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

SMSFOA Members' Newsletter

#2 /2016

Dear Members

In this newsletter:

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PM changes the game on tax policy

To state the obvious, the tax policy landscape has changed dramatically over the past two weeks.

The Prime Minister has taken an increase in the GST off the Government's policy agenda…and removed it as an issue for the election due later this year.

Going by what the Prime Minister has said, tax changes are likely to be announced in the May Budget which has now taken the place of the Tax White Paper. Some indication of the Government's plans may be given before the Budget.

Changes to the taxation of superannuation are still very much on the cards.

Last month we wrote to the Treasurer, Scott Morrison and the Assistant Treasurer, Kelly O'Dwyer, about a better way to tax superannuation. This month we've followed up with a letter to Malcolm Turnbull to make the same point to him – see below.

You can help us drive the message home to the Coalition

In the next few weeks, while the Government decides the tax policies it will announce in the Budget and take to the election, it's important we get key messages get through to Ministers but also to the backbench Coalition Members and Senators.

- Changes should only be brought in if they make superannuation more efficient and effective as a savings vehicle.

- The Budget should be brought into balance by reducing spending, not raising more tax and especially not by snatching savings. The nation's savers should not have to pay for Labor's reckless spending in government.

- Any changes to superannuation tax should not be retrospective. This would be highly unfair to people who have saved for retirement under the existing rules.

- Tax incentives are given to encourage people to save for the future. People who have successfully done what the Government wants them to do should not be penalised for their success.

- Claims that superannuation tax concessions unfairly benefit those on higher incomes are based on incorrect use of Treasury numbers (Tax Expenditures Statement) which even Treasury says should not be relied on as a measure of the cost to the Budget of super tax incentives.

- The TES does not take into account future savings to the Budget in Age Pensions because superannuation gives people the opportunity to look after themselves.

- The top 20% of income earners get a greater share of super tax concessions (57%) simply because they contribute more, but they also pay an even greater share (64%) of income tax in the first place.

- People who set up SMSFs have made the commitment to be financially independent in retirement and old age – they don't want ever to fall back on the Age Pension.

- There are one million members of SMSFs who expect the Liberal-National Coalition Government to protect their savings.

Please consider writing to your Coalition Member and Senators to make these basic points in your own words and any other messages you want to get across.

You can either do it the old-fashioned way by writing and posting a letter or you can do it via email or making a comment on the politicians' Facebook and Twitter accounts.

We'd like to give you a handy list of email addresses but Parliament House does not publish an overall email list.

However, it's easy enough to check your particular Member's/Senator's email – go the this address:
http://www.aph.gov.au/Senators_and_Members/Guidelines_for_Contacting_Senators_and_Members

Or just Google your Member's/Senator's name and this will take you to their own websites where you can leave a message. Politicians tend to be more responsive if their own electors write to them.

Remember, you are one in a million – let them hear your voice.

Our letter to the PM

SMSF
Owners'
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8 February 2016

Hon Malcolm Turnbull MP
Prime Minister
Parliament House
CANBERRA ACT 2600

Dear Prime Minister

The SMSF Owners' Alliance speaks for the one million Australians who are trustees/members of self-managed superannuation funds, the largest segment of the superannuation sector.

They have a significant interest in the outcome of the Government's tax reform process, particularly as it applies to superannuation.

With regard to superannuation tax policy, the Government should be guided by these principles:

1. Changes should be made only to make the system work better and should not be driven by revenue needs.
2. No new taxes should be applied to retirement income, in contrast to Labor's policy.
3. Any changes to superannuation should not have an adverse retrospective effect on people who have saved under the existing rules.
4. The money in superannuation belongs to the people who saved it – tax incentives amount to a fraction of fund balances with the main sources being contributions (concessional and non-concessional) and accumulated earnings.

We have noted with interest media reports in recent days that you may be attracted to changing the front-end structure of superannuation tax by replacing the current flat tax rate on contributions with an equal tax rebate.

We strongly support this approach.

SMSF Owners proposed in our submission to the Taxation White Paper process and in our Pre-Budget submission that the Government adopt a tax rebate in conjunction with lowering the income tax scales to address the issue of bracket creep. We were pleased to see that our recommendation was later supported in the Deloitte Access Economics 'Myth Buster' report.

The Government could go further and remove the tax on superannuation fund earnings in the accumulation phase. Combined with a tax rebate on contributions for individuals, this would mean there would be no tax applied to superannuation funds at all, resulting in a much simpler, more efficient and less costly system and the potential for fund balances to grow faster.

Our modelling shows this could be achieved with a positive impact on revenue so long as the front-end adjustments to contributions and the tax scales are made.

This would be more consistent with the International Standard EET approach than the TTE approach that has developed in Australia with ad hoc policy changes over time.

It is too late to turn the ship around and revert to an EET system, but moving to a TEE system would be a constructive step.

Our modelling shows that with these changes, a reasonable replacement rate of 60-70% of pre-retirement, post-tax earnings could be achieved on the current contribution caps. However, if these changes are not made, the contribution cap would need to be at least doubled to $60,000.

We would be pleased to discuss our ideas and modelling further with the Government.

On one other issue that may be in the tax policy mix leading up to the Budget, dividend imputation was introduced, correctly in our view, to eliminate double taxation of corporate profits. Criticism that Imputation distorts the market is incorrect. Removing or reducing imputation credits to investors, including superannuation funds, would be devastating to an already depressed and nervous share market.

Yours sincerely

Bruce Foy
Chairman
SMSF Owners' Alliance

Copies:

Hon Scott Morrison, MP
Treasurer

Senator the Hon Mathias Cormann
Minister for Finance

Hon Kelly O'Dwyer MP
Assistant Treasurer

Martin Parkinson PSM
Secretary, Department of Prime Minister & Cabinet

John Fraser
Secretary, The Treasury

Attachments:

1. SMSF Owners' Supplementary Submission to the Better Tax review – 24 July 2015
2. SMSF Owners' Pre-Budget Submission – 4 February 2016
3. Media Releases
    a. Change super tax only to make it work better – 4 February 2016
    b. Memo to Treasurer – drop all taxes on superannuation earnings – 20 January 2016
    c. Equal super tax concessions for all can work – 10 November 2015
    d. Change super tax for the better, tax it less – 3 June 2015

Leave imputation alone

Among the tax changes being pushed by interest groups is getting rid of dividend imputation – suggested by the Australian Industry Group as a trade-off for lowering company taxes. We say in this media release that company tax should be lower but not at the expense of shareholders.

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Getting rid of imputation to reduce company tax is a bad idea

11 February 2016

In the lead-up to the Budget, all sorts of ideas for tax reform will be floated. Some will have merit, others won't.

The suggestion by the Australian Industry Group to withdraw dividend imputation to pay for a lower company tax rate is one without merit.

Of course Australia's corporate tax rate of 30% should be lower to compete for investment with other countries, particularly in Asia.

But lowering the company tax rate to 20% whilst dropping imputation as proposed by AIG will immediately drop the value of Australian companies to their Australian shareholders by 20%! It would knock the market for six at a time when it is already reeling.

This simple table shows how a shareholder on a marginal tax rate of 37% (or any other marginal rate) would get a 20% lower return, therefore reducing the value of the company's shares to investors by 20%.

	30% company tax rate with Imputation	20% company tax rate without imputation	
Company profit	$100	$100	
Company tax	$30	$20	
Dividend paid	$70	$80	
Imputation credit	$30	$0	
Total shareholder taxable income	$100	$80	
Tax paid by shareholder@37% marginal rate	$37	$29.6	
Net return	$63	$50.4	
Loss in investment return		$12.6	20%
Therefore drop in value of company share to investor			**20%**

On the example above, the investor’s effective tax rate is increased from 37% to 49.6%.

Imputation is not a tax concession. It is a credit to shareholders for tax on company profits that has already been paid. Without imputation, returns on investment would be double taxed, first via the corporate tax on profits and then on dividends issued to shareholders.

This credit is only available to Australian taxpayers. So removing imputation would disadvantage Australians who invest in Australian companies and the lower tax rate gives an advantage to foreign investors. This does not have political appeal.

Another bad outcome of removing imputation would be to distort the balance between equity and debt in corporate capital raising.

Imputation puts equity on the same effective tax basis as debt. Without full imputation, debt finance will be relatively cheaper, inevitably leading to greater use of debt funding and an increase in corporate gearing with consequent increase in risk.

Removing or reducing the imputation credit would distort and devastate the Australian equity market. The impact on an already depressed and nervous market would be catastrophic.

SMSF Owners supports constructive change to the taxation system in accord with the Government’s objective to make the tax system work better and foster economic growth. Dropping imputation to fund a cut in the company tax rate is not the way to achieve this goal.

Shareholders’ Association Conference

SMSF Owners has a good relationship with the Australian Shareholders’ Association and we have similar views on policy issues – after all, most SMSF owners hold shares. So we’re pleased to promote to our members the ASA’s **2016 Grow Your Portfolio Conference** to be held from **16-17 May at Sheraton on the Park, Sydney**.

The ASA have built an impressive program with high calibre, thought-provoking speakers ensuring you receive the maximum return on your registration investment. The comprehensive program includes the following streams:

1. Buying and selling shares
2. Investor’s toolkit
3. Investor’s opportunities
4. Investor’s alternatives

Registrations are now open for the two day conference with an optional third day. **Register before 15 March 2016 to take advantage of the Early Bird price of $515 per person, which includes a discounted Green e-Membership to the ASA.**

For further information on ASA membership, please visit the ASA website
https://www.australianshareholders.com.au/membership-options/member-plans

Optional extras include the always popular Conference Dinner, Investment Disruptors full day seminar on Wednesday 18 May and the following Site Tours:

- Lend Lease site tour – tour Barangaroo site – 18 May
- Stockland site tour – 18 May

- Virtus Health site tour – 18 May
- Woolworths site tour – 19 May

There are a strictly limited number of places available for these Site Tours which will be allocated on a first come first served basis, and are **only available to conference delegates and their partners**.

Full details and more information about the conference are available on the ASA website: https://www.australianshareholders.com.au/conference-2016

Professor Sloan nails it again

We regularly quote Professor Judith Sloan in this newsletter because her commentary is relevant, well-based and exposes the fallacies in attacks on superannuation tax concessions. Here's her latest demolition job on the much-quoted but unreliable Treasury Tax Expenditures Statement.

THE AUSTRALIAN

Treasury struggles with the mathematics of super forecasts

- JUDITH SLOAN
- THE AUSTRALIAN
- FEBRUARY 16, 2016 12:00AM

CONTRIBUTING ECONOMICS EDITOR

MELBOURNE

JUDITH SLOAN IS AN ECONOMIST AND COMPANY DIRECTOR. SHE HOLDS DEGREES FROM THE UNIVERSITY OF MELBOURNE AND THE LONDON SCHOOL OF ECONOMICS. SHE HAS HELD A NUMBER OF GOVERNMENT APPOINTMENTS, INCLUDING COMMISSIONER OF THE PRODUCTIVITY COMMISSION; COMMISSIONER OF THE AUSTRALIAN FAIR PAY COMMISSION; AND DEPUTY CHAIRMAN OF THE AUSTRALIAN BROADCASTING CORPORATION.

I can be a serious sad sack — I much prefer fun Judith — and I have been poring over a lot of figures on superannuation taxes and the Treasury's quaint estimates of tax expenditures associated with superannuation tax concessions.

And I have found some remarkable discrepancies, which really make you wonder how competent the Treasury is when it comes to forecasting revenue and estimating the cost of the tax concessions.

But, perhaps more important, these errors are completely ignored by the various commentators pushing for higher taxes on superannuation.

Let's start with the superannuation taxes the government collects. These take two main forms: the 15 per cent tax on contributions (30 per cent for those earning more than $300,000 a year) and the 15 per cent tax on earnings.

This financial year, the government expects to collect a tad over $7.7 billion in superannuation taxes, according to the mid-year economic and fiscal outlook. This is down by $1.35bn from the figure predicted only seven months before at the time of the 2015 budget. That's a difference of 17.5 per cent.

If we look over a longer timeframe, the forecasting errors are even more substantial.

Consider Wayne Swan's last budget in 2013. He was always keen to massage the figures to make the budget bottom line look better. The 2013 budget projection of superannuation taxes for this financial year (2015-16) was $12.65bn. Oops — the actual figure will be only just more than 60 per cent of that figure, a tiny fraction of the difference attributable to the decision to defer the rise in the superannuation guarantee charge.

If you go to the budget papers, you can read all the excuses put forward for the large forecasting errors in superannuation taxes that have been evident for many years. In real the-dog-ate-my-homework style, there is talk of lower than expected capital gains, tax losses, weaker wage growth and foreign exchange losses. But, hang on, don't we expect Treasury officials to be expert at predicting these sorts of eventualities?

And the boon in tax revenue that was to result from large super funds being forced to pay superannuation taxes on a monthly pay-as-you-go basis — another Swan special — has failed to make any material difference to the flow of taxation receipts.

Now, the real trouble with Treasury's inability to provide accurate figures on future superannuation tax revenues is that the government spends the revenue willy-nilly. (This is true at the broader level, of course.) But when the final day of reckoning is reached, the budget is found to be in much worse shape than expected. But if you think the forecasting errors in relation to superannuation taxes are something to behold, hang on to your hat when it comes to Treasury's estimates of the cost of superannuation tax concessions provided in the annual tax expenditure statements. That the cost has been written down by nearly 30 per cent from one year to another doesn't seem to faze the relevant Treasury officials one little bit.

According to the 2014 tax expenditure statement, the cumulative tax expenditures associated with the concessional taxation of superannuation entities (the 15 per cent on earnings and other bits and pieces) was $78bn. Twelve months on and the figure miraculously has shrunk to $55.5bn.

Strangely, I didn't see any of the zealous commentators who gleefully but mistakenly quote the supposed $30bn odd a year that the concessional taxation of superannuation is costing the government — nearly the size of the age pension bill is also thrown in for good measure — mention this very substantial writedown. Here's the headline: superannuation concessions cost us less.

It turns out that Treasury had vastly over-estimated the returns that superannuation funds would make and so the figures have had to be significantly scaled back. While Treasury notes that the reliability of the figures are low — no kidding — this point is never picked up in those advocating even higher taxes on superannuation, at least for those on middle and high incomes.

But the Treasury continues to stick with its flawed methodology of using personal income tax as the benchmark rather the GST (which is a tax that encourages saving) because other forms of saving are taxed as personal income tax.

What the Treasury doesn't acknowledge is that other forms of saving are not locked up for decades until individuals reach their preservation age — a point that differentiates superannuation from other forms of saving. And notwithstanding the fact most submissions made to the parliamentary committee that investigated this matter recommended a change in the tax benchmark, there was no change in the latest tax expenditure statement.

At least there is acknowledgment by Treasury that by failing to account for the effects on the age pension (superannuation reduces the outlays on the age pension), the meaning that should be attached to the superannuation tax expenditure figures is very limited.

"Some commentary argues that expenditure (on the age pension) savings should be recognised in the estimates of the superannuation tax expenditures. Tax expenditures are a more limited construct than a budget costing and, by their nature, do not seek to measure the full budgetary impact on related current or future government expenditure since they are not taxes."

I just wish other commentators bothered to read the appendix that outlines the qualifications (my sad-sack status confirmed).

As the government considers changing yet again the taxation that applies to superannuation, the relevant ministers should bear in mind that Treasury is not a reliable source of information (or advice?) on this matter.

The key policy challenge is to support those who are likeliest to be able to fund their own retirement or claim only a part pension. This cannot be achieved by hitting middle and upper-middle income earners with more tax — let's call it $6bn a year, a rise of 80 per cent.

And the government may consider setting free low-income earners, who are completely dudded by compulsory super. They are forced to forgo current consumption, pay too much tax, then rely solely on the full age pension — it's a terrible deal and the government knows it.

Just don't expect the superannuation funds to agree.

Among the many comments online in response to Professor Sloan's article is this pertinent one from 'Timothy':

Timothy 1 HOUR AGO

You are not the only commentator that has, over the last several years, time and again pointed out the outrageously misleading and inflated estimates of the cost to the revenue of the so called tax "concessions" for superannuation that are so blithely put about in the media and by the commentariat. Treasury itself has repeatedly warned about the misuse of the statistics it produces. Despite this self proclaimed "respectable" and "independent" economic commentators such as the Grattan Institute and the Australia Institute (more aptly described as left wing think tanks) have repeatedly trotted out these grossly inflated numbers in support of their advocacy for the elimination or restriction of these so called "concessions". They do this by simply ignoring and without ever seeking to rebut the arguments of those who point out the obvious flaws in the methodology behind the falsely inflated numbers that they cite. The only conclusion that can be drawn is that these think tanks are either incompetent or, more likely, are more interested in pushing a left wing ideological political agenda based on class envy than they are in accuracy, professional rigour, or independence and will stop at nothing, including misleading the public, to advance their socialist prescriptions. No self respecting economist or public figure should have anything to do with them.

Shock report: young people get a smaller share of tax concessions

The latest effort from one of the left wing think tanks Timothy refers to in his comment is the astounding revelation that young Australians get a smaller share of tax concessions than older Australians.

So astounding that the Sydney Morning Herald and The Age gave headline treatment to a report from their Chief Political Correspondent, Mark Kenny.

THE AGE
Federal Politics

Tax breaks on rentals and super unfair to young

So what's the story?

The Australia Institute commissioned the National Centre for Social and Economic Modelling (NATSEM) at the University of Canberra to look at the distribution of tax concessions by age.

NATSEM produced a 3-page briefing note. It found that the share of negative gearing, CGT discount and superannuation tax incentives going to people under the age of 30 is only 6.4%.

Those aged 30-39 get a 15% share; 40-49 get $25%; 50-59 get 28% and 60+ get 26%. No account was taken of the number of people in each age category or their incomes.

The result is about what you would expect given young people tend to earn less and be more focused on raising a family and buying a house while middle-aged people have a greater capacity to save and invest.

This unremarkable 3-page ‘research’ finding nevertheless got a headline and story in leading Fairfax papers.

The NATSEM brief is similar to the claim often made that people on higher incomes get a larger share of superannuation tax concessions. Of course they do, but they also pay an even larger share of income tax in the first place. This is never acknowledged by those who claim super tax concessions are unfair.

And why were we not surprised that the NATSEM/Australia Institute brief blithely adds together the tax concessions on contributions and earnings which Treasury clearly warns should not be done? Maybe they need a tutorial from Professor Sloan.

The Australia Institute says it is “the country’s most influential progressive think tank” with “no formal political ties”. But it has plenty of informal ones. Its Executive Director, Chief Economist, Deputy Director and Strategist were all previously senior staffers for the Greens and the Australian Democrats.

The Australia Institute says it is funded by donations – unlike its counterpart the Grattan Institute which lives off funding of $30 million by previous Labor Federal and Victorian governments.

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