, and because there is no mandatory requirement of SG contribution he has not got a super scheme. They divorce. There is no super splitting there. We have an increasing number of small business people—

Dr EMERSON—That is right. Self-employed.

CHAIR—Self-employed, contracted out. That tends to be the trend. Those two factors are a concern when you are treating people differently. You have some degree of safety net in terms of super splitting and so on, but where they have not made adequate provision, then again you have a disadvantaged arrangement.

Mr Lonsdale—It is very difficult for us to comment on particular cameos that you put to us.

CHAIR—But it would not be that unusual because of the large number of small businesses—

Dr EMERSON—and growing.

Ms GRIERSON—and patterns are established.

Mr Gallagher—The issue really is how the property of the marriage is divided, it is not superannuation. Superannuation and divorce; as a policy it does not deal with it because there is no superannuation, but there is a lot of divorce law which goes to the issue of matrimonial property.

CHAIR—It still does not—

Mr Gallagher—If instead the investment has been in the person's own business, I presume there is some degree to which the family law takes that into account.

CHAIR—You do not deal with as many cases as members do.

Mr Gallagher—No, obviously not.

CHAIR—With child support, to know how contentious that area is.

Ms GRIERSON—Split with child support.

CHAIR—You are creating a lot of marginalised women in terms of super for the future, which is a concern of the committee. Anyway, perhaps we are not going to resolve it now.

Dr EMERSON—You would not easily be able to do this modelling but it seems to me it would not be impossible. You said at the outset that you have done modelling on the adequacy of nine per cent, and you are getting high replacement rates—that is, it is basically adequate. The chairman is saying that there are a whole bunch of people who are not getting the nine per cent, to which you are then saying, 'That is true but we now have the co-contribution, super splitting and so on.' Is it possible, given the very short period of the life of the co-contribution, to do some sorts of projections or educated modelling to see how many people could end up effectively falling through the cracks? Because you are not going to get the same sorts of conclusions about adequacy for these people as you have for the 'nine per centers'.

Ms GRIERSON—Of course this is assuming continuous employment, which is not a pattern that most women enjoy—more and more yes, perhaps.

Dr EMERSON—That is right, it assumes they all get the nine per cent.

Mr Gallagher—It is easier to do the cameo analysis which relates to broken work patterns. In fact, the cameo analysis of that sort is already published because it was in our submission to the Senate select committee.

CHAIR—Do you know what it is in terms of?

Mr Gallagher—In terms of doing the modelling for the population, as Dr Emerson has requested, I think that is more complex because the dynamics involved in terms of the overlap of the co-contribution population, and particularly the divorcing population, are not captured in our major population model ring group. The sort of question that you are putting to me is what the National Centre for Social and Economic Modelling is pushing—the development of a dynamic micro simulation model, because it has to be addressed in much more finer detail than the current modelling. I cannot do a population analysis. I can do an analysis of a given family and say: 'They have this asset and this contribution pattern, and this happens at this point. What does the retirement income look like?'

Dr EMERSON—Could you not do, either now or fairly readily, at the very least, the changing proportion of the population whose income will be derived as sole traders, individual contractors and so on?

Mr Gallagher—Yes, we can do that.

Dr EMERSON—Which has to be a very rapidly rising proportion.

Mr Gallagher—It tends to be age based. It tends to rise significantly after the age of 45. People start off their working lives as employees. As they become more skilled they get to the point where they can manage the business themselves. In those situations you get the situation where a person will likely still have preserved superannuation from their period in employment, but when they become self-employed and establish the business, they may not contribute in that period because of the nature of their cash flows.

CHAIR—We appreciate the figures on that of the numbers that we are talking about. Also, what was the reasoning in the first place for them not having the same level of tax concession as an employee? Do you know what the reason is?

Dr EMERSON—We are talking about an unincorporated small business.

CHAIR—Yes.

Mr Coles—For self-employed? I can only provide a general summary. It goes back over time. It goes back to before broad superannuation was introduced through the award superannuation and through SG. I guess it goes back to the 1980s as well, so it is a bit of a long tawdry story. If I can just provide a summary—

CHAIR—Tawdry; that sounds interesting!

Mr Coles—In the eighties there was a general reduction provision for moneys put aside for provision of a life insurance or superannuation benefit where you were not in receipt of some sort of employer support, or some other support for superannuation; that was a general deduction provision. I think that back in the eighties it was about $1,200. So it was a significant change. Through that time there was the introduction of award superannuation, and then later through broader changes to the retirement income and superannuation system. With that there became a distinction around the 1990s between people who are unsupported, who receive no employer support and no other support, and those who receive support from their employer. With the introduction of the awards—and this is where I am going to get a little bit fuzzy—I am not entirely certain that the awards were incorporated as part of the employer support; I think it was an outside agreement. People in receipt of awards were considered to be supported. This meant that they were able to claim a deduction for life insurance and superannuation.

We had the introduction of the super guarantee in 1992. If I go back to the 1990s, in order to distinguish between the people who were in receipt of awards and those who were receiving no superannuation, the government introduced the mechanism of the 75 per cent rule. So the self-employed or unincorporated person, or the person with no superannuation support, got their deduction plus 75 per cent of their other contributions as a deduction to distinguish them from the fact that people who were in receipt of awards were getting employer support or some sort of additional money for their superannuation for retirement income purposes.

In 1992, we had the introduction of SG. Also around about that time, the government removed the fact that people could claim a deduction for their personal contributions. They were not eligible where they had receipt of employer support. They kept the rules in place for people who were unincorporated or self-employed individuals—the $3,000 plus the 75 per cent of additional moneys. Then I think in about 2002, the $3,000 was increased to $5,000. It is a long story but it goes against the change of employment practices and retirement income practices to allowing everyone a deduction, to allowing a limited deduction.

CHAIR—The problem is that you have two systems working side by side; one is compulsory and one is voluntary. One is fully deducted and one is partially. That is the problem.

Mr Coles—The other story in all of this is that—and I could only hear part of their evidence—the Office of Small Business seem to indicate that there is a distinction between deductibility, particularly in relation to unincorporated individuals. It was said that individuals could incorporate and get the same deduction provisions. People who do not want to incorporate can also contribute to their business, and often they do want to build their business and they do not want to contribute to their superannuation; they grow their business as their form of retirement income. If they meet the CGT rules, those people are exempt from the application of the capital gains tax up to $500,000, where that is rolled into their superannuation fund. That means it is a rollover. It is not treated as a contribution, so the money can be used for their superannuation fund to fund their retirement income. The deduction provision is one aspect of the package that is available to small business people and to the unincorporated self-employed. There is this other aspect that allows people to build their retirement income through their business.

Mr Lonsdale—I think when looking at self-employment that is the important point. It needs to be a holistic look, so not just on the deductibility side but also on the CGT side. I think that is the key point.

CHAIR—Mr Gallagher might know the answer to this: what percentage of small businesses fail within the first five years?

Mr Gallagher—I do not know that off the top of my head,.

CHAIR—It is relevant in terms of your saying, 'Well, people can use the investment in their small business for their retirement.' If the figure that is often bandied is that around 90 per cent of them fail in the first five years then that argument becomes redundant, except for about 10 per cent of the ones that go ahead.

Dr EMERSON—Commissioning a bit of work; you said you would come back on the paid maternity leave issue. Can I just confirm that what I am asking is this: in the private sector and also in the public sector where an award or agreement says that you will get paid maternity leave, does that include the nine per cent superannuation guarantee? And, irrespective of whether it does or not, is there any merit in—and I know it is difficult because you do not create policy but you advise on it—in having Commonwealth provided paid maternity leave to include a nine per cent superannuation contribution, as a good employer. That is the first one. The second is goes back to the $450 limit. I think, Mr Coles, you made the point that in 1992 about $200 was seen as being a level where the transactions costs through fees would wipe out any benefit in any event.

Mr Coles—$250.

Dr EMERSON—Since then the superannuation industry has matured, there have been technological advances and it has become more competitive. I would wonder whether that $200 is still right, and even if it were, would that not be an argument for taking the $450 down towards the $200 if we do accept that there is some level at which fees would wipe out any benefit? I am wondering whether $200 is still the relevant figure, given that in 1992 the superannuation industry was not very mature.

Ms GRIERSON—We still see teenage unemployment rates at over 27 per cent. One has to wonder whether there is a problem of people not being paid proper salaries.

Dr EMERSON—I think it would be an easy piece of modelling in terms of my final point. You said something really, really profound at the outset, and that is, nine per cent for a person who has pretty much continuous employment is in fact an adequate retirement income, and you had very high replacement rates coming out of that figure. Is it possible to just put in 12 per cent and see what that does in terms of replacement rates and so on, without prejudging whether that is compulsory? Just say hypothetically people went to 12 per cent, what would it look like?

CHAIR—I think it is an interesting question.

Mr Coles—Can I just go back to that last quick point. I refer you to appendix D at page 59 of the submission. It actually does have super guarantee plus three per cent additional savings. It has a range of impacts.

Mr Gallagher—That is right. It has been done in a way that it is best financially to do it, so for someone on a lower income it is done with a co-contribution. And for someone on a higher income the analysis is done with salary sacrifice at higher incomes.

CHAIR—Yes, we have it.

Mr Gallagher—We gave you the full paper at our last appearance. The paper that is referenced there I tabled at the last appearance.

CHAIR—I refer to some comments in paragraph 15 of the submission by the Small Business Office and you might want to come back to us on it. It states:

> Members of the Small Business Council, and its predecessor, the Small Business Consultative Committee, have considered this differential treatment, suggesting that it appears to be inequitable for business operators to be subjected to separate superannuation deductibility arrangements purely because they operate under different business structures.

That has been in their official submission, so appreciate that in light of what we said on small business.

Ms GRIERSON—It has been suggested to us in one submission that, given young people have so many competing needs now with HECS, mortgages et cetera, and that the patterns of work are changing, particularly for women who are in and out, or part-time workers, the age based deduction limits should be done away with—they should have a lifetime deduction limit rather than be age based. This would mean that people can put more in when they have the opportunity, and not put so much in. Do you have any view on that?

CHAIR—It was raised with us several times and it seems quite an interesting proposal.

Mr Lonsdale—As you know, the government provides a very significant tax concession for superannuation, around $16 billion I think is the latest tax expenditure statement. There are two key limiters to that tax concession in the system. One is the RBL system, which aims to limit the tax concession of the stock of superannuation coming out.

CHAIR—Which has the age component within it, hasn't it? I am sorry; it has not.

Mr Lonsdale—The age based limit is at the front end. It aims to limit the flow of funds going in and it does that according to three key age brackets. It is very much a policy issue and one that we highlight in the submission. I think the pivotal issue here is that if you are going to remove or amend these limiters in any way, the question then becomes: what would you put in its place? Is anything needed in its place? Would that create a behavioural impact into superannuation and affect the sustainability of the system?' It is that key question that would need to be addressed.

CHAIR—Because we are looking at possible recommendations, the key factor is in knowing why the age limit was there in the first place. I presume it was to try and limit the number of tax concessions that were occurring, but the reality is, in terms of voluntary contributions, it is relatively low in this age cohort, and would this be an issue?

Mr Lonsdale—For the under-40s we highlight in the submission that very few people come close to the age based limit. The vast bulk of people would contribute up to around $5,000 in deductible contributions, and I think the limit is around $14,500 or $15,000. There are very, very few people up around that mark, and I think we have a chart in the submission that illustrates it.

Ms GRIERSON—What about the co-contribution? You have had enough time to draw some conclusions about who is taking that up?

Mr Gallagher—We tabled the results at the last hearing of the committee, which I have not brought again with me, in terms of the contributory pattern. There is also material in our submission in terms of the age distribution of the co-contribution.

Ms GRIERSON—Does it validate my personal experience that the only people I know who are putting it in are wealthier parents for their children?

Mr Coles—There would be no way that we would know.

Ms GRIERSON—It would be hard to know, wouldn't it?

CHAIR—Aside from the discussion about those who would use it as a tax avoidance mechanism, chances are they are going to be into negative gearing or some other aspect of tax avoidance anyway.

Dr EMERSON—I guess our point is—without thinking one way or the other because I am not sure—if the aged based limits are not a binding constraint, the first argument is, 'Why have them?' The answer could be to prevent not diligent savers but young merchant bankers who are saying, 'How can I find a little tax opportunity here,' and then just whacking three quarters of their pay into super. Is that why the limits exist? Is it effectively an anti-avoidance device?

Mr Coles—I guess the key issue here is one of balance. A balance has to be chosen somewhere and we have the balance of the age based limits. The larger limit is for older people to put more money away on the basis that they may not have had an opportunity to save a bit earlier; younger people have a lot longer to save.

The other key thing is that we do not limit contributions, you can still put money into your super, it is still a concessional environment, you just limit the amount of tax concessions directly available to that person.

CHAIR—There are some whose earnings earlier are going to be larger than later—sports people, those who are involved in a lot of physical activity. The other item is in terms of contributions tax, all the industry groups and taxation people recommended that we abolish the contributions tax. We understand that is worth about $3.3 billion in terms of revenues.

Mr Gallagher—That is an industry estimate, it is not a Treasury estimate. The Treasury estimate would be appreciably higher than that.

CHAIR—What would it do if you abolished the contributions tax on those under 30? The lower tax rate may be an incentive on the way in for people as they mature and get onto higher incomes such as those on 47½ per cent, but those who are on lower tax rates below 30 per cent, it is almost a disincentive. If you actually abolish the tax contribution for under-30s, what would be the tax implications for that and what would be the problems?

Mr Lonsdale—There are a whole range of issues. Part of the issue with contributions tax removal or reduction is how you define and design that. Different people have different views about that; that impacts very much on the costs. In terms of the proposal that you put forward, a targeted reduction in contributions tax, complexity is one issue that comes to mind. We have a superannuation tax system at the moment that is quite complex. That complexity is concentrated very much at the back end but I think that to separate contributions tax would add incrementally to that complexity.

Another key policy consideration would be the impact of such a cut on savings, firstly private savings, and whether there would be an increase. Would there be switching from one form of savings to another? If there were to be a significant cost to the Commonwealth budget, if that were not offset by taxes elsewhere or reductions in government expenditure, that would be a negative on the public savings side. It would need to have careful consideration of the overall effect on savings.

Ms GRIERSON—What about removing it as an incentive for people for the very first time, young people or women who have not ever taken up super and have never paid a voluntary contribution? There will always be complexity but what about looking at young people, people under 40 who have never started, they are under 40 but have never made a voluntary contribution to super. Is that much of an incentive, a 15 per cent saving on putting that in? Can you target it only at people who might like to kick start their super?

Mr Lonsdale—It depends on what you are trying to achieve. I have raised complexity, but the other issue is what effect that might have on someone’s savings over all and it is very difficult to know. Somebody may put more into super because we are providing more of a tax concession but on the other hand they may wind back savings elsewhere.

Ms GRIERSON—There is a long-term saving to government eventually down the track as well, if people do start increasing their retirement income or retirement savings, is there not?

Mr Lonsdale—The point is that there is a trade-off. There is also a key equity issue as well; careful consideration would need to be given to who would benefit most from a cut in contributions tax. Those people who are best equipped to put in and make contributions will have the largest tax benefit.

Ms GRIERSON—That perhaps did not apply when you introduced the co-contribution scheme?

Dr EMERSON—We talked about the model which you reported on in this document in terms of going to 12 per cent. We also have separate figures, not from Treasury but from the *Intergenerational report* to which you referred. Concerning the age pensioners’ share of GDP now and in the early 2040s, if super went to 12 per cent, what would the age pension be as a share of GDP in the 2040s?

Mr Gallagher—An earlier analysis of that type may well be in the document that I have offered the table, which is the 1997 conference paper.

Dr EMERSON—Given that you have the *Intergenerational report*, you would be able to do that. It would be interesting to see in today’s dollars how much saving in the age pension could be achieved by moving from nine per cent to 12 per cent.

CHAIR—That comes into the figures that you talked about before.

Mr Gallagher—I will take that on notice.

CHAIR—A submission that interested the committee from the Australian Administration Services industry and Fiona Galbraith put it forward in terms of a cash-back scheme for under-40s whereby, at the end of the financial year, there would be a cash-back in terms of super productions. I presume this is just another way of government incentive and pay out and so on. I believe we should be asking for your response.

Mr Lonsdale—We have looked at it in a very high-level sense. It is always difficult to comment on specific proposals because of the design issues. Broadly the issues are as we have outlined them already. If the government were to contribute to a cash-back proposal how would that match with overall savings, how would that match with the complexity of the system?

Mr Coles—The other issue left unclear from that submission is its interrelationship with the co-contributions. Are these people going to get the co-contribution and the rebate? Will they have to have a choice? How is that determined, by the superannuation fund or by the government, considering that there is automatic reporting by funds of contributions which are not deductible or after-tax contributions by the individual? It is an interesting proposal; it would cost money and would impose a range of complexity issues for both the ATO and for industry.

Ms GRIERSON—It seemed to be very attractive to the ‘want it now’ generation. That is the way they are.

Mr Coles—Does it produce a culture of saving?

CHAIR—The committee I think would be in general agreement with you. What about the consolidation of accounts in terms of all these small accounts; is this feasible from your perspective? All the small ones, and maybe there is a limit that is put on how much these small accounts can be consolidated, a dollar value. It has been pointed out that one of the ways that young people lose interest is because with multiple jobs they lose track, the admin fees chew it up and there is nothing left. What is the feasibility of consolidating into one fund? Who should administer it?

Ms GRIERSON—Cheap brand super you want that does it as a cheap product.

CHAIR—The website you have where people can access, does that seem to be working or do we need something simpler? Should it be Treasury that does it?

Ms GRIERSON—When we had Mr Turnbull here, he was quite keen for everyone having their own personal email addresses.

CHAIR—Email ID which they keep for life, as a way of tracking them down.

Mr Coles—I get enough spam as it is; I am not sure that another email address is going to help. I did not quite understand how that email address would work.

CHAIR—It would be like an identity card. The problem is tracking people down, they change addresses.

Ms GRIERSON—It stays with them for life. Somebody has to be the provider and I guess it might have to be government.

Mr Coles—The general philosophy of the government's position in relation to these accounts is that choice and portability is the most effective way for people to keep control of their superannuation. They have introduced these changes to enable people to consolidate their accounts.

CHAIR—Be careful of the extent to which you are speaking in terms of the government. The choice and portability is fine, but in terms of this particular age cohort I do not think you could effectively say that it is the government's view that it all should be separate and portable and choice when you are talking about this lower end of the spectrum.

Mr Coles—As a philosophical basis I think the position is that to give people ownership of their monies is to engender interest into maintaining that. Prior to the choice, prior to the portability arrangements, an employer could put people into various accounts and different superannuation funds that suited the employer at that time. By having individuals able to consolidate those monies is a good thing. Is it sufficient? There are quite a few lost members out there. The definition of lost member is someone who is uncontactable by their fund in one or two years, depending on the rules of the superannuation fund. Once those people are not able to be contacted, that money is then listed on the register and that fund keeps maintains that money. It is not lost in the sense that the person can find their monies by finding themselves in the lost member register. The ATO is the organisation that is in charge or responsible for maintaining the lost member register. There are two mechanisms in place to help individuals find their superannuation. The first is the SuperSeeker. From a personal point of view I did look and see if I had any lost superannuation monies because I thought I did. I did find it on the ATO website and once I got to it on the ATO website I found it quite easy to use; all I needed was my name, date of birth and tax file number. Once I found it on the website I was not able to find any lost money. My wife then discovered that when I was in my 20s I actually took my money and ran. At the time it was less than $500 and I am sure that I spent it on something that was very important to me at the time.

From an individual's perspective, it is a relatively easy mechanism to use for people who have access to the IT technology and can find the ATO website. SuperSeeker also enables people to ring up the ATO with their information and the ATO will search for them.

Organisations and superannuation funds use SuperMatch. They are given authorisation by the ATO to search for monies to help people consolidate their accounts. I know through our discussions with industry groups and individuals that superannuation funds would now have included in their form, authorisation to enable automatic search for superannuation moneys on the lost member register or other superannuation accounts, and to have those automatically consolidated into the new superannuation fund. The key thing is that funds are required to provide information to the member as to where lost monies are.

CHAIR—What about the advantages of consolidation where you have a young person who might be contributing to three separate accounts concurrently?

Mr Coles—That comes down partly to the education of the community to show them the benefits of actually consolidating into a single account.

Ms GRIERSON—What about a once off tax deductible financial planning session for young people? Some have suggested in submissions that they should be able to use their super money to pay for a good financial plan. Other suggestions are that it be a tax deduction for young people to get some financial training, advice or education. Another suggestion is that the burden of a one-off planning session be shifted to the superannuation funds, so that they have some idea what it is about, because it is very complex.

Mr Coles—Superannuation funds do a lot of training and education of their members.

Ms GRIERSON—Not individual, not one to one. At a fee there is one to one but it is generally information sessions for mass groups and they are usually over 50.

Mr Coles—I do not know about the aspect of being over 50. My relationship with industry tells me that they try to target their education campaigns as much as possible. I agree that there is an issue. The tax deductibility of financial advice is a broader issue. As a general tax principal, deduction is only allowed for assessable income and the time differential generally of gaining advice and investing in superannuation is deemed by the ATO or ruled by the ATO as not being an allowable deduction provision. I think there is case law on that as well. From a government point of view, would someone with two or three superannuation accounts actually be the ones looking for financial advice? My guess is they probably would not.

Ms GRIERSON—That was the example, but in general terms being available to all young people.

Mr TANNER—What would the damage be on the complexity front to, rather than abolish the contributions tax, to have a tax-free threshold? Say the first $5,000 or another figure is tax-free and then the 15 per cent applies thereafter.

Mr Lonsdale—Again it depends on how you do it. The design features of changing the contributions tax level and rate do not just happen at the front of the system, there are also implications for the back end of the system. For example, those people that take an income stream currently receive a rebate for contributions tax paid. One question would be, ‘Should that rebate remain or should that rebate be changed?’ This is an issue that the Treasurer highlighted last week.

Mr TANNER—There is a consequential question that you have to deal with.

Mr Lonsdale—It is consequential but it is a very significant design issue; changing the contributions tax rate would be a very significant change to the superannuation taxation arrangements.

Dr EMERSON—Time and time again the contributions tax comes up, the cost of it comes up and you have called it appreciably bigger than $3.3 billion, which in Treasury speak would be at least 20 per cent greater. So, getting ridding of it is very expensive. That leads to people saying, 'What about an age related reduction or a removal of contributions tax or alternatively what about an income related reduction or removal of contributions tax, say for everyone earning less than X thousand dollars a year?' Could you come back to the committee with a report on the complexity issues associated with that and the benefits too, so that we do not blindly say that this is a good idea and then find that it makes the superannuation tax surcharge look like a double in terms of design and implementation.

Mr Lonsdale—That is fine.

CHAIR—Thank you for that.

Mr Lonsdale—I am conscious that we have taken a significant amount of questions on notice and will require modelling and other work. It is our standard procedure to consult our responsible ministers, they have a keen interest in this. We will be doing that.

CHAIR—That is great.

[2.37 p.m.]

WHITTAKER, Mr Noel, Private capacity

CHAIR—Welcome. This hearing has the same standing as proceedings of parliament. The committee has not received a submission to this inquiry from you. Would you like to outline your views as a man who is well versed, an expert in the field?

Mr Whittaker—I was amazed how complex Treasury was making this.

CHAIR—Were you there during the Treasury?

Mr Whittaker—Half of it and I saw the rest on television. You talk about self-employed and unemployed and they tried to give the history of that. At the moment we have a strange situation in that if I am a business person and I am incorporated I get a full deduction. If I am a sole trader I get $5,000 and three-quarters of the balance.

On top of that, any person whose boss makes a contribution for them cannot claim a tax deduction. Again you have two types of workers; those workers whose bosses offer salary sacrifice which government departments do, and those workers who are not offered salary sacrifice. The ones who offer it, their employees get a deduction because it comes out of pre-tax dollars but if the employer does not offer it, they have to pay their super out of after-tax dollars. There is an anomaly there.

CHAIR—That is right, a very good point.

Ms GRIERSON—We are thinking that it is available to everybody, but it is not, is it?

Mr Whittaker—Also the greatest way to avoid capital gains tax is to make a large tax deductible contribution to super in the year you sell the investment property. Under the laws anybody under 65 can contribute with no work test. Say you are a retired couple, you are 61 or 62, there is now no employer making contributions for you, therefore you can contribute and claim a deduction of $5,000 and 75 per cent of the balance. You are a couple, you get rid of your investment property and say you make a $400,000 taxable capital gain. After discount it is $200,000 which is $100,000 each. Therefore you put $300,000 into super or whatever you wish and then claim $100,000 each as a tax deduction and the capital gains tax is wiped out. Where it gets tricky is if they are between 65 and 70 they have to pass the work test which is 40 hours in 30 days. Therefore they go back to work and mow lawns and do something. If they earn more than $450 in that month the boss must contribute to super and they cannot get it. We tell them, ‘Okay, you work 14 days in this month and 14 days next month.’ You have all these types of people. The unemployed can claim it and the workers whose boss offers salary sacrifice can claim it, but the workers whose boss does not offer salary sacrifice cannot claim it. It is a mish mash.

Dr EMERSON—Why would an employer not offer salary sacrifice up to that amount of the age limit?

Mr Whittaker—I gave a talk to some people at the Wesley Hospital on Tuesday night who were breast cancer victims and their main issue was release of super prior to age but we also went through salary sacrifice. Some people were saying, 'Well my husband's boss just will not do it, he is too lazy.' One was a Dutch corporation and they could not be bothered going to head office in Amsterdam.

Ms GRIERSON—Often it is part of a separate package, people who are on an individual contract not an AWA.

Mr Whittaker—Everyone I talk to has staff shortages; there is a massive pressure to find decent people. The one benefit the boss can offer which costs them nothing is salary sacrifice because it costs the boss nothing at all.

Ms GRIERSON—Then we do not get the young people salary sacrificing.

Mr Whittaker—To me they should not be salary sacrificing.

Ms GRIERSON—That is what I am going to ask you about. Your advice to young people would be, 'Acquire wealth, get yourself some security, do some investment before super', is that right?

Mr Whittaker—The name of the game is to get compounding working for you. To get compounding working you need to build your asset base. Let us say that you are 30 and you can afford to contribute $10,000 into super or another program. If you put $10,000 into super by salary sacrifice, there is $8,500 working for you after contributions tax. If I went out and got an $150,00 loan for shares the interest would be a tax deductible $10,000. So, it is still costing me $10,000 of pre-tax but by doing it by borrowing for investment I have $150,000 working for me not $8,500, which means a massive number up the track.

Dr EMERSON—And, you will be subject to a concessionary capital gains tax on your shares but you still get a concession on the—

Mr Whittaker—You get franked dividends as well. With the franked dividends and the concessionally taxed capital gains tax and the fact that you will keep it for the next 40 years, it is a beautiful tax system.

Dr EMERSON—Just about everyone who has appeared here has said, 'Get rid of the 15 per cent contributions tax.' We have heard from Treasury that it is appreciably more expensive than $3.3 billion. For the purpose of the income tax act, contributions are no different from the earnings of the fund and you would need to get rid of the tax on the earnings of the fund as well.

Mr Whittaker—Yes, which is why Treasury is saying it is complex, because in fund income there is interest and dividends et cetera, and there is deductible contributions which for fund income tax is 15 per cent. That is why the contributions tax is 15 per cent. If you try to reduce the contributions tax then the income of the fund will be taxed at two different rates or else you would reduce the income tax on the fund, which no-one is going to do. If you try to reduce it for a certain type of person—

CHAIR—Our problem is we have gone into these marginalised people, and the younger people where the tax incentive is doubtful, they may need something else. Part of the problem is looking at what ways we would have an incentive. There have been various proposals, the ability to take part of the super out for mortgage relief—

Mr Whittaker—Which is crazy, which is plain stupid.

CHAIR—We are not likely to recommend it. We started off being interested, but—

Ms GRIERSON—We do not like it either.

Mr Whittaker—The reason is you have competing interests. If I have a home loan, I want the lowest rate possible; if I have superannuation, I want the highest rate possible.

CHAIR—What about this question of consolidation of accounts? We have struck this problem with young people because so many young people have part-time jobs and are students. A lot of them lose interest in super because it is all whittled away by admin fees and they have about 10 different accounts and so on.

Mr Whittaker—All we can do is publicise it. It is publicised reasonably well. As Treasury said, there is a good website unclaimedsuper.com.au.

CHAIR—It is a question of the ability for those who are not earning that much in terms of super, to go on a separate fund for that so they know—

Mr Whittaker—There are RSAs, they are simple cheap funds, low-cost funds. That is only a savings account in the superannuation system. It is fairly simple to find your super, but it is education. How many times do you tell people, if you are going to chase 15 per cent you will lose your money.

CHAIR—In my electorate there is a group of investors who wanted to blame the government and ASIC for it.

Dr EMERSON—Can you pick up on the concept we have been exploring which is an opting out concept? That is, that there is a lot of inertia: if they are in something they probably will not opt out; if they are out of something they probably will not opt in. In the case of these marginalised young people who go from one job to another, is there a concept where you could say, 'We will consolidate these accounts for you, unless you tell us not to?'

Mr Whittaker—That would be a great idea.

Dr EMERSON—There would be some consolidating done by the state, the Commonwealth of Australia, unless the young person said, 'I happen to like having 17 different super accounts.' Most of them would say, 'Yeah stick them all in one account for me, cut my fees and I will be able to find them.'

Mr Whittaker—A few years ago Treasurer Costello told me that they might not think much about superannuation now but once their balance gets to $30,000 or $40,000 they will think about it. I was in a golf shop recently and a guy said, ‘I actually found $31,000.’

Dr EMERSON—What could you consider the consolidated to be? It would be some sort of default fund.

Mr Whittaker—I think it is a good idea.

Ms GRIERSON—I think it is a good idea.

Dr EMERSON—The government is setting up a future fund and it is getting people to manage that money, basically private sector. Or you could have a private agent that says, ‘We will do it and we will spread it across the five most successful superannuation funds in Australia.’ Call that a default superannuation fund, say to young people, ‘All your money is going to end up in there unless you say, ‘No I have this rip snorting outfit called Macquarie Bank, I want you to put it in there.’’

Mr Whittaker—Once they get a balance they will take good care of it.

Ms GRIERSON—It is an incentive just to see it there in print.

Mr Whittaker—I think Treasury made the point that young people do not care about their future much. For the first 30 years they are playing around and then between 30 and 50 it is the kids and the mortgage and over 50, it is too late.

Ms GRIERSON—In your experience what do you find does motivate them to start thinking about their financial security? Not super necessarily. Is it an income level, what is it that gets those people? Is it education?

Mr Whittaker—I think it is peer pressure. There is now a realisation among younger people that there will not be a pension, even though there will be but there is a general feeling—

Ms GRIERSON—They think all the baby boomers are going to use everything up.

Mr Whittaker—The papers are running this thing at the moment that the baby boomers are going to spend it all, which sells papers.

Ms GRIERSON—We are the greedy generation.

CHAIR—What about the problem we had of the women going out of the workforce and what you do with them? They have become a marginalised group and a lot of them you are condemning later down the path to go on the pension. We have been trying to throw around ways that we can try and assist with that. Do you have any ideas on that?

Mr Whittaker—The great thing is this new spouse superannuation splitting; that is one of the best incentives we have ever had.

CHAIR—That is good. What about if they are self-employed, unincorporated self-employed small business people and there is no—

Dr EMERSON—Most do not really have any super anyway.

Mr Whittaker—As you said before, 90 per cent fail anyway. One thing about super is that it is the one asset the trustee in bankruptcy cannot get off them. That is why when I give talks to small business people I say, ‘Look, if you incorporate, super is a tax deduction and it is the one thing they cannot take off you if you go broke.’

Ms GRIERSON—Someone submitted that if instead of income splitting every year, why not do it at the end point? Then you can make a proper adjustment.

Mr Whittaker—Every year is easier.

Ms GRIERSON—They said it was administratively difficult because you do not know how much you are going to need.

Mr Whittaker—RBL is your main thing. We see a lot of people where the guy is up to his RBL, a high-income earner and his wife has no superannuation. He can now transfer 85 per cent. This superannuation split from 1 January has been one of the most popular things that the government has done. Again it has a funny thing in there which is perception. The funds, Treasury and taxation are telling people you cannot split to your wife if she is retired and many women have not worked and think they are retired. APRA issued a new paper yesterday on this saying that retirement is a state of mind. People are saying, ‘My wife is only 58 but they tell me I cannot split to her.’

Ms GRIERSON—Many women have sacrificed career and their salary and therefore super and have supported the other partner and the partner’s career. I know it would be hugely attractive, it is a discussion point at most gatherings these days.

Mr Whittaker—The biggest issue now for single women, given that they are a growing number over 50, is that they are retiring as their parents are dying. ‘At last I am finished work and I am 65 or 66, the parents are 86 and now they need full-time care.’

Ms GRIERSON—All these measures benefit couples but there is no benefit for the many people now who are single. That is a real pattern, women are not marrying and if they are having children it is much older. There is a growing group of people who will never benefit from that sort of thing and they will be whinging loudly, what do they do?

Mr Whittaker—I do not know. The aged pension is generous for couples but it is hard on single people.

CHAIR—What about the question of these thresholds, the age limits?

Mr Whittaker—What the Treasury did not say was they used to be income based. Prior to 1994 your contribution was based on income, so doctors were the main contributors then. In

1994 they brought out a standard RBL. Your RBL was based on your income and your contribution was based on your income prior to 1994.

Ms GRIERSON—It is not now.

Mr Whittaker—In 1994 they made it a straight $400,000 lump sum, $800,000 pension and now it has been indexed up to about $650,000 and $1.3 million, which is good. It makes a lot of sense to abolish certainly the lower age based limit, which is about $15,000 at 35 and about $42,000 up to 50. It is $105,000 over 50.

CHAIR—They say that very few actually reach the limit at that age group anyway.

Mr Whittaker—Again because they might not want to but it might be there if they wanted to. The people it will help are the young professional females who do have a high earning job then they stop for a long time. It might be only a small group.

Ms GRIERSON—What about their argument about $450 threshold, they are very reluctant to get rid of it.

Mr Whittaker—On the SGC? That is a funny one.

Ms GRIERSON—There does not seem any point of not dropping it, it does not make sense. Why should there be this arbitrary figure? Why would not everybody have to absorb some of that?

Dr EMERSON—They were saying that in 1992 when the $450 limit was first established, there was a calculation that below $200 it just was not worth it because it would be gobbled up by fees anyway. It has to be more than $200, but not too high.

CHAIR—They have frozen it since that time.

Ms GRIERSON—Yet work patterns have changed considerably.

CHAIR—It is just the way that employers are structuring it, particularly in certain sectors, restaurants and catering.

Ms GRIERSON—Or young people tutoring, doing tutoring services.

Mr Whittaker—Also kids with three jobs. If you have three jobs at $400 each you have nothing.

Ms GRIERSON—It does not seem to worry them.

CHAIR—If you were part of our committee, what would be your key recommendations?

Mr Whittaker—To me the under-40s ought to be doing other things.

Ms GRIERSON—But you would still support amalgamation?

Mr Whittaker—Investing in negative gearing and doing things.

CHAIR—Are you concerned about the different tax rates? If you are buying your own place you are paying tax on the way in, but there is no capital gains tax; negative gearing is a different—

Mr Whittaker—Negative gearing does not save much tax, it honestly does not. If you gear shares there is no tax saving. If you gear franked shares, franked up dividends you actually are not even negative. If you gear property, if interest rates are seven per cent and the net yield is four per cent then you are $3,000 short for every $100,000 you borrow. Therefore if you bought a $300,000 property you are only saving $4,000 in tax, it is not a massive tax saver. People like to think that they need a tax break, but negative gearing does not save much tax.

Ms GRIERSON—It is the investment in property, the realisation of a dividend—

Dr EMERSON—It is capital gains.

Mr Whittaker—What it lets you do, if you borrowed $100,000 for investment you save $20 a week tax, it is nothing. But you are now controlling $100,000 for $20 a week. It is the ability to control, to get the compounding going that is the benefit of gearing. It is not the tax breaks, even though it is touted as such.

Ms GRIERSON—For people who are looking at that tax benefit, how does superannuation stack up against all those other types of investment opportunities, taxation wise?

Mr Whittaker—Since the surcharge has gone it is the best. Once you earn $21,600, if you take a bonus you lose 31.5 per cent; into super it is 15 per cent.

Ms GRIERSON—Do you think people out there understand that? Do they not still think that investment in property is going to get them a bigger return than super? Is there not a view that super is compulsory and therefore it cannot ever be as good as an investment opportunity?

Mr Whittaker—Papers ask silly questions, it is not a question of property or super. It is a question about having assets inside super or outside super, because super is not an asset; super is a vehicle.

Ms GRIERSON—It is going to be very difficult to write a report that is meaningful to young people, that has any appreciable difference to young people's behaviour. Some of the most practical ones are assisting amalgamations.

Mr Whittaker—Why can some people claim a tax deduction and why can some not claim? Why should it be $5,000 and three-quarters as opposed to all?

CHAIR—That is a very good point. Thank you for coming. If you have ideas, please send them to us.

Resolved (on motion by **Mr Baird**):

That this committee authorises publication, including publication on the parliamentary database, of the transcript of the evidence given before it at public hearing this day.

Committee adjourned at 3.01 pm