1. In response to your invitation to make a submission to Australia's future tax system (AFTS), I am pleased to make a submission on the subject of Comsuper Defined Benefit Schemes.
2. My wife and I have been on a CSS pesion for the past 14 and 20 years respectively. We seem to have lost about 1/3 of our purchasing power compared to Age Pensioners through poor indexation; Age Pensioners are still inadequately financed by the Commonwealth and should receive some early increase in pension as an economic stimulus. We are in the same categary.
3. I would be pleased for the AFTS review to properly address our concern and initiate some relief in the 2009/10 budget.

Geoff Henkel

Henry Taxation Review "Australia's Future Taxation System" Submission on Taxation of Comsuper Defined Benefit Schemes

The Simpler / Better Super changes commencing 1 July 2007 provide for no taxation on superannuation pension payments received from a taxed super fund, but for full taxation except for a 10% tax offset for recipients of superannuation pensions from untaxed super funds. This mostly affects Commonwealth superannuants (CSS/PSS/DFRDP or military superannuant pensions), because successive Governments have chosen not to pay monies into a superannuation fund/s from which to pay their employees' superannuation pensions.

The following assessment reviews the situation in the light of the remaining major inequities for Commonwealth superannuants with the Simpler / Better Super regime. These inequalities comprise: the CPI indexation treatment of Commonwealth superannuants' pensions, the now apparent unfairness of the small 10% tax offset; and the large and increasing loss of purchasing power for Commonwealth superannuants over the last 18 years in contrast with Age Pensioners who have rightly received MTAWE indexation formally over the 10 year period since 1998 and it or other favourable increases for the 8 years or so prior to 1998. The Superannuated Commonwealth Officers Association (SCOA) and others have been running a long 10 year campaign on the inequality of the differential indexation treatment

Three Senate Committee enquiries that made recommendations on the indexation of Commonwealth super schemes (2001, 2002 & 2008) have endorsed changing their indexation to a wage-based index, such as MTAWE,. The third Senate enquiry in 2008 entitled "*Cost of Living Pressures on Older Australians*" has endorsed the Superannuated Commonwealth Officers' Association, SCOA campaign for upgrading indexation and possibly other inequality matters. Senator Sherry has set up the current Matthews Inquiry into essentially the benefit design (including indexation) of the Comsuper Schemes, now administered by ARIA. The Matthews Secretariat advises that taxation matters are outside of its Inquiry and should be addressed by Australia's Future Tax System review, commonly known as the Henry Taxation Review.

This submission addresses the inequitable taxation of defined benefit/untaxed superannuation schemes such as Comsuper and Federal parliamentary superannuation schemes, adversely taxed under the Simpler / Better Superannuation regime.

The currently available large budget surplus and the new ALP Government initiatives to address deficiencies and neglect of the Howard Government provide an opportunity for restoring a fair indexation methodology of Commonwealth Superannuation pensions; politically neglected/prejudicially opposed by the former Government... **Fairness and equity is now needed and is affordable**

Tax Offset Approach for Taxation of Benefits from Untaxed Superannuation Schemes

The Simpler / Better Super changes commencing 1 July 2007 provide for no taxation on pensions from taxed superannuation funds, but for standard taxation except for a

10% tax offset for Commonwealth superannuation pensions because the bulk of these are paid from an untaxed source. i.e. they are paid from consolidated revenue, not from a superannuation fund.

SCOA understands that the 10% tax offset was arbitrarily set, rather than comparatively assessed. SCOA assessed the worth of the 10% Tax Offset Proposal in 2006 in comparison with a change in indexation from CPI to MTAWE in commenting on the *Simpler Super* changes proposed by the last government. SCOA concluded that the 10% tax offset was worth some 10 years of improved indexation and thus should be accepted gratefully as a first step towards improving purchasing power and as an interim measure. It is now time to review this situation in comparison to that for the recipients of other Government pensions..

It is appropriate to consider the tax contribution status of taxed superannuants who have paid 15% tax to the Commonwealth on both contributions and growth of their superannuation funds in asset value - while at a superannuation accumulation status. The appropriate comparison is with Allocated Pension contributors and increasingly compulsory superannuation contributions (9%), both of whom have generally utilised a Salary Sacrifice method of developing their taxed source superannuant fund accumulation.

The simplest approach is to treat the Commonwealth superannuation Pension as a condition of service, rightfully available, and comparable to a private superannuation scheme, in regard to assessing the tax foregone by the Commonwealth. On the simplest approach, the foregone tax is 15% and the tax offset should therefore be 85% rather than 10%.

However, it is also appropriate to consider the interest on tax foregone by the Commonwealth. The following assessments can be made for several interest rates and periods of service:-

- 10 years @5% rate = 12.6x1.5%pa = 18.9% - corresponding tax offset = 81%.
- 10 years @10% rate = 16x1.5%pa = 24% - corresponding tax offset = 76%.
- 20 years @5% rate =33.1x0.75%pa = 24.8% - corresponding tax offset = 75%.
- 20 years@10% rate=57.3x0.75%pa = 43% - corresponding tax offset = 57%
- 20 years@8% rate = 45.8x0.75%pa =34.4% -corresponding tax offset = 65.6%
- 30 years @5% rate = 66.4x0.5%pa = 33.2% - corresponding tax offset = 67%
- 30 years @10% rate 164.5x0.5%pa = 82.3% - corresponding tax offset = 18%

The 20 year service period is probably the average or typical period of service. The 10% interest rate is on the high side, the 5% maybe a little on the low side, and an 8% interest rate is probably the most appropriate - and for 20 years service would yield a tax offset of 65.6%; thus a two thirds (66.7%) tax offset is probably the most appropriate to adopt. This approach, irrespective of the interest rate or the period adopted, would indicate a far more generous tax offset than 10% is warranted. In fact, with the discriminatory indexation inequality between Commonwealth superannuants and Centrelink and Veteran's Affairs pensioners for over 10 years there is a strong case for the superannuation pensions paid to most existing Commonwealth superannuation pensioners to be given tax free status.

SCOA understands that some state government defined benefit superannuation schemes, generally similar to the Commonwealth schemes, have been given taxed status and thus their benefits are tax free. This is a serious inequity!

Past Tax Inequality

The loss of past indexation inequality amounts to some 30% for 18 years of retirement, and of course for a lesser length of retirement a lesser amount has been lost. It is a genuine loss of purchasing power and a lowered standard of living for Commonwealth Superannuants compared with Age Pensioners, retired parliamentarians and veterans..

Since the former Government introduced a wage-based index for the Age Pension and most other Government pension, those pensions have rightly increased by 51% whereas the pensions of the Government's former employees has increased by only 29%. The average Commonwealth superannuant pension is now some $22,000 cf $23,000 for a married Age Pensioner couple.

The equitable action would be to treat every Commonwealth retiree on a personal basis as the records and technology are available to treat every retiree on a personal and separately calculated basis.

The cost is difficult to assess: there is a wide age range of retirees; and then there are tax offsets from higher tax clawback and SATO. The cost may be of the order of $100m. So, it warrants an investigation and net cost assessment. In addition, from a funding perspective the Government may wish to either stage it or make it initially available to say 65+ year olds.

The Prime Minister recently commented that there is a need to keep Australia's production of goods and services running at sufficient rates to help offset the global economic downturn and thereby prevent or slow an increase in unemployment.

Adopting my suggestion would make a not inconsiderable contribution to the Prime Minister's objective and result in an immediate boost to the depressed economic outlook. At the same time it would demonstrate that Labor's pre-election promises of fairness and decency are being honoured for successive Governments' former employees and former serving members of the Defence Force and their dependents, mostly spouses/partners. They number approximately 300,000.

Conclusions and Other Considerations

The inequality is present and any delay in adopting an upgrading of CSS/PSS/DFRDP pension indexation simply continues an unfair/inactive status of the past government. Every year we lose on average another 1.5% of income and purchasing power. There is extreme concern that any changes to the indexation of the Comsuper schemes will be delayed to the 2010/11 tax year, (unless Treasury makes specific provision to incorporate the Matthews Inquiry results in the 2009/10 budget.) A set date, such as

24/11/07 (the date of the new government) ought to be adopted, unless there is a catchup provision adopted in the coverage of the upgrading value.

There is currently parallel action being undertaken for an increase in the level of Age Pensions. Any such upgrading also ought to be provided for Comsuper pensioners. In addition, the Garnaut Review is advocating additional payments to low socio-economic households such as Age Pensioners. Comsuper pensioners ought to be included in such a grouping.

The most important priority relates to income improvement. Therefore revised indexation is No 1 priority, followed preferably by an investigation into the appropriate means of tax offset and catchup for Commonwealth Superannuants; this may take some time. An interim measure would be to make CSS/PSS/DFRDP pensions taxable for 1/3 of their value or a 66.7% tax offset, pending the outcome of a catchup reassessment. Any additional outlays would be reduced by tax clawback and SATO, and thus would be of a moderate cost and affordable.

Recommendations

It is recommended that Australia's Future Tax System review:-

1. **The taxation arrangement for Australians receiving superannuation from untaxed superannuation schemes, amending the tax offset approach to the assessed lost taxation (some 2/3 tax offset or 1/3 taxable); possibly also to reflect the past inequality in loss of purchasing power; ie be tax free.**

2. **Adopt an implementation date for revised indexation (Trevor Matthews' Inquiry), to stem the loss of purchasing power, that has now been going on for some 18 years, ie adopt it in the 2009/10 Budget, at the latest.**

3. **Consider a one-off catch-up payment to Comsuper retirees, which reflects the MTAWE differential level and any increase in Age Pension levels in the parallel review.**

4. **Include Comsuper retirees in any Climate Change offsets adopted.**

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