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Senate Standing Committees on Economics
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Parliament House
CANBERRA ACT 2600

By email: economics.sen@aph.gov.au

19 December 2011

Subject: MINERALS RESOURCE RENT TAX BILLS AND RELATED BILLS

Dear Sir/Madam

Mercer is please to make a submission in relation to the package of Bills referred to under the Minerals Resource Rent Tax Bills and Related Bills.

Our comments are limited to issues in relation to the:

- Superannuation Guarantee (Administration) Amendment Bill 2011 (the gradual increase of the SG charge percentage from 9 to 12% and the removal of the age limit for Superannuation Guarantee (SG) contributions)
- Tax Laws Amendment (Stronger, Fairer, Simpler and Other Measures) Bill 2011 (in particular the low income superannuation contribution)

Who is Mercer?

Mercer is a leading global provider of consulting, outsourcing and investment services, with more than 25,000 corporate and trustee clients worldwide. Mercer consultants help clients design and manage retirement, health and other benefits and optimise human capital. The firm also provides customised administration, technology and total benefit outsourcing solutions including the running of the Mercer Super Trust in Australia with over $15 billion of assets. Mercer's investment services include global leadership in investment consulting and multi-manager investment management. We also provide personal financial advisory services for individuals including Self Managed Superannuation Funds.

Executive Summary

Mercer strongly supports the increase in the SG to 12% as this will increase retirement savings and reduce future reliance on the age pension. This is particularly important in the light of increased longevity and Australia's ageing population.

The SG system is often referred to as the second pillar in Australia's three pillar retirement income system (the other pillars being the Government funded age pension and voluntary superannuation savings). In any analysis of superannuation and the cost of its tax concessions, it is important to take a holistic perspective by allowing for the three pillars. That is, concentration on the taxation support provided for superannuation, without reference to the effects on future age pension costs does not consider the full picture. We have therefore included with our submission, a copy of a report on research we undertook in 2010 entitled "The fairness of government support for retirement income". The conclusion from this research was that, contrary to the opinion of some groups, the total Government support for retirement incomes, taking into account both superannuation tax concessions and the age pension, is remarkably consistent across a range of lifetime income levels.

Another significant conclusion from our research is that an increase in the SG to 12% will generally result in a reduction in the total level of Government support for retirement incomes. In other words the increase in SG will reduce the costs of supporting retirement incomes and will therefore increase the sustainability of Australia's retirement income system.

Since the completion of our analysis, various announced changes to tax concessions have been made and we propose to update our research early next year to take these issues into account. We will forward a copy of our findings when they become available although we would expect that these changes would not materially change the outcomes.

It is also important to acknowledge that any increase in the SG rate will reduce the ability of high income earners to make voluntary salary sacrifice contributions and remain within the concessional contributions cap. If the cap is exceeded, excess contributions are generally taxed at 46.5%.

Mercer also supports the removal of the age limit for SG contributions and the introduction of the Government contribution for low income earners. The Government contribution will reduce one of the current perceived "inequities" resulting from the 15% superannuation contribution tax which is potentially greater than the income tax rate paid by many low income earners. However, we have concerns with some of the details and have suggested ways of improving this initiative.

We elaborate further on these points below:

1. Increases to Superannuation Guarantee (Superannuation Guarantee (Administration) Amendment Bill 2011)

This Bill includes provisions to gradually increase the SG charge percentage from 9 to 12%.

Mercer strongly supports this gradual increase and believes it will improve the adequacy of retirement benefits provided to Australians and Australia's retirement income system.

The SG system has now been in operation for 19 years and has resulted in a sound retirement savings base for many Australians. It is one of the reasons that the Australian retirement system ranks second in the Melbourne Mercer Global Pension Index.

An increase to 12% will further enhance the system and, based on Mercer analysis (refer below) will actually lead to a reduction in Government support for retirement incomes over the long term (i.e. higher short term tax concessions are more than offset by long term savings in funding the age pension).

We note that there are often assertions from different sectors and interest groups that the distribution of superannuation tax concessions benefits higher income earners. However such criticism generally ignores the fact that Australia has a three pillar retirement income system:

- Pillar 1: the Government funded age pension (means tested)
- Pillar 2: the compulsory Superannuation Guarantee system
- Pillar 3: voluntary superannuation savings

and often fails to take into account the direct link between the level of retirement savings resulting from the second and third pillars and the consequent reduction in the Government age pension.

Mercer believes that a more appropriate approach is to consider the total level of Government support for retirement income over a person's lifetime, i.e. taking into account the cost of superannuation concessions as well as the cost of the Government age pension. We have attached a copy of our 2010 research into this total level of Government support ("The fairness of government support for retirement income").

Our research highlights that:

- for a single person, the total level of Government support towards retirement income is almost constant across most individuals notwithstanding their different lifetime incomes and will generally reduce if contributions increase from 9% to 12% (The analysis at the 12% rate was based on a 3% voluntary employer or salary sacrifice contribution however the same outcome would arise if the SG is increased to 12%)

- for a dual income couple, the level of Government support generally decreases as incomes rise. It also decreases as superannuation contributions increase (from 9% to 12%).

When looked at over an individual's lifetime the total government support for retirement incomes is remarkably consistent across a range of income levels. Increased superannuation contributions will provide higher superannuation benefits in the future, which should reduce future age pension costs across almost all income levels.

Tax concessions for high income earners in the short term will generally be more than offset by long term savings in funding the age pension.

We also note that tax concessions for high income earners are significantly restricted by the concessional contribution cap. These restrictions will become more severe due to:

- the expiry of the transitional $50,000 cap for those aged 50+ from 1 July 2012
- the proposed freeze on indexation of the $25,000 concessional contribution cap

Further, any increase in the SG contribution rate will limit the ability of high income earners to make voluntary salary sacrifice contributions whilst remaining within the $25,000 concessional contribution limit. As contributions in excess of the limit are generally taxed at the rate of 46.5% (although the tax rate can be as high as 93%), contributions are generally restricted to the cap.

It is worth noting that our 2010 analysis did not take into account the following:

- The current Government co-contribution. The co-contribution provides additional government support for low/middle income earners with no to minimal impact on high income earners. It is therefore disappointing that the Government has announced a reduction in the level of co-contribution and the consequent reduction in Government encouragement for low income earners to save for retirement.
- The proposed low income superannuation contribution. This concession will increase the Government support for some low income earners
- The proposed freeze of the indexation of the concessional contribution cap which will reduce the tax concessions available to high income earners

We will shortly update our analysis and will forward a copy of our findings when they become available. We would expect that these changes would not materially change the outcomes.

2. Removal of the maximum age limit for Superannuation (Superannuation Guarantee (Administration) Amendment Bill 2011)

This Bill includes provisions to remove the age limit of 70 currently applicable to SG. Mercer supports this removal and its broadening of the range of employees covered by the SG.

Mercer considers further improvement to the adequacy of the SG system will be achieved by widening its coverage to include many of those currently excluded. Those who remain excluded (i.e. the self employed, unemployed, disabled, those on workers compensation or paid parental leave and those earning less than $450 a month) for long periods of time are significantly more likely to need to rely on the age pension rather than their own retirement savings. We believe more consideration needs to be given to additional initiatives to assist these groups.

3. Low Income Superannuation Contribution (Tax Laws Amendment (Stronger, Fairer, Simpler and Other Measures) Bill 2011)

We welcome the opportunity to comment on and support the amendments to the *Superannuation (Government Co-Contribution for Low Income Earners) Act 2003* which are included in the Bill. These amendments will broadly result in a full offset for contribution tax on Superannuation Guarantee (SG) contributions (at least at the 9% level) of individuals earning up to $37,000.

We believe the Low Income Superannuation Contribution will address the current anomaly whereby low income earners effectively receive low or no income tax concessions on their SG contributions – in some cases these contributions are taxed more heavily than normal income. However, we believe that the provisions relating to this Government contribution could be improved in the following areas:

Lack of indexation

The $37,000 income threshold is not indexed. As a result, the number of low income earners entitled to the Government contribution is likely to diminish over time.

Further, the maximum $500 contribution is not indexed. As the SG contribution rate increases above 9%, the Government contribution will not fully offset the contribution tax on SG contributions for all those earning less than $37,000.

Indexing the maximum amount in line with the SG increases and indexing the $37,000 threshold would improve the value of this initiative to low income earners. For example, once the SG reaches 12%, a Government contribution of $666 would be required to offset the contribution tax on SG contributions for a person earning $37,000 (15% x 12% x $37,000 = $666).

Lack of phase out

The low income super contribution is payable for incomes up to $37,000 and then ceases abruptly. Earning one dollar of additional income can therefore result in up to $500 of lost tax benefits. This concern would be higher for older workers who are potentially working part-time as they phase into retirement.

Phasing out the Government contribution over an income range of say $37,000 to $42,000 would reduce the potential disincentive to work that might arise for those earning around this level.

Complexity

Entitlement to the low income superannuation contribution requires satisfaction of two income tests with two different definitions of income:

- ***Adjusted taxable income*** must not exceed $37,000
- At least 10% of ***total income*** must result from business or employment

The use of different income definitions for these tests adds to complexity and confusion for members as well as for superannuation funds and financial advisors who will need to explain these different definitions. We note that the definition currently used for the purposes of the Government co-contribution is *total income*. From a consistency point of view it would be logical if the same income definition applied to both tests.

If you have any queries on our comments or would like further information please contact John Ward on (03) 9623 5552.

Yours sincerely

David Anderson
Managing Director & Market Leader
Australia/New Zealand

MARSH & McLENNAN COMPANIES