4

Superannuation taxation issues

Impact of contributions tax

4.1 Superannuation contributions made by an employer on behalf of an employee, and contributions by unincorporated self-employed individuals, are taxed at 15 per cent in the superannuation fund. Superannuation contributions made by an employer include Superannuation Guarantee (SG) and salary sacrifice amounts.

4.2 Personal voluntary superannuation contributions or 'undeducted contributions' are not subject to the 15 per cent superannuation fund tax, having already been taxed at an individual's marginal income tax rate.

4.3 Prior to 1988, contributions to a superannuation fund were not subject to tax. Lump sum payments from a fund attributable to post-30 June 1983 service were generally subject to a maximum marginal tax rate of 30 per cent.

4.4 Effective from 1 July 1988, the then government reduced the tax on the post-30 June 1983 component of a lump sum to 15 per cent, at the same time imposing a 15 per cent tax on the taxable income of the fund, including employer and deductible personal contributions. The government also introduced a rebate of 15 per cent to apply to income streams.

4.5 It has been suggested that in order to provide further incentive for people to make contributions and to ensure that the full value of contributed amounts is put to work for fund members (given the 'magic of compound earnings'), that contributions should be tax exempt either for everyone, or at least the under 40s.

4.6 The Association of Superannuation Funds of Australia (ASFA) were among many to advocate the removal of contributions tax given it reduced the compounding on SG contributions from the outset:

> For instance, an individual receiving employer contributions at the standard Superannuation Guarantee rate of 9% of their applicable earnings only receives net contributions of 7.7% once the tax on contributions is taken out.[1]

4.7 ASFA estimated the cost to revenue of a full exemption to be $3.3 billion while Treasury estimated that it would be 'appreciably higher'[2].

4.8 Whether the actual number is $3.3 billion or appreciably higher, it is a lot of revenue. AMP Financial Services (AMP) made the following point:

> Such a significant reduction in tax would come at a large fiscal cost and would need to be assessed against other national priorities, including extending other, existing incentives for superannuation such as the co-contributions regime.[3]

4.9 Although the Small Independent Superannuation Funds Association (SISFA) pointed out that over time it is not a one way street:

> As identified by Treasury itself, the concessions conferred on superannuation will amount to savings to revenue in the longer term in the form of reduced Age Pension outlays. Such estimated savings must be factored into any assessment of the true cost of superannuation tax concessions as they represent an investment in the future (i.e. capital versus revenue expenditure).[4]

4.10 Numerous submissions contended that the current nine per cent rate of SG is insufficient. While proposed targets ranged between 12 and 15 per cent (as a combination of both employer and employee contributions), it was calculated that the impact of removing the contributions tax would be to reduce the target savings rate by three percentage points. CPA Australia noted this:

> As a result of this tax, the effective level of the compulsory SG contribution going to some superannuation accounts is not nine

1 ASFA, *Submission no. 16*, p. 19.

2 Mr P Gallagher, The Treasury, *Transcript*, 10 February 2006, p. 64.

3 AMP Financial Services (AMP), *Submission no. 48,* p. 7.

4 SISFA, *Submission no. 20*, p. 3.

> 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.[5]

4.11 The removal of contributions tax may enable some very high income earners to salary sacrifice much of their income and thereby minimise their marginal tax rates. On this scenario Australian Administration Services (AAS) commented:

> Not removing (or reducing) the contributions tax simply because a very small number of high income individuals may salary sacrifice what are considered to be excessive amounts, thereby denying the vast majority of the Australian people the benefit afforded by the reduction in the contributions tax, could well be considered to be 'using a sledgehammer to crack a nut'. [6]

4.12 AAS further noted:

> This is especially the case given that currently there exist two mechanisms designed to effectively limit the amount of superannuation which is subject to concessional tax treatment - the existence of age deduction limits and the reasonable benefits limits.[7]

4.13 The flipside of the argument to reduce or remove contributions tax is that superannuation is already concessionally taxed. At an estimated cost in 2005–06 of $15.9 billion, it is the Commonwealth Government's largest tax expenditure.[8] Treasury stated:

> This [the tax rate on contributions] compares favourably with most marginal income tax rates. Investment income from superannuation is also taxed at 15 per cent, which again compares favourably to the tax rates that apply to most other investment income. Superannuation benefits are also taxed concessionally…..Concessional taxation arrangements make

5 Mr M Davison, CPA Australia, *Transcript*, 10 February 2006, p. 14.

6 AAS, *Submission no. 67 (supplementary)*, p. 2.

7 AAS, *Submission no. 67 (supplementary)*, p. 2.

8 Commonwealth Government, *Tax Expenditures Statement 2005*, pp 113 and 163.

> superannuation relatively attractive compared to other investments and help to boost superannuation savings.[9]

4.14 AMP made the following comment:

> AMP believes a far reaching, forward looking review of superannuation taxation is required, but we recognise that any changes to the taxation of superannuation should preferably be neutral in terms of the tax collected as a proportion of national income.[10]

4.15 In an attempt to limit the impact on the Commonwealth budget, a number of suggestions were made that attempt to target tax cuts to those needing the most assistance and/or those requiring greater enticement to save in superannuation. The Industry Funds Forum (IFF) proposed a reduction in contributions tax for those on low incomes:

> It is proposed that this reduction be by way of providing a tax credit of 15% on employer superannuation contributions for those with taxable incomes up to $28,000 scaling back to zero for those with taxable incomes above $58,000…Many of whom would be under age 40.[11]

4.16 AAS suggested that consideration could be given to introducing an age-based tax deduction or rebate for voluntary contributions made to superannuation:

> Akin to the Lifetime Health Cover loadings but in reverse, commencing with the maximum available deduction at age 18 and phasing out to zero after age 40. This could be achieved by means of allowing 1) a sliding scale percentage (subject to a maximum amount) or 2) a fixed dollar amount. As a matter of policy, interaction with the existing co-contributions measure will need to be determined.[12]

4.17 A number of witnesses believed that targeting concessions at particular age groups added complexity to an already complex system. In fact the AAS commented that it was 'difficult/impossible to base contributions tax on age/income'.[13]

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9 The Treasury, *Submission no. 47*, p. 17.

10 AMP, *Submission no. 48*, p. 7.

11 Industry Funds Forum, *Submission no. 22*, p. 16.

12 AAS, *Submission no. 17*, p. 5.

13 AAS, *Submission no. 67 (supplementary)*, p. 4.

4.18 Treasury commented that changes to the taxation of contributions, including a reduction in the tax rate, would generally increase complexity.

4.19 It was also pointed out that existing complexity tended to overshadow existing concessions. Mercer Human Resource Consulting stated:

> Australian superannuation is taxed in a concessional manner. However, there are significant issues in the current arrangements that adversely affect many younger members. These include…the perception that there is no concession… This lack of a clear tax concession, together with preservation, means that additional superannuation contributions by the employer (eg as part of a remuneration package) is perceived as unattractive.[14]

4.20 SISFA agreed:

> The principles of superannuation as embraced in the governing legislation (principally the Superannuation Industry (Supervision) Act 1993 (S/S *Act))* are relatively straight forward, and most would accept a degree of complexity with any system subject to regulation by statutory law. The real complexity with superannuation lies in the layers of taxation—complexity, actual or perceived, results in negative public sentiment.[15]

4.21 Tower Australia noted the disincentive to salary sacrifice to superannuation or for unincorporated self-employed persons to make contributions due to the lack of understanding about pre-tax and post tax contributions. Tower Australia stated in evidence:

> The system as it stands, from a tax perspective, is still quite attractive. Even though there is complexity it is still very attractive. It is about getting the message across. Referring back to the contributions tax issue, an example is that when many of our customers get their statements they see a dollar go into their super fund and all of a sudden they have lost 15 per cent. They do not understand. They think: 'What sort of investment is this? I have lost 15 per cent already. I put a dollar in and now I have 85 cents.' They do not understand the nexus between pre-tax money and post-tax money and the relationship associated with the contributions tax. So it discourages them straightaway.[16]

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14 Mercer Human Resource Consulting, *Submission no. 44*, p. 5.

15 SISFA, *Submission no. 20*, p. 3.

16 Mr G Evans, Tower Australia Limited, *Transcript*, 18 October 2005, p. 57.

4.22 Similarly, the Australian Chamber of Commerce and Industry (ACCI) felt that people did not understand the tax implications arising from investing in superannuation:

> ACCI argues that the super tax system should be made simpler. This will make it easier for individuals to understand the tax consequences of decisions relating to super. [17]

4.23 This divergence between perception and reality in relation to how contributions tax fits into the bigger picture was illustrated in a recent article written by Peter Haggstrom in the *Australian Financial Review*.

4.24 He makes the point that it is a 'trivially true observation' that a tax on contributions reduces the end benefit. There are a number of basic points that need to be included in the discussion that are continually overlooked or misunderstood. Haggstrom states:

> The first point is that we have a superannuation system that produces extremely low effective tax rates on retirement income for the vast majority of people.[18]

4.25 This is due to a combination of rebates, such as the low income rebate, the Senior Australians Tax Offset and the 15 per cent pension rebate along with common financial planning strategies. Haggstrom noted:

> The effective tax rate for someone aged 65 with [superannuation] pension income in the first year of about $46,000 is a tad over 3 per cent.[19]

Taxation of benefits

4.26 The government announced a number of proposed changes to the laws governing superannuation in the 2006–07 budget handed down by the Treasurer on 9 May 2006. This included changes to the taxation of superannuation benefits, which were outlined in the government's *Plan to Simplify and Streamline Superannuation*[20] (superannuation plan).

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17 ACCI, *Submission no. 41*, p. 7.

18 P Haggstrom, 'Retirement is not really too taxing', *Australian Financial Review*, 3 April 2006, p .63.

19 P Haggstrom, 'Retirement is not really too taxing', *Australian Financial Review*, 3 April 2006, p. 63.

20 The Treasury, *A Plan to Simplify and Streamline Superannuation*, Canberra, May 2006.

4.27 The main effect of the proposal is that from 1 July 2007 superannuation benefits would be exempt income when paid to a person over the age of 60. This means they would not incur any tax nor would they push other income into higher tax brackets. Superannuation taxation is also simplified for those under the age of 60.

4.28 Prior to the budget a number of submissions recognised that the taxation of end benefits is complicated and quite often problematic. Rice Walker Actuaries submission, for example, recognised explicitly that the contributions stage is not the only point at which tax applies and that any changes to the taxation of superannuation need to be considered from a whole of system perspective:

> There are constant calls for lower taxation of superannuation funds. At various times, economists have argued for the removal of taxes on contributions, investment earnings or end benefits. There are valid reasons for all of these but we question whether any can be considered in isolation. Clearly, the removal of a significant tax must result in lower levels of government services or higher taxes from other sources.[21]

4.29 Treasury also pointed out that a great deal of the complexity lies in how end benefits are taxed.

> When we look at the way we tax end benefits now, we see that we have seven or eight different lump sum components and they are taxed in seven or eight different ways. And that is without looking at how people can access pension arrangements. The majority of the complexity lies at the back end of the system—at the end benefit stage of taxing superannuation. We point out in our submission that for someone making superannuation contributions it is reasonably straightforward.[22]

4.30 The Financial Planning Association (FPA) talked about this other end of the tax time line. They raised the tax treatment of investment bonds, whereby after a certain period of time, and assuming various rules are abided by, the benefit is tax free on withdrawal.[23]

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21 Rice Walker Actuaries, *Submission no. 64*, p. 12.

22 Mr J Lonsdale, Treasury, *Transcript*, 14 October 2005, p .3.

23 Ms A Esler, FPA, *Transcript*, 18 October 2005, p. 37.

Other taxation issues

4.31 While the vast majority of discussion on taxes involved the taxing of contributions and benefits, there was some discussion of other taxation issues.

4.32 A number of submissions, including the Australian Bankers Association, called for personal superannuation contributions to receive tax concessions. Personal superannuation contributions are those made after an individual's marginal rate of income tax has been levied (undeducted contribution). The Australian Bankers' Association support the idea of an individual being able to claim a tax deduction for their undeducted contributions:

> ABA believes that tax deductions on personal contributions would likely provide an incentive for employees to make additional voluntary contributions, particularly medium income earners. This approach would balance long-term savings accumulation with current consumption.[24]

4.33 Not all employers offer salary sacrifice arrangements so for many employees their only avenue to boost their superannuation savings beyond SG is to make post-tax, personal contributions.

4.34 It was suggested a number of times, that in terms of targeting age groups, education would be a more useful option than tax cuts. ASFA made the following comment:

> We do not support policies that are age based, per se. If you follow a system that says, 'Something is available for just the under 40s,' it is likely to add to the complexity of super, create other anomalies and inequities…But to the extent that your inquiry is about putting super on the radar of people under 40 and getting them to save more at an earlier age, that is obviously going to make it much more likely that they will get to the goal of an adequate retirement income down the track.[25]

4.35 Many of the submissions and witnesses focussed on the immediate benefits of reducing or removing tax on various elements of the superannuation system, for example, 'the removal of tax on contributions would ensure that the full nine per cent SG contributions would

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24 Australian Bankers' Association, *Submission no. 28*, p. 11.

25 Ms P Smith, ASFA, *Transcript*, 28 July 2005, p. 2.

experience the magic of compounding'. However very few talked about the net value gained for each public dollar. AMP was an exception:

> We believe that before we consider extending existing tax concessions to encourage savings, it is important that we undertake more extensive research to understand what policy changes will deliver the greatest improvements in savings behaviour for a given dollar of public expenditure.[26]

4.36 AMP also questioned whether further tax concessions were needed at all:

> In many respects, the Australian system already has the basic tenets to achieve more saving through superannuation: compulsory or voluntary. This puts Australia in a much better position than most other developed countries. The real questions are to what extent should these be varied or extended, and to what extent could Australians benefit more from existing arrangements, were we able to improve financial literacy and offer greater access to scaleable and affordable financial advice.[27]

Conclusions

4.37 Australia's superannuation system enjoys significant tax concessions. These concessions will be considerably increased from 1 July 2007 under the government's proposed *Plan to Simplify and Streamline Superannuation*, particularly for those who are aged 60 or over when they receive their benefits.

4.38 The committee broadly endorses the proposed budget amendments to the taxation of superannuation benefits, because they address two key barriers preventing under 40s from contributing to superannuation. The first barrier is the perception that superannuation is not concessionally taxed. The second related barrier is the reality that superannuation taxation is very complicated.

4.39 The committee believes that one of the keys to encouraging greater investment in superannuation, particularly for the under 40s, is to simplify how it is taxed. The committee notes that the government's budget proposals will largely achieve this goal. The next step, in the committee's view, is to promote the simplified end benefit tax concessions so that they are more apparent to all people.

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26 AMP, *Submission no. 48*, p .2.

27 AMP, *Submission no. 48*, p. 5.

4.40 If people can more clearly understand the tax concessions that apply to their superannuation savings, they are more likely to contribute more money to superannuation. Emotive statements such as 'superannuation is taxed three times' are misleading at best, because they do not reflect the lower tax rates, the tax-free thresholds and rebates that apply to superannuation. To this end, the government's simplification and streamlining of the tax on superannuation payments will be beneficial.

4.41 A change to the taxation of contributions may have the undesirable effect of further complicating the overall taxation regime from the point of view of both fund members and the administration of the fund itself.

4.42 Furthermore, the tax system is so complicated, that merely processing transactions in a particular order can result in a higher or lower tax liability on superannuation benefits. Similarly, the form in which superannuation benefits are accessed can impact on a person's eligibility for the Age Pension and associated benefits.

4.43 The government has proposed removing the existing 50 per cent assets test exemption for certain income streams. Consistent treatment of all assets for Age Pension means test purposes will remove further complexity from the retirement income system.

4.44 Reducing system complexity should lead to financial advice being geared towards increasing savings rather than unravelling the complexity of tax concessions or contriving to qualify for age pensions.

4.45 Given that the taxation of contributions and earnings within a fund is already concessional, coupled with the 2006–07 budget's proposed simplification of taxation of end benefits, the committee did not see the need to also reduce or eliminate the tax applying to contributions.

4.46 The committee believes that targeted incentives that do not further complicate the system for fund members, such as the co-contribution scheme (see Chapter 7), simplification of the superannuation tax system, and education (see Chapter 5), remain the most effective methods of increasing the superannuation savings of under 40s.

Limits on superannuation tax concessions

Reasonable Benefit Limits

4.47 Because of the scale of superannuation tax concessions, limits apply to the amount of superannuation savings receiving these concessions. The reasonable benefit limit (RBL) is the maximum amount of retirement and termination of employment benefits that a person can receive over their life time at concessional tax rates.

4.48 However, the government's superannuation plan would abolish RBLs from 1 July 2007. The proposals in the plan are subject to public consultation and being passed by parliament. As a result, the following paragraphs address the existing RBL system.

4.49 Currently, if more than half of a person's benefits are withdrawn as a lump sum then their RBL is $648 946 in 2005–06. Any amount in excess of the lump sum RBL is taxed at either 38 per cent or 47 per cent depending on the components of the lump sum.

4.50 If more than half of a person's benefits are withdrawn in the form of a certain type of annuity or pension[28], then their RBL is $1 297 886. Any excessive amount will reduce the proportion of the pension that qualifies for the 15 per cent pension rebate.

4.51 Therefore, the way in which a person takes their end benefit of superannuation affects the amount of superannuation that is entitled to a concession.

4.52 A person on average earnings is unlikely to reach the lump sum RBL, let alone the pension RBL, without significant salary sacrifice, especially when undeducted contributions (those where income tax has already been paid) are not included in the calculation of excess benefits. Of the 308 000 lump sums paid in 2002–03, only 518 were in excess of the RBL.[29]

4.53 There was conflicting evidence given on the impact that RBLs have on saving practices. Some suggested that due to the resource constraints on most under 40s the existence of the RBL is unlikely to affect their decision to make additional superannuation payments.

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28 Among other things, the pension or annuity must: be payable for life or life expectancy; be paid at least annually; only be commuted in limited circumstances, and not have a residual capital value.

29 Australian Taxation Office (ATO), *Tax Stats 2002-03*, Canberra, 2005, p. 14.

4.54 CPA Australia suggested that there were more transparent reasons that people under 40 were not contributing to superannuation:

> Younger Australians have competing demands for their income, such as housing, family and education, and when they do save it is generally through more accessible investment vehicles than superannuation.[30]

4.55 Some said that the RBL was clearly a disincentive, including the Financial Planning Association (FPA):

> With most people in the under- 40 age group uncertain of their futures and hopeful that their income will increase over the years, there is little incentive to contribute to superannuation early in life if it will simply push you over your RBL so that later in your working life, when you would be better placed to take advantage of the superannuation system, you would receive no benefit. [31]

4.56 While others questioned whether it was a disincentive at all. Tower Australia stated:

> Also, I think the question of whether it would change people's habits if we removed the RBL is in doubt. The ability for people to have excess benefits in an allocated pension and just pay normal income tax while it accrues, tax exempt, is there today, and people use that environment. I do not think removing that is really going to change people's habits.[32]

4.57 The FPA questioned how the government can at the same time encourage and limit the accumulation of retirement benefits:

> However, when encouraging people to work longer and build up retirement benefits, there is a contradiction between wanting people to become self-sufficient and limiting the amount of superannuation that can be received.[33]

4.58 The FPA also suggested that the existence of age-based deduction limits (see *Age-based deduction limits below*) removed the need for RBLs:

> So the fact that you have the member deductible limits, which, based on your age, limit the amount that your employer or your

30 CPA Australia, *Submission no. 18*, p .2.

31 Mr J Anning, Financial Planning Association, *Transcript,* 18 October 2005, p. 30.

32 Mr G Evans, Tower Australia Limited, *Transcript*, 18 October 2005, p. 59.

33 Mr J Anning, FPA, *Transcript,* 18 October 2005, p. 30.

> salary sacrifice contributions equate to, means that it is unnecessary then to have the reasonable benefit limits as well.[34]

4.59 Representatives from Tower Australia Limited did go on to talk of the compliance burden involved with RBLs. Presumably this cost is passed on to members, including those under age 40:

> I will mention one other thing on RBLs, just so the committee is aware of it. RBL reporting does represent a substantial burden for the financial services industry in having to report these benefits. There is enormous complexity in that reporting process, and that complexity should only be maintained if it is delivering a benefit to the community.[35]

4.60 While most suggestions regarding the removal of the RBL were based on the effectiveness of the age-based deduction limits, Rice Walker Actuaries suggested that the RBL and the age-based deduction limits (discussed below) both be replaced by a life-time deduction limit on contributions:

> It would be relatively easy to replace this with a system of maximum lifetime contributions. Under an old Coalition policy introduced in the 1993 election campaign, it was proposed that contributions be limited to $300 000 (appropriately indexed) over a life time to attract maximum tax deductibility. A life-time limit would be easier to maintain and it would be fairer for members who made erratic payments from year to year...People starting to contribute earlier in life would get higher benefits in retirement for the same levels of contributions. This occurs because of the longer period on which they would generate investment earnings on these contributions. There is no particular reason why they should be penalised via a RBL for being an early contributor, given that we want to encourage early savings.[36]

4.61 The Small Independent Superannuation Funds Association (SISFA) noted that RBLs would encourage the use of income streams (because the pension RBL is higher than the lump sum RBL):

> There must be an increased focus on encouraging retirement income streams in preference to lump sums—this could be achieved by increasing pension RBLs and tightening eligibility, or

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34 Ms A Esler, Financial Planning Association (FPA), *Transcript*, 18 October 2005, p. 32.

35 Mr D Glen, Tower Australia Limited, *Transcript*, 18 October 2005, p. 60.

36 Rice Walker Actuaries, *Submission no. 64*, p. 9.

> by capping lump sums (explicitly, or by implication through the introduction of harsher tax treatment).[37]

4.62 AMP had a similar suggestion, however they also advocated simplification:

> The reasonable benefit limits (RBLs) regime needs to be simplified and the levels at which they cut in need to be reviewed to make the rules simpler for people to understand, and to strengthen the incentive to take an income stream.[38]

Age-based deduction limits

4.63 There is no limit to the amount of superannuation contributions that can be made by, or in respect of, a member in any one year. There is an age-based limit, however, to the amount that can be claimed as a tax deduction by each employer in respect of each employee, and that can be claimed by a self-employed person.

4.64 However, the government's superannuation plan would abolish age-based deduction limits from 1 July 2007. They would be replaced with an annual limit for all individuals of $50 000 for deductible contributions and $150 000 for undeducted contributions.

4.65 The proposals in the superannuation plan are subject to public consultation and being passed by parliament. As a result, the following paragraphs address the current age-based deduction limits.

4.66 As at 1 July 2005 the maximum deductible contribution in respect of a person under age 35 was $14 603; between age 35 and under 50 was $40 560 and 50 and over was $100 587.

4.67 The maximum SG that is payable by an employer in respect of each employee is approximately $12 000[39]. Therefore an employer's SG contributions are always fully deductible.

4.68 A person aged under 35 who earns a salary of $50 000 would have to salary sacrifice approximately $10 000 in a year in addition to the SG payment of $4500 to reach the tax deductible contribution limit.

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37 SISFA, *Submission no. 20*, p. 6.

38 AMP, *Submission no. 48*, p. 13.

39 If an employee's salary or wages exceed the maximum superannuation contribution base of $33 720 for each quarter in 2005–06, SG is calculated on $33 720. Therefore the maximum SG payable for the year is ($33 720 x 4) x 9 per cent = $12 140.

4.69 However, a person who has turned 35 years of age, on the same salary, would have to salary sacrifice an additional $36 000 each year (above the SG contribution) before reaching their deduction limit.

4.70 Treasury provided evidence suggesting that the age-based limits are not a barrier for the vast majority of individuals under age 40 to contribute voluntarily to superannuation.

> Chart 13 [of Treasury's submission] shows that few people under age 40 made annual contributions greater than $5,000 (14 per cent of self-employed and 13 per cent of employees). For the 2002–03 financial year the average employer annual contribution for those under age 40 was about $3,000. Contributions made by the self-employed averaged about $4,000.[40]

4.71 A number of submitters to the inquiry have voiced concern that the age-based limit should be raised or removed as it provides a disincentive to place funds into superannuation for under 40s who have the capacity to make substantial voluntary contributions early in their retirement savings phase.

4.72 It has been proposed that the nature of some under 40s work is that they have the capacity to earn more when they are young because their income earnings are essentially linked to good health and youth. ACCI believes that these income earners are penalised for their ability to make early superannuation contributions in careers where their earnings are likely to trend down:

> Yearly contribution limits penalise people with fluctuating income compared to those with steady incomes. Depending on design, RBLs can treat people with the same life-time contributions the same. In addition, it is not clear why contribution limits should be related to age. The lower limits for younger people discourage them from planning for retirement. It particularly penalises those with very high incomes when they are young, such as sports people.[41]

4.73 The trending down of disposable income was raised as an issue for women taking time out of paid work after having children. It was argued that the age-based limit restricted some females with large savings capacity to place more into superannuation when they could most afford to:

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40 The Treasury, *Submission no. 47*, p. 29.

41 ACCI, *Submission no. 41*, p. 5.

> The present model is such that it caters basically for a typical average life time of some 40 years and it does not take into account unusual working patterns which include those taking breaks from work, which would include those people who choose to retire early, those people who have a sea change, possibly going from a high-income profession to a low-income profession, and perhaps women who want to cease work temporarily to raise a family.[42]

4.74 Treasury raised the issue of behavioural change if the limits were removed:

> 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?[43]

4.75 AMP said that these limits introduced complexity and disincentives when the potential for tax abuse was more effectively dealt with elsewhere:

> Limits on how much can be contributed to superannuation were established to prevent people abusing the tax advantages that superannuation offers. However, these limits have introduced complexity to the system and reduce the incentive to save. It would be preferable to remove any barriers to save and instead, reduce the potential tax abuse by placing restrictions on how people can access their money when they retire. In effect, moving the brake on the system from the front to the back end which, in some respects is already achieved through the Reasonable Benefit Limits (RBLs).[44]

4.76 ASFA agreed:

> The other thing we have highlighted is the removal of the age based contribution limits. We see it as not being necessary. It reduces the flexibility to save when they can. The RBL limits would still be there, so that would be the mechanism in terms of putting a cap on the amount of concession or savings, if you put it that way. We see the two things in combination as not being necessary.[45]

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42 Mr S Woods, *Transcript*, 18 October 2005, p. 67.

43 Mr J Lonsdale, The Treasury, *Transcript*, 10 February 2006, p. 63.

44 AMP, *Submission No. 48*, p. 6.

45 Mrs P Smith, ASFA, *Transcript*, 28 July 2005, p. 4.

4.77 While ideally advocating their removal entirely, Mercer Human Resource Consulting suggested that if the deduction limits were to stay there should be an increase in the amount that under 35's could contribute tax effectively:

> However, this inquiry is concentrating on members under age 40. Mercer therefore recommends, as a minimum:
>
> - That the separate limit on deductible contributions for members under age 35 be abolished and that the same contribution limit apply to all members under age 50.[46]

4.78 AAS suggested a single annual deduction limit but also an alternative path based on remuneration:

> …consideration could be given to amending the deduction as follows:
>
> - abolishing the age-based deduction limits and replacing with one deduction limit (say $70,000 - $80,000) indexed annually; or
> - replacing the current flat dollar based limits with 'percentage of total remuneration' limits, whereby an employer (or self-employed person) would only be able to contribute up to a certain proportion of 'total remuneration' - salary plus all employer superannuation contributions (notional in the case of defined benefit) plus reportable fringe benefits for employees and 'income' for the self-employed.[47]

4.79 CPA Australia and ACCI believe that a life-time contribution limit is more appropriate because it smooths when extra savings may be placed in superannuation in a tax concessional way at times when an individual can most afford to do so. One proposed model of the life-time limit used a flat limit per year across an individual's working life of $40 000. CPA Australia also suggested a carry forward of unused limit amounts whereby:

> 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 life time.[48]

4.80 Moving to life-time contribution limits would require the maintenance of life-long records and this may increase the Australian Taxation Office's administrative resource requirements.

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46 Mercer Human Resource Consulting, *Submission no. 44*, p. 10.

47 AAS, *Submission no. 67 (supplementary)*, p. 3.

48 Mr M Davison, CPA Australia, *Transcript*, 10 February 2006, p. 23.

Conclusions

4.81 The government's 2006–07 budget superannuation plan to abolish RBLs addresses a number of concerns raised during this inquiry including the disincentive for under 40s to contribute for fear of eventually breaching the RBL, and administration expenses for superannuation funds in reporting payments.

4.82 However, the committee is concerned that when combined with additional tax concessions on benefits, particularly tax-free benefits for over 60s, significant tax concessions could be enjoyed by high wealth individuals.

4.83 The committee notes that this will be reduced to some extent by the proposed introduction of contribution limits on both deducted and undeducted contributions.

4.84 The proposed increase in the deductible contribution limit for people under 50 to $50 000, as announced in the 2006–07 budget, will also assist those under 40 whose income earning capacity, and therefore saving capacity, peaks in their younger years.