‘Australia’s Future Tax System - Retirement Income Consultation Paper’:

As a Trustee of a SMSF and also a recipient of a Comsuper pension I have benefited from the recent changes introduced by the former Howard government but I believe they are unfair and unsustainable.

I would like to make the following points.

The retirement income system
Q1.1 In considering the future of Australia’s retirement income system, which objectives are relevant in setting retirement income policy? Does the current system of the Age Pension and compulsory and voluntary savings meet these objectives? If not, how should the system be changed to meet these objectives?

Yes – there will always be a need for the age pension because for many people, their incomes will be inadequate to fund a reasonable pension in retirement via the SG system. Also women who take time off to have children lose out in the amount of money that can be put into superannuation.

A broad and adequate retirement income system
Q2.1 As the SG system matures, it will become a greater part of an employee’s retirement income. What are the implications for individuals partially or fully excluded from the mature SG system (the self-employed, individuals with broken work patterns such as carers, women and migrants), and how can the retirement income system best accommodate these groups?

See above comment in 1.1

Q2.2 Noting that the adequacy of the Age Pension is being considered by the Pension Review, what is an appropriate concept of adequacy for the retirement income system? Should it be to ensure there is a minimum level of income in retirement, to replace a proportion of income earned prior to retirement, or some other alternative?

The age pension should be restricted to those people who have not been able to put enough money into superannuation. Too many people with large assets, such as >$1million homes are able to access the Age Pension. This is a very difficult issue to address because quite modest size homes in the capital cities are far more expensive than homes in the bush. The family home could be used as income by a reverse mortgage down to a certain level. However a certain amount of asset in the family home must be retained as a deposit for entry into age care facilities.

Q2.3 What should the role of the government be in assisting individuals to meet their retirement income expectations in relation to the support provided by the Age Pension, the level of compulsory savings and incentives to make additional savings? Should the role of government change as an individual’s income increases over their working life?

There ought to be a more widely available system of Government financial advisers/planners who are not biased in their advice due to their fee structure, as are private financial advisers. In this current financial crisis, I do not know of any Financial Adviser that suggested a change in investment strategy as the Equity markets fell. They all indicated a “well diversified portfolio would ride out the storm”. This is proving not to be the case with all sectors of the market falling by large amounts. A reliable Financial Adviser should have been suggesting moving out of Equity funds into more cash or cash equivalent. None of them dare suggesting this because it would add to the run on the funds and also reduce their fees.

An acceptable retirement income system
Q3.1 Do the settings of the retirement income system, such as the level of SG and access to concessions, adequately consider the needs and preferences of individuals both before and after retirement?

Yes - individuals can choose a wide variety of investment strategies, investment funds, SMSFs.

Q3.2 Is the current level of superannuation income tax concessions appropriate and sustainable into the future? Are the current concessions properly targeted, and if not, how should they be reformed?

The changes introduced by the Howard Government are both unfair and unsustainable for the following reasons.

1. Tax Free Withdrawals and The Overall Tax Arrangements

(a) The Howard changes to the taxation of superannuant pensions has created three classes of taxpayers.

i. The first category of 'taxpayers' are pensioners with a fully funded pension. Their pensions, of any amount, are not taxed, not declared as income and therefore the recipient does not pay the medicare levy or medicare surcharge if their pension is higher than $70,000 and they don't have private health insurance. They also have not used up their $6,000 tax-free allowance with their pension so they can **'earn'** another $6,000 from bank interest, investments, rental properties etc without paying any tax. They might have a pension fund with a few million dollars in it and drawing down >$100,000 p.a. and **yet they pay no tax.**

ii. The second category of taxpayers are pensioners on defined benefits schemes such as CSS, PSS and certain State schemes. Their pension is recorded as income but they do get refund off their tax bill equivalent to 10% of their pension. These pensioners pay the medicare levy and medicare surcharge if they don't have private health insurance. They have **used up their $6,000 tax-free allowance** and so any additional income from bank interest, dividends, rent is then taxed at their marginal rate. They are worse off than category (i) but are better off than category (iii) below.

iii. The third category are normal workers. They pay tax on their income and get no relief as above. They pay medicare and medicare surcharge if no private health and income > $70,000.

The idea that a pensioner with a fully funded pension can get any level of pension without paying tax is **immoral, unethical, unfair and, in the long term, unsustainable**.

Simpler scheme
It would be far better to allow anyone to put any amount of money into superannuation; for there to be no tax on contributions; little or no tax on the earnings of the fund BUT TAX ALL WITHDRAWALS AS NORMAL INCOME JUST LIKE EVERY ONE WHO IS WORKING.

I'm retired and I have a bit of pension from category (i) and one from category (ii) and therefore have benefited from the new scheme but it doesn't get round the fact that it is unfair (my pension is nearly as big as my son's income but he is paying more tax, more medicare, trying to buy a house etc); it is unethical since the tax system is supposed be based on the ability to pay - the more income you have from any source the more tax you should pay; it is unsustainable since on the one hand the report on aging indicates we must all work longer because of the increasing number of aged people and on the other hand John Howard dispenses tax free pensions to the retired - STUPID.

Irresponsible - In the long term the scheme is **unsustainable** and will have to changed yet again. 25 yrs down the track 2.5 workers paying tax and medicare levy will be supporting 1 retiree not paying either. The Government is relying on the retirees boosting tax revenue via GST purchases of old age services.

Unethical - Tax should always be about the rich paying more and the poor paying less. This Super scheme has created an opportunity for the fairly rich to create tax free wealth. The extremely rich can't put enough in to make it worth their while. The statistics are interesting: **10% of the population has 60% of the money in super** and the other 90% have less than $100,000 in Super which will hardly give them much of a lifestyle in retirement.

A robust retirement income system
Q4.1 At what age should an individual be able to access their superannuation and at what age should they become eligible for the Age Pension?

The original retirement age of 65 was introduced 100 years ago when the life expectancy wasn't much more than 65 and hence the cost of the pension was not great. Now the average life expectancy of a man is around 80 yrs and of a women about 5 yrs longer. The idea of forcing people to work past 65 yrs of age is not acceptable. The whole purpose of retirement is to enjoy a few years without the stress of work, to do some travelling, to look after the grandkids, to take up some other pastimes. Whilst the life expectancy has increased due to medical improvements and the defeat of many diseases, it still doesn't alter the fact that arthritis sets in and you slow down dramatically post 65 yrs old. Most people have a window of enjoyment for travel of 65 – 73 before it starts to become tedious. As a consequence the Age Pension should stay at 65 yrs for both men and women.

Q4.2 What is the role of individuals in dealing with investment and longevity risk in accumulating and drawing down their retirement income? Do financial markets provide the means to deal with these risks? If not, is there a role for government to address these shortcomings?

This past year has shown up the lack of understanding or lack of advice on investment. Some of the cases of companies going bankrupt – Westpoint, Storm, Lift capital all indicate the lack of investment strategy by many retirees and also the poor advice from Financial advisers.
1. Never put all your eggs in one basket – in fact never put more than 6-8% in one investment.
2. Don't invest everything in different investments from the same company (Westpoint example).
3. If the return is much more than bank interest + 3% then there is definite risk.
4. Diversify across sectors and countries.
5. Have 2 years of pension in a cash or cash equivalent fund so that withdrawals can be made without causing capital losses of equity investments.
6. The Government i.e. Centrelink should have much better financial advice available to pensioners whether they are in SMSFs, Industry funds or other Retail funds.

A simple and approachable retirement income system
Q5.1 In what ways does the retirement income system impose undue complexity and cost on retirees and workers? How could this complexity be reduced?

Over the years the superannuation system has got more and more complex. The latest changes created a mass of complaints from people in defined benefits schemes and "fixes" were created that were unfair on other taxpayers. The scheme should be made much more simple – put as much as you like into super; no contributions tax; little tax on earnings or capital gains in the fund; all lump sums to be treated as normal income and taxed at the marginal rate; all pensions to be also treated in the same manner.

A sustainable retirement income system
Q6.1 The Age Pension serves two roles, as a safety-net for individuals who are unable to sufficiently save for their retirement and as an income supplement for many individuals who do save. What should be the role for the Age Pension and means testing in a future retirement income system and what impact does this have on its sustainability into the future?

The age pension and the tax-free pensions for self funded retirees has produced a scheme that is unsustainable. In 25 years, 2.5 people working and paying tax will be supporting 1 retiree paying no tax and no medicare – unsustainable and unfair.

Q6.2 In what ways does retirement income policy affect workforce participation decisions and what, if any, changes might reduce disincentives to work? Does the sustainability and cost of the retirement income system affect the workforce decisions of younger generations of workers?

There are far more important issues to younger workers to get employment than worrying about a retirement income policy. Retirement is too far away in the distance – they have their eyes only on buying a house and family.

Q6.3 What impact could financial intermediation have on the effectiveness of retirement income policy?

Intervention in the way of setting investment options i.e. forcing people to opt for low return, safe investments such as cash, bonds etc would make superannuation much less desirable. There is a lot of scope for educating people on choosing the right investment strategy as they age; such as – 20-30 yrs old very aggressive; 30 – 40 yrs old aggressive; 40 – 50 yrs old more balanced; 50 – 60 yrs more conservative to make sure capital is not lost in the final years before retirement; post retirement much more conservative but still with some capital growth component and 2 yrs pension amount in cash to ride out volatile markets.

A further issue – Foreign pensions, not listed in the above items

Foreign pensions, such as the UK Old age pension, are treated as Foreign income in Item 20 of the tax return with no consideration to them being pensions, rather than investment income or salary etc. There is a small undeducted component, 8% for the UK pension but this pension is treated differently to Australian pensions. The argument for treating defined benefit schemes differently from fully funded schemes is that the superannuant put none of his/her money into the scheme to pay for the pension. No Foreign pension **has been a cost** on the Australian Government and in most cases has been funded in whole or part by contributions from the Pensioner whilst working in overseas. In addition receiving a Foreign Pension reduces the likelihood of the Pensioner gaining access to the full Australian Age Pension. If the current tax treatment of Australian Pensions is to remain (I argue against it but reality is that there are votes in it and changes are unlikely), then Foreign Pensions should be treated in like manner. They should either be (a) tax free if fully funded; or (b) given the 10% or pension tax rebate if partly funded.

David Roberts

Addendum

Further to my submission of 27 February, I draw your attention to two recent articles:

1. the article by Brian Toohey in the Financial Review on Sat 28 Feb (p.63) "Time to close the Canberra soup kitchen" in which his arguments support my submission on the excesses, unfairness, unsustainability and distortions to the tax and welfare system that were introduced by the Howard government; and

2. the article by Daryl Dixon in the Canberra Times 1 Mar 2009 (p 37) about the adverse effect that the lowering of company tax, and hence lower imputation credits, would have to (a) the performance of superfunds with a majority holding of fully franked shares; and (b) the share prices of fully franked shares which would be driven down by a shift toward higher yield unfranked shares. With the massive losses on the stockmarket over the last 2 years and the large negative returns of superfunds, the last thing anyone wants is for their funds to be driven down further by a loss or reduction of imputation credits.

David Roberts