ACTU SUPER

ACTU SUPERANNUATION TRUSTEES NETWORK NEWSLETTER
No. 2, May 2006 ~ Special Budget Edition

EDITOR: Nixon Apple Fax: 03 9663 4051 Email: napple@actu.asn.au

The editorial staff of Super News is pleased to provide our readers with this special budget edition dealing with the changes to the superannuation system that the Treasurer proposed in the May 2006 budget. In future editions of Super News we will provide more commentary on the specific changes that are now subject to consultation between Government, the super industry and the Australian public.

However, given the significance of the changes we asked ACTU President Sharan Burrow to provide a union perspective on the big picture issues the budget changes raise. The focus is on what was included in the budget changes as well as key issues that were not dealt with.

A Super New System?

ACTU President, Sharan Burrow

After considering the May 2006 budget and the proposed changes to superannuation, the ACTU has reached the following conclusions.

The overwhelming majority of low and middle-income earners who are over 50 today will never pay tax on their super when they withdraw it at retirement at age 65. This is the way it is today before any of Peter Costello's changes to Super announced in the May budget.

Why?

Currently, if they take it on retirement as a lump sum and their account has less than $130,000 it is almost always tax-free.

The overwhelming majority of low and middle income workers over 50 today will not have more then $130,000 in Super when they retire. They have not been around long enough to benefit from the 9% SGC to build a decent account balance.

In the mid 1980's more then 50% of private sector workers had no super at all and many of those who did only got the employers contribution if they stayed with the company for 15 to 20 years.

This is the generation who missed out on the full benefits of the 1980's labour movement created system of compulsory super. It is the generation who will be dependent more than the next on the age pension. And what this generation needs is a much bigger nest egg for retirement.

Similarly, if the low and middle income over 50's had taken their super under the pre Costello arrangements (when they retire) as an annuity, or allocated pension and are within the RBL (Reasonable Benefit Limits), they pay no tax on their Super drawdowns as an income stream.

These outcomes are highlighted in the table below showing the Treasury estimated outcomes for those retiring now under the proposed new system.

Example 1: Couple: Superannuation Pension

Combined benefit at retirement age 65	Effect of new Super tax changes: Changes in total average weekly retirement expenditure	
	$ per week	% charge
(a) $ 200,000	0	0
(b) $1,200,000	$193	16.1%

Example 2: Individual: Lump Sum

Benefit at retirement age 65	Effect of new Super tax changes: Changes in after tax benefit	
	$	% charge
(a) $100,000	0	0
(b) $400,000	$43,522	12.2%

Clearly as the tables suggest, there is little or no gain for those near retirement who haven't had time or the income over their working life to accumulate more than $130,000 in super. As for a worker aged 45 with 20 years of work before retirement, the table below from Treasury also shows that the big gains go to high income earners with little or no benefit to lower-middle income workers earning less than $40,000 a year.

Example 3: Worker age 45 getting only 9% SGC and retiring in 20 years (takes lump sum)

Weekly Income	Benefit at Retirement	Change in after tax lump sum as result of Super tax changes	
		$	%
$ 400	$ 95,125	0	0
$ 800	$194,082	$ 2,400	1.3%
$2,000	$490,981	$51,389	11.7%

Yes, for younger workers the proposed new system will help.

Yes, the Government has proposed more generous arrangements for the self-employed and self-funded retirees.

Yes, we acknowledge the benefits of what the government proposes to do in terms of simplifying a major part of the existing system in terms of end benefit taxation.

However, it would have helped more by abolishing the contribution tax. As ASFA points out.

- Take a worker on $50,000 who works 30 years. Abolishing the contributions tax now will make their end benefit 15.8% higher. Abolishing the tax on end benefits will only increase the lump sum by 4.8%. This could be made more equitable by means testing the withdrawal of the contributions tax so that it only applied to low and middle income workers. We acknowledge the additional administrative complexity involved with this and are still looking at ways it could be done in a simple way.

- In addition, we could have made the existing co-contribution scheme even more generous for the low and middle income over 50s, to help them onto a fast track to enlarge their super balances before retirement. Last night's budget and future budgets could also have developed a means tested system for one off government payments into the accounts of older retiring workers with very low account balances. I will not talk about that any more today as we are conducting research into the available options.

The ACTU acknowledge that there is also a legitimate debate with our ALP colleagues about contribution tax and whether this is the best use of the $3.3 billion that it would cost (half that amount if means tested) today on an annual basis to abolish the contribution tax. The Costello package costs just over $2 billion a year. Until a full detailed actuarial assessment of the costs and benefits of Costello's package over the next 20 years is provided it cannot be properly assessed. This must include a distributional analysis that shows who gets what.

As Fred Argy put it in a letter to the *Australian Financial Review dated 15/05/2006:*

"Some commentators have been getting too excited about the budget superannuation reforms. The federal government has simplified the system, and that's a plus. But what will they do to national savings and distributional equity?

The reforms overwhelmingly favour the rich: so one can expect that many of them will merely switch from other forms of saving and buy themselves bigger cars and houses. So any net effect on private saving could turn out to be fairly small.

On the other hand, government saving will be doubly affected.

The increase in the already generous tax concessions on superannuation will further reduce future tax revenue. And, as the reforms make lump sums more attractive, some middle-to high-income people will be tempted to flog their lump sums so as to qualify for the age pension, causing a further drain on revenue.

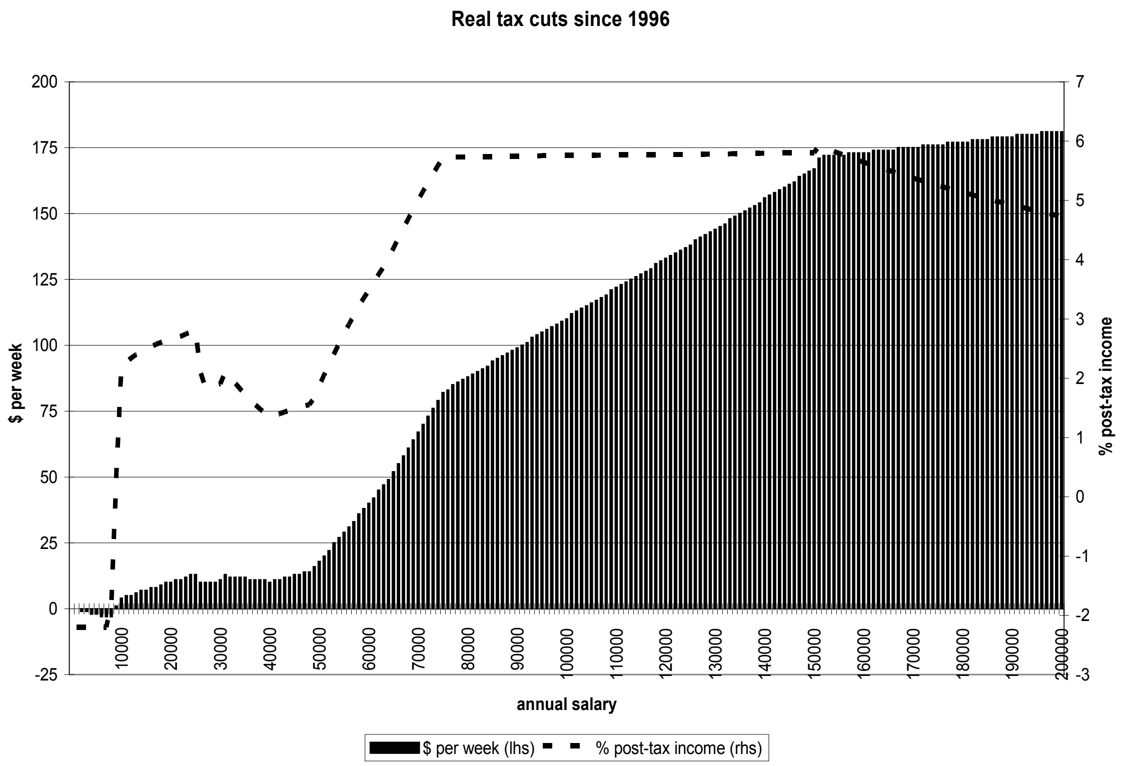
In short, the net effect on national savings may even be negative."

The way forward here is for a committee to be established comprising the Australian Institute of Actuaries, ASFA, IFSA and Treasury's retirement income modelling team. Modelling scenarios of the costs, benefits and distributional effects of the new package need to be put on the table for critical public scrutiny.

In terms of the distributional effects let's not forget what has happened since 1996 in terms of tax cuts. As shown in the graph below (which adjusts for bracket creep and the GST since 1996), high-income earners who are the main winners out of super have also been the main winners on tax cuts. Since 1996, seventy per cent of the benefits have gone to the one-third of tax payers earning more than $50,000 a year. While households with dependent children have done well from family benefits, more than 60% of low and middle income households dependent on wage and salary income don't get those benefits. And many of those who do face high effective marginal tax rates for each extra dollar of income earned.

It is time to put equity back on the agenda and restore the ethos of a fair go.

Instead, what the Prime Minister and Treasurer have given us is a flat tax super system where a disproportionate share of the benefits go to the top end of town with no proof that (like the Coalition critique of Medicare Gold) the costs won't blow out beyond the forward estimate time horizon. Finally, when the resources boom moderates and commodity prices come back, a Howard-Costello Government is likely to respond to the slow down in revenue growth by adjustments to spending programs (health, education and welfare) rather than backtracking on the tax cuts.



In the ACTU's view, abolishing the contributions tax would have been a big step towards the shared labour movement goal of a retirement income system that delivers workers a retirement income equating to at least two thirds of their gross pre retirement income.

The ACTU also believes it is a disgrace that Peter Costello has not abolished the super income threshold test where an employer who pays a worker less than $450 a month doesn't have to pay them any superannuation. And the Government has before it the Report from the Business Regulation Review Unit recommending that the threshold be increased to $800 a month!!!

While over 90% of Australian wage and salary earners in their main job get 9% super or more, only 50% earning less then $200 per week get paid super. That's nearly 400,000 mainly low paid part time and casual workers who miss out on being paid super and the main reason is the earnings threshold test. That number would almost double if Costello raises the threshold to $800. Then there are the tens of thousands of workers in a second or third job who also don't get paid super because of the threshold test.

The solution here is straight forward. Abolish the income threshold test. As in Finland, establish one Government account for employers to pay employees super into. The money would be invested in a capital guarantee mix of asset classes by the Future Fund. When a low paid worker accumulates enough income in their account or earns a higher income, they can move their account to the private sector fund of their choice. Such a change to assist low paid, part-time and casual employees is long overdue.

It is also the case as suggested earlier that the ACTU has real concerns about high-income earners with very large account balances not having any tax to pay on their super payouts. We will be looking at this issue more closely.

Finally, the Costello package does nothing to integrate the future of Super and healthcare. This is a major failure given the ageing of our population.

Many Australians are concerned that their retirement income will be short of their needs as they live longer, and that the purchasing power of their pension will be eroded by unforeseen additional costs. This is particularly the case with health services and prescription medicines. This problem is most pressing today for nearly two million Australians who are already in receipt of the age or service pension. It is also of concern for those over 40 and under 65 who have not had the benefit of accumulating the 9% SG contributions for a sufficiently long period of time.

It is also a significant issue for those under 40 in two important respects. First, many of the under 40's are starting a family, trying to find ways to save to purchase a home while at the same time saving and meeting the additional costs of health services. And secondly, the under 40's are faced with the uncertainty of who will pay the rapidly escalating national health care bill associated with the ageing population and retirement of the baby boomers.

The ageing of the population holds even more challenging problems for how the nation pays for health services. As a number of official reports have demonstrated:

- Over the next 40 years the proportion of the Australian population over the age of 65 will double to around 25%;

- Over the same period the ageing of the population will (on unchanged policies) be associated with a reduction in the proportion of the workforce that has a job or is looking for one from close to 64% today to around 56%;

- The average expenditure per year on health and age care services for people over 65 is almost four times more than for those under 65 and six to nine times higher for older groups. As a result health care spending by Government could rise from 5.7% of GDP in 2003 – 2004 to 10.3% in 2044-45.

Not surprisingly many Australians are wondering how this will be paid for. Once again the present Government has failed to provide any answers notwithstanding that it has revenue running out of its ears. Of course, policies to increase workforce participation, stronger productivity growth and other factors can help to cushion the impact of the ageing population. Nevertheless a substantial challenge remains.

This scenario has significant consequences for all Australians in terms of the future purchasing power of their government aged pension. It also raises profound economic, social and moral issues, not just about paying for health services but for access to such services. In the future new technologies, drugs, and medical procedures will offer the hope for treatments and cures unimagined by previous generations. But who will pay for them and will access be rationed inequitably by the sole principle of capacity to pay? What can Government promise to its citizens and how can it deliver on that promise? What will people be expected to pay out of their pension in retirement, or will paying more today, if that is required, ensure and protect the future purchasing power of the pension?

It is not just about income adequacy, important as that is. It is also about the nation's citizens having a sufficient degree of certainty to plan and make provision for the future.

Today Australians are experiencing unacceptably long waits for elective surgery, and the consequences of the gutting of the Government's "iron clad, rock solid" guarantee to protect the Medicare Safety Net thresholds. In addition, they face increased costs of prescription drugs and the uncertainty about access to such drugs through PBS.

In addition there are more then 600,000 waiting (many for more then 18 months) in the queues faced by elderly pensioners, the low paid and disadvantaged for subsidised public dental care. This is largely because of the abolition of the Commonwealth Dental Program in 1997.This comes at a time when three of the five major medical conditions afflicting the largest number of Australians are gum disease, loss of teeth and tooth decay.

The challenges for both sides of politics at the State and Federal levels as well as the broader community will intensify in the decades ahead. Already we are seeing worrying trends such as the rise in the out of pocket expenditure by individuals on health care, which have increased by more than 8.0% per annum since 1996.

That is why the interface between the nation's retirement income system and its health care system is one of the most important issues for public policy. And that is why the ACTU is concerned about current notions of retirement income adequacy and the future purchasing power of the pension. The Costello package addresses none of these issues on the interface between the retirement income system and the healthcare system. That and increasing the Super account balances and retirement incomes of the over 50s who are low and middle-income earners are among the major challenge the nation faces.