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Sensible Changes for a Fairer System

Superannuation Tax Reform
December 2024

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- discuss any matter that may be perceived as being cooperation by competitors in a market to influence that market;
- discuss any matters that could be regarded as fixing, maintaining or controlling prices, allocation of customers or territories, coordinating bids and/or restricting output or acquisitions in any circumstances;
- share commercially sensitive information relating to their employer; or
- share information for an anti-competitive purpose.

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The Actuaries Institute acknowledges the traditional custodians of the lands and waters where we live and work, travel, and trade. We pay our respect to the members of those communities, Elders past and present, and recognise and celebrate their continuing custodianship and culture.

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Introductions

Richard Dunn, FIAA

Jennifer Shaw, FIAA

Michael Rice, AO FIAA

Alun Stevens, FIAA

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Agenda

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Where are we today?

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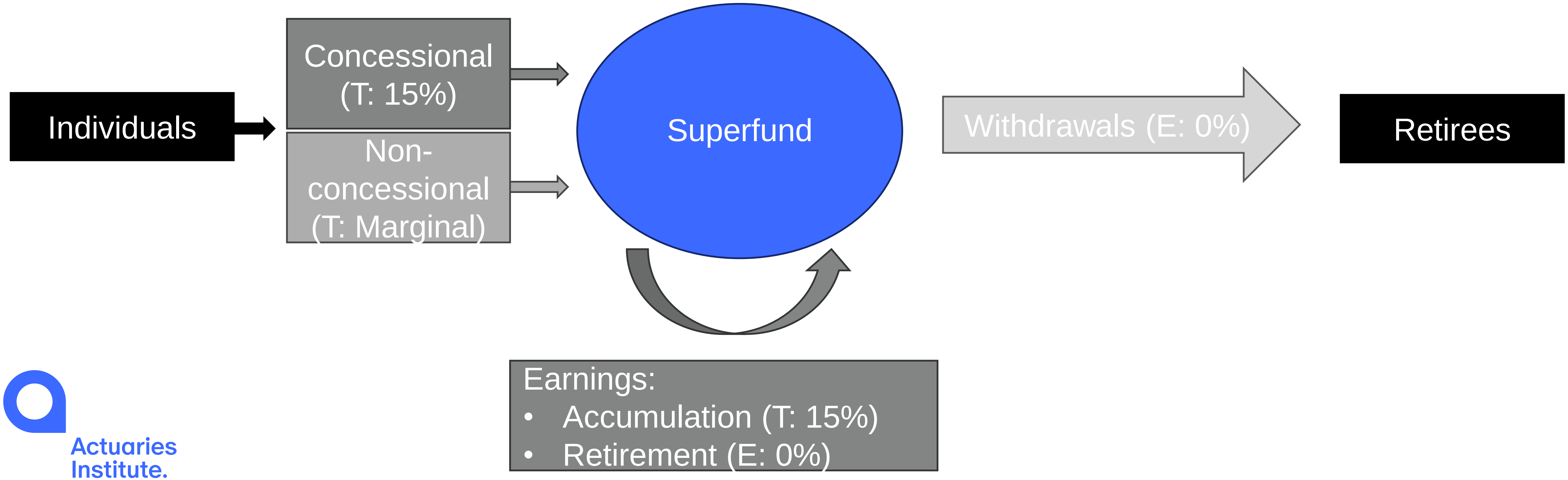
01

Current superannuation tax environment

The 3 points where super can be taxed are when:

- Contributions are made into a super fund
- Superannuation fund assets earn investment returns (earnings)
- Benefits are paid from a superannuation fund.

Tax concessions associated with super are an incentive for individuals to contribute more to super but higher-income earners typically benefit from these concessions more than lower-income earners.



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Superannuation tax reform - Past policy observations

2010
Henry Tax Review

- Relating to personal income tax having a high tax-free threshold ($25,000) and a constant marginal rate for most people (35 per cent);
- Treating employer superannuation contributions as income in the hands of individuals, taxed at marginal personal income tax rates, with a flat-rate refundable tax offset for all contributions up to an annual cap of $25,000 (indexed); and
- Tax rate on superannuation fund earnings to 7.5 per cent.

2015
Rice Warner – Re-think tax discussion paper

- Existing high levels of tax concessions can be cut by taxing pension earnings at 10-15% and/or by curbing the values on large accounts. Bequests (including pension payments made in the last year of life above defined thresholds) could also be taxed at a higher rate.

2020
Retirement Income Review

- Most retirees leave the bulk of the wealth they had at retirement as a bequest, despite the fact that superannuation savings are supported by tax concessions for the purpose of retirement income;
- There has been insufficient attention given to assisting people to optimise their retirement income through the efficient use of their savings; and
- People with very large superannuation balances receive very large tax concessions on their earnings.

2023
Grattan Institute – Super savings: Practical policies for fairer superannuation and a stronger budget

- Tax all earnings in retirement at 15 per cent, as already applies to earnings in the accumulation phase.
- Limit earnings tax breaks for balances of more than $2 million by implementing a High Super Balance Surcharge, whereby earnings on balances in excess of $2 million are taxed at 30%.

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Positioning of our report

This Discussion Paper examines the existing taxation framework for superannuation and suggests changes which could benefit the system in many areas. Our work aimed to identify improvements in relation to the **Simplicity**, **Efficiency**, **Equity**, **Adequacy** and **Sustainability** of the system.

We acknowledge that there are a variety of changes that could be applied to the taxation of the superannuation and retirement system. This is in addition to the much wider scope of changes that could be made if considering a complete redesign of the system.

Our Discussion Paper **aims to generate debate on an important matter**, with the intention of ultimately improving the system across and within generations of members. It is not intended to be a final position statement.

Analysis of current position

Simplicity

- Surveys found that 60% of respondents expressed various levels of uncertainty and negativity about being financially prepared or not having enough money to live in retirement.
- Lack of engagement, contribution and tax rules are complex; the choices of superannuation fund, investment options, insurance benefits, retirement

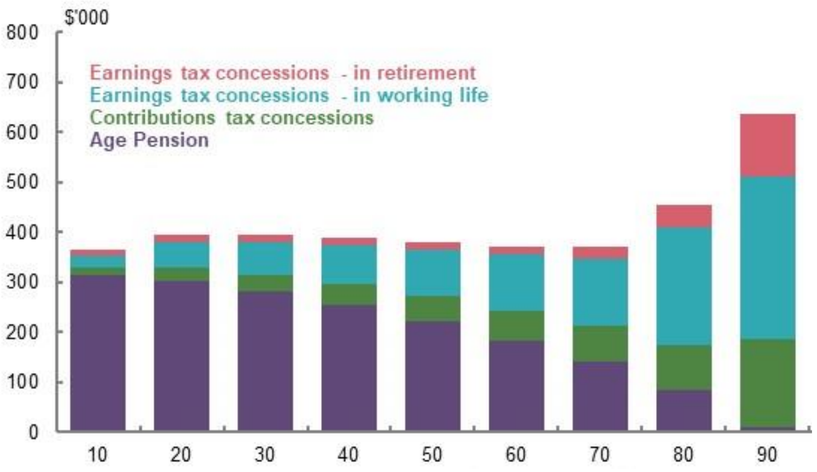
National Seniors 2023, Quality of Advice Review

Adequacy

- Current replacement rates for middle to higher income earners are generally adequate.
- For many lower income earners, the replacement rate is estimated to be above 100%, however, the quantum of benefits is low.

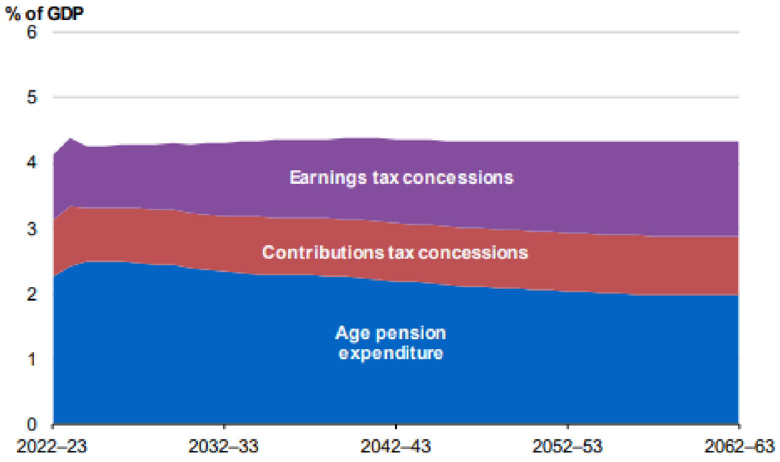
Retirement Income Review

Equity



Retirement Income Review

Sustainability



Intergenerational Report 2023

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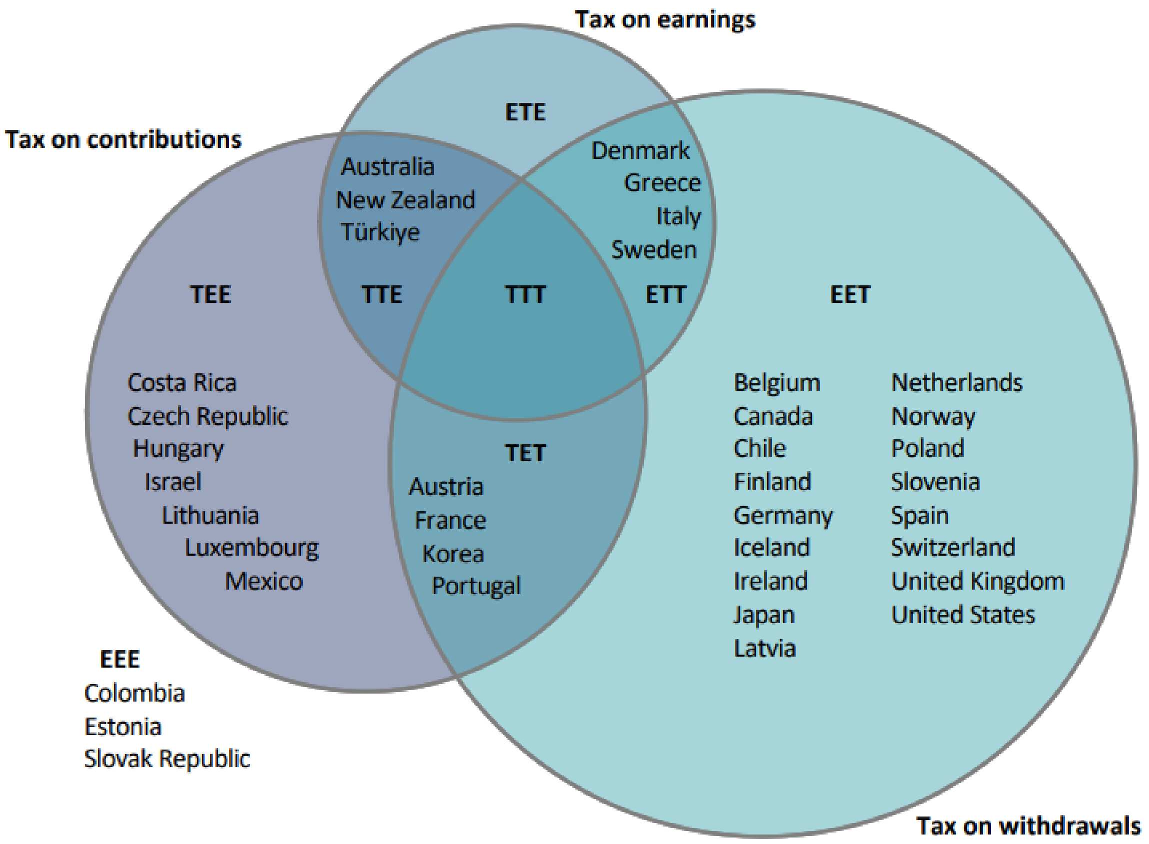
Levers for change

02

Tax treatment of retirement income

- Funded contribution schemes for retirement savings, similar to Australia's super system, operate in most OECD countries.
- Schemes vary in terms of their coverage, the degree to which contributions are mandatory or voluntary, and how the schemes are managed.
- Australia's super system can be denoted as TTE because it taxes contributions and earnings but not withdrawals



PBO presentation of Organisation for Economic Co-operation and Development (OECD) (2022) Annual survey on financial incentives for retirement savings, OECD country profiles 2022.

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Proposed reforms

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03

Analysing the impact of reform – approach

1 **Earnings**

2 **Benefits**

3 **Contributions**

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Uniform low tax rate on lifetime earnings in super

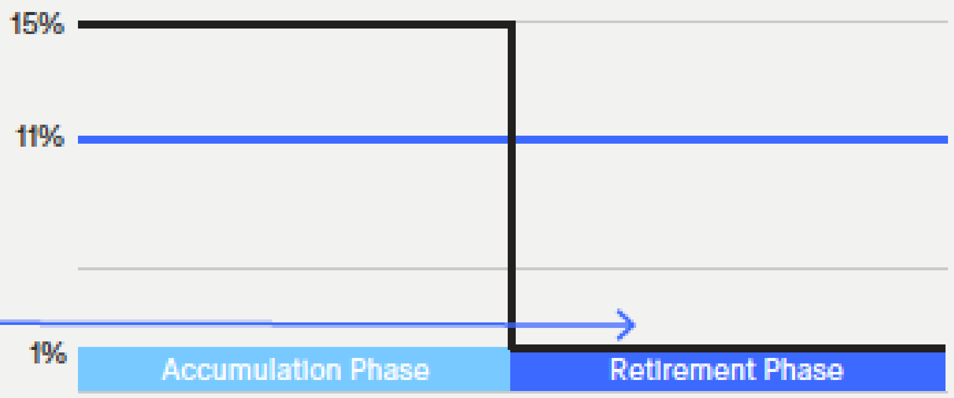
Proposed Reform 1: Earnings

Apply a single rate of tax on earnings across all accumulation and retirement accounts to improve the simplicity, sustainability and equity of the system

Current Rules

- **15% tax in Accumulation Phase**
- **No tax in Retirement Phase** Subject to moving super into a retirement account and the Transfer Balance Cap ($1.9m as of 1 July 2024)

Figure A: Headline Tax Rate on Earnings in Super



Note: Government has proposed an additional 15% tax on earnings from superannuation balances exceeding $3 million.

Proposed Rules

A uniform rate on earnings

- For example, a uniform rate of ~11% would be revenue-neutral for one decade

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Impose tax on very high benefits

Proposed Reform 2: Benefits

Impose a tax on very high benefits drawn in retirement and on death benefits, beyond the levels expected to be required to provide a suitable retirement income

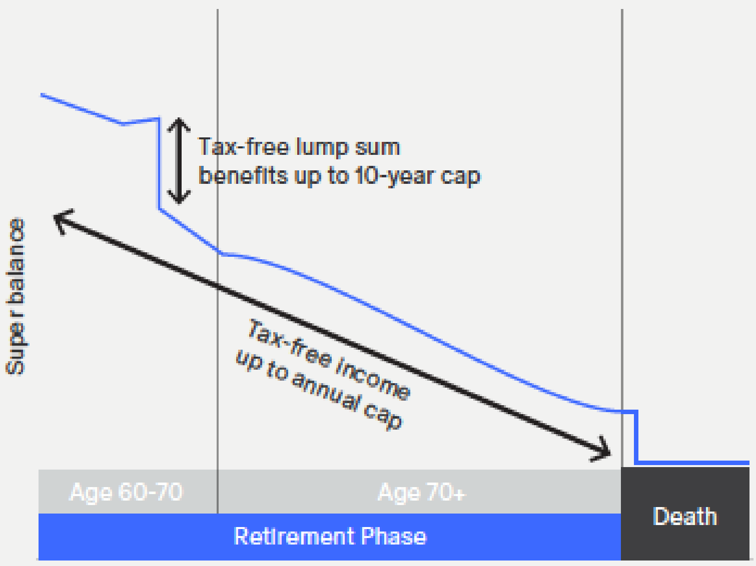
Current Rules

Tax-free retirement benefits from age 60 for both income and lump sum withdrawals (no upper cap)

Bequests for age 60+

- 17% tax on bequests to a non-dependent beneficiary
- No tax on bequests to a dependent beneficiary

Figure B: Taxation of retirement benefits (illustrative scenario)



Proposed Rules

- **Tax-free lump sum benefits from Age 60-70** Up to ~$250,000 - $566,000 in total
- **Tax-free retirement income benefits** Up to ~$150,000 - $190,000 each year
- **Excess withdrawals taxed** added to personal income and taxed

Bequests for age 67+

- 17% tax on any part of a bequest that exceeds ~$500,000
- A higher tax-free threshold of ~$2m could apply for dependent beneficiaries

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Treat all contributions into super the same once made

Current state:

- Concessional contributions are tax-deductible for the payer, usually an employer or a member making a personal
- Conversely, non-concessional contributions are made from after-tax funds.
- Both types are subject to annual thresholds BUT each contribution type is treated differently once made to a fund.

Issues with the current state:

- Separation of contributions adds unnecessary complexity to the system.
- Introduction of perverse outcomes, including so-called ‘recontribution strategies’

Proposed Reform 3: Contributions

Remove the distinction between concessional and non-concessional superannuation contributions once they have been made to the fund. Concessional contributions would remain assessable in the year they are received

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Impact of reforms

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Analysing the impact of reform – approach

Members

Government

Funds

Impact - Uniform low tax rate on lifetime earnings in super

Members

Table 2 - Expected Income to Age 92 for the 30-Year-Old Cohort — Couple

Taxation scenario	Estimated annual income to age 92 (wealth percentiles) – couples				
	10th	30th	50th	70th	90th
Current taxation system	$36,000	$50,300	$60,200	$70,000	$90,500
Uniform 10% tax on earnings in accumulation and retirement phases	$36,200	$50,300	$59,900	$69,500	$90,700

Table 3 - Expected Income to Age 92 for the 60-Year-Old Cohort — Couple

Taxation scenario	Estimated annual income to age 92 (wealth percentiles) – couples				
	10th	30th	50th	70th	90th
Current taxation system	$28,400	$36,700	$50,000	$73,800	$104,500
Uniform 10% tax on earnings in accumulation and retirement phases	$28,300	$36,200	$48,900	$71,500	$100,900

Table 4 - Expected Income to Age 92 for the 75-Year-Old Cohort — Couple

Taxation scenario	Estimated annual income to age 92 (wealth percentiles) – couples				
	10th	30th	50th	70th	90th
Current taxation system	$24,700	$31,200	$51,300	$72,500	$138,500
Uniform 10% tax on earnings in accumulation and retirement phases	$24,600	$30,900	$50,100	$70,300	$133,300

Younger couples (and individuals) benefit while older couples pay higher tax*, though some of this is 'paid back' through the retirement phase.*

Higher wealth households typically feel a greater impact *when compared to the lower wealth households.*

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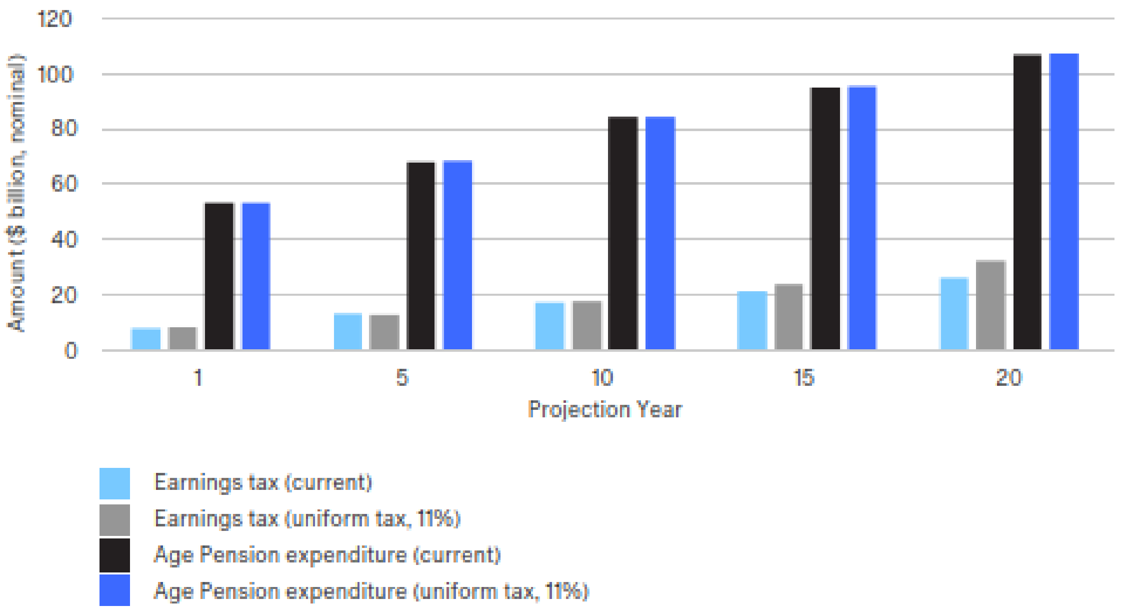
Impact - Uniform low tax rate on lifetime earnings in super

Government

Table 5. Comparison of Uniform Tax Rate of 11% with Current System

Projection year	Current tax ($b)	Uniform tax ($b)	Change ($b)
1	8.1	8.7	0.6
5	13.5	13.3	–0.2
10	17.5	17.8	0.3
15	21.6	24.2	2.6
20	26.6	32.9	6.3

Figure 5. Projected Earnings Tax and Age Pension Expenditure



Implementation of a uniform rate of around ***10-11% would collect approximately the same tax as the current system*** *over a 10-year period*

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Impact - Uniform low tax rate on lifetime earnings in super

Funds

- A single set of investment portfolios and unit prices for all accounts.
- Simpler documentation on investments
- A reduction in the number of accounts held by retirees.
- The elimination of a complex, and expensive, set of administrative tasks to move assets between accumulation and retirement phases.
- Easier record-keeping as there may be no need for the Transfer Balance Cap.
- Removing inefficiencies for those who stay (unintentionally) in accumulation phase.

We estimate that fee savings could be at least $850 million per year

Impact - Tax very high benefits

Members

- Imposing tax on very high benefits would leave the system mainly unchanged.
- Those receiving annual benefits exceeding about $180,000 would pay any tax, if they had no other personal income.

Government

- Taxing retirement income streams above $150,000 per year would yield approximately $200 million in tax revenue which is currently forgone.
- Equity between younger and older taxpayers.

Funds

- Period of upfront change and costs for superannuation funds.
- Processes could be streamlined going forward, leading to efficiencies.

Impact – Remove distinction between contributions

Members

- Single record of all contributions made into the fund
- Reduce ability to artificially benefit from recontribution strategies

Government

- No budgetary impact except on benefit payments.
- ATO would still maintain limits on levels of concessional and non-concessional contributions for each member.

Funds

- No longer be necessary to separate contributions into different types within fund accounts and to track them over time.
- Separate treatment when determining the tax on benefits removed.

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Combined system reform

If implemented as a complete tax-neutral package, we estimate that our combined reform would

- ***Reduce the level of complexity*** *within the system.*
- *Produce around* ***$1 billion in annual cost savings****, which could be passed on to members.*
- ***Improve the equity between*** *cohorts in the system without impairing intergenerational equity.*

Implementation and other considerations

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Implementation and other considerations

Winners and losers

As with any proposed reform, there are expected to be winners and losers

Age Pension adjustments

Potential to use Age Pension adjustments to compensate certain cohorts

Passage of time

Impact on those in retirement phase reduce over time

Behavioural impacts

Proposed reform could lead to withdrawals of excess assets from superannuation

Retirement products

Consideration of treatment for existing products, with consideration of complexity

Defined Benefit

Consideration of treatment for existing arrangement, with consideration of complexity

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Authors’ Answers to Audience Questions

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As the peak professional body in Australia, the Actuaries Institute represents the profession to government, business and the community, and serves the public interest by using data for good.

Actuaries use data for good by harnessing the evidence to navigate into the future and make a positive impact. They think deeply about the issue at hand, whether it’s advising on commercial strategy, influencing policy, or designing new products. Actuaries are adept at balancing interests of stakeholders, clients, and communities. They’re called upon to give insight on complex problems, they’ll look at the full picture. Actuaries analyse the data and model scenarios to form robust and outcome-centred advice.

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