TREASURY SUBMISSION
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“Australia's Future Tax System - Retirement Income”

Self Managed Super Fund Professionals’ Association of Australia Limited (SPAA)
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Association of Australia Limited
('SPAA')

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ABOUT SPAA

1. The Self Managed Superannuation Fund Professionals' Association of Australia Limited ('**SPAA**') is recognised as the peak umbrella association representing Self Managed Superannuation Fund ('**SMSF**') standards, advice and education within the SMSF Industry. SPAA represents all SMSF professional advisors within Australia, including but not limited to auditors, actuaries, tax agents, accountants, financial planners, lawyers, risk providers, administrators, barristers, educators and so on.

2. With self-managed super funds currently representing 98.6 % of all funds, SPAA is the only voice representing professional advice and services to this significant component of the Australian superannuation system. There are currently 394,996 self-managed super funds in Australia accounting for 30.9% of the total Australian superannuation pool.[1]

3. SPAA's key objectives are maintaining professional standards for the SMSF Industry. SPAA provides vital support, independent certification of education and dissemination of regulatory and other industry specific technical information to professional advisors to ensure that their competency is at the very pinnacle of knowledge and skills. Through a stringent professional accreditation designation process, SPAA members are endorsed as SMSF Specialist Advisors™ (SSA™) or SMSF Specialist Auditors™ (SSAud™) in their field regardless of their existing professional accreditation, qualifications or affiliations, after having proved their competency in SMSF advice.

4. Importantly, SPAA engages all industry participants in raising advisory standards within what is a critically important sub-industry within the superannuation services industry, supporting the future financial well-being of many hundreds of thousands of Australians. SPAA recognises the significance of establishing the highest possible industry standards, and ongoing professional development of all industry participants in the attainment of excellence, and to the future 'integrity' of the industry.

OBJECTIVE OF SUBMISSION

5. SPAA has restricted the scope of this submission to issues and considerations which we believe we are suitably qualified to comment on. As discussed with Treasury, the views expressed in this submission represent high level draft proposals which in most cases have not been subject to any detailed cost/benefit analysis. We would be happy to present the proposals referred to in this submission in more detail if need be.
6. SPAA would also be happy to provide the review committee with any further information relating to the SMSF sector if required.

[1] APRA Statistics for Superannuation as at 30 September 2007 (27 December 2007)

7. Overview and summary of key proposals

7.1. SPAA supports the three pillar retirement income system approach. SPAA considers that superannuation tax concessions and incentives are an essential feature of a three pillar retirement income system which denies access to voluntary savings until retirement.

7.2. SPAA also considers that participation can and does play an important role in encouraging individuals to save for their own retirement and in addressing issues of adequacy and longevity. SMSFs facilitate participation and the flexibility and control aspects of SMSFs are an integral part of the Australian Superannuation landscape.

7.3. SPAA considers that the retirement income system could and should be improved by measures which broaden, simplify and promote a sustainable and approachable system. Proposals considered by SPAA to be worthy of further consideration include:

7.3.1. The inclusion of the self-employed in the Superannuation Guarantee (SG) system.

7.3.2. The introduction of a co-contribution catch-up for individuals with interrupted or broken work patterns.

7.3.3. The removal of the 10% employee rule for contribution deductibility.

7.3.4. The removal of work test rule for individuals over age 65.

7.3.5. The extension of the 3 year contribution averaging provisions for individuals over age 65, to accommodate lifestyle changes.

7.3.6. The introduction of the option to retain death benefits paid to a non-taxed dependent in the superannuation accumulation phase.

7.3.7. The introduction of a 3 year averaging system for pension payments, to overcome pension liquidity issues

7.3.8. Compensation for low income earners whose compulsory superannuation contributions effectively afford them no concessional tax benefits.

7.3.9. The encouragement of the use of government CPI index bonds to provide full or partial support of life time annuities and/or defined benefit type income streams.

7.4. As there appears to be research available which suggests a mature SG system will provide a significant proportion of pre-retirement income, SPAA recommends that further research on the issue of adequacy be undertaken before any change to the current level of SG is considered.

7.5. To assist with the completion of this submission, SPAA conducted workshops in Sydney and Adelaide. This submission includes the views of SPAA members obtained during these workshops and subsequent discussions, and which are considered by the SPAA Executive as worthy of further investigation and consideration by government.

7.6. SPAA has restricted the scope of this submission to issues and considerations which we believe we are suitably qualified to comment on. As discussed with Treasury, the views expressed in this submission represent high level draft proposals which in most cases have not been subject to any detailed cost/benefit analysis. We would be happy to present the proposals referred to in this submission in more detail if need be.

8. The retirement income system

8.1. In considering the future of Australia’s retirement income system, SPAA believes the Australian three pillar retirement income system approach provides an appropriate and desirable retirement income system framework. The three pillar approach is supported to different degrees by the financial resources of government, employers and individuals and which in-turn provides an appropriate framework from which to address the key policy settings of equity, participation, adequacy, sustainability and longevity.

8.2. The challenges and opportunities faced by Australia's retirement income system requires a system based on the sharing of responsibilities and financial contributions throughout the Australian community. A retirement income system based on a means tested government guaranteed pension with mandatory saving and non-mandatory saving opportunities provides this framework.

8.3. SPAA considers that measures which encourage individuals to participate in the management of their own retirement savings (both in terms of contributions and the level of control) are important and necessary features of a sustainable retirement income system. SPAA considers that measures which increase participation and voluntary savings are positively correlated such that measures designed to increase participation will at the same time increase voluntary savings.

8.4. SPAA supports the view that superannuation should be regarded by government and the community as the preferred retirement savings vehicle. For reasons of adequacy, sustainability and longevity, SPAA does not support the view that retirement savings should be available for other non-retirement related purposes (other then those currently available).

9. A broad and adequate retirement income system

9.1. SPAA supports the concept of adequacy of retirement incomes. This could be provided as a partial replacement of pre-retirement income or as a present value of post retirement expenses. An adequacy benchmark based on the present value of post retirement expenses would require research into spending patterns of retirees which may take some time.

9.2. As an interim measure, an adequacy benchmark and the superannuation funding arrangements could be based on pre-retirement incomes. As an extension to the concept of adequacy, measures which link an individual's adequacy benchmark to their contribution limits could also be considered. This approach, however defined, would have the advantage of assisting individuals who, under the current contribution limits, may not have the opportunity to appropriately fund their retirement.

9.3. SPAA favours the retention of the Age Pension as a replacement of pre-retirement income and as a safety net arrangement. The Age Pension should continue to be supplemented or complemented via a funded contributions system with appropriate taxation concessions. Adequate safeguards should be put in place to ensure superannuation is used prior to commencement of the Age Pension by the retention of means testing.

9.4. While Australia's three pillar retirement income system plays a major role in providing a retirement income for the vast majority of the population, for some groups the three pillar approach provides inadequate coverage. In particular, the self employed are excluded from the SG system and many choose not to save either through superannuation or other sources.

9.5. Given the availability of the small business CGT concessions, and tax deductions for contributions, it could be argued that the self employed are sufficiently encouraged to contribute to superannuation. However, many self employed individuals, such as tradespersons for instance, may not have any tangible or intangible business assets that can be realised to provide a reasonable retirement income, or the means to contribute to their superannuation and without access to the SG system are likely to have inadequate retirement savings.

9.6. Therefore, SPAA supports the view that the self employed should be included in the compulsory superannuation system by broadening the SG system to include the self employed. For this purpose, the SG contribution should be based on assessable income.

9.7. For other groups, such as those with interrupted or broken working patterns, the three pillar system may not always provide an adequate or appropriate opportunity to save for retirement. For these groups, consideration should be given to introducing a co-contribution "catch-up" period or targeted co-contributions. For example, the government co-contribution and the associated non-concessional contribution could be increased by the number of financial years that an individual remained out of the work force. Alternatively, the current co-contribution system could be adapted by applying an average income over a period of time to determine eligibility for the co-contribution – rather than on a year-by-year basis. This would assist those such as women returning from maternity leave who might otherwise be excluded from participating in the co-contribution system and should operate to encourage them to increase and "catch up" their superannuation savings.

10. An acceptable retirement income system

10.1. SPAA considers that the issues of adequacy and what constitutes an adequate level of retirement savings needs to be determined and whether current superannuation guarantee arrangements are able to provide that level of income throughout various ranges of wealth. Research has shown that at lower income levels a fully mature SG system will provide a significant proportion of pre-retirement income.

10.2. SPAA considers that in order to encourage participation and voluntary savings, individuals need to be appropriately compensated for the inability to use these savings for other purposes. Therefore, compensation by way of tax concessions and incentives is an essential feature of a robust retirement income system.

10.3. However, it is recognised that certain inequities in relation to the SG system need to be addressed. Research suggests that a significant number of taxpayers either receive negligible or no concessions on their superannuation contributions due to their contributions being taxed at higher levels than their individual tax rate. To improve taxpayer equity, SPAA supports a system of SG contribution tax refunds to the fund for individuals with average tax rates of 15% or less. This system would operate to remove the disincentive that currently exists for this group of taxpayers to take remuneration by way of superannuation rather than salary and wages.

10.4. The imputation system is an important and now integral component of the superannuation tax concessions and incentives. SPAA strongly supports the retention of the imputation system and access to franking credits by superannuation funds.

10.5. SPAA considers that the inequities in the superannuation system relating to the treatment of superannuation death benefits paid to non-taxed dependants, needs to be addressed. Requiring non-taxed dependants to withdraw the proceeds of a death benefit is inconsistent with other measures designed to address the issues of adequacy and longevity. SPAA supports the introduction of an option for non-taxed dependants to retain the proceeds of a death benefit as a preserved benefit in the superannuation accumulation phase by way of an internal, or fund to fund roll-over, without benefit taxation.

10.6. As a long term solution, and to address the current issues with individuals in the superannuation pension phase having to sell assets in a depressed market in order to fund the payment of a statutory minimum pension payment, consideration should be given to the introduction of a three year averaging system similar to contributions where an individual would be required to withdraw at least three times the annual minimum amount over a three year period. For example a 65 year old who was to commence an account based pension with $500,000 would be required to take three times the annual minimum amount (ie 3 x $25,000) over a three year period. The minimum pension payment rules would be satisfied as long as a total of $75,000 had been withdrawn by the end of the third year. To accommodate market movements and the impact this may have on the annual minimum pension amount, the three year average amount would be re-set on 1 July each year.

11. A robust retirement income system

11.1. SPAA understands and accepts the arguments for an increase in the preservation and/or Age Pension age. However, SPAA is concerned that any increase in the preservation age may exclude certain individuals who are over age 55, and are unable to work, from being able to access their superannuation savings. SPAA considers that any increase in the preservation and/or Age Pension age should accommodate individuals who have attained age 55 but who are unable to work. This would apply to individuals who have attained at least age 55 and do not ordinary satisfy a superannuation cashing condition of release.

11.2. SPAA considers that the markets for annuities, guaranteed non-commutable income streams and defined benefit style pensions are not well developed or encouraged through the concessions that are currently available. Historically, unless accommodated by generous social security concessions, annuity based income streams have, in the main, proven unpopular.

11.3. To overcome issues of longevity and investment risk which arguably are not adequately dealt with by the retirement income system, SPAA supports the concept of a pension product, backed partially or in full, by the issue of government CPI indexed bonds. However, SPAA does not support the compulsory use of guaranteed income stream products. The most appropriate outcome would be for diversity of choice in relation to retirement income stream options, which would then allow members to choose the income stream product that best suits their circumstances and needs.

11.4. Consistent with the theme of improving participation and voluntary saving, and to reduce the investment and longevity risks, SPAA considers that the financial markets need to accommodate individuals who desire higher levels of participation, control and flexibility. Within appropriate legislative constraints and regulatory supervision, the SMSF sector provides these options. The control and flexibility elements of a SMSF are, and should remain, an integral part of the Australian Superannuation landscape.

12. A simple and approachable retirement income system

12.1. SPAA also supports proposals aimed at simplifying the superannuation system and which also provide further incentives to contribute to superannuation across the income scale. In particular, SPAA supports the view that the 10% rule as a condition of contribution deductibility should be removed. With the introduction of flat dollar deductible contribution limits, the benefits of maintaining such a rule are outweighed by the additional complexities associated with such a rule.

12.2. In addition, grandfathering which has in the past added to the complexity of the retirement income system, should be eliminated from the superannuation system. This could be achieved by identifying further opportunities for the crystallisation and simplification of certain benefit components. For example, the correct calculation of preservation components in many situations requires a significant amount of historical contribution data to the retained by funds. Reducing the number of preservation components to just two could significantly simplify the calculation process and record keeping requirements. Similarly, the existence of untaxed benefit components introduces a range of complexities which could possibly be addressed by the crystallisation of these benefit components.

12.3. The current $150,000 non-concessional contribution limit for individuals over age 65, provides limited flexibility for individuals over age 65 to contribute or to maximise the value of their retirement savings after age 65. For many individuals “downsizing” their accommodation requirements in retirement means selling the family home or retirement unit which then releases funds for retirement income purposes. Therefore, to accommodate lifestyle changes, the current age 65 limit applying to the 3 year contribution averaging provisions, should be removed. To accommodate this change, and to further simplify the contribution rules, the contribution work test rule which requires individuals over the age of 65 to be gainfully employed on at least a part–time basis in order to contribute to superannuation, should be removed.

12.4. SPAA believes that promoting financial advice by making it more affordable via tax concessions would have a positive impact on retirement outcomes. SPAA also believes education and improvements in household literacy is a necessary step to improving retirement income outcomes.

13. A sustainable retirement income system

13.1. SPAA considers that the role of the Age Pension is to act as a safety net for those who do not have adequate retirement funding and believes sustainability may be difficult to attain where there is no direct link between superannuation and qualifying for the Age Pension. SPAA believes that access to the Age Pension should continue to be tested by reference to superannuation in addition to other appropriate assets and income. This would ensure that superannuation savings are sufficiently used before access to the Age Pension is permitted, as it is at present.

13.2. As a measure to improve workplace participation, SPAA supports providing an actuarially fair deferred Age Pension and re-education initiatives for older workers.

FURTHER INFORMATION

We would be pleased to provide you with any further information in support of our submission.

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