Chapter 2

Taxation aspects of the bill

2.1 The government provides substantial taxation concessions for superannuation savings. There are two main justifications for these concessions. The first is a concern that Australian citizens may be myopic and not make sufficient provision for their retirement incomes if they are not encouraged into superannuation by attractive taxation concessions. The second is that citizens taking responsibility for their own retirement incomes impose a smaller burden on future taxpayers as they will not be claiming the age pension. These rationales also explain why the government prevents Australians withdrawing from their superannuation accounts before retirement (other than under certain exceptional circumstances).

2.2 These arguments do not apply to temporary residents. It is not the Australian government's concern whether they make adequate provision for their retirement and Australian taxpayers will not be paying them an age pension if they do not. For this reason, they are allowed to withdraw their superannuation when they leave Australia, as what is known as a 'departing Australian superannuation payment (DASP)'.

2.3 As the rationale for encouraging superannuation does not apply to them, the government recoups (some of) the tax concession they have been given on their superannuation by applying a final tax on the DASP. (An alternative would be to exempt temporary residents from being paid compulsory superannuation. However, as Treasury pointed out, 'exempting employers from paying super guarantee on temporary residents …[would make] foreign workers cheaper to employ than local Australian workers'[1].)

2.4 This tax is criticised, as are all taxes. In this case it is argued that it discourages skilled workers from coming to Australia (or staying):

> We are trying to make it easy and pleasant for skilled workers to come here. We are not going to do that if we are going to impose an enormous rate of tax on their superannuation. [2]
>
> …these changes are likely to make it more difficult and more expensive for employers to recruit skilled temporary residents. In some cases, current temporary residents may decide to leave Australia earlier than otherwise planned in order to avoid the higher proposed tax rates.[3]

2.5 At best, there is grudging acceptance of the tax but criticism of the rate:

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1 Mr Nigel Murray, Treasury, *Proof Committee Hansard*, 3 November 2008, p. 20.

2 Mr John Fauvet, PricewaterhouseCoopers, *Proof Committee Hansard*, 3 November 2008, p. 2.

3 Mercer, *Submission 6*, p. 1.

> We do not have, and I cannot imagine that our clients have, any great concern with people paying tax on early access to super… It is just really a question of the rate…[4]

2.6 It could be argued Australia is treating temporary residents more generously than Australians temporarily residing overseas are treated. Australians abroad often contribute to the pensions of the locals by paying a 'social security contribution' (essentially an income tax surcharge like the Medicare levy) from which the Australian will never benefit.

2.7 Price Waterhouse Coopers (PwC) take issue with this argument, which they see as a misleading comparison. They argue 'superannuation is not social security. It is saving for retirement.'[5] But it is still an amount deducted from incomes for the purpose of funding retirement incomes, and temporary residents in Australia should appreciate that they are allowed to take most of their contribution away with them.

Increase in the tax rate

2.8 This bill does not introduce the DASP tax; it has been in place since 2002. However, the bill increases the rate from 30 to 35 per cent. *[#check*- However, for many temporary residents this still means superannuation is less taxed than are other savings vehicles.[6]]

2.9 One criticism of the increase in the tax rate concerns a lack of consultation. Treasury concedes it was not discussed in the original public consultation paper, issued in May. However, the potential increase was mentioned during further targeted consultation which occurred with certain key industry groups and associations in the process of finalising the legislation.[7] ASFA informed the committee that Treasury had informed it of the possible increase in the DASP tax rate in correspondence from early September.[8]

Impact on deliberate balances

2.10 Not all superannuation of departed temporary residents is 'lost'. The Association of Superannuation Funds of Australia argues the bill may impose an

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4 Mr John Fauvet, PricewaterhouseCoopers, *Proof Committee Hansard*, 3 November 2008, p. 2.

5 PriceWaterhouseCoopers, *Submission 2*, p. 2.

6 For example, a top executive who is paid $100 as salary is taxed on it at 46.5 per cent. If she then puts it in a bank deposit, and earns 6 per cent (again losing 46.5 per cent of this in tax) for three years, she will have $59. If instead she receives the $100 as superannuation, it is initially taxed at 15 per cent, the 6 per cent return is not taxed, and after paying 35 per cent tax on the DSAP she is left with $66. Workers, such as backpackers, on lower marginal tax rates may find their small amounts of superannuation more heavily taxed than would a bank deposit.

7 Mr Nigel Murray, *Proof Committee Hansard*, 3 November 2008, p. 22.

8 Mr Robert Hodge, *Correspondence*, 3 November 2008.

additional tax on some temporary residents who have deliberately rather than inadvertently left funds in Australian superannuation accounts.[9] Some high-earning temporary residents may even have 'salary sacrificed' to build up superannuation. Unfortunately, none of the witnesses were able to provide an estimate of the proportion of temporary residents' superannuation which is deliberate, although AFSA did say it was likely to be only 'a small number of cases'.[10]

2.11 ASFA argues that 'the sums involved for each individual could be substantial' and that they should be given relief. [11] ASFA do not explain why it should be the role of the Australian taxpayer to subsidise an ongoing savings vehicle for wealthy former residents who have left the country.

Retrospectivity

2.12 This concern about temporary residents who deliberately leave superannuation in Australia leads to an objection to the bill on the grounds of retrospectivity. In other words, the changes apply to current and former temporary residents as well as future temporary residents. Temporary residents who have accumulated superannuation savings in Australia in the past have done so on the basis that when they turn 60, they can access their superannuation on the same terms as Australian citizens could. Under the measures proposed in the bill, once they leave and a six month period elapses, their superannuation funds will be transferred to the ATO and will be subject to the DASP.

2.13 Price Waterhouse Coopers (PwC) was particularly critical of this aspect of the bill. In verbal evidence to the committee, a Partner at PwC elaborated:

> You put 100 grand into super, let us say, you are expecting to get 85 grand out after your contributions tax, and somebody is going to charge you another 25 grand 20 years after you have left.[12]

2.14 He suggested that the bill could easily be amended such that it only applies to people who enter Australia after the date of effect. PwC's submission also recommended that to exempt 'serious savers', the committee should consider a threshold ($10 000) over and above which temporary residents are allowed to 'opt out' of the proposed measures.[13]

2.15 Hillross Financial Services was also critical of the retrospective application of the bill and also suggested that the measures should not apply to temporary residents

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9 Mercer also makes this criticism; *Submission 6*, p. 3.

10 Association of Superannuation Funds of Australia, *Submission 5*, p. 5.

11 Association of Superannuation Funds of Australia, *Submission 5*, p. 5.

12 Mr John Fauvet, *Proof Committee Hansard*, 3 November 2008, p. 2.

13 Price Waterhouse Coopers, *Submission 2*, p. 2.

entering Australia prior to the date of effect of the legislation.[14] Their submission noted that these temporary residents not only have significant exposure to poorly performing growth assets, but the bill's measures will terminate their fund membership and transfer their reduced balances to the ATO.[15]

2.16 Mercer, a superannuation consultancy, was another submitter recommending that any changes should be restricted to future temporary residents. As with PwC and Hillross, it noted that many former temporary residents have deliberately chosen to leave their superannuation savings in Australia expected that under current laws, they could claim their investment on retirement at the normal tax rates applicable to superannuation benefits. Mercer also argued that former temporary residents may not be aware of the changes and their Australian superannuation fund 'is unlikely to know whether any of their members are former temporary residents'.[16] It recommended that if the bill is to be retrospectively applied, it should be deferred to enable former temporary residents to be contacted to give them an opportunity to act before the changes come into force.[17]

2.17 Treasury was asked its view on the retrospective application of the bill. Mr Nigel Murray, Manager of the Contributions Unity in Personal and Retirement Income Division, responded:

> …the Australian taxpayer is funding the taxation concessions which are going into superannuation which these individuals are taking advantage of. The government does not consider it appropriate that those taxation concessions are provided to those individuals as they will not be retiring in Australia.[18]

Committee view

2.18 The committee acknowledges the concerns of many submitters that the bill will affect the taxation treatment of both former and current temporary residents. However, these investors have benefited from Australia's superannuation tax regime and were given no guarantee that the taxation treatment of their accounts would not be altered. Should they claim their funds before the bill is passed, they will enjoy the full benefit of the current law. Moreover, the committee notes that it is the Australian taxpayer that has funded the generous tax provisions from which many former and current temporary residents have benefited. It is only fair that the full extent of these provisions should benefit those who invest *and* retire in Australia.

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14 Hillross Financial Services, *Submission 1*, p. 1.

15 Hillross Financial Services, *Submission 1*, p. 2.

16 Mercer, *Submission 6*, p. 3. The challenge of communicating the bill's measures is discussed below.

17 Mercer, *Submission 6*, p. 5.

18 Mr Nigel Murray, *Proof Committee Hansard*, 3 November 2008, p. 20.

2.19 Having different rules for people with amounts over an arbitrary threshold in their accounts and allowing them to 'opt out' of the provisions would introduce further complexity into the legislation. There are doubts about the practicality of requiring people to be allowed to 'opt out' when the bill is concerned about a group of people who mostly have superannuation remaining in Australia because their whereabouts are unknown.

Other criticisms

2.20 Hillross argue it is unfair that the funds are not indexed while they are held by the ATO.[19] Of course, as the experience of recent months shows only too well, the private superannuation funds do not guarantee to preserve the real value of superannuation balances either. On the other hand, funds with the ATO are not subject to fees. In some cases, small amounts left in superannuation funds may be totally whittled away by flat rate fees.

2.21 Hillross also claims that an unintended consequence of the bill is that superannuation provided by international companies with staff temporarily posted to an Australian subsidiary would be captured by the legislation. But such companies can avoid this by simply advising their staff to make a DSAP withdrawal when they complete their posting.

2.22 The committee notes it is not surprising that superannuation funds disapprove of the bill as they would prefer to continue managing the unclaimed funds, and earn fees or margins on them, than hand them over to the government.

Recommendation 2.1

2.23 The committee recommends that the Senate pass the bill.

19 Hillross Financial Services, *Submission 1*, p. 1.