SMSF
Owners' Alliance
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The Cracks Are Beginning to Show

Three days after the Government announced its grand solution for super the cracks are beginning to show.

- Many more than 16,000 will be affected by the new tax on super fund earnings
- The new contribution cap for over 50s and 60s is not indexed and its value will be whittled away by inflation
- The new $35,000 contribution cap for over 50s and 60s doesn't allow them to save enough to support themselves in retirement without relying on the age pension
- Even if the new cap is extended to younger workers, it's not enough to give them financial independence in retirement
- And, under the course set by the Government, eventually everyone will hit the $100,000 super tax threshold and be taxed on their super savings

Friday's statement was all about fixing a political problem. It did nothing to make the superannuation system more sustainable.

16,000 and counting

The Government claims only 16,000 people will be affected by assuming a $2 million super fund earning a 5% return will produce $100,000, triggering the new 15% tax. But in years when super funds earn more than 5%, smaller funds will be hit. For example, a rate of return of 12% will enable a fund of $850,000 to generate more than $100,000. In their recent report on super fund performance, Chant West revealed that for the first 8 months of this financial year, super funds achieved a rate of return of 13%, powered by a surge in share prices.

Depending on fund returns each year, many people may be pushed over the $100,000 threshold and be subject to the new tax. Revenue to the Government will be difficult to predict.

Anyone on an income of about $200,000, hardly 'fabulously wealthy', would need to have super earnings of $100,000 to achieve an adequate level of retirement income. The 'reasonable replacement rate' referred to in the Henry tax review is 60-70% of after-tax, pre-retirement income.

The $100,000 threshold may also be exceeded if a fund sells assets, e.g. an investment property and creates a capital gain. Under the present rules, capital gains are not subject to CGT but under the new arrangement they will be subject to a 15% tax when they push fund earnings for the year above $100,000.

To avoid this new tax, it is possible that people will sell assets, particularly 'lumpy' assets such as property before the new CGT rules come into effect, creating distortions in market values.

The $100,000 threshold is to be indexed by CPI, averaging around 2.5%. But income growth is faster, averaging around 4%, and over time more and more people will exceed the threshold.

The new contribution cap is not what it seems

First, the new contribution limit of $35,000 initially for over 60's and then over 50's is a watered down version of the higher caps for over 50's promised two budgets ago and not delivered. So people may be entitled to some scepticism about the new cap becoming reality.

Second, the contribution limit is not indexed. This means that over 8 years, the new limit of $35,000 will be whittled back by inflation to the equivalent of the current figure of $25,000. These mature age super savers will be back to where they are now.

SMSFOA supports higher contribution caps, especially for people in their 50s and 60s who need to supercharge their super savings in the final years of their working lives. But this measure does not go far enough.

Voluntary contribution caps need to be increased to at least $50,000 for everybody. The tax expense for super savings incentives will be repaid times over in public pension costs.

Two perverse outcomes

If the rules announced by the Government remain in place, we are set to achieve two perverse outcomes:

- Nobody will be able to save enough under the non-indexed contribution cap to be able to spend their retirement years without having to rely on the aged pension
- Everybody will at some stage exceed the $100,000 super savings threshold and be taxed on their fund earnings

While it is to be hoped that some future government will rectify this problem, this is the course on which the country is now set under the Government's new super measures.

The analysis to support our contention is attached.

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