SMSF Owners' Alliance
Limited ABN 96 161 052 464
Not-for-profit public company

Members' Newsletter #10/15

In this newsletter:

- SMSF Owners congratulates Malcolm Turnbull on becoming Prime Minister
- We again challenge the $32 billion myth
- We question Westpac's chairman on why his bank thinks it's OK to put a new tax on its customers.
- Professor Sloan gets it right again

Memo Malcolm: No new tax on super

SMSF Owners has written to Malcolm Turnbull to congratulate him on his appointment as our new Prime Minister and to urge him to resist calls for a new tax on retirement earnings that will hit SMSFs.

Our Chairman, Bruce Foy, wrote:

"At the next election Australians will have a choice between the Labor Party, which wants to impose a new tax on superannuation savings, and the Coalition which currently has no plans for additional taxes on superannuation.
We hope that will continue to be the case."

Our letter goes on to say that *"changes to the superannuation system should only occur after a comprehensive and thorough review of its purpose and performance. The taxation of superannuation should not be increased because the budget has been mis-managed by the previous government or in response to perceptions of unfairness based on faulty mathematics."*

As we've mentioned in previous newsletters, the stage is set for the taxing of the retirement income of superannuation fund members to be a central issue at the next federal election – whenever it comes.

As Prime Minister, Tony Abbott took a firm line against Labor's new superannuation tax and ruled out any adverse and unexpected changes.

We hope that Mr Turnbull will also resist the pressure to increase superannuation tax and make other changes to the rules without a comprehensive review of the whole of Australia's retirement income system.

Here's our letter to the new PM.

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17 September 2015

Hon Malcolm Turnbull MP
Prime Minister
Parliament House
CANBERRA ACT 2600

Dear Prime Minister

We wish to join many other Australians in congratulating you on your election as Leader of the Liberal Party and your commission as Prime Minister.

Many hope that you will lead the Coalition to victory at the next federal election – none more so than the one million Australians who have taken responsibility for their financial independence in retirement by setting up their own self-managed superannuation funds.

At the next election Australians will have a choice between the Labor Party, which wants to impose a new tax on superannuation savings, and the Coalition which currently has no plans for additional taxes on superannuation.

We hope that will continue to be the case.

Superannuation is a lifetime investment, spanning work, retirement and old age, in which Australians must have confidence. Talk of changes to the taxation of retirement savings creates uncertainty, anxiety and loss of confidence.

This is not to say that changes should never be made. Superannuation is an evolving system and can be improved. But change should only occur after a comprehensive and thorough review of its purpose and performance.

The taxation of superannuation should not be increased because the budget has been mis-managed by the previous government or in response to perceptions of unfairness based on faulty mathematics.

The Financial System Inquiry made some comments on superannuation but they did not amount to a holistic review. We are yet to see the outcome of the Tax White Paper process.

In our submissions to the Tax White Paper Taskforce, we pointed out some common fallacies about superannuation and suggested ways the system could give better outcomes for savers with neutral budget impact. We showed that while tax concessions provide a necessary incentive for retirement savings, they are a relatively minor source of superannuation assets with by far the strongest driver of asset growth being the accumulated earnings on contributions.

Claims that the taxation concessions for retirement savings are unfair are often based on the claim that they cost the budget $32 billion and more. This claim is drawn from the Tax Expenditures Statement (TES) issued by Treasury but it is misleading and erroneous. As the Assistant Treasurer and the Treasury have pointed out, this figure is the result of a double counting error and can't be used to indicate revenue savings if tax concessions are removed or reduced. Further, it doesn't take account of increased Age Pension costs if less money flows into superannuation as the result of increased taxation.

A structural issue with the TES is that it will produce significantly different numbers depending on the benchmark used. Treasury uses a benchmark that is not used by most comparable countries.

The other claim often made by those who want to tax superannuation more because it is ‘unfair’ is that more than half of the tax concessions go to the top 20% of income earners. This is true but ignores the fact that the same top 20% pay two thirds of the income tax collected and pull their weight when it comes to paying tax.

These fallacious claims have been used to justify the superannuation taxation policies of both the Labor Opposition and the Greens.

Challenging and dispelling myths about the cost of superannuation is a key focus of SMSF Owners’ which is an independent voice for the trustees and beneficiaries of self-managed funds. We are a not-for-profit advocacy group actively engaged in a policy debate overly dominated by the special interests of the large industry and retail funds, by left-leaning think tanks and by those envious of the success of others in achieving financial independence in retirement.

We have a good working relationship with the Assistant Treasurer and his office and look forward to continuing to work with your Ministers in the best interests of all Australians with superannuation and especially those who have shouldered responsibility for managing their own retirement savings.

Yours sincerely

Bruce E Foy
Chairman
SMSF Owners’ Alliance

Tackling that $32 billion number again

Readers of this newsletter will know that we have mounted a sustained challenge to the credibility of Treasury’s annual Tax Expenditures Statement (TES) on which claims that superannuation tax concessions cost $32 billion a year, and more, are often based. We have kept up the pressure on this issue because it’s the starting point for the argument that tax concessions on retirement savings are too expensive for the budget and unfairly benefit high income earners. It’s not and they don’t.

The latest episode is an inquiry by the House of Representatives Standing Committee on Tax and Revenue which is currently examining the TES. One of the things the Committee wants to know is why improvements recommended by the Australian National Audit Office as far back as 2008 have not been implemented by Treasury. Lack of resources has been Treasury’s response in Committee hearings.

We are more focussed on why Treasury uses a different benchmark than other countries for calculating the TES number on superannuation and why it hasn’t been more pro-active in pointing out that the two components of superannuation tax concessions – on contributions and earnings – can’t simply be added together as some commentators and politicians often do, intentionally or not. Both the Labor Party and the Greens double count the TES numbers to justify their policies for a new tax on retirement incomes which will mostly hit self-managed fund beneficiaries.

SMSF Owners has lodged a submission with the Tax and Revenue Committee and we are waiting for the Committee’s approval (under the rules that apply to Parliamentary Committees) for us to publish it. We’ll post it to our website.

In the meantime, if you would like to see the submissions already published, go to:

http://www.aph.gov.au/Parliamentary_Business/Committees/House/Tax_and_Revenue/Tax_Expenditures/Submissions

We recommend the submissions by Robert Carling and Mercer as particularly worth reading.

A question for Westpac - why do you want your customers to pay more tax?

In our last newsletter we questioned the propensity of associations in the superannuation sector to propose taxes on their customers.

We've also raised this issue with one of the major banks – Westpac – since it supported a limit on superannuation accounts in its Tax White Paper submission and the CEO of the Westpac funds manager BT gave a speech to a business audience advocating such an approach.

Following concerns expressed by members, we wrote to the Chairman of Westpac, Lindsay Maxsted, to ask why his bank thought it was OK to offer up its customers' money in advocating a new tax.

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Lindsay Maxsted
Chairman
Westpac Group
275 Kent Street
SYDNEY NSW 2000

Dear Mr Maxsted

I refer to Westpac Group's submission to the Taxation White Paper and a more recent speech by the CEO of BT Financial Group, both of which advocated that a cap should be placed on tax free earnings on superannuation accounts of $2.5 million. Above that limit, according to Westpac/BT, earnings should be taxed.

Accounts of this order are commonly held in self-managed superannuation funds.

Concern has been expressed to us by our members who are customers of Westpac, including customers of the Private Bank, about the Bank's position on this issue. They want to know why the Bank is proposing a new tax on them when they believe the Bank's role is to safeguard their investments and to help them grow their wealth.

Self-managed funds are significant investors in Westpac and other banks and hold a substantial amount of cash in banks. The ATO statistics show that self-managed funds held $177 billion in shares at June 14. Based on the Big Four banks' 27% share of ASX 200 market capitalisation, self-managed funds hold about $48 billion in bank shares.

The ATO statistics show that in June 2014 self-managed funds held $158 billion in cash and term deposits.

Self-managed funds and their members also entrust their assets to BT and other wealth management providers. The ATO figures show that self-managed funds held $22 billion in 'other managed investments' which would include accounts with BT.

As well as their self-managed fund investments, SMSF owners are most likely to hold personal, business and other accounts with their bank.

I am sure you would agree that Westpac's first duty is to its shareholders and that it also should act in the interests of its customers.

Then why is Westpac/BT advocating a new tax on them?

Westpac's White Paper submission proposed a limit on tax-free superannuation savings of $2.5 million: "To the extent that a small number of very large superannuation holdings are adversely affecting the perception of fairness in the superannuation system, we support appropriate changes to address these concerns. We favour specific, highly targeted measures aimed at curbing any distortions instead of widespread changes to the existing scheme that impact all members." Subsequently, the CEO of BT Financial Group argued in a speech to the Trans Tasman Business Circle that tax free superannuation benefits should be set at a level "that affords a decent quality of life" which he estimated at $150,000 or twice average weekly earnings.

We question whether "perceptions of fairness" are a proper basis on which to base public policy decisions that will affect many Australians now and in the future.

We also question whether highly paid bank executives should be judging what is "a decent quality of life" for others.

This is surely for people to judge for themselves and set their savings goals accordingly.

It is often claimed by those promoting limits and new taxes on superannuation savings that they are justified by the cost to the budget of superannuation tax concessions and that the value of these concessions unfairly benefit people on higher incomes.

Both of these claims have been debunked.

The Assistant Treasurer, for one, does not accept them. In a speech on 3 June he said: "The numbers in the TES (Tax Expenditures Statement) are not budget costings...the TES is not meant to show how much better off the budget would be if the tax concessions were removed". He also stated that the components of superannuation tax concessions - tax on contributions and tax on fund earnings - cannot simply be added together to come up with a large number. And the head of Treasury's Revenue Group has cautioned that the TES figures on superannuation tax concessions is not the amount that could be saved if the concessions were removed and cannot be relied upon in setting policy.

So much for the often quoted but mythical '$32 billion' cost of superannuation tax concessions.

Secondly, are they unfairly targeted? Much is made of the fact that the top 20% of income earners get 57% of the value of superannuation tax concessions. However, there is little recognition that those same income earners pay 64% of income tax. As the Treasurer has pointed out, the top 2% of taxpayers pay 26% of income tax.

The CEO of BT Financial Group referred to "incredibly high levels of wealth" in some superannuation funds. Only a small fraction of self-managed superannuation accounts have more than $5million (0.4%), the larger ones having been accumulated legitimately under earlier tax regimes. Under present contribution limits, it is unlikely such amounts can be amassed in the future. We agree that there should be some limits on the availability of tax concessions so that the superannuation system's objectives can be achieved at the lowest cost to the Government budget. However, these limits are already there as annual limits on tax-deductible contributions. This is the appropriate place for such constraints. Any serious economist would know that taxing or constraining super earnings or balances is economically inefficient.

Furthermore, the experience of the previous Government was that trying to impose an earnings tax on a relatively small number of high balance accounts was practically difficult and would not raise much revenue.

We would welcome a response from you that we can provide to our members who are concerned about the position Westpac has taken.

There is much in Westpac's submission to the Tax White Paper with which we agree, particularly the need for a more flexible contributions regime.

In SMSF Owners' submission, based on research findings from our Pension Sustainability Model, we showed how the present system could be improved to give better savings outcomes and reduce the overall taxation of superannuation with a neutral impact on the budget.

Consistent with the wishes of the Treasurer, we also made a brief supplementary submission demonstrating a strong consensus among some leading organisations regarding some key retirement income principles. We attach this for your information and invite you to join this group if you agree with these principles.

We would be pleased to discuss these matters with you at your convenience. We look forward to your response which we will send to our members.

Yours sincerely

Bruce Foy
Chairman
SMSF Owners' Alliance
0411 551 855

In his reply, Mr Maxsted noted that Westpac had always been a vigorous participant in in debate over the development of the economy in accordance with the bank's understanding of the current economic and social challenges at play.

He said that Westpac would keep in touch with SMSF Owners and "appreciate and respect" our views in the ongoing policy debate. He asked the CEO of BT, Brad Cooper, to stay in contact with us. We'll let you know if and when this happens.

Mr Maxsted's response is on the next page.

Westpac GROUP

EST. 1817

LINDSAY MAXSTED CHAIRMAN, GPO BOX 1, SYDNEY NSW 2001 **TELEPHONE** (02) 8253 3037 **FACSIMILE** (02) 8254 6578

28 August 2015

Mr Bruce Foy
Chairman
SMSF Owners' Alliance
PO Box R1490
Royal Exchange,
SYDNEY NSW 1225

Dear Mr Foy,

Thank you for your letter, which I received on 19 August 2015, raising concerns over a recommendation in Westpac Group's submission to the Tax White Paper and recently covered in a speech by Brad Cooper.

I appreciate your raising these concerns directly with me and acknowledge your support of other recommendations we have made in that submission including advocating for more flexible contributions.

Brad Cooper's speech was a genuine attempt to contribute ideas for debate on the best framework for our future superannuation system. While the media have focused on the tax framework applied to high balances, I do hope you see our contribution to this debate as something much broader. As Australia's oldest bank, Westpac has always been a vigorous participant in the development of the economy, offering solutions and having discussions about how we can help our communities to prosper and grow. When we participate in such discussions we endeavour to do so with our understanding of the current economic and social challenges at play.

To provide the broader context to the specific recommendation over which you raise concern, I have asked that you be forwarded a copy of Brad's entire speech.

I have also asked Brad to stay in contact with you and gather any other feedback you may have regarding the speech and the overall framework proposed. As part of the ongoing debate, Westpac would appreciate and will respect your views on other proposed solutions or improvements designed to assist Australia's superannuation framework meeting the needs of all Australians in the future.

Yours sincerely,

Lindsay Maxsted
Chairman

Finally, another excellent article by Professor Judith Sloan of Melbourne University. We've run several articles by Professor Sloan – she just keeps getting it right.

Few minor tweaks will bring a super system that works for all

- by: *Judith Sloan*
- From: *The Australian*
- September 15, 2015 12:00AM

Contributing Economics Editor
Melbourne

I am really pleased the government decided against having a separate inquiry into retirement incomes. Apart from the fact there are wall-to-wall inquiries already going on, a separate retirement incomes inquiry would greatly increase the flow of loopy ideas on the topic.

Let's face it, these loopy ideas have been coming thick and fast without a separate inquiry. This month we have had the bizarre report of the Committee for Economic Development of Australia entitled: "The super challenge of retirement income policy."

And the report of the Institute of Actuaries, also released last week, was not much better.

Entitled For Richer, For Poorer, it has as one conclusion that "there is a 50-fold difference in wealth between those in the top 5 per cent income bracket and about to retire and those at the bottom 5 per cent. This reduces to 10-fold for those who will retire in 30 years' time, confirming the importance of the Superannuation Guarantee in providing an element of social equity."

Is this a joke? You make people on modest incomes give up 9.5 per cent of their wage — and increasing to at least 12 per cent if groups such as the Institute of Actuaries have their way — year after year.

They forgo important expenditures such as buying a home, meeting expenses related to children, paying bills and food even, but that's OK because the gap in the wealth between the top 5 per cent and bottom 5 per cent will be narrower in 30 years. That will really make those on low and middle incomes feel better.

But it gets worse. The report shows that "the least wealthy sections of the community, both now and in the future, will continue to be entirely dependent on the age pension to maintain even a modest lifestyle". In other words, they are forced to save in the form of compulsory superannuation and end up where they would have anyway. That's social equity for you.

And for middle-income earners, their rational response to enforced savings is to prolong the period of their mortgages (many people in their 60s now have mortgages) and to use the modest lump-sum superannuation payout to pay off the house, renovate the house, buy a new car and perhaps have a much anticipated overseas trip. After all, a full or part pension awaits them when they turn 65.

One of the issues that really gets the retirement income rent-seeker crowd into a lather is the supposed need to specify the objectives of the superannuation system.

For reasons that are not very clear, this was one of the recommendations of the Murray report into the financial system.

I'm not sure what hangs on the answer. But the real point is that syrupy efforts such as CEDA's really do not progress the debate.

According to CEDA, "our retirement system should ensure Australians can retire with dignity and an adequate living standard, while providing a social safety net for those who cannot afford to save enough for retirement".

It's hard to argue against dignity but, then again, it's hard to define dignity.

And there is no acknowledgment of the moral hazard in the system. If taxpayers provide the wherewithal to allow retirees to live with dignity and an adequate living standard, it's perfectly rational to spend, spend now, rather than save, save now, subject of course to the enforced savings that is superannuation.

Then there is this contribution from the Institute of Actuaries: "to provide income in retirement to substitute or supplement the age pension". How does having that as the stated objective help at all? Mind you, it's one thing to live with a largely meaningless legislated definition of the objective of superannuation, it's another thing altogether to buy into the quite bizarre proposals of these two reports.

They include allowing first-home owners to pay their mortgages using pre-tax incomes; making super contributions post-tax (yes, that's right, making people pay the full marginal tax on their contributions to be locked up for 40-odd years); reviewing superannuation tax concessions; including the family home in the assets test for the age pension (which would leave wealthy people completely unaffected); taxing bequests; and raising the superannuation guarantee charge (of course).

So if everyone is having their two bob's worth, I think I can state what I think are the most important principles that should govern retirement incomes policy:

• People should be encouraged to provide for their own retirement as much as possible.

• People who work hard and make a lot of money should not be penalised for their efforts in retirement.

• Some people have a legitimate objective of leaving money and assets to their children.

• The tax system should acknowledge that superannuation is a long-term saving product, not annual income, and be taxed accordingly.

• The ideal system would be tax exemption for superannuation contributions and earnings and full tax for retirement earnings.

• It is just too difficult to achieve this ideal from our current starting point and so it is best to leave the taxation of superannuation well enough alone.

• People make long-term plans in relation to their retirements based on reasonable assumptions about government policies.

• The need for stability is paramount — any radical overhaul of the system should be avoided.

If I had my druthers, I would scrap the system of compulsory superannuation, in part because it is such a dud deal for low and middle income workers. What it mainly does is create an artificial industry of overpaid fund managers, managers and trustees. That is not an appropriate objective of government policy.

But I'm prepared to live with it — although the SGC should be kept at 9.5 per cent indefinitely — subject to the absence of the much-promoted "major overhaul" of retirement incomes policy.

Having said that, I want a superannuation system that is competitive, well-governed and charges low fees, all of which can be achieved by some minor tweaks.

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That's all until our next newsletter.

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