Treasury Laws Amendment (Better Targeted Superannuation Concessions) Bill 2023

Submission from Lorraine Graham 17 October 2023

Thank you for the opportunity to comment on the proposed legislation to impose an additional 15% tax on the earnings of individuals with a total superannuation balance above $3m.

This legislation has major faults, but some of them are relatively easily fixed. In this submission I have listed the problems I see with the new tax and suggested ways the legislation can be improved to overcome them. I have first summarised the problems and then covered them all in more detail with some constructive suggestions.

In summary the problems are:

1. The new tax applies to unrealised capital gains, creating adverse effects for some individuals. It may result in tax being paid on money which is never received and the possible necessity to sell assets to pay the tax. This can easily be fixed so that only normal taxable gains are included in the calculation of the new tax.

2. Individuals who currently have a superannuation balance above $3m should be given the opportunity to take out the excess without adverse capital gains tax consequences. This should also apply to individuals with excess balances who have not yet reached preservation age. These people contributed to their superannuation in good faith, believing that the rules would remain stable.

3. The proposed lack of indexing will disadvantage future retirees in comparison to current ones. Index this amount in the same way as the transfer balance cap.

4. Pension-mode super should be exempt from the new tax even if this is above the $3m threshold. There is already a transfer balance cap on pension-mode super, so it should never be considered an excess amount.

5. The current superannuation legislation makes it difficult for individuals to accumulate very large superannuation balances, so the existing large balances will eventually disappear from the system as current retirees fall off the perch. Why add this extra complication when the problem will completely resolve itself over the next twenty years or so? If the tax concessions on existing large superannuation balances (accumulated under rules which no longer apply) are considered to be such a problem, there are far better ways than this to address the issue.

6. This new tax adds to the already over-complex rules around superannuation. The current system has become so unwieldy that it is beyond the comprehension of most retirees and is scarcely fit-for-purpose. Retirees need rules that they can understand. Simplify the whole system to make it more fair and more straightforward. This could free up accountants, financial planners and Centrelink staff to do more productive work, thereby increasing the productivity in our economy.

The new tax applies to unrealised capital gains

The new tax has been designed to be calculated using information already available to the ATO for an individual's super, namely the opening and closing balance and the contributions and withdrawals. The taxable amount includes increases in the value of assets which are unrealised gains, and which can disappear again in an instant, leaving the person with a tax bill on gains that will never be crystallised. Carrying forward losses to later years just doesn't cut it. There may never be another gain, and around 3% of retirees on average will be dead by the following year.

Since the tax is levied on unrealised gains, individuals may not have the cash to cover the tax owing without selling the asset.

Is this calculation method really the only way this can be done?

For SMSFs, the increase in value is currently reported to the ATO for each fund member, as well as the taxable income for the overall fund, adjusted for pension mode earnings. These SMSFs could easily apportion the taxable income among their members in the same way as they apportion the total increase in value of the fund.

It would only take one extra figure to be calculated and submitted to the ATO for each member to allow the extra 15% tax to be calculated on the earnings that are taxable within the fund for that person.

Any competent SMSF administrator could easily calculate this value in their system and report to the ATO the actual taxable income in the fund for each member.

It beggars belief that large retail and industry funds cannot do a similar calculation for their members. It is not as if we still have rooms full of clerks manually adding up numbers to work out member balances. Computers can do this in micro-seconds and reporting one more figure for each member is not going to overload the systems already in place.

There are two more years at least for super funds to upgrade their reporting systems before this legislation comes into effect. This is plenty of time for the reporting change to be made.

Managed funds send out statements of taxable income to all their investors. Why is it so difficult for super funds to do the same?

If the retail and industry funds won't come to the party, at least give SMSF members the option of having the new tax applied to their real earnings, not fairy-tale asset value increases.

If the taxable earnings for each individual is reported to the ATO, then the new tax can easily be calculated using this amount rather than the increase in value as currently proposed.

Give individuals with a balance above $3m the opportunity to take out the excess

Australians contribute to superannuation in good faith that they are following the rules that apply at the time, and will not be adversely affected by future changes. Those with a

balance above $3m, legitimately obtained, now have to consider whether super is still the best place to leave their savings.

This new tax will also affect those under 60 who have excess balances and are currently not permitted to withdraw funds even though super may no longer be the best place for their money. These people should be given the opportunity to take out the amount above the $3m threshold.

For many people, taking the excess over $3m out of their super would generate a capital gains tax liability. Where the asset in question is a farm or a business property, these people are between a rock and a hard place. They may have to sell the asset to raise the new tax owing if they leave the asset in super, or they may have to sell it to pay the capital gains tax owing by the super fund if they transfer it out.

I would suggest giving a one-off opportunity to withdraw non-liquid assets such as farms or business premises from super without a capital gains tax event being triggered, so the farmer or business owner can choose to retain the original cost base of the asset when it is transferred out of super into a trust or an individual's own name.

This opportunity should also be extended to those under 60 who wish to reduce their balance to avoid the new tax.

Index the amount of the large balance threshold

The proposed lack of indexing will disadvantage future retirees in comparison to current ones. Index this large balance threshold in the same way as the transfer balance cap.

Pension mode super should be exempt from the new tax

The new tax should not be applied to the earnings of pension-mode super, although the value of the pension-mode super would still be included when calculating the total superannuation balance.

Pension-mode super should remain tax free, even if it grows to exceed the large superannuation balance threshold. The transfer balance cap was set to give a reasonable amount of retirement income, and individuals who grow their pension-mode super in spite of having to take out a minimum each year should not be penalised with extra tax.

Is this new legislation really needed?

The current superannuation legislation makes it difficult for individuals to accumulate very large superannuation balances, and the existing large balances will eventually disappear from the system as current retirees fall off the perch. Why add this extra complication when the problem will completely resolve itself over the next twenty years or so as these larger legacy accounts are wound up?

If the few very large legacy balances are such an important issue, there are better ways to deal with the problem.

The best way is already in place – restricting non-concessional contributions to super by individuals who have reached the transfer balance cap of $1.9m. If these individuals manage to increase the balance in their super to be above the cap by successful investing, surely this is a good thing, as it allows the income of the retiree to keep up with inflation. The current large balances will leave the system in time.

Another simple fix is to introduce a total superannuation balance cap of $5m (or $3m), indexed in the same way as the transfer balance cap. All super above this level would be withdrawn as a one-off. However if balances subsequently rose above this, they could be left in place. This would be far less complex to introduce than the previous transfer balance cap changes were, and far less complex to administer than the proposed new tax.

Another approach would be to require anyone over the retirement age to take out a percentage of their total superannuation balance each year, rather than just their pension mode super. The large balances would rapidly reduce. Easy!

Again, special consideration would need to be given to farms and business properties, but with the current contribution rules, these are unlikely to be held in the super funds of younger Australians, and will work their way out of the system in time.

The new tax will add yet another layer of complexity

This new tax adds to the already over-complex rules around superannuation. The current system has become so unwieldy that it is beyond the comprehension of most retirees.

Simplify the whole system to make it fairer and more straightforward.

Two ways to do this:

Eliminate the difference in the tax treatment of accumulation and pension-mode super, so the normal 15% tax applies to all super fund earnings. At the same time, give a tax rebate of up to $15,000 to everyone over retirement age, with an obligation for them to take out the established age-based percentage of their total superannuation each year.

To allow for this, the retail and industry super funds, as well as SMFSs, would give the earnings amount and tax paid amount for each member to the ATO at the end of the financial year, and the ATO would rebate the lower of the tax paid and $15,000 either to the fund of choice or directly to the retiree. This would effectively give a maximum of $100,000 of earnings within super tax free. This option would eliminate conversion to pension mode, the transfer balance cap on the amount that can be converted, and the need for actuarial calculations. It would be straightforward to administer and easy for retirees to understand.

Alternatively, the system could be made really simple and absolutely fair to all retirees by giving everyone over 67 a full government age pension, but requiring them to pay tax at normal rates on their super fund earnings, which would simply be reported to them at the end of each financial year by their super fund (in the same way as managed funds now report) along with the amount of the 15% tax already paid by the fund on their behalf. Tax would be paid by the retiree on their total income, including the super earnings, with a refundable offset for the tax already paid within the fund. This would be no more complex

for the retiree than employment income and PAYG tax paid, or dividend income with associated franking credits.

This option would also eliminate the complex calculations (ie the assets and income tests) for government pension entitlements. Individuals would still contribute to super as now (with tax benefits to reward them for saving for their retirement) and could leave their money in their super fund during their retirement years. On retirement they would be obligated to take the usual percentage each year as an account-based pension, and would pay tax at normal income-tax rates on the earnings reported by the fund. Retirees could then plan to maximise their retirement assets without the need to consider how their balance would affect the amount of age pension they were likely to receive.

Both of these options would free up accountants and financial planners to do more productive work. The second option would also free up Centrelink staff who are currently involved in age pension administration. This would contribute to the overall productivity of the economy.