SECURITIES INSTITUTE

18 June 2004

Dr Sarah Bachelard
Secretary
Senate Standing Committee on Economics
Parliament House
CANBERRA   ACT   2600
economics.sen@aph.gov.au

Dear Dr Bachelard

Re: Comments to Senate Standing Committee on Economics

The Securities Institute of Australia ("the Institute") welcomes the opportunity to make a submission to the Senate Standing Committee of Economics ("the Committee") inquiry into the following bills:

- Superannuation Budget Measures Bill 2004 ("Budget Measures Bill")
- Superannuation Laws Amendment (2004 Measures No. 1) Bill 2004 ("2004 Measures No. 1 Bill")
- Superannuation Laws Amendment (2004 Measures No. 2) Bill 2004 ("2004 Measures No. 2 Bill")

The Institute strongly supports the proposed measures to amend the superannuation co-contribution scheme and the superannuation contributions surcharge. The Institute endorses measures that to go providing a greater incentive for Australians to save for their retirement by encouraging a higher level of superannuation savings.

We consider that promoting voluntary retirement savings will provide all Australians with a better standard of living than what the superannuation guarantee and aged pension can provide. Attached are some comments on the particular Bills. We hope that our comments assist in the development of a more effective and efficient superannuation system.

If you have any queries about any issues raised in this submission, please contact me on (02) 8248 7651 or the Institute's Policy consultant, Tony Negline on 0412 109 256 or via email negline@bigpond.net.au

Yours sincerely

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Brian Salter SIA (Aff)
Chief Executive Officer

General comments

In the 2004-05 Federal Budget, the Government announced that it would introduce measures to enhance superannuation savings. The Government aims to increase incentives for low to middle income earners to save for their retirement through the superannuation system by enhancing the co-contribution scheme (through increasing both the level of matching and the maximum threshold) and reducing the superannuation surcharge.

The Institute welcomes the Government's proposals. We believe that the reforms will foster a savings culture by providing incentives for individuals to consider their long-term financial position, and therefore encourage improved standards of living for retired Australians.

Specific comments

Budget Measures Bill

Superannuation co-contribution scheme

The Budget Measures Bill proposes to restructure the superannuation co-contribution scheme by:

- Increasing the level of Government matching of personal superannuation contributions to 150%
- Increasing the maximum amount of Government co-contribution payable to $1,500
- Increasing the income threshold up to which the maximum co-contribution applies to $28,000
- Reducing the rate by which the maximum co-contribution phases out to 5 cents for each additional dollar of income (consequently the co-contribution will phase out completely at $58,000).

The Institute believes that encouraging Australians to lock their savings away for retirement (a period that may be up to 40 years) needs to be supported by the Government through provisions of significant incentives. The expanded superannuation co-contribution scheme will give Australians the opportunity to structure and tailor their retirement incomes more effectively to their circumstances and needs. This is particularly beneficial for individuals that may have broken income patterns, for example women who may enter and exist the workforce overtime.

Recent data released by the Investment & Financial Services Association (IFSA) indicates that:

- In the $30,000 - $40,000 annual income range, personal contributions are likely to made by about 42% of people aware of the opportunity, compared to up to 29% of people under the previous scheme, 20% of people currently make a personal contribution.
- In the $40,000 - $50,000 annual income range, personal contributions are likely to be made by about 41% of people aware of the opportunity. No co-contribution was available to this group under the previous scheme, and 25% of people made personal contributions.

Low to medium income earners will receive a substantial tax cut and can leverage off these measures by opting for the increased co-contributions. We highlight that the IFSA research reinforces that many lower income earners were greatly encouraged to make additional superannuation contributions because of the co-contribution.

The Institute believes that the changes to the superannuation co-contribution scheme will target the area of low to medium income employees and their families, and as such it will make a difference to the level of retirement savings. The measure will significantly broaden the coverage of the concession and will bring savings closer to adequacy levels for retirees.

Co-Contribution Modelling

We have modelled what the co-contribution is worth over a twenty-year period. We looked at two scenarios: (1) the person contributes $1,000 of their own money to superannuation and (2) the person makes no personal contributions.

The following assumptions have been made: account balance at commencement is $7,000; assessable income (average weekly earnings) increases by 3% each year and no reportable fringe benefits are received throughout the period; employer contributes of 9% of annual salary contributed each quarter to a superannuation fund; and superannuation fund earns 7% per annum and pays 15% without offsets (no management fees, expenses or commissions have been taken into account).

Assessable Income	Increase in Net Benefit	Percentage Increase In Net Benefit
$20,000	$91,470	107%
$25,000	$91,470	90%
$30,000	$81,921	70%
$35,000	$59,943	45%
$40,000	$45,470	30%
$45,000	$40,720	25%
$50,000	$38,594	21%
$55,000	$36,780	19%

Based on our modelling, the Institute strongly supports the restructure of the superannuation co-contributions scheme.

Superannuation contributions and termination payments surcharge

The Budget Measures Bill also proposes to reduce the maximum rates of the superannuation contributions surcharge (determined by the *SCT Imposition Act 1997*) and termination payments surcharge (determined by the *TPT Imposition Act 1997*) from their current levels. The reduction would be implemented in three stages. The maximum rates will be reduced to 12.5% for 2004-05 FY, 10.0% for 2005-06 FY and 7.5% for 2006-07 FY and subsequent years.

The Institute commends the Government's decision to further scale back the superannuation contribution surcharge and the terminations payment surcharge. We particularly applaud the policy of allowing the reduced surcharge to increase over the same income increases as the original policy.

However, while we acknowledge that the surcharge structure is aimed at high-income earners, we believe that it does not capture the intended target group, but captures a much wider sector of the working community. For example, those income earners with Adjusted Taxable Incomes (ATI) that spike from financial year to consecutive financial year may exceed the minimum threshold from time to time. This means that they will be subject to the surcharge, yet over a particular longer-term period, their average ATI may not exceed the minimum threshold. Contractors, consultants, employees who enter and exist the workforce, employees who receive lump-sum payments, and so forth, will be penalised as there is no provision for assessing average income.

Surcharge Modelling

We have estimated the level of tax savings that may be made by various levels of ATI and the amount of surcharge made on $10,000 of super contributions subject to the surcharge. We have assessed the period 2004/05 to 2006/07 inclusive. We have assumed that the surcharge thresholds in 2005/06 and later years have been increased by an AWOTE rate of 4% per annum. We compare the total savings available from the current policy (maximum surcharge rate is 2003/04 – 14.5%, 2004/05 – 13/5%, and 2005/06 and later years – 12.5%) and the new policy over the 2003/04 – 2006/07 period. The original policy had a maximum surcharge rate of 15% throughout the entire period.

Adjusted Taxable Income	Total Savings Between 2004/05 and 2006/07 Current Policy less New Policy	Original Policy less New Policy
$ 95,000	$ -	$ 0
$ 96,000	$ -	$ 3
$ 97,000	$ -	$ 5
$ 98,000	$ -	$ 8
$ 99,000	$ -	$ 10
$100,000	$ 0	$ 13
$101,000	$ 5	$ 27
$102,000	$ 10	$ 41
$103,000	$ 14	$ 56
$104,000	$ 19	$ 70
$105,000	$ 35	$ 107
$106,000	$ 51	$ 145
$107,000	$ 68	$ 182
$108,000	$ 84	$ 219
$109,000	$ 118	$ 284

$110,000	$	156	$	354
$111,000	$	195	$	424
$112,000	$	233	$	494
$113,000	$	271	$	564
$114,000	$	309	$	634
$115,000	$	347	$	704
$116,000	$	385	$	772
$117,000	$	423	$	839
$118,000	$	461	$	907
$119,000	$	499	$	974
$120,000	$	537	$	1,042
$121,000	$	575	$	1,110
$122,000	$	609	$	1,166
$123,000	$	642	$	1,222
$124,000	$	676	$	1,277
$125,000	$	709	$	1,333
$126,000	$	741	$	1,387
$127,000	$	763	$	1,420
$128,000	$	785	$	1,453
$129,000	$	807	$	1,486
$130,000	$	829	$	1,519
$131,000	$	850	$	1,550
$132,000	$	850	$	1,550
$133,000	$	850	$	1,550

The Institute concludes that the level of tax savings is indeed a welcome initiative.

However, there are outstanding issues that remain unresolved in relation to the surcharge.

Averaging income

The Institute recommends that the Government consider income averaging for the surcharge. We would suggest that as this is a significant unintended consequence of the surcharge policy, and therefore amendment is required to introduce assessment based on average ATI over a certain period. This would especially help those taxpayers who find they ‘creep’ over the minimum threshold due to a spike in their ATI.

Furthermore, in order to support a more flexible and adaptable retirement income system, the Government should consider retrospective treatment for those individuals that have been captured by the surcharge in a particular financial year (or years) where their average ATI is determined to be below the minimum threshold. It would be appropriate to ensure all Australians are not disadvantaged.

The Institute acknowledges that this proposal would increase the complexity of taxation collection. However, we consider that this is a vital aspect of the functioning of the surcharge that requires amendment.

Increase thresholds

As noted above the Institute applauds the policy of increasing the reduced surcharge over the same income bands as the original policy. However, we believe that it may be appropriate for the Government to increase the surcharge thresholds by more than $10,000. The Institute strongly believes that the surcharge was designed to apply to high-income earners. We note that some preliminary research indicates that many taxpayers subject to the surcharge payable are individuals that have an account balance of less than $100,000.

Alternative approach

The Institute has considered an alternative policy, which would see both these superannuation policies reduced and replaced with a lower superannuation fund tax rate. Without an opportunity to thoroughly assess the precise details of this alternative policy, the Institute has not been able to determine the full impact.

2004 Measures No. 1 Bill

The Institute supports the policy objectives of this particular Bill.

2004 Measures No. 2 Bill

The Institute supports the policy objectives of this particular Bill.

Conclusion

The Institute strongly supports these two measures as encouraging greater retirement savings and contributing to the improved standard of living for retired Australians. These incentives and tax concessions will deliver against this objective of supporting a more flexible and adaptable retirement income system.

Having said that, the Institute would suggest that the Government be cognisant of the outcomes of particular strategies, in that they do not result in artificial or unintended consequences. We encourage the Government to consider how further reforms may increase the effectiveness of our compulsory superannuation system, promote greater individual savings and enhance the standard of living for all Australians.